

**OWNERSHIP STRUCTURE AND EARNINGS QUALITY OF LISTED
INSURANCE COMPANIES IN NIGERIA.**

BY

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Declaration

I declare that the work in this Thesis entitled Impact of Ownership Structure on Earnings Quality of Nigeria Listed Insurance Companies has been carried out by me in the Department of Accounting Ahmadu Bello University Zaria. The information derived from the literature has been duly acknowledged in the text and a list of references provided. No part of this thesis was previously presented at this or any other institution.

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CERTIFICATION

This thesis entitled “**Ownership Structure and Earnings Quality of Listed Insurance Companies in Nigerian**”, by Hajara Maiturare BABA meets the regulation governing the award of the degree of Msc. Accounting and Finance of the Ahmadu Bello University for its contribution to knowledge and literary presentation.

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DEDICATION

This Thesis entitled Impact of ownership structure on Earnings Quality of Nigerian Listed Insurance Companies is dedicated to all my well-wishers.

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ABSTRACT

The Earnings figure is one of the most important economic variables in the financial statement that measures the financial position and performance of an entity. However the earnings reported may not really reflect the true performance of a company due to management manipulation as a result measures are raised to curb this situation among which is ownership structure (distribution of company ownership among its shareholders). The main objective of this study is to determine the impact of ownership structure on earnings quality of listed insurance companies in Nigeria. The study formulates three hypotheses and applied Generalised Least Squared (GLS) Techniques to analyse the relationship between dependent variable earnings quality and the independent variable, institutional ownership, managerial ownership and ownership concentration of the sampled Insurance Companies. Data were extracted from the annual reports and accounts of the Insurance Companies over the period 2008 to 2013. Kothari et al 2005 performance adjusted discretionary accrual model was employed in this study to determine earnings quality. The data analysis technique was regression using STATA version 11. The study found that: Institutional ownership negatively influences earnings quality, Managerial ownership negatively influences earnings quality and ownership concentration negatively impacts on earnings quality but not significant. The study recommends that Nigerian Insurance companies should reduce the shareholding of their managers, motivates their institutional investors to become long term institutional investors and reduces the shareholding of their major investors.

Keywords: *earnings quality, managerial ownership, ownership structure, institutional ownership, ownership concentration, insurance companies.*

CHAPTER ONE

INTRODUCTION

1.1 Background to the Study

Insurance business involves pooling of funds from many individuals and entities known as policy holders to indemnify losses and damages incurred by any of the contributors. The compensation of the risk and losses is dependent upon the terms and conditions of the insurance policy. Insurance policy is therefore, a form of risk management primarily designed to hedge against the risk of a contingent and uncertain loss. Hence, insurance business is a major part of the financial service industry, and as such a vital factor in the protection of the national economy as no modern economy can survive without the support of a viable and disciplined insurance industry (Arena, 2006).

In response to the expansion and sophistication of the operations of insurance firms in Nigeria, together with the effort to realize the goals and objectives of the industry, the National Insurance Commission (NAICOM) recently launched a Code of Corporate Governance for the insurance industry in Nigeria. This is part of the Commission's strategic effort to rebuild and sustain the waning confidence of stakeholders in order to promote the quality and efficiency of insurance industry in Nigeria. Some of the issues that the code clearly defined are that; (1) the accounting system should contain the information needed by investors, customers, supervisors, and other stakeholders, as it will aid them in their decision making about the future prospect of the company, and (2) accounting methods shall provide real performance and also information about shareholders who own directly and/or indirectly a minimum per cent shares of a company. One of the major issues that the code emphasized is the ownership structure of the firms in the

industry, this is in cognizance to the principal-agent conflict in which managers are serving their self-interest and opportunistic behaviour in particular, which usually tend to affect reported earnings adversely.

According to Bello (2011), earnings and earnings determination constitute one of the central functions of accounting as it determines wealth transfer between persons. He adds that, earnings is widely considered as the most important economic variable in financial statements that measures the performance of business entity as well as provides decision base for different users of accounting information. However, management opportunistic behaviours together with inherent flexibility in Generally Accepted Accounting Principles (GAAP) are often regarded as factors that usually affect the quality of earnings adversely. Globally, earnings quality became questionable due to a number of accounting scandals around the world such as Enron, WorldCom, Cadbury etc., and this refocused many firms on the benefits of a high quality earnings reporting. The stakeholders (shareholders, potential investors, employees, suppliers, creditors, financial analysts and government agencies) will be able to make effective and efficient decisions when reported earnings reflect the true performance of the company. Ownership structure is one of the most effective measures that monitor management behaviours (Jensen & Meckling, 1976).

Based on the studies conducted on ownership structure, the proxies of ownership structure are; foreign ownership, family ownership, managerial ownership, institutional ownership and ownership concentration (Hashim & Devi, 2006; Ali Saleh & Hassan, 2008; Hassan & Abubakar, 2012). This study looked at ownership structure from institutional, managerial

ownership and ownership concentration perspectives. This is due to lack of data for other variables of ownership structure as documented in the analysis of the ownership structure of Nigerian Insurance Companies in the Nigerian Stock Exchange (NSE, 2010) fact book.

When institutional investors exert their control over a company's management, it is expected that earning quality increases because they are enabled and motivated to encourage high quality earnings reports (Velury & Jenkins, 2006). In a study by Hashim and Devi (2006) they concluded that family ownership and institutional ownership play significant roles in explaining the reported earnings quality. On the other hand, some institutional investors are short term investors that are more interested in immediate profit, therefore, they motivate the managers to manipulate the earnings reported leading to lower quality of earnings.

Empirically, it was suggested that the informativeness of accounting earnings varies systematically with the level of managerial ownership. For example, Warfield, Wild and Wild (1995) argued that because of less influence from capital market, and high investment by the managers they are more likely to make accounting choice that reflect firm performance rather than personal interest. In the same vein, Demsetz (1983) illustrated that lack of market discipline may also be a factor inducing lower earnings quality on firm with high managerial ownership.

Furthermore, Rahmanay and Chashmi (2010) stated that large shareholders have a greater incentive to monitor managers since the cost of monitoring is less than the benefit due to the large investment they have in the company. Supporting this view, Stiglitz (1985) found that, large equity holders have incentive to bear the fixed cost of collecting information and to engage

in monitoring managers. Also, Ramsey and Blair (1993) added that, increased ownership concentration provides large block holders with sufficient incentives to monitor managers. Evidently, ownership concentration is expected to impact positively on earnings quality.

This study is motivated by the 2007 reform that has led to the expansion and sophistication of the operations of insurance firms in Nigeria, which also increased the capital base of the insurance firms substantially. Moreover, the recent efforts by the regulators to realize the goals and objectives of the industry have necessitated the setting up of the Code of Corporate Governance for the insurance industry in Nigeria. An important area that is significantly affected by the reform in respect of the code is ownership structure which is a vital mechanism in controlling the earnings manipulation of managers; as such improve the quality of reported earnings.

In addition, the dearth of empirical researches on the relationships between ownership structure and earnings quality in Nigeria particularly in the insurance companies prompted this study. It is against this background that this study examined the relationship between ownership structure and earnings quality of listed insurance companies in Nigeria.

1.2 Statement of Research Problem

With the separation of ownership, managers tend to favour their interest, which is usually through their discretion in the preparation and presentation of financial statements. While the essence of the statements is to communicate to users the true and fair financial performance and position of firms during a specified time period, with the view of aiding decisions and judgments, financial information, particularly earnings figure in the statements suffer managerial

manipulations. To overcome this and other issues in the corporate world, control mechanisms are being put in place, and the one that is directly related to the managers is the ownership system of firms.

Following the increasing focus on the role of institutional investors in monitoring, discipline and influencing corporate managers, several studies have been conducted on the implication of ownership structure and earnings quality. While some studies found institutional investors to have some degree of effectiveness in forcing managers to focus on economic performance and to refrain from opportunistic self-serving behaviour (Shah & Durrani 2009; Yang & Ramadili, 2009), others found that institutional investors focus on short term performance even to the detriment of the long-term prosperity of the firm, thus, ineffective (Alves, 2012). On the other hand, earnings are said to be of high quality when managers of the company are also part of the shareholders, thus, the relationship between earnings quality and managerial ownership becomes positive (Ali & Hassan 2008; Alves, 2012). On the contrary, some empirical studies reported that when a controlling owner effectively controls a firm, the controlling owner also controls the quality of accounting information and accounting reporting process. Consequently, the controlling owner will have a high level of motivation to report accounting information out of self-interest rather than the reflection of true underlying economic situations (Johari & Jafar, 2008). This suggests that managerial ownership is negatively associated with earnings quality.

Ownership concentration entails that large block holders have greater incentive to monitor management as the cost of monitoring is less than the benefit to be derived. When ownership is concentrated, it impacts positively on earnings quality (Roodposhti & chashmi, 2010; Alves,

2012). However, other studies found that the relationship between earnings quality and ownership concentration is negative (Klai & Omri, 2011; Andy, 2012).

Although series of arguments are found in the literature as to the impact of ownership structure on earnings quality, some of the arguments are conflicting and are mostly based on studies conducted in advanced countries in which the financial systems are more matured compared to the developing countries. This therefore prompts the need for studying ownership structure in relation to earnings quality, while considering a specific sector in order to ascertain the effect of components of firm's ownership structure (managerial ownership, institutional ownership and ownership concentration) on the quality of earnings.

There is also a methodological gap on the model used in segregating discretionary and non-discretionary accruals. Most of the studies on this aspect used models of discretionary accruals like Jones (1991), Modified Jones (1995), Dechow and Dechev (2002) among others. Although these models are being used in estimating residual values, they are deficient in not recognising performance in the non-discretionary portion of accruals, which may influence total accrual, thereby leading to wrong conclusion (Kothari, Leone & Wasley; 2005). Being that Nigerian Insurance companies have experienced reforms that increase their performance, Kothari *et al* (2005) model was considered the best model to be used in determining the earnings quality parameters of specific Nigerian Insurance companies. Therefore, this study covered the gap by using Kothari *et al.* 2005 performance adjusted discretionary accrual model.

In view of the fact that the Nigerian insurance industry has undergone a series of reforms particularly that of 2007 in order to have an effective and efficient insurance sector, there is a need to identify the effectiveness of ownership structure of the insurance companies in mitigating managerial unethical practices. This has become essential due to the critical role the insurance industry plays in economic growth and development, and the threat of earnings management to the survival of insurance companies. Dearth of studies in this sector clearly indicates a gap that needs to be filled. Therefore, this study investigated the impact of ownership structure on the earnings quality of listed insurance companies in Nigeria.

