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Effect of Ownership Structure on Earnings Management of Listed Industrial Goods Companies in Nigeria

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Abstract: *This study examined the effect of ownership structure on earnings management of listed industrial goods companies in Nigeria from 2008 to 2017. The study adopted Ex-post facto research design and panel regression model was used to analyze the data. The results revealed thatdomestic institutional ownership has positive significant effects on earnings management, foreign institutional ownership has positive insignificant effects on earnings management,managerial ownership has insignificant effects on earnings management and number of block holders has negative significant effects on earnings management.The study draws an overall conclusion that ownership structures have positive insignificant effects on earnings management of listed Industrial goods companies in Nigeria.The study therefore, recommended that the management of Industrial goods companies should put in more measures to reduce the domestic ownership in order to have a fair and reliable financial statement. Finally, the Number of Block holders have significant effect on the earnings management as such, the companies should encourage combined ownership in their companies.*

Keywords: *Block holders, Domestic ownership, Earnings management, Foreign ownership, Ownership Structure* **Word count:** 161

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I. Introduction

Ownership structure is a mechanism that operates in an organization as an instrument of corporate governance to facilitate and increase efficiency of a firm. These structures are of major importance in corporate governance because they determine the incentives of managers and thereby the economic efficiency of the corporations they manage (Jensen &Meckling, 1976). The term ownership structure has two widely applied dimensions: ownership concentration and owner identity. Ownership concentration measures the degree of concentration of voting right in listed corporations, it is measured by the voting right of the largest shareholders. Owner identity is based on the type of the largest shareholder (Saseela&Thirunavukkarasu, 2017).Hui and Khine (2017) argued that one feature of the modern listed companies is the wide-spread ownership structure. Shareholdings of various shareholders generate the conflicts of interest among shareholders, thereby influencing firm performance of companies. Thus, appropriate ownership structure may support companies to have a good performance in market. For instance, although concentrated ownership by institutional owners can bring a positive effect on firm performance (Elyasiani&Jia, 2010), inappropriate level of ownership concentration can bring negative effects on firm performance (Dahya, Dimitrov, & McConnell, 2008). The political shareholding can also have negative impact on firm performance (Chang & Wong, 2004).

Earnings Management is the transformation of accounting figures from what they actually are to what preparers desire by taking advantage of the existing rules and ignoring some or all of them (Naser,1993). Earnings management is known as a situation where management alter reported earnings through the use of exact accounting systems either by expense increase or revenue decrease, or by other means designed to influence short term incomes. The term is normally assumed as systematic falsification of the true earnings as well as company's assets. Earnings management happens when managers use discretion in reporting to structure items as to adjust annual reports, to either misinform some stakeholders regarding the underlying economic performance of the entity, or to influence contractual outcomes that depend on reported income.

Nedal, Bana and David (2009) study the association among earnings management and ownership combination of some Jordanian industrial companies spanning 2001 to 2005. Earnings management as determined by discretionary accruals, insiders, institutions as well as block holders are determinants of ownership composition used. Employing the Generalized Method of Moment, outcome revealed insider ownership is significant as well as positively influence earnings management. The result of the study also shows that responsibility ofinstitutions and block holder are not significant in monitoring managerial behaviour of earnings management. The discovery containssome crucial strategic consequences since it supports the drive for corporate governance rules in order to stimulate institutions as well as block holders to present successful monitoring of managers. Therefore, credibility of reported earnings may be improved.The influence of management in the preparation of financial statement has been questioned. This is due to the fact that Earnings are the transformation of accounting figures from what they actually are to what preparers desire by taking advantage of the existing rules and ignoring some or all of them (Naser,1993). With this, confidence in the prepared reports are weak.Warfield et al (1995) argued that managers who hold a considerable segment in the equity of a company have a lesser amount of incentive to influence reported accounting information. Balsam, Bartov and Arquardt (2002) state that institutional investors, who happened to be complicated investors, are more competent in noticing earnings management than non-institutional investors because they have extra access to appropriate and relevant information.