1.3 Objectives of the Study

The major objective of this study was to examine the impact of ownership structure on the earnings quality of insurance companies in Nigeria. The specific objectives were to:

- i. Examine the impact of institutional ownership on earnings quality of insurance companies in Nigeria.
- ii. Determine the impact of managerial ownership on earnings quality of insurance companies in Nigeria.
- iii. Assess the impact of ownership concentration on earning quality of insurance companies in Nigeria.

1.4 Research Hypotheses

In line with the objectives of the study, the following null hypotheses were formulated:

HO1: Institutional ownership has no significant impact on earnings quality of insurance companies in Nigeria.

HO2: Managerial ownership has no significant impact on earnings quality of insurance companies in Nigeria.

HO3: Ownership concentration has no significant impact on earnings quality of insurance companies in Nigeria.

1.5 Significance of the Study

The study is significant owing to the importance of insurance industry in an economy. This study is beneficial in the following ways: Firstly, it is beneficial to investors, as earnings is one of the fundamental attributes that indicates the financial performance and direction of a firm, but, with unethical behavior managers tend to report manipulated earnings which does not translate into true activities of a firm, as such led to misallocation of fund. Hence the findings of this study will guide the Nigerian Insurance Companies' investors on whether to continue to invest in companies or to sell their ownership stake.

Secondly, the findings of this study are useful to insurance companies' operators in deciding on their share composition, and whether their ownership structure really translate into intended result of effective monitoring of their managers' financial activities. As such insurance companies' operators will know how best to distribute their shareholdings. Finally, the study

adds to the existing literature on the relationship between ownership structure and earnings quality, especially of Nigerian insurance companies.

1.6 Scope of the Study

The study assessed the impact of ownership structure on the earnings quality of insurance companies in Nigeria. The dependent variable is earnings quality which is measured by discretionary accruals. The independent variable, ownership structure is represented by; institutional ownership, managerial ownership and ownership concentration. The study covered the Insurance companies listed on the floor of Nigerian Stock Exchange as at 1st of January of the year 2013. The period covered six (6) years from 2008-2013. The choice of this was based on the fact that, it was the period that the insurance industry experienced recapitalization which was said to have improved the industry performance and also increased the number of insurance companies listed on the floor of Nigerian Stock Exchange (N S E).

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter explains the concept of earnings quality and ownership structure and how they are being measured in the literature. Empirical literatures on the relationship between earnings quality and ownership structure (institutional ownership, managerial ownership and ownership concentration) were reviewed. Lastly the theoretical frameworks that underpin the relationship between the variables of the study were also discussed.

2.2 Conceptual Framework

In this part, the concept of earnings quality, ownership structure, managerial ownership, institutional ownership as well as ownership concentration are discussed. This chapter begins with earnings quality.

2.2.1 Earnings Quality

Earning quality has various definitions in the literature, and there is no generally accepted definition (Khajavi & Nazemi, 2005). This diversity could be as a result of different views of researchers on the different dimensions of the concept. Therefore, earnings quality is of a complex nature, and no researcher has ever been able to define it comprehensively or has found a complete index for it (Karami *et al.*, 2005). Different researchers have suggested different concepts for earning quality, among which are that earnings quality is the degree of conservatism applied in calculating earnings (White *et al.*, 2003) and accruals volume (Dechow, Sweeney, & Sloan 1995). While Hicks (1939) defined earnings quality as the extent to which reported

earnings correspond to economic income: The amount that the firm can pay out as dividends (that is, the amount that can be consumed) during a period, while leaving the firm equally well off at the beginning and the end of the period.

Dechow and Dichev (2002), Balsam, Krishnan, and Yang (2003), Francis, Olsson and Schipper (2003) and Myers, Myers and Omer (2003) used accruals quality to draw conclusions about earnings quality and view earnings to be of higher quality if accruals quality is high. But, Beneish and Vargus (2002), Penman and Zhang (2002), and Richardson (2003), viewed earnings to be of higher quality when an earnings is more persistent. On their part, Mikhail, Walther, & Willis (2003), defined earnings quality as the extent to which a firm's past earnings is associated with its future cash flows, where high earnings quality occurs when a firm's earnings has high predictability.

On the other hand, some studies such as those of Lang, Raedy and Yetman (2003) and Ball and Shivakumar (2004), argued that earnings is said to be of higher quality when it has less earnings management and more timely recognition of bad news. They viewed earnings from the angle of earnings management (discretionary accrual) and timeliness. Earlier, Pratt (2003) defined earnings quality as the extent to which net income reported on the financial statement differs from income.

Schipper and Vincent (2003) and Dechow and Schrand (2004), looked at earnings quality in the context of earnings management. They stated that the ability of reported earnings to reflect the true performance of a firm is an indication that the earnings are of high quality. This definition is

consistent with earnings management concept as proposed by Healy and Wahlen (1999), who specifically stated that earnings management is where “managers use judgment in financial reporting and in structuring transaction to alter financial reports to either mislead some stakeholders about the underlying economic performance of the company or to influence contractual outcomes that depend on reported accounting number”. Therefore when managers do not manipulate accounting numbers and transactions, earnings reported by firms would reflect the true performance of the firms, since the earnings are the product of genuine business transaction and events.

From the aforementioned definition of earnings quality it can be deduced that, there is no single accepted definition of earnings quality. But, looking at earnings quality from the perspective of accrual is given more preference in the literature. Earnings that are persistent and predictable may not be of high quality if this results from earnings management (Dechow & Shrand, 2004), this view is also supported by Van Tendeloo and Vanstralen (2005), Chen *et al.*, (2007) and Barth, *et al.*, (2008), who often use the term earnings quality to denote the absence of earnings management. In addition, Levitt (1998) stated that, when earnings management increases, the quality of financial reporting declines. Therefore, this study adopted the definition of earnings quality by Dechow and Schrand (2004), where earnings quality is represented by earnings management, and measured by discretionary accrual.

Earnings quality has no generally accepted measure, but empirical literature has developed several metrics to proxy for earnings quality. These proxies include persistence, predictability, smoothness, abnormal accruals, accruals quality, value relevance, timeliness, conservatism,

among others. Some studies use one of these proxies and others a combination of two or more. Previous studies (Dechow, Sloan & Sweeney 1995; Dechow & Dichev, 2002; Chung, Firth & Kim, 2002; Chung, Ho & Kim, 2004; Cormier & Martinez, 2006; Han, 2005; Jenkins & Velury, 2006; Wang, 2006; Hashim & Devi, 2006; Gul, Srinidhi, & Tsui, 2007; Ball & Shivakumar, 2008; Radziah & Fauziah 2010) have used earnings management (discretionary accruals) to measure earnings quality. However Sharon (2006) used discretionary accruals and timely loss recognition, Kriengkrai (2004) and Latiff and Talib (2010) used accruals quality, persistence, predictability and smoothness to measure earnings quality. The most widely used among the proxies is accruals which is considered the most committed fraud in the capital market (Ahmed & Ali, 2009).

Accounting accrual items have attracted much attention as a measure of earning quality. Dechow and Dechev (2002) proposed and tested a bench-mark for measuring of earnings quality. This measure is obtained from the relationship between current accrual items with cash flows of past period, current period and future period. Earning is of high quality when discretionary accrual is low, that is, the relationship between earnings quality and discretionary accrual is inversed.

Accrual is defined as the difference between earnings and cash flow from operating activities. Accruals are further classified into two; discretionary and non-discretionary accruals. Discretionary accruals are accounting adjustment to the firm cash flows mandated by the accounting standard setting bodies, whereas discretionary are adjustments to cash flow selected by the managers (Rao & Dandale, 2008). Accounting accruals which is the difference between earnings and cash flows has been used in different terms in the previous literature.

Researchers measure accruals differently. Some measure it based on total accruals or change in total accruals (Healy & Wahlen, 1985; De angelo, 1986); whereas others measure it by segregating total accrual into non-discretionary and discretionary accrual, in order to obtain the accrual at managers' discretion, which is discretionary accruals. Discretionary accruals represent the extent of earnings management. Discretionary accruals reflect subjective accounting choices made by managers (Chung, *et al.*, 2002). Researchers have developed several models for estimating this discretionary accrual.

The models of accrual range from the simple, in which total accruals are used as a measure of discretionary accruals to the relatively sophisticated ones in which regression is used to decompose accruals into discretionary and non-discretionary components. Discretionary accruals imply earnings management and lower quality earnings. The most popular among the models are the ones developed by Healy (1985), Jones (1991), Jones (1995), Dechow and Dechev (2002), Francis *et al.*, (2005), and Kothari *et al.*, (2005).

Early studies attempted to measure the quality of accruals using simpler measures such as total accruals (Healy, 1985) and change in total accruals (DeAngelo, 1986). Using total accruals to measure abnormal activities assumes that normal accruals are zero and are unrelated to other financial accounting variables or firm activities. Using the change in accruals assumes that all accruals should persist, and therefore any changes in total accruals are abnormal. Healy (1985) used total accruals to measure earnings management.

Subsequent studies attempted to partition accruals into non-discretionary and discretionary accruals. Jones was the first to have made such an attempt. Jones criticized the Healy (1985) model for taking the total accrual as manipulated earnings; her argument is that total accruals include non-discretionary accruals which reflect non manipulated accounting accruals items because they are out of manager's control.

Jones (1991) model came up six (6) years after the Healy model; the model was built upon the assumption that the changes in revenue and gross property, plant and equipment are non-discretionary. The idea of the Jones Model is that Sales Revenues control for current non-discretionary accruals, while gross Property Plant and Equipment (PPE) controls for non-discretionary accruals related to depreciation expense. The Discretionary accrual is arrived at after regressing the changes on revenue and PPE on total accruals. One problem with the Jones model is the use of reported change in revenues, since managers may manipulate reported revenues, for example, by delaying or bringing forward recognition of credit sales. If changes in revenue include this discretionary portion, then the Jones model will remove part of the managed earnings from the abnormal accrual estimate. Therefore, Dechow, Sloan, and Sweeney (DSS, 1995) proposed a modification to the Jones model.

Dechow, Sloan and Sweeny (1995) criticized the Jones (1991) model for assuming the changes in revenue as non-discretionary; therefore they modified the Jones (1991) model by adjusting the change in revenue by the change in receivables. The modified Jones Model assumes changes in credit sales in the event period result from earnings management that all credit sales are discretionary. The rationale behind the adjustment is that it is easier to manage earnings by

exercising discretion over the recognition of revenue on credit sales than on cash sales. The reliability of modified Jones in estimating abnormal accruals depends on the validity of the assumption that all changes in credit sales are discretionary

Subsequently, Dechow and Dechow (2002) developed a model of accrual and argued that the quality of accruals and earnings is decreasing in the magnitude of estimation error in accruals. The DD model uses firm specific regression of changes in working capital on last year, present and one year ahead cash flow from operations and defines accrual quality as a standard deviation of the residual from firm specific regression.

In the same vein, McNichols (2002) proposed a modification of Dechow and Dechow model, arguing that the changes in sales revenue, property plant and equipment are important in forming expectations about current accruals, over and above the effect of operating cash flows. She pointed out that applying variables in the Jones (1991) and modified Jones (1995) into the cross sectional Dechow and Dechow model significantly increases its explanatory power and thereby reduces measurement error.

Similar to the Jones and modified Jones with the addition of ROA is the Performance Adjusted Current Discretionary Accruals (PACDA) Model suggested by Kothari, *et al.*, (2005). The reason for including a performance variable in the discretionary accrual regression model is that Kothari *et al.*, (2005) indicated that firm performance and estimated discretionary accruals exhibit a mechanical relationship after controlling the effect of performance, and those discretionary accruals have higher reliability. This measure improved the discretionary accruals

estimated by the Jones and modified Jones models in mitigating type 1 error in which the firms having no earnings management are wrongly recognized as having engaged in earnings management. The Kothari *et al* (2005) embodiment of two modifications of the Jones and the modified Jones Models serve as an intercept to mitigate heteroskedasticity; deflating by lagged assets in the Jones 1991 model is meant to mitigate heteroskedasticity. Finding that heteroskedasticity is still an issue, Kothari, Leone, and Wasley also included an intercept to mitigate it. They found that an intercept yields higher symmetry around zero discretionary accruals, which enhances the power of tests for type I error, and an additional control for the lagged rate of return on assets, ROA_{t-1} . But it was pointed out that performance adjusted discretionary accrual model mitigate misspecification in samples with extreme ROA and exaggerate misspecification in samples with extreme firm size, implicitly assuming that any distortion due to firm growth is minimal.

None of the above mentioned models is free from criticism. Even though the most widely used among the models is the modified Jones model (Dechow *et al.*, 1995). Guayet *al.*, (1996) argued that the modified Jones is the most powerful model for estimating discretionary accruals among the existing models.

2.2.2 Ownership Structure

Incentives to engage in earnings management could be mitigated through effective corporate governance mechanisms such as board structure, ownership structure and capital structure. Among all the corporate governance mechanism, ownership structure as proposed by agency theory is one of the most important corporate governance mechanisms.

Ownership structure is the distribution of a company stock among its major shareholders. The separation of ownership and control gives rise to the conflict of interest between owners and their managers who run the day to day business of the company. Jensen and Meckling, (1976) stated that managers (agents) act on behalf of the shareholders (the principal), who are the actual owners of the firm. This relationship empowers the manager's position and leave the firm shareholders with no control over the decision making process. Literature shows that, ownership structure is in two forms, firstly, insiders or managers of a firm who also act as shareholders if they possess some portion of the company shares. Secondly, outsiders who own significant number of the company shares have more power and incentive to monitor management actively especially the financial reporting process, thereby reducing the earnings management probability, also increasing earnings quality. As such, ownership structure is expected to have a positive relationship with earnings quality.

Institutional Ownership and Earnings Quality

Institutional investors are large investors, other than natural person. Organizations which are considered as institutional investors are insurance companies (life and non-life), pension funds, investment trusts (including unit trusts), financial institutions (including banks, finance companies, building societies and credit cooperatives), investment companies, and other nominee companies associated with the above categories of institutions (Lang & McNichols,1997). Institutional investors have the opportunity, resources and ability to monitor, discipline and influence a manager's decision in the firm (Monks & Minow, 1995).

Institutional investors are classified into two main groups. The long term institutional investors who invest in a firm with the intention of holding their ownership stake for a long period. Therefore, they have strong incentive to monitor managers because of the huge investment they have in the firm. In this case the relationship between institutional ownership and earnings quality is expected to be positive. The second class is the short term institutional investors, they focus mainly on current earnings rather than in long term earnings, they engage less in monitoring management activity, if they are unhappy with the performance of a firm they sell their ownership stake rather than monitor or remove inefficient managers (Coffee, 1991). In this situation, institutional ownership is negatively associated with earnings quality.

The power of institutional ownership is however, a function of the degree of ownership by the institutions. McConnell and Servaes (1990), Nesbitt (1994), Smith (1996), Del Guercio and Hawkins (1999) and Hartzell and Starks (2003) have found evidence that corporate monitoring by institutional investors can constrain managers' behaviour. Pin Seng Koh. (2005) and Bita Mashayekhi (2008) too argued that institutional share ownership may have implications for earnings management as they are able to influence the company's management. Moreover, they showed that an increase in the number of institutional investors plays a positive role in determining earning quality.

Managerial Ownership and Earnings Quality

Insider or managers of a firm act also as shareholders if they possess some portion of the company shares; this reduces the agency conflicts and aligning the interest of management and that of shareholders. Agency theory predicts that low insider ownership implies poor alignment

of interest between managers and shareholders (Jensen & Meckling, 1976). This insider with low ownership manages earnings for better compensation, relax contractual constraint or avoid debt covenants (Healy, 1985; Houlthausen *et al*, 1995). It is suggested that they will be more involve in the firm when they own larger ownership, thus, the need for outside monitoring will be reduced, as long as the interest of insider and outsider converge. There are two views concerning managerial ownership. The convergence hypothesis states that insiders will be seen as monitoring mechanism when they acquire some portion of the company equity, they will prevent managers' opportunistic behavior, and the magnitude of discretionary accruals is predicted to be negatively associated with insider ownership (Warfield *et al.*, 1995).

On the other hand, when there is little separation between managers and owners (that is, when the managers are also part of the owners), management face less pressure from capital markets to signal the firm value to the market and they pay less attention to the short term financial report (Jensen, 1986; Klassen, 1997). Then highly invested managers are more likely to manipulate earnings, since the lack of market discipline, may lead managers to make accounting choice that is out of self-serving interest .

Ownership Concentration and Earnings Quality

Ownership concentration is a measure of the existence of large block holders in a firm (Thomsen & Pedersan, 2000). Normally, a shareholder who holds 5% or more of a corporation common stock is considered a major shareholder or block holder. The shareholding of an owner should be significant enough to provide for monitoring the action of the management. The major shareholder can be an individual, a domestic foreign corporation, an institutional investor and or

the state. Large block holders have greater incentive to monitor management as the costs involved in monitoring is less than the benefits to large equity holdings in the firm. Ramsey and Blair (1993) pointed out that increased ownership concentration provides large block holders with sufficient incentives to monitor managers. Demsetz and Lehn (1983) and Stiglitz (1985) found that large block holders have the incentive to bear fixed cost of collecting information and to engage in monitoring mechanisms. In contrast dispersed ownership leads to weaker management monitoring. That is in a situation where the shareholders hold lower stock in a firm the incentive to monitor management is low because the costs involved in monitoring outweigh the benefits to be derived. Hence, dispersed ownership is expected to impact negatively on earning quality.

Theoretically, the presence of a majority of shareholder in the company can result in agency problems between controlling and minority shareholders (Shleifer & Vishny, 1997.). Following this argument, some studies find nonlinear relationship between ownership concentration and profitability. To this end Mork *et al.*, (1988) claimed that, management entrenchment occurs causing a moral hazard and information asymmetry problem between the owner and outside investors.

2.3 Review of Empirical Studies

Nekounam, Sotudeh, Kohandel and Mohseni (2013) studied a relationship between institutional ownership and accounting conservatism in accepted Companies in Tehran Stock Exchange, the Sample consisted of 85 companies in Tehran Stock Exchange in 5 years (2007-2011), with institutional ownership as independent variable and accounting conservatism as dependent

variable. The linear regression results showed that there is direct (positive) relationship between institutional ownership level and accounting conservatism and there is reversed (negative) relationship between institutional ownership concentration and accounting conservatism. Nekounam, Sefiddashti, Goodarzi and Khademi (2012) investigated a Relationship between Ownership Concentration and Accounting Conservatism. A sample of 74 companies was selected for 2006-2010 (5 years). Linear regression result revealed a significant negative relationship between ownership concentration and accounting conservatism.

Chalaki, Didar and Riahinezhad (2012) investigated all the firms listed in TSE; the sample was arrived at after using filter, as a result, a sample of 136 firms was selected, for the period of 2003 to 2011. Financial reporting quality was measured by residual standard deviation of two models of McNichols (2002) and Collins and Kothari (1989). The F statistics for both models indicated overall models fitness at all level of significance (0.000 and 0.000, respectively). The regression result showed that ownership concentration has negative association with financial reporting quality, but, the result is insignificant. They further regressed variables individually with the control variables; it also proved multiple regression results.

Shaikh, Iqbal, Shah and Bhutto (2012) studied Institutional Ownership and Discretionary Accruals using a sample size of 68 listed non -financial companies from a population of 652 companies listed on Karachi Stock Exchange (KSE). The data was gathered for the period of 5 years, starting from 2006 up to 2010. Modified Jones Model was employed for the study to quantify discretionary the result revealed a negative but not significant relationship between institutional ownership and discretionary accruals.

In another study by Alves (2012) examined the relationship between corporate ownership structure in Portugal and earnings management. Using a sample of 34 non-financial listed Portuguese firms for the period between 2002 to 2007, discretionary accruals were estimated using both the cross sectional variation of the Jones model (1991) and the cross sectional variation of the modified Jones model proposed by Dechow, Sloan & Sweeney (1995). They found that, the coefficient of institutional ownership variable was positive and significant, the result was without control variables. However, the result was not corroborated when control variable was added; the coefficient on institutional ownership was negative, but not statistically significant; while discretionary accruals as a proxy for earnings management was negatively associated to ownership concentration. The study's result suggested that ownership concentration improved the quality of annual earnings by reducing the levels of earnings management. Furthermore, discretionary accrual management was negatively related to managerial ownership. This means that when managers also form part of equity owner, they report earnings that represent the true performance of the firm.

Al-Zyoud (2012) analysed the effects of chairman independence and ownership structure on earnings management. The sample consisted of 91 largest companies by market capitalisation of listed on the London Stock Exchange (LSE), in 2005 .Earnings management was measured by modified Jones model. The findings are; chairman independence is negatively associated with earnings management and significant, institutional ownership is negative and significant and managerial ownership is negative but not significant. Andy (2012) too studied the relationship between institutional ownership and earnings quality using cross-sectional expanding Jones model. The paper demonstrated that there is statistically significant non linear relationship

between institutional ownership and the quality of accruals according to sample 2004-2006. However, the result according to sample 2007-2009 does not found any significant relationship between institutional ownership and earnings quality.