Earlier studies on earnings management like Sen and Inanga (2004), Domash (2002), Amat, Blake and Dowds (1999) Naser (1993), Schiff (1993), and Alam (1988) most of these studies were conducted outside Nigeria which have difference in style of corporate governance and some of them focused mostly on the effects of earnings management on investors' decisions in the stock market without stressing importance on the factors that may determine that chances of earnings management and most of all, none of these studies was specifically carried out in industrial goods companies in Nigeria. It is on that backdrop that this study examined effects of ownership structure on earnings management of listed industrial goods companies in Nigeria.

1.1 Objective of the Study

The major objective of the study is to examine the effects of ownership structure on earnings management of listed industrial goods companies in Nigeria.
Therefore, the specific objectives are to:

i. determine block holder effects on earnings management of listed industrial goods companies in Nigeria.
ii. ascertain foreign Institutional ownership effects on earnings management of listed industrial goods companies in Nigeria.
iii. determine domestic institutional ownership effects on earnings management of listed industrial goods companies in Nigeria.
iv. examine managerial ownership effects on earnings management of listed industrial goods companies in Nigeria.

1.2. Hypothesis of the study

Based on the objectives, the following hypotheses were formulated to test the effects of the following proxies on earnings management:

H_{01} Block holder has no significant effect on Earnings management of listed industrial goods companies in Nigeria

H_{02} Foreign Institutional Ownership has no significant effect on Earnings management of listed industrial goods companies in Nigeria

H_{03} Domestic institutional ownership has no significant contribution to Earnings management of listed industrial goods companies in Nigeria.

H_{04} Managerial Ownership has no significant impact on Earnings management of listed industrial goods companies in Nigeria.

II. Literature Review

Conceptual Framework

Ownership structure is the distribution of equity with regard to votes and capital but also by the identity of the equity owners. These structures are of major importance in corporate governance because they determine the incentives of managers and thereby the economic efficiency of the corporations they manage. A classic reference is Jensen and Meckling (1976). An excellent newer reference on the topic is Holderness, Kroszner, and Sheehan (1999). Ownership structure is an internal control system exercise over a firm management team (Gonzalez & Garcia-Meca, 2013).They assert that, apart from other firm-level factors which influence earnings management, firm's board formation and composition structure could also provide an opportunistic platform for managers to engage in behaviours that are self-serving.

Block holder: McConnell and Servaes (1995) and Zeckhauser and Pound (1990) stated that block holders can enhance the quality of corporate governance and increase management efficiency by monitoring managers, which may determine the debt level. Specifically, in firms with dispersed ownership and control, small shareholders have less motivation to monitor managers, and less influence, because they hold a small proportion of shares and the loss caused by manager discretion is shared among many investors. In addition, the cost of having information and monitoring may outweigh its benefits. Conversely, in firms with concentrated ownership, large shareholders have both motivation and power to monitor managers to protect their investments (McConnell &Servaes 1995; Zeckhauser& Pound 1990). Supporting this idea, Shleifer and Vishny (1986) and Wiwattanakantang (1999) argued that block holders play an active role in firm performance. Large investors can take control of the firm, replace managers or cut managers' benefits if the firm's performance is poor. As a consequence, large ownership could serve as an alternative for debt financing to boost the monitoring of managers.

Foreign Institutional Ownership: Foreign investors investing in Vietnam stock markets are mainly institutional investors (Vo, 2011) who have the experience and motivation to influence managers to protect their investment (Brailsford, Oliver &Pua, 2002; Friend & Lang, 1988). Institutional shareholders invest in firms on behalf of other individual investors or their customers, and their responsibility is to ensure a high return on these investments. In addition, it is believed that institutional or foreign investors have better access to information as well as better knowledge for using this information to interpret firm performance (Agrawal &Mandelker, 1992).

Domestic institutional ownership: Institutional ownership refers to sophisticated investors who control managerial discretion (Ferreira & Matos, 2008). Koh (2003) argued that there are two opposing views of institutional ownership that affects managers' financial reporting discretion. The author affirms that the activities of short-term oriented (passive) institutional shareholding encourage managers' irrational behaviour. Short-term oriented investors exhibit a strong desire for short-term (current) earnings which render a misleading economic performance of the firm (Koh, 2003). On the other hand, active involvement of long-term oriented institutional shareholders limits managerial incentives to adopt aggressive earnings management and opportunistic behaviour in general (Koh, 2003).

Managerial Ownership: Managerial ownership represents the interest of managers in the equity shareholding of a firm. Managerial ownership assumes that managers' equity holding encourages them to act in a way that maximizes the value of the firm. Warfield, Wild and Wild (1995) suggested that the interest of both shareholders and management starts to converge as the management holds a portion of the firm's equity ownership. This implies that the need for intense monitoring by the board should decrease (Jensen &Meckling, 1976).

Healy and Wahlen (1999) are of the opinion that earnings management happens once managers use discretion to report financial statement and organize dealings to manipulate financial information to either misguide some stakeholders about the fundamental organizational financial performance or to manipulate contractual results that hinge on reported accounting facts. Earnings management is the actions by divisional managers to either increase or decreases present reported earnings of a division without an equivalent increase or decrease of the long-term economic profitability (Fischer &Rosensweig, 1995).

Discretionary accruals are adjustments to cash flows chosen from the opportunity set of generally accepted accounting procedures as stipulated by the standard setting bodies. For instance, "the depreciation method, bad debts provisioning, loan loss reserves and the allocation of fixed factory overhead cost among cost of goods sold and inventories are the specific accruals that have been employed in accomplishing earnings management (Healy, 1985).

Empirical Review

Ling and Pavinee (2012) determined the influence of block holders on earnings management, employing accounting discretional accruals as earnings management determinants. Block holder is measure by outside block holders and owners. Theyfound thatincome diminishing earnings management circumstances,therefore, the study does not establisha significant outcome. This may be due to diverse characteristics as well as outside block holders' difference in time zone. Since the greater part of external block holders are institutional shareholders, it then ascertains ownership correlation as well as institutional shareholders among diverse characteristics and earnings management. Exclusively, it discovers significant positive association among ownership by part term institutional investors who hold diverse portfolios with more returns and accounting discretional accruals. Though, there is no significant outcome among ownership by devoted institutional shareholders who hold concentrated portfolios with fewer returns and accounting discretional accruals.

Sani, Bany, Hairul and Siti (2015) determined institutional ownerships impact on earnings management. They employed both modified Jones (1991) as well as Roychowdhury (2006) models to measure accrual and actual activity behaviours. Institutional ownerships were determined by Conservative and Neutral Pressure Groups. The outcome showed that Malaysian Initial Public Offering companies connect in both real and accrual earnings around Initial Public Offering corporate event. Multivariate analysis indicates institutional investors limit real accrual earnings management which supports the various regulatory reforms by Securities

Commission as well as Bursa Malaysia. The study indicates the need to persuade the Neutral Pressure Group of institutional investors to employ more in shareholders' activism in order to preserve the value of their investments and for investors to determine real activity behaviours in making their investment policy while standard setters and regulatory agencies need to implement additional determinant to limit real activity discretionary behaviour.Teshima and Shuto (2008) studied managerial ownership effects on earnings management employing discretionary accruals. 18,790 Japanese companies were used covering 1991-2000. Kasznik (1999) model was used to proxy the discretional accruals. The outcome revealed a significant positive association among ownership composition with earnings management.