Ghabdian, Attaran and Froutan (2012), conducted a study on the relationship between ownership structure and earnings management of listed companies from Tehran between 2002 and 2009. Thirty one family samples were identified according to the research criteria and were grouped in a separate portfolio with their related industry following TSE classification According to proportion of each industry in the first portfolio, 31 non-family companies were selected randomly and put into second portfolio. Jones adjusted model (Dechow *et al.*, 1995) was employed to measure earnings management. The regression results showed a significant negative relation between earnings management and ownership structure of family firms whereas, in non-family firms it was a significant positive relationship which means non family firms engage in earnings management more often than family ones.

Likewise, Osta and Naderi (2012) studied the effects of ownership structure on corporate value in the Tehran Stock Exchange (TSE) for 90 companies between 2001 to 2008. The results show that corporate ownership has positive effect on corporate value; however, the degree of corporate ownership concentration and corporate value is not significant, which means that there is no significant relationship between degree of corporate ownership concentration and corporate value. According to the results of the institutional ownership and corporate value a statistically negative relationship was revealed, but, the degree of institutional ownership concentration and corporate value did not indicate a not statistically negative relationship. Also, for management

ownership ratio is a statistically negative association with corporate value. As for the degree of management ownership concentration, there is no significant relationship between management ownership concentration and corporate value.

Ramezani, Pouraghajan, Emamgholipour, Khanalizadeh and Hashemi (2012) on their part investigated the Relationship Between Institutional Investors and Corporate Performance, with a Sample size of 540 firm for the period 2006 to 2010. The variables of returns on sales (ROS), profit growth rate (GP) and cash flows(CF) were used to measure corporate performance and institutional investors was an indicator of corporate governance. Regression model was used to test the relationship between them. They firstly performed robustness tests for using regression models which include heteroscedasticity, auto correlation and significance tests of fixed effects. After this, OLS and GLS techniques were used for regressing model. The finding indicates that there is no significant relationship between the percentage of institutional shareholders and return on sales, profit growth rate and cash flows.

Foroughi and Fooladi (2012) in another study examined the relationship between ownership concentration and firm performance in the Tehran Stock Exchange. The population of the study is all firms listed in TSE, excluding financial firms for the period of 2002-2004. The final sample of study is equal to 40 listed companies. In other to strengthen the external validity of research, they decided to increase the sample size to 45 listed companies. The results of test statistic indicated that companies' ownership concentration has a negative relationship with firm performance which is statistically significant at 5% significance level. This indicates that higher ownership concentration provides shareholder with more opportunity and incentive to

expropriate a firm's resources at the expense of minority shareholders which is in line with expropriation hypothesis.

Alimehmeti and Paletta (2011) investigated ownership concentration as a governance mechanism and its implications over firm value. The sample consists of 203 listed firms in Italy for the period between 2006 to 2009. The research is in pre and post situation. Ownership Concentration is measured as percentage of ownership shares (votes) of the largest shareholder. The results show a positive relationship between ownership concentration and firm value except in 2008, when the results show a non-linear relationship, suggesting that the financial crisis has enhanced the expropriation effects.

Abdoli (2011) studied the relationship and effect of performance of non executive directors and ownership concentration on earnings manipulation of 435 Tehran corporation for the period 2005-2010. Herfidal HitchMan Index (HHI) was used to estimate ownership concentration and Modified Jones Model was used to measure earnings manipulation. The finding revealed a significant negative relationship between ownership concentration and earnings management.

Zanjirdar and Kabiribalajadeh (2011), examined all the companies listed in Tehran Stock Exchange in the years 2003 to 2009, with a sample of 80 companies per year and a total of 560 year company. The hypotheses were tested using simple and multiple linear regressions. They found a negative and significant relationship between institutional ownership and performance of intellectual capital. In other words, increasing institutional ownership, performance of intellectual capital and its components is reduced. They also found a negative and significant relationship between managerial ownership and performance of intellectual capital. Managerial

owners seek to increase their personal interests and by decreasing the investments will cause the capital value of company to decrease in long term which as a result has a negative impact on performance of intellectual capital

Klai and Omri (2011) investigated the association between ownership concentration and financial reporting quality. The results indicated that ownership concentration is negatively associated with financial reporting quality, implying that shareholders use their power to expropriate firm resources which increases earnings manipulation and information asymmetry. Alipour and Amjadi (2011) examined the effect of ownership structure on corporate performance of listed companies in Tehran Stock Exchange. They found a significant negative association between managerial ownership and firm performance.

Ebrahimi, Kordlar and Aerabi (2010) studied Ownership Concentration and Earnings Quality in the Listed Companies in Tehran's Stocks Exchange. They used 148 listed companies in the Tehran's Stocks Exchange during a 5 year period from 1381-85. The results indicated that outside block holders significantly improve EQ, while they found no evidence of such impact by insiders. In a different study by Yang, Lai and Tan (2008) the researchers examined the relation between managerial ownership structure and earnings management. They classified insiders into executives, outside directors, and block holders. Earnings management is captured by discretionary accruals that are estimated using the modified Jones model. Over the period 1997 and 2004, they found that, discretionary accruals first increased and then decreased with executive ownership, forming an inverted U-shaped relationship. However, discretionary accruals are positively affected by director ownership and blockholder ownership which means

when directors owned a company share it increases the chances of earnings management, also, if the ownership stake is in the hand of a few individuals who are also involved in the management of the company, the managers manipulate the earnings reported.

Al-Fayoumi, Abuzayed and Alexander (2010) investigated Ownership Structure and Earnings Management in Jordan Emerging Markets. The population used in the study comprised the listed industrial companies in Amman Stock Exchange between 2001 and 2005. The final sample consists of 195 firm-year observations for accrual estimation and empirical analysis. The correlation between institutional ownership and earnings management is negative and significant at 5%. The regression results showed that; institutional ownership has a negative but insignificant association with earnings management. This insignificant association indicated that institutional investors are not a major consideration in managers' aggressive earnings management strategy, and ownership concentration has negative association with earnings management but not significant.

Roodposhti and Chashmi (2010) examined the Tehran Stock Exchange for the period between 2004 and 2008. The sample was arrived at after excluding financial firms which was up to 196 firms. Earnings management was measured by modified Jones model of discretionary accruals. Panel data method was employed as technique to estimate the model. They found discretionary accruals as a proxy for earnings management and it was negatively related to ownership concentration. This suggests that the presence of block holders could effectively monitor the management to avoid opportunistic behavior of the management including earnings management.

Javid and Iqbal (2010) studied the determinants of ownership concentration, the effect of ownership concentration on a firm's performance with the sample of fifty representative firms from different manufacturing sectors of the Pakistan's economy during 2003 to 2008. The measure of ownership concentration is defined as percentage of share owned by the largest five shareholders in a firm, and a block is defined to be any entity owning more than 10 percent of a firm. The results suggested that there is statistically negative relationship between ownership concentration and corporate performance.

Yang, Chun and Ramadili (2009) examined the Effect of Board Structure and Institutional Ownership Structure on Earnings Management in Malaysia. The sample consists of 613 firms from construction, industrial products and consumer products sectors selected from the main board. The time period covered for the study was from year 2001 to 2003. Modified Jones Model with cross sectional approach was employed to measure discretionary accruals. Multiple regression result revealed that institutional ownership has a negative relationship with earnings management, however, the result is not statistically significant. The findings indicate that in contrast to the evidence in developed markets, institutional shareholders in Malaysian firms are not an effective mechanism to constrain the earnings management.

Shah, Zafar and Durrani (2009) investigated 654 listed companies in Karachi Stock Exchange. The sample consists of 120 listed companies from different sectors. Discretionary accrual was measured using cross sectional modified Jones 1995. The correlation result shows that institutional ownership is statistically negatively correlated with discretionary accrual. They found a statistically negative relationship between institutional ownership and earnings

management; this suggests that the presence of institutional investor prevent management from manipulating the reported earnings.

Ali, Salleh and Hassan (2008) investigated the impact of ownership structure on earnings management in Malaysia between the period of 2002 and 2003. The sample was reduced to 1001 from 1484, as some firms that lacked the information were excluded. Earnings management was estimated based on Jones (1991) model. The result indicated that institutional ownership has negative and significant relationship with discretionary accruals at $p < 0.05$ in the same vein, managerial ownership has a negative and significant relation with discretionary accruals at $p < 0.001$. Ferreira and Matos (2008) investigated the institutional investors' role around the world using a comprehensive data set of equity holdings from 27 countries. The results showed that firms with higher ownership through foreign and independent institutions have higher firm value, higher operating performance and lower capital expenditures.

Johari, Saleh and Jaffar (2008) examined the Influence of Board Independence, Competency and Ownership Structure on Earnings Management in Malaysia. Earnings management was measured based on Jones 1991 model of discretionary accruals. They found that managerial ownership is positively related with discretionary accrual and significant. This showed that when managers owned ownership stake in a company they manage the earnings. The study was in contrast to that of You, Tsai and Lin (2003) who examined the relationship between managerial ownership, earnings management, and audit quality in Taiwan. They used criteria to arrive at 2030 firm-year observations, drawn from 393 corporations for the period of 1991-2000. They found a negative relation between managerial ownership and absolute discretionary accruals,

suggesting that, with low managerial ownership earnings quality reduces. Zhong, Donald and Zheng (2007) examined the effect of block-holders on earnings management. Their sample comprised of 5,475 firms for the period between 1994 and 2003. Earnings management was measured by cross-sectional modified Jones (1991) model. They found block-holder ownership to be positively associated with discretionary accruals.

Namazi and Kermani (2008) analysed the impact of ownership structure on firm performance of listed companies in Tehran Stock Exchange. The sample consisted of 66 companies, panel data was used to test the hypotheses. They divided the ownership into institutional and private ownership categories. Private ownership was further divided into corporate, management and external shareholders. They found that managerial ownership has a negative association with performance. In a similar study by Mirada (2008) who examined the controlling role of institutional investors, the result suggested a positive relation between institutional investors and earning quality.

According to Hashim and Devi (2006) who investigated corporate governance, ownership structure and earnings quality of companies listed on Bursa Malaysia's Main Board. The population of the study was 592 non-financial companies, the final sample comprised of 280 non-financial companies with complete data for computing earnings quality and corporate governance variable. They looked at earnings quality from the perspective of accruals which is measured based on modified Dechow and Dichev (2002) accrual quality model by Francis *et al.* (2005). The study used two different models in estimating the relationship between earnings quality and the test variables. They found a positive significant association between institutional

ownership and earnings quality. Although the result is only significant when the control variables were excluded, this means concentrated shareholdings in the hand of institutional investors have greater incentives to closely monitor firms' activities. Regarding managerial ownership, the study fails to find any significant association between managerial ownership and earnings quality. After segregating managerial ownership into inside and outside ownership, it also revealed insignificant findings on the relationship between inside and outside ownership with earnings quality. However, the result is only significant when the control variables were excluded.

In a similar study, Han (2005) examined ownership structure and financial reporting quality. The sample consists of all firm year observations for the period 1997 to 2001, uses both modified Jones (1995) and Dechow and Dechev (2002) model to measure earnings quality. Apart from measuring institutional ownership and managerial ownership he further calculated per capital institutional and managerial ownership which is measured as the number of top officers and directors and institutional investors listed in the database for each firm. He found that the univariate and bivariate results provided evidence that higher institutional ownership has a positive effect on the quality of earnings. Also a multiple regression approach was run after controlling factors that are likely to affect the association. He found that the coefficient estimates on total institutional ownership (INST) and institutional ownership per institution (PINST) are all significantly positive at the 1% level for both absolute value of discretionary accruals and the standard deviation of residuals from the Dechow and Dichev model (2002).

However, this finding implies that a higher level of institutional ownership may improve corporate governance of a firm as institutional owners would actively monitor management's decision as for Managerial ownership (MGR), the result is positive and statistically significant at the 10% level for the absolute value of discretionary accruals and at 1% level for the standard deviation of residuals from the Dechow and Dichev (2002) model. In the case of per capital managerial ownership (PMGR), he finds that PMGR has a significantly positive association with both absolute value of discretionary accruals and the standard deviation of residuals from the Dechow and Dichev model (2002) at the 1% level. This suggests that not only at the managerial ownership level, but also the degree of controlling power affects the reporting quality of a firm.

Hsu and Koh (2005) suggested that transient and long-term institutional investors co-exist and have differential effects on earnings management. Transient institutions are associated with upward accruals management while long-term institutions constrain this activity. This is because when the institutions invest in the long term period, they are more concerned about the underlying profitability of the companies and are wary of the use of discretionary accruals to manage the earnings. In another study, Mitra and Cready (2005) found that institutional shareholders intervene and mitigate the self-serving behavior of corporate managers in financial reporting based on a sample of 136 companies that belong to the S&P 500 group and 237 that belong to non- S&P 500 category for eight years period (1991-1998). Also, Velury and Jenkins (2006) examined all firms listed on Compact Disclosure, for the period 1992–1999. Earnings quality is measured from the FASB's conceptual framework. They documented a positive association between institutional ownership and earnings quality, suggesting that, institutional investors serve as effective monitoring mechanism that improves the quality of reported

earnings. In addition, the results indicated that concentrated institutional ownership may negatively affect earnings quality.

Chung *et al.* (2002) found evidence that the presence of large institutional shareholdings restrain managers from managing accruals to achieve desired level of earnings. Their results showed that when managers have incentives to increase or decrease reported profits as revealed from the cash-flow performance for current versus future periods, they accomplish the objective by using income-increasing or income-decreasing discretionary accruals to maintain a desired earnings stream. However, when investment institutions collectively own a large percentage of outstanding common stock in firms, managers are deterred from fully using discretionary accruals to opportunistically manage earnings.

Wahal and McConnell (2000) analyzed corporate expenditures for property plant and equipment (PP&E) and research and development (R&D) for more than 2,500 firms and found no support for the contention that institutional investors discourage managers to invest less in a project with a long-term pay-off. In fact, they document a positive relationship between industry-adjusted expenditures for PP&E and R & D and the fraction of shares owned by institutional investors. Similarly, Eng and Shackell (2001) found a significantly positive relationship between firms' R&D intensity and shareholdings of institutional investors; indicating that institutional investors do not enforce managers to focus exclusively on short-term earnings performance. The institutional investors are found to have a positive influence on the level of R & D spending in firms implying that they encourage firms to invest in long-term value enhancing projects.

Duggal and Millar (1999) advanced two arguments in favor of institutional monitoring on firms. First, institutional investors perform quality research in order to identify efficient firms to invest funds, thus directing scarce capital to its most efficient use. Second, the large institutional stake in public corporations provides strong economic incentives for institutional managers to monitor the firm performance to maximize their investment value. This vigilant institutional monitoring enhances managerial efficiency and the quality of corporate decision-making. Given that they own substantial shareholdings it is difficult for them to sell shares immediately at prevailing price, the institutional investors have greater incentives to closely monitor companies with high free cash flow (Chung *et al.*, 2005).

Bushee (1998) conducted an investigation as to whether institutional investors create or reduce incentives for corporate managers to reduce investment in Research and Development to meet short term earnings goals. The result reveals that managers are less likely to cut Research and Development to reverse earnings decline when institutional investors are high. El-Gazzar (1998) observed that managers of firms with a large institutional ownership may be induced to voluntarily release a high level of predisclosure information to gain confidence of institutional stockholders

According to Potter (1992) institutional investors focused more on short term earnings, and as such, they are incapable of monitoring management. Fearing that a decline in short-term profit will lead to the liquidation of institutional ownership in the firm and at least a temporary decline in equity value, managers are compelled to take actions that increase short-term profit and resort to earnings manipulation in case the actual earnings are expected to fall short of predictions. Barton (2005) found that among former Andersen clients, firms with greater institutional

ownership defected faster than those with lower levels of institutional ownership. Hessel and Norman (1992) found that institutions with a large stock ownership within a firm are likely to trigger more voluntary disclosures by managers of that firm and can impose their investment objectives on firms by introducing motions and proposals at annual meetings, which counter management policies. Jones (1993) claims that institutional investors have contributed to the resignation of CEOs of major corporations such as IBM, GM and Kodak, because institutions believed that management did not serve owners' interest.

McConnell and Servaes (1990) investigated the cross-sectional relation between Tobin's Q and management equity ownership for a sample of 1,173 firms in 1976 and for a sample of 1,093 firms in 1986 that are listed on either the New York Stock Exchange or the American Stock Exchange. Both samples report a statistically significant relationship between the value of a firm (as measured by Tobin's Q) and percentage shareholdings of institutional investors. As for the managerial ownership, a significant curvilinear relation between Tobin's Q and the management ownership was found. Q first increases, then decreases, as the shares become concentrated in the hands of managers and members of the board of directors. In a similar study by, Morck, Shleifer and Vishny (1988) found a positive relationship between Tobin's Q and managerial ownership for ownership levels between 0 and 5 percent and above 25percent. For intermediate levels, the relationship is negative.

Hassan and Abubakar (2012) investigated the Nigerian manufacturing firms. The sample consists of 25 non-financial firms listed on the Nigerian Stock Exchange (NSE) for the period between 2008 to 2010, making 60 firm-year observations. A cross-sectional regression of the modified

Jones Model (1991) was used to measure discretionary accruals. The study found the relationship between institutional shareholding and the discretionary behaviour of managers as negative and significant at 5%. Also, Hassan (2011) investigated the effect of corporate governance on financial reporting quality with a sample of 63 banks listed on the Nigerian Stock Exchange for the period between 2007-2010. The study found a positive and significant relationship between institutional shareholding and financial reporting quality.

In another study by Isenmila and Elijah (2012) they examined earnings management and ownership structure of Nigerian Banks for the period between 2006-2010. The sample consists of 10 commercial banks as at 2012. Earnings management was measured based on Jones (1991) and modified Jones (1995). The results indicate a significant positive relationship between External block ownership and Earnings Management. The relationship between Insider Ownership and Earnings Management was also observed to be positive and statistically significant. Also, a positive relationship between Institutional Investors Ownership and Earnings Management was found; however, the relationship was not statistically significant.

Hassan and Abubakar (2012) studied the interaction between ownership structure and earnings management in quoted food and beverage firms in Nigeria, for the period 2006 to 2010. OLS multiple regression was used as a tool for data analysis. Modified Jones model was used to measure discretionary accruals. The study documented an inverse relationship between institutional shareholding and discretionary accruals. While ownership concentration and family ownership positively impact on earnings manipulation. Ogbulu and Emeni (2006) examined the Nigerian Stock Exchange as at 31st December, 2006. The sample size comprises of twenty

companies quoted on the Nigerian Stock Exchange. In analyzing the data collected, the simple Ordinary Least Square (OLS) was used for the estimation of the data for the study. The regression result showed that managerial ownership is negatively associated with performance of Nigeria quoted companies and the finding is significant at 5%.

Hassan and Yero (2012) examined ownership concentration and earnings management in the conglomerate firms listed in Nigerian Stock Exchange as at 31st December, 2009. The population of the research consists of all the conglomerate firms listed in Nigerian Stock Exchange as at 31st december, 2009, which are 8 companies but two were screened out due to unavailability of annual report. They proxy earnings management by time series, modified Jones model, and they used panel regression. They found ownership concentration to be negatively associated with earnings management and significant at 1%. Their finding is consistent with the agency theory of Jensen and Mecklings (1976), which posits that concentration of ownership has a negative relation with earnings management.

However, the findings on the relationship between earnings quality and ownership structure are mixed. Almost all the studies reviewed, measured discretionary accruals with modified Jones model. Even though it is given more preference than other model, Kothari *et al* (2005) model, is also ranked the best in dictating earnings management (Kothari *et al* 2005; Roodposhti *et al.* 2012). The studies that used Kothari et al model are few and are foreign studies, also research has not documented any domestic study that determine ownership concentration through Herfindal Hitch man Index (HHI). Also not available is a study of this nature on the insurance sector. Therefore, this study has filled these gaps.

2.4 Theoretical Framework

The separation of ownership from control and the emergence of principal-agent relationship in modern business posit serious challenges to corporate organizations, and led to the establishment of governance mechanisms that are expected to guide and monitor the operations of organization in achieving desired goals. These mechanisms according to Yu (2006) included internal governance devices (managerial ownership) and external governance devices (institutional ownership and ownership concentration). For internal governance devices, it is presumed that, when the managers of a company also form part of the equity shareholders, it makes the managers to act in the best interest of the shareholders. While for external governance device, the existence of large shareholders is good for governance, because large shareholders play a more active role in monitoring and disciplining managers than small shareholders. In the same vein, institutional ownership is good for governance, since institutional investors have stronger incentives and more resources to discipline managers than small individual investors. The appropriate theories that explain the linkage between ownership structure of firm and earnings management in this study, are the involvement theory and concentration theory from the purview of management opportunistic behaviour. It is based on these views that Jong and Semenov (2006) regarded ownership structure as one of the main features of systems of corporate governance. They added that, ownership structure of a firm significantly influences its behaviour and performance.

Involvement theory according to Mintzberg (1983) regarded involvement (and its opposite, detachment) as trying to distinguish between owners who influence the decisions or actions of a

firm and those who do not. While Concentration Theory (and its opposite, dispersion) is trying to distinguish corporations whose stocks are closely held from those whose stocks are widely held. Ownership from these two theories according to Chaganti and Damanpour (1991) produced four types of ownership: dispersed-detached, dispersed-involved, concentrated-detached, and concentrated-involved. The more involved the owners, and the more concentrated their ownership, the greater the power they should have in influencing the managements and the corporation at large (Mintzberg, 1983). Thus, this includes controlling unethical management behavior through which managers pursue their self-interest. Jensen and Meckling (1976) gave operational explanation where they state that, if a wholly-owned firm is managed by the owner, he will make operating decisions that maximize his utility. And these decisions will involve not only the benefits he derives from pecuniary returns but also the utility generated by various non-pecuniary aspects of his entrepreneurial activities. However, with the involvement and concentration of individual and institutional owners, managers tend to behave differently. This is because of the influence that external ownership has on the overall affairs of the organization.

Morck, Shleifer, and Vishny (1998) and Clay (2000) pointed out that, given substantial interest involved, large shareholders play a more active role in monitoring and disciplining managers than small shareholders, and are usually considered to be a positive factor in corporate governance. While Yu (2006) stressed the increasing role of institutional investors in financial markets, that institutional investors hold a significant fraction of the shares of public firms and actively monitor the firms in their investment portfolios. Therefore, with substantial stakes, institutional investors have much stronger incentives to discipline managers than small individual investors; meanwhile, they also have less incentive and access than inside block

holders to collude with management. On the other hand, Fahlenbrach and Stulz (2007) argued that increases in managerial ownership are associated with increases in performance, and vice-versa.

In an analysis of the framework of ownership structure and management opportunistic behavior, Oyejide and Soyibo (2001) asserted that, the discretionary control rights of managers are further increased by the existence of asymmetric information between themselves and external investors. Under this situation, managers conceal some pieces of information from external investors, and such action serves to increase the cost of monitoring and enables managers to pursue their own interest rather those of the equity investors, by engaging in behavior that could be sub-optimal for the equity investors. The possibility of higher monitoring costs is particularly strong if there is a large number of dispersed external investors, because a free-rider problem emerges if there are large costs to monitoring while the benefits accruing to each individual are relatively small. The free-rider problem could be minimized and internal constraints on managerial discretion can be imposed if ownership is concentrated in the hands of large block of shareholders (either individuals or investment funds). Hence, large block shareholders or institutional investors will be more likely to be able to utilize their voting power to influence managerial behavior.

Generally, Klein (2006) opined that equity ownership is one of the major governance mechanisms that are used to monitor firms. He adds that, non-management directors with large block holdings are more apt to closely monitor a firm than directors with insignificant shareholdings. Based on this assertion, he documented a significantly negative relation between earnings management and managerial shareholdings; and also finds a positive relation between

earnings management and CEO shareholdings, a result consistent with the view that CEOs may manipulate earnings to increase their short-term stock returns.

Therefore, this study is underpinned by the involvement and concentration theories in the context of opportunistic management perspective to study the impact of ownership structure (managerial ownership, institutional ownership, and ownership concentration) on earnings quality of listed insurance companies in Nigeria. In this study, managerial ownership is taken the form of internal device in terms of stockholding of managers (view as disperse-involved), while institutional ownership and ownership concentration are a form of external mechanisms in terms of stockholdings by corporate bodies, that is institutional (view as dispersed-involved), and ownership concentration is translated into the concentrated-involved of stockholding (that is, concentration of holdings by few individuals).

2.5 Summary

In this chapter, the various measures or models of discretionary accrual were discussed. Empirical literature of both the dependent, Earnings Quality and independent variables, institutional ownership, managerial ownership and ownership concentration were reviewed. The theoretical frameworks that underpin the study were also discussed in order to provide a basis for the research.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter presents the methodology of the research and the justification of the methods and the techniques employed in the study. It discusses the research design, population and sample of the study, sources of data and method of data collection. It also specifies the variables of the study and their measurement, and explains the method of data analysis.

3.2 Research Design

Following the quantitative variables and objectives of this study, correlation research design is employed; correlation research examines the strength and direction of relationship between the dependent and independent variables. The selection of this design is informed by the quantitative nature of the problem of the study, and its suitability for the study of ownership structure and earnings quality as confirmed by vast empirical studies. Therefore, research design explains the plan and procedures of a study to arrive at valid conclusion, thus, correlation design is preferred to determine the relationship that exists between ownership structure and earnings quality among the listed insurance companies in Nigeria. The research design is based on the assumption that ownership structure has influential power on managerial behavior. The study is designed in two parts; in the first part, the measure of earnings quality is estimated, while in the second part, the effects of ownership structure on earnings quality is examined. This is achieved through the examination of significant coefficient of the components of ownership structure (managerial ownership, institutional ownership, and ownership concentration) using multiple regression model.

3.3 Population of the Study

The research population consists of all the 35 Insurance companies listed on the Nigerian Stock Exchange as found in the 2012/2013 fact book. Using the insurance companies as the population of this study is prompted by the fact that the industry has undergone reforms that increased the size and volume of transactions and activities of the insurance companies. Therefore, this makes them suitable for studying earnings quality because of the following reasons; there are large volume of premiums and provision for unexpired risks and claims which are accruals in nature, thus an ample opportunity for managerial manipulations; second, there are large business activities as a result of increase in capital base as well as operations.

In line with variables of the study that has to do with testing for the impact of ownership structure on earnings quality, lack of data in some of the insurance companies led to the following criteria; That is, for any insurance company to be selected it must have all the data for the variables of the study for all the period of the study. As a result, 12 firms were dropped and the population of the study comprises of 23 listed insurance companies.

3.4 Sources and Method of Data Collection

The study used secondary sources of data; this is due to the fact that, the models of the study require the use of quantitative data. The method of data collection for the study is specific insurance company's annual account and report for the study period.

3.5 Method of Data Analysis

The technique of data analysis in this study was Generalized Least Square (GLS) regression model. This is because the objective of the study is to assess the impact of ownership structure components on the earnings quality of listed insurance companies in Nigeria. And, GLS is effective in providing the effect of independent variable(s) on the dependent variables. Therefore, a panel data multiple regression technique is used to determine the relationship between ownership structure and earnings quality.

3.6 Variables Measurement and Model Specification

Following the two stage design of this study, the variables in the first stage are used to estimate discretionary accruals to proxy earnings quality. However, the measurement of the variables of interest in the study, and from which the hypotheses of the study were tested consist of one dependent variable, earnings quality, and three independent variables, institutional ownership, managerial ownership and ownership concentration. Furthermore, control variables of firm size and leverage are added. Firm size is used in this study to control the likely impact of firm size on the discretionary accruals of the sample companies, and, leverage is to control for those companies facing financial difficulties.

Models Specification

Consistent with Kothari *et al.*, (2005), the performance Adjusted Current Discretionary Accrual (PACDA) is used as follows:

$$TA_{it} = \beta_0 + \beta_1 \Delta REV_{it} / A_{it-1} + \beta_2 PPE_{it} / A_{it-1} + \beta_3 ROA_{it-1} + \mu_{it} \dots \dots \dots i$$

All variables are scaled by lagged total asset

Where;

TA_{it} = is defined as the difference between net income before tax (NI) and cash flow from operating activities which is as follows:

$$TA = NI - OCF \dots\dots\dots ii$$

TA_{it} = Total Accruals for firm i in year t

A_{t-1} = Total assets for firm I in previous year

ΔREV_{it} = Change in Revenue of firm i between year t and t-1

PPE_{it} = Gross Property, Plant and Equipment for firm i in year t

ROA_{it-1} = Net income /lagged total asset

$\beta_0, \beta_1, \beta_2$ and β_3 are the parameters estimate for each firm and each year.

μ_{it} = Residual and discretionary accruals portion

The residuals from this industry-year specific regression model are used to determined earnings quality.

Following the estimation of the earnings quality from model 1, the model of the study from which the hypotheses of the study is tested is as follows;

$$EQ = \beta_0 + \beta_1 INTOWN_{it} + \beta_2 MANOWN_{it} + \beta_3 OWNCON_{it} + \beta_4 FIRMSZ_{it} + \beta_5 LEV_{it} + \mu_{it} \dots\dots\dots iii$$

Where;

EQ = Earnings Quality

INTOWN = Institutional Ownership

MANOWN = Managerial Ownership

OWNCON = Ownership Concentration

Control variables

FIRMSZ = Firm Size

LEV = Leverage

B0 is the intercept and $\beta_1 \dots \beta_5$ are Parameters of the model to be estimated

ϵ_i = Error term

The measurement of the variables is presented in table 3.1 below;

Table 3.1 Variables Measurement

Variables	Measurement
EQ	Earnings Quality measured by discretionary accrual as residual of accrual model of Kothari et al (2005). $TA_{it} = \beta_0 + \beta_1 \Delta REV_{it} / A_{it-1} + \beta_2 PPE_{it} / A_{it-1} + \beta_3 ROA_{it-1} + \mu_{it}$.
Institutional Ownership	Percentage of shares owned by institution.
Managerial Ownership	Percentage shares held directly (shares own by the director only) or indirectly (When the director represent the interest of others) by directors.
Ownership Concentration	Herfindal index is used to determine the ownership concentration. $HHI = \sum I^2$
Firm Size	Natural log of total assets
Leverage	Ratio of total liabilities to total assets

Following the role firm size is playing in estimations, it is believed that larger firms are typically more politically visible than smaller firms, suggesting a lower proportion of earnings management (Watts & Zimmerman, 1990). In the same vain (Park & Shin,2004) stated that larger firms are more closely scrutinized than smaller firms that encourage them to produce higher quality of reported earnings compared to the smaller firms. Leverage is to control those

companies that are currently facing financial difficulties (Hashim & Devi, 2006). Trueman and Titman (1988), added that managing earnings enables managers to reduce estimates of various claimants of the firm about the volatility of its earnings process and so lowers their assessment of the probability of bankruptcy.

While in an effort to capture the presence of earnings management as well as earnings quality, prior studies mostly used discretionary accruals. Discretionary or abnormal accruals measure the degree of earnings management in a company's financial figure, companies use accruals as accounting adjustment to distinguish reported earnings from cash flow operations. Part of these accruals are due to natural business activities of the company and part comes from discretionary decision of managers (Jones 1991; Dechow, Sloan & Sweeney 1995), accrual based research intends to unveil this discretionary accrual as an indicator of earnings management.

As noted earlier most study on earnings quality use discretionary accruals to represent earnings quality, and this discretionary is being measured by several models but the most widely used and popular is the modified Jones model. Despite the superiority of cross sectional modified Jones (1995) as pointed out by Dechow *et al.*, 1995; Guay *et al.*, 1996 it cannot be used to measure discretionary accrual in this study; the reason for this is that, insurance companies have undergone series of reforms, using a model that embodied performance variable (ROA) . As such, performance adjusted discretionary accruals model by Kothari *et al.*, (2005) is used to measure earnings quality as used by Ferdinand and Judy (2007) and Sa'adiyah and Norman (2009), moreover, it is also considered as a powerful measure in detecting earnings management. Roodposhti, Rezaei, and Salehi (2012) analysed the Power and Specification of Accruals -Based

Models to detect Earnings Management in a population of all listed companies in Tehran Stock Exchange during the period of 2005 to 2010. They used filters to arrive at 437 observations (firm-year) which include 73 firms. They found that the performance-matching model (Kothari *et al.*, 2005) provides the most powerful test of earnings management.

3.7 How the hypotheses were tested

The study hypotheses were stated in null form between each of the independent variables (Institutional ownership, managerial ownership and ownership concentration) and the dependent variable (earnings quality) and the hypotheses were tested using Generalised Least Square (GLS) multiple regression technique which provides bases for failure to reject one of the hypotheses; there is no significant influence between ownership concentration and earnings quality;but rejecting two of the hypotheses formulated; managerial ownership does influence earnings quality and institutional ownership has no influence on earnings quality.

3.8 Summary

In this chapter, the research designs proposed for the study was discussed. Population of the study was also discussed. Finally, the variables used in the study and the model adopted to test the dependent variable, the method of data collection, data analysis and how the hypotheses were tested were also highlighted.

CHAPTER FOUR

DATA PRESENTATION AND ANALYSIS

4.1 Introduction

In this chapter the results of data analysis are presented. The hypotheses testing were also carried out and on which basis the null hypotheses were rejected or supported.

4.2. Descriptive Statistics

The summary of descriptive statistics of the variables used in this study is presented in Table 4.2.1.

Table 4.2.1: Summary of Descriptive Statistics

Variables	Mean	Std. Dev.	Min	Max
EMGT	.110	.149	.000	.823
INSTOWN	.397	.200	.070	.790
MANOWN	.237	.233	.010	.850
OWNCON	.416	.213	.040	.960
TA	22.607	1.609	15.689	25.291
LEV	44.432	429.368	.038	4953.190

Source: Output generated using stata

Table 4.2.1 shows the summary of empirical distribution of all the variables used in the study.

The full result is attached as appendix A. The mean and standard deviation of earnings management is .110 and .149 respectively. The percentage of institutional ownership ranged from 7 to 79 percent with an average of 40 percent. The share holdings of managers ranged from 1 to 85 percent with 0.24 as average. Ownership concentration ranged from 4 to 96 percent. The

control variables of firm size and leverage ranged from 15.69 to 25.29 and 0.04 to 4953.19 with averages of 1.609 and 429.37 respectively.

To check for normality of data, Shapiro-wilk test was conducted. This is a test conducted in order to check if the data are normally distributed or not. The evidence of the test is presented in Table 4.2.2 below:

Table 4.2.2 Summary of Shapiro wilk test for normality.

Variables	Probability
EMGT	.000
INSTOWN	.001
MANOWN	.000
OWNCON	.000
TA	.000
LEV	.000

Source: Output generated using Stata

Shapiro-Wilk w test of normality revealed non normal distribution of the data. This is obvious from the p values of the dependent variable (Earnings Quality), independent variables (institutional ownership, managerial ownership and ownership concentration) and control variables (firm size and leverage) which are less than .05 significant level.

4.3 Correlation between variables.

Pearson correlation was computed to determine the degree of relationship between the dependent variable (earnings quality) and independent variables of the study (institutional ownership,

managerial ownership, ownership concentration firm size and leverage). Summary of the results are in Table 4.3.1 below.

Table 4.3.1 correlation matrix

VARIABLES	EMGT	INSTOWN	MANOWN	OWNCON	FIRMSIZE	LEVERAGE
EMGT	1					
INSTOWN	.017	1				
MANOWN	.140	-.004	1			
OWNCON	-.003	.408	-.014	1		
FIRMSIZE	.064	-.108	-.182	-.066	1	
LEVERAGE	-.056	-.020	-.037	-.038	-.038	1

Source: Output generated using stata

This indicates that institutional ownership and managerial ownership is positively correlated with earnings management; This indicates that the higher its shareholdings in those firms the more the earnings management and consequently the lower the quality of the earnings they report. Also the relationship between managerial ownership and earnings management is positive, indicating a negative correlation with earnings quality. Meanwhile, the correlation between earnings management and ownership concentration is negative, suggesting that ownership concentration reduces earnings management, thereby increases earnings quality. Furthermore, the correlation between earnings management and the control variables revealed that; earnings management is negatively correlated with leverage, thus positively correlated with earnings quality, and positively correlated with firm size, hence negatively correlated with earnings quality.

4.4 Multicollinearity Test

A multicollinearity test was conducted to ensure that there is no existence of exact linear relationship among some or all the explanatory variables in the regression model. This is shown in Table 4.4.1 below.

Table 4.4.1 Result for Multicollinearity Test

VARIABLE	VIF	Tolerance
INSTOWN	1.21	.827
OWNCON	1.20	.832
MANOWN	1.04	.964
LEV	1.01	.995
FIRMSZ	1.05	.952

Source: Output generated using stata

A multicollinearity test is necessary because the presence of multicollinearity can affect the parameters of a regression model (Field, 2000). The tolerance values and variance inflation factors (VIF) value appeared normal as seen in Table 4.4.1 above, details of the result is attached as appendix E . As suggested by Menard (1955), a tolerance value less than 0.1 certainly indicates a serious collinearity problem. Myers (1990) also suggested that a VIF value greater than 10 calls for concern. A heterokedasticity test was further conducted and the result revealed a significant p-value at 1 %, postulating that the data are heterokedastic.

4.5 Results and Discussion of Regression Analysis

In order to determine the best fitted estimate of the model of the study, pooled Ordinary Least Squared (OLS) was run first to determine the coefficient. This was followed with heterokedasticity test. The null in this test is homoscedasticity. The result showed a P-value that is significant at 1%, thereby indicating the presence of heterokedasticity. The full result is attached as appendix E. Since the pooled OLS revealed heterokedasticity, Generalised Least Squared (GLS) technique was further employed in order to capture the special features or heterogeneity of each entity or cross-sectional unit, , which was used to run both the fixed and

random effects. In addition, the FE Hausman specification test was carried out in deciding between FE and RE estimate of the coefficients, based on the estimate of the two models (FE and RE). The Hausman specification test suggested FE as evidence with $p > 0.02$. The result of Fixed Effect (FE) proved fitted with $\text{Prob} > F = 0.0032$. The details can be found on appendix G.

Table 4.4.2 Summary of Fixed Effect Regression Result

Variables	beta value	t value	p value
C	-.01	-.36	.72
INSTOWN	.53	2.59	.01
MANOWN	.22	2.25	.03
OWNCON	.07	.83	.41
FIRMSIZE	.00	-.59	.56
LEV	.00	-.51	.61
R ²	.15		
F-Stat	3.81		
	.00		

Source: Output generated using Stata

Since this study is on earnings quality and the model employed was developed for earnings management, the sign of the coefficient derived from the result would be interpreted as opposite. This is due to the fact that earnings quality and earnings management have inverse relationship, that is, higher earnings management indicates lower earnings quality and vice versa. The analysis therefore revealed that institutional ownership has a significant positive relationship with earnings management ($t = 2.59$; $p < .01$). This translates to institutional ownership having significant negative relationship with earnings quality. This also indicates that the presence of institutional investors in the ownership structure of Nigerian insurance companies increases the

level of earnings management in these companies and thereby reduces the earnings quality they report.

This result contradicted the involvement theory that underpins this study which stated that institutional investors reduce earnings management, thereby, improve earnings quality. The reason for the deviation from the theory could be that Nigerian Insurance Companies institutional investors are myopic or short term institutional investors who are more interested in immediate earnings in short term than long run, as a result they do not engage in monitoring the activities of the management, instead they sell their ownership stake and invest somewhere else if anything unfavourable happens. .

This result is consistent with the findings of Alves (2012) and Isenmila *et al.*, (2012), who found significant positive relationship between institutional ownership and earnings management. It also does not follow with the study of Chung *et al.*, (2002) who showed that institutional shareholding restrain managers from managing accruals. In terms of earnings quality however, the study contradicts Koh (2012), who revealed that institutional investors play a positive role in determining earnings quality. This study also fails to agree with Hashim and Devi's (2006) study, who found a significant relationship between institutional ownership and earnings quality. Therefore, the result of this study did not support the null hypothesis, which stated that there is no significant relationship between institutional ownership and earnings quality. With this empirical evidence the study rejected the null hypothesis, as it is showing that institutional ownership has a significant negative impact on earnings quality of insurance companies in Nigeria.

Managerial ownership is significantly positive related with earnings management ($t = 2.25$; $p < .03$). This also shows that managerial ownership has a significant negative relationship with earnings quality. It therefore suggests that, having the managers among the shareholders increases earnings management; this is based on the fact that they have access to the financial statement, as a result earnings management may occur, resulting in poor earnings quality. Considering the findings of the research this study has sufficient evidence to reject the null hypothesis which stated that managerial ownership has no significant impact on earnings quality. The result confirmed the studies of Isenmila *et al.*, (2012) and Yang *et al.*, (2008) and contradicted the study of Han (2005). In the same vain this finding disagrees with involvement theory that underpins this study. The contradiction could be due to the percentage of shares owned by this management, as seen in the result the managerial shareholding is 22 percent which is a very substantial holding that makes them among the highest block holders who have more right in the company, apart from the prudential access they have to the financial statement, as such for any unsatisfactory outcome they will use their personal interest to alter the financial figure in order to achieve their goals , consequently reducing earnings quality.

Ownership concentration and earnings management are positively related but the relationship is not significant ($t = .83$; $p = .41$). This also means that there is a negative but not significant relationship between ownership concentration and earnings quality. Revealing that, the more concentrated the shareholdings are the higher will be the earnings management. Thus, the more concentrated the ownership structure the poorer will be the earnings quality. Even though this result is not significant, but it also contradicts the study theory which postulates that ownership concentration improves earning quality, the violation could be that the concentration falls in the

low concentration ratio as pointed out in the model used in determining concentration ratio Herfindal Hitchman Index that 10 percent concentration indicate low concentration and from the result depicted above the concentration ration is less than 10 percent, as a result the shareholders may not have sufficient resource to monitors the financial activities of managers as the cost of monitoring is more than the benefit therefore they engage in monopolistic power of dictating to managers what to do rather than monitoring financial activities in other to prevent them altering the accounting figures. This result however confirmed, in terms of direction, the study of Zhong (2007), Isenmila *et al.*, (2012), and Hassan and Abubakar (2012) among others. In addition, the positive direction in the relationship between ownership concentration and earnings management, contradicted the study of Hassan and Yero (2012) and Roodposhti (2010), while in relation to earnings quality, contradicts the study of Ebrahimi *et al.*, (2010). Based on this result, there is no sufficient evidence to reject the null hypothesis that ownership structure has no significant effect on earnings quality.

For leverage as a control variable, the result revealed a positive but not significant relationship with earnings management. The result contradicted the saying of Trueman and Titman (1988) who added that managing earnings enables managers to reduce estimates of various claimants of the firm about the volatility of its earnings process and so lowers their assessment of the probability of bankruptcy. Also firm size showed a positive but not significant relationship with earnings management. This result does not support the statement of Watts and Zimmerman (1990) who pointed out that larger firms are typically more politically visible than smaller firms, suggesting a lower proportion of earnings management. In the same vain, this outcome disagrees with Park and Shin (2004) statement that larger firms are more closely scrutinized than smaller

firms which encourage them to produce higher quality of reported earnings compared to the smaller firms. The control variables; firm size and leverage are included in earnings management model with the believe that they have influence on earnings management order than that of the independent variable, but from the result of the study the control variables are not significant; this could be due to the fact that, the influential power they have on the dependent variable is so insignificant. These findings are in line with that of Hashim and Devi (2006).

Testing the overall significance of a multiple regression in terms of R-Squared, this study found an R^2 of 0.15%, indicating that the extent to which the independent variables (Institutional ownership, Managerial ownership and Ownership Concentration) influenced the dependent variable (Earnings Quality) is 0.15%. F-Statistics which is an indicator of the overall model fitness, proved that the model of the study is fit with f-value significance at less than 1%; the p-value is 0.000.

4.6 Policy Implications

The study is on the distribution of company's ownership and its influence on the earnings of Insurance companies. Empirically, studies on this aspect revealed positive, negative or inconclusive inference between ownership structure and earnings quality. Whichever way, it has some implications on policy. The findings of this study are useful to insurance companies' operators on their share composition, and to understand whether the earnings quality reported depends on these compositions. It will also expose to both the shareholders and the management of the insurance companies the true reflection of the earnings quality reported, that is, whether or not it is being manipulated.

This discovery is expected to inform management decision in dealing with the internal situation of earnings manipulation, so that the confidence of the investors is not eroded, which has the implication of the investors adjusting or even withdrawing their shareholdings. Furthermore, the stakeholders can intervene in terms of the composition of the shareholding structure and how it influences earnings manipulation. This can be done by ensuring that policies are made to checkmate these excesses, as well as curtailing the power of any ownership structure to influence management negatively.

4.7 Summary

This chapter explained the findings of the study. The findings were linked with the null hypotheses formulated earlier which provided the ground to either rejecting or failing to reject the hypotheses.

CHAPTER FIVE

Summary, Conclusion and Recommendation

5.1 Summary

From the analysis of the hypotheses tested, the following are the summary of the findings:

The researcher found a significant negative relationship between earnings quality and institutional ownership. This postulated that an increase in ownership stake of institutional investor reduces the earnings quality. This led to the rejection of the null hypothesis which stated that institutional ownership does not impact on earnings quality.

Secondly, the result revealed a significant negative relationship between earnings quality and managerial ownership. This indicated that, the more shares owned by insider the less the quality of earnings they report. As a result, this study rejected the null hypothesis that managerial ownership does not impact earnings quality.

Thirdly, the result of the analysis showed that ownership concentration does not influence earnings quality. This suggested that, the ownership concentration does not matter in earnings quality reported. Also based on the result the study failed to reject the null hypothesis, which stated that, ownership concentration has no effect on earnings quality.

5.2 Conclusion

After testing and analyzing the hypotheses of the study on ownership structure and earnings quality of quoted insurance companies in Nigeria, the researcher therefore infer the followings:

Institutional ownership does influence the earnings quality of Nigerian insurance companies. Managerial ownership has a significant negative influence on earnings quality. Ownership concentration does not improve earnings quality. Leverage and firm size as control variables have no significant relationship with earnings quality.

5.3 Recommendation

Following the hypotheses formulated and the findings of the study the researcher recommends the following:

The Nigerian Insurance Companies should carefully study their institutional investors in order to find out the best way to make them long term institutional investors, who will never sell their ownership stake even if something unsatisfactory comes up due to the confidence they have in the firm, since long term institutional investors have more power to monitor the affairs of managers, as such the earnings reported is expected to be high.

The Nigerian Insurance Companies should reduce the percentage of shares owned by managers which is up to 22%. Since as insiders they have more access to the financial statement of the company, this gives them the power to manipulate the earnings which consequently affects the earnings they report negatively.

Nigerian Insurance industry concentration of ownership is low as depicted in the result at less than 10 percent. That is, with this low ratio, it clearly showed that they engage in monopolistic power of dictating to managers how the company should be run rather than monitoring their financial activities. Therefore, the Nigerian Insurance Companies should increase the shareholding of their major investors, so that they will effectively monitor management activities due to the high investment they have in the companies. As such, management manipulation of earnings will reduce, thereby improving the quality of earnings they report.

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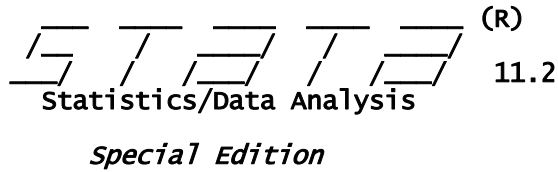
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Appendix A: Summary statistics



(R)

11.2

Copyright 1985-2009 StataCorp LP
StataCorp
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College Station, Texas 77845 USA
800-STATA-PC <http://www.stata.com>
979-696-4600 stata@stata.com
979-696-4601 (fax)

Single-user Stata license expires 31 Dec 9999:
Serial number: 71606281563
Licensed to: STATAForAll
STATA

Notes:

1. (/m# option or -set memory-) 50.00 MB allocated to data
2. (/v# option or -set maxvar-) 5000 maximum variables

. edit

. *(8 variables, 138 observations pasted into data editor)

. summarize emgt intown manown owncon ta lev

Variable	Obs	Mean	Std. Dev.	Min	Max
emgt	138	.1098621	.1488437	.000156	.823235
intown	138	.3973188	.2004977	.07	.79
manown	138	.2373913	.2325527	.01	.85
owncon	138	.4155797	.2127849	.04	.96
ta	138	22.60671	1.609447	15.6891	25.2905
lev	138	44.43235	429.3679	.038191	4953.19

.

Appendix B: Normality test

. swilk emgt intown manown owncon ta lev

Shapiro-wilk w test for normal data

Variable	Obs	W	V	Z	Prob>z
emgt	138	0.64024	38.980	8.268	0.00000
intown	138	0.96555	3.733	2.973	0.00147
manown	138	0.87183	13.888	5.939	0.00000
owncon	138	0.94935	5.488	3.843	0.00006
ta	138	0.60221	43.101	8.495	0.00000
lev	138	0.07879	99.814	10.390	0.00000

Appendix C: Correlation matrix

```
. correlate emgt intown manown owncon ta lev
(obs=138)
```

	emgt	intown	manown	owncon	ta	lev
emgt	1.0000					
intown	0.0170	1.0000				
manown	0.1396	-0.0043	1.0000			
owncon	-0.0029	0.4079	-0.0140	1.0000		
ta	0.0642	-0.1077	-0.1821	-0.0659	1.0000	
lev	-0.0561	-0.0201	-0.0365	-0.0380	-0.0377	1.0000

Appendix D: Pooled OLS Regression

```
. regress emgt intown manown owncon ta lev
```

Source	SS	df	MS	
Model	.093392086	5	.018678417	Number of obs = 138
Residual	2.94176687	132	.022286113	F(5, 132) = 0.84
Total	3.03515896	137	.022154445	Prob > F = 0.5249
				R-squared = 0.0308
				Adj R-squared = -0.0059
				Root MSE = .14929

emgt	Coef.	Std. Err.	t	P> t	[95% Conf. Interval]
intown	.0225356	.0699607	0.32	0.748	-.1158536 .1609249
manown	.0991483	.0558609	1.77	0.078	-.0113499 .2096466
owncon	-.0061398	.0657198	-0.09	0.926	-.1361401 .1238606
ta	.0086301	.0081215	1.06	0.290	-.007435 .0246952
lev	-.0000162	.0000298	-0.54	0.588	-.0000751 .0000428
_cons	-.1144573	.1926733	-0.59	0.553	-.4955842 .2666695

Appendix E: Heteroskedasticity Test

```
. hettest
```

Breusch-Pagan / Cook-Weisberg test for heteroskedasticity

Ho: Constant variance

Variables: fitted values of emgt

chi2(1) = 24.00

Prob > chi2 = 0.0000

Appendix F: Multicollinearity test

. vif

variable	VIF	1/VIF
intown	1.21	0.826773
owncon	1.20	0.831839
ta	1.05	0.952120
manown	1.04	0.963953
lev	1.01	0.994802
Mean VIF	1.10	

Appendix G: Fixed effect, random effect regressions and Hausman specification test

. xtreg emgt intown manown owncon ta lev, fe

Fixed-effects (within) regression
 Group variable: id
 Number of obs = 138
 Number of groups = 23
 R-sq: within = 0.1477
 between = 0.0049
 overall = 0.0049
 Obs per group: min = 6
 avg = 6.0
 max = 6
 corr(u_i, Xb) = -0.7548
 F(5,110) = 3.81
 Prob > F = 0.0032

emgt	Coef.	Std. Err.	t	P> t	[95% Conf. Interval]	
intown	.5330163	.206111	2.59	0.011	.1245527	.94148
manown	.2224336	.098648	2.25	0.026	.0269365	.4179308
owncon	.0669328	.0807128	0.83	0.409	-.0930209	.2268866
ta