Theoretical framework

Agency Theory

Agency Theoryis a supposition that explains the relationship that exists between the principal or owner and the agent or manager in the business. The separation of ownership from management in a modern organization,provide background designed for the functions of agency theory. Contemporary corporations have generally isolated ownership, in the form of shareholders, who are not more often than not involved in the management of their entity. This good connection needs to be treated with the good faith of transparency and accountability by managers. It, therefore, connotes that stakeholder's interest is the most paramount compared to the manager's interest, as such managers must act to pursue stakeholder's interest. This distinction among ownership as well as control establishes the possibility for conflicts of interest among shareholders or managers as well as the principals/shareholders, whose outcome relates to cost by resolving these conflicts (Jensen &Meckling, 1976; Eisenhardt, 1989). Managers are always motivated by their own individual gains and work to exploit their personal interest rather than the interest of the stakeholders which has become the most relevant basis of agency theory.

Accordingly, management has a motivation to manage the entity's financial report process in order to attain earnings target as a result, to receive any bonuses that may be tied to the firm's earnings performance. This establishes an information asymmetry that managers can work out the discretion they have on accruals, which in turn minimize the significance and reliability of reported earnings and the whole financial reports. Thus, the major dilemma revealed by agency theory is ensuring that managers hunt interests of shareholders and not only their own interests. In order to effectively limit agency costs caused by the separation of ownership and control, Fama and Jensen (1983) suggest that organizations need a system that can separate decision management from decision control. This may limit agency costs through the controlling power of management as well as ensuring the proper consideration of shareholders' interest.

Signaling theory

In AccountingSignaling theory is for describing behaviour when two parties (individuals or organizations) have access to different information. Typically, one party, the sender, must choose whether and how to communicate (or signal) information, and the other party, the receiver, must choose how to interpret the signal. The purpose of the signal is to indicate a certain quality.Signaling theory was developed by Michael Spence in 1973. In his seminal 1973 article, Michael Spence proposed that two parties could get around the problem of asymmetric information by one party sending a signal that reveals some piece of relevant information to the other party. That party will then interpret the signal and adjust her purchasing behaviour accordingly. Usually by offering a higher price than if she had not received the signal.

Voluntary disclosure is one of the Signaling means, where companies would disclose more information than the mandatory ones required by laws and regulations in order to signal that they are better (Campbell et al., 2001).Signaling theory is fundamentally concerned with reducing information asymmetry between two parties (Spence, 2002).

III. Methodology

The study adopted the Ex-post facto design. The ex-post facto research design was used because the study relied heavily on already existing secondary data ofownership structure on earnings management of listed industrial goods companies in Nigeria. The population of the study was all the twenty-one (21) industrial goods companiesin Nigeria and the sample size was only the thirteen listed industrial goods companies in Nigeria.They remained listed for the period under review. The choice of listed industrial goods companies in Nigeria was based on availability and reliability of their financial data. Census sampling technique was adopted for the study.

The study used panel data from secondary sources which were obtained from the annual reports of individual companies. The technique of data analysis employed in this study is the multiple regression analysis. The study adopted this technique to ascertain the effect of ownership structure on earnings management of listed industrial goods companies in Nigeria. A model was adapted thus:

ERNMGT = f (BH, INOS, FIOS, MGOS, OWC)
The model specification is thus;
$ERNMGT_{it} = \beta o + \beta_1 NBH_{it} + \beta_2 FIOS_{it} + \beta_3 DIO_{it} + \beta_4 MGOS_{it} + e_{it}$
Where:
$ERNMGT_{it}$= = the residuals from the regression of modified Jones Model by Dechow et' al (1995) which TAit = β01/Ait−1+ β1(ΔRevit−ΔRecit) + β2PPEit + µit
Where:
TA is total accruals scaled by lagged total assets;
A is total assets;
ΔRev is revenue;
PPE is gross property, plant, and equipment scaled by lagged total assets,
ΔRec is net receivables scaled by lagged total assets.
NBH_{it}=Block holder for firm i at time t
FIO_{it} = Foreign Institutional Ownership for firm i at time t
DIO_{it}=Domestic Institutional Ownership for firm i at time t
MGO_{it} = Managerial Ownership for firm i at time t
β1 – β5 = Coefficient of explanatory variables
βo = Constant or Intercept
e = Error Term.

IV. Results

Table1: Descriptive Statistics

	ERNMGT	DIO	FIO	MGO	NBH
Mean	1.563517	13.98540	12.35036	11.09204	1.839416
Median	1.576122	15.00000	0.000000	4.430000	2.000000
Maximum	5.287829	70.00000	86.00000	92.87000	5.000000
Minimum	-2.596080	-67.00000	0.000000	0.000000	0.000000
Std. Dev.	1.266473	15.56910	21.89399	17.60842	1.290426
Skewness	0.029287	-0.335845	1.985271	2.846144	0.280483
Kurtosis	4.184805	8.005251	5.679619	12.15686	2.680112
Jarque-Bera	8.032727	145.5837	130.9810	663.5950	2.380434
Probability	0.018018	0.000000	0.000000	0.000000	0.304155
Sum	214.2018	1916.000	1692.000	1519.610	252.0000
Sum Sq. Dev.	218.1378	32965.97	65191.18	42167.68	226.4672
Observations	137	137	137	137	137

Source: Researcher's Computation 2018

The descriptive statistics table (1) comprised of the variables used in the study with their mean, median, standard deviation, skewness, and kurtosis. The mean describes the average value in the series and the standard deviation measures the deviation of the data from the average. The skewness measures whether the distribution of the data is symmetrical or asymmetrical. Mean of ERNMGT shows the series around 1.563517 with a standard deviation of 1.2596080 while the skewness is 0.029287 and kurtosis of 4.184805.

Domestic Institutional ownership (DIO) has a mean value of 13.98540 with a standard deviation of 15.56910. Furthermore, DIO has skewness value of -0.335845 with kurtosis positive value of 8.005251. In addition, foreign institutional ownership has a mean value of 12.35036 with a standard deviation of 21.89399 and the skewness of 1.985271 and kurtosis of 5.679619 while managerial ownership indicates a mean value of 11.09204 with a standard deviation of 17.60842 and the skewness of 2.846144 with a positive kurtosis of 12.15686. A number of block holders has a mean value of 1.839416 with a standard deviation of 1.290426 and the skewness of 0.280483 and kurtosis of 2.680112.

Table 2: Correlated Random Effects - Hausman Test

Equation: Untitled				
Test cross-section random effects				
Test Summary		Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random		10.622243	6	0.1008

Cross-section random effects test comparisons:				
Variable	Fixed	Random	Var(Diff.)	Prob.
DIO	0.046218	0.027410	0.000047	0.0061
FIO	0.004295	0.007764	0.000044	0.6019
MGO	-0.003811	0.001727	0.000014	0.1325
NBH	-0.107377	-0.159481	0.019431	0.7086
Cross-section random effects test equation:				
Dependent Variable: BMS				
Method: Panel Least Squares				
Date: 01/12/18 Time: 22:19				
Sample: 2007 2016				
Periods included: 10				
Cross-sections included: 14				
Total panel (unbalanced) observations: 137				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	2.470004	0.722865	3.416964	0.0009
DIO	0.046218	0.011357	4.069611	0.0001
FIO	0.004295	0.008475	0.506769	0.6133
MGO	-0.003811	0.007235	-0.526804	0.5993
NBH	-0.107377	0.181907	-0.590286	0.5561
	Effects Specification			
Cross-section fixed (dummy variables)				
R-squared	0.378667	Mean dependent var		1.563517
Adjusted R-squared	0.277767	S.D. dependent var		1.266473
S.E. of regression	1.076303	Akaike info criterion		3.119105
Sum squared resid	135.5362	Schwarz criterion		3.545380
Log likelihood	-193.6587	Hannan-Quinn criter.		3.292333
F-statistic	3.752889	Durbin-Watson stat		2.362502
Prob(F-statistic)	0.000005			

Source: Researcher's Computation 2018

The coefficient of determination R-square is 37.9%. This means that the variables captured in the model explained variation in earnings management to the extent of the percentage while the remaining variation is explained by other variables that are not captured in the model. The model is fit with F-statistics of 0.00005.

Domestic institutional ownership has positive significant effects on earnings management with a P value of 0.0061. This shows that domestic institutional ownership causes variation on earnings management. Foreign institutional ownership has positive insignificant effects on earnings management with a P value of 0.6019. This shows that foreign institutional ownership does not cause variation on earnings management. Managerial ownership has insignificant effects on earnings management with a P value of 0.1325. This shows that managerial ownership does not cause any variation in earnings management. A number of block holders has negative significant effects on earnings management with a P value of 0.7086, which implies that the number of block holders does not cause any variation on earnings management.

The coefficient intercept of domestic institutional ownership is 0.046218 which means that earnings management will increase by 0.046218 whenever domestic institutional ownership is at zero. The coefficient of foreign institutional ownership is 0.004295. In addition, managerial ownership structure coefficient is -0.003811, anda number of block holder's coefficient is -0.107377.

Discussion of Findings

From the findings of the regression result above, it is evident that domestic institutional ownership has positive significant effects on earnings management which means that an increase in domestic institutional ownership will also increase earnings in management practice. For the result of foreign institutional ownership, it shows that foreign institutional ownership has positive insignificant effects on earnings management, which means that an increase in foreign institutional ownership will not result to increase or decrease in earnings management. Also, managerial ownership has negative insignificant effects on earnings management, which implies that an increase in managerial ownership will lead to a decrease in earnings management. Furthermore, a number of block holders has negative insignificant effects on earnings management, which means that an increase in the number of block holders will not result in an increase or decrease in earnings management.

Similarly, the hypothesis revealed that foreign institutional ownership has significant effects on earnings management of listed industrial goods companies in Nigeria. The result is consistent with the findings of: Number of block holders,Pascual, Jordi and Josep (2005), Institutional, Vince, Mohamad and Oluwatoyin (2016), Sani, Bany, Hairul and Siti (2015), Thanatawee (2014), Namazi and Ebrahimi (2013), Setayesh and Ebrahimi (2012), Shehu (2011), Klai and Omri (2011), Managerial: Obigbemi, Omolehinwa, and Mukoro, (2017), Hidetaka (2010), Johari, Mohd, Jaffar& Hassan (2008), Teshima and Shuto (2008), Yeo, Tan, Ho, and Chen (2003), Koh (2003), that ownership structure has positive effects on earnings management, but inconsistent with the findings of:Khamoussi and Abir (2015), Musa and Shehu (2014), Baba (2015), Esta (2011), Hashemi and Kamali (2011), Huy (2016), Tsai and Lin (2003), Chung, Firth and Kim (2002), that ownership structure has negative effects on earnings management.

V. Conclusion And Recommendations

Based on the findings that ownership structure has negative insignificant effects on earnings management of listed industrial goods companies in Nigeria, the study concluded that, foreign institutional ownership has positive insignificant effects on earnings management of listed industrial goods companies in Nigeria, which means that an increase in foreign institutional ownership will not result to increase or decrease in earnings management.

Therefore, the study draws an overall conclusion that ownership structures have positive insignificant effects on earnings management of listed industrial goods companies in Nigeria.

From the findings and conclusions drawn of the study, it is recommended that:

i. The management of industrial goods companies should put in measures to reduce domestic ownership in order to have a fair and reliable financial statement.
ii. The industrial goods companies should maintain the level of foreign institutional ownership since it does not have a significant effect on the earnings management of the companies.
iii. The managerial ownership shows a negative relationship which depicts the influence they have on earnings. Their stake in the companies should be increased in order to reduce earnings manipulations.
iv. The number of block holder have an effect on the earnings management as such, the companies should encourage combined ownership in their companies.

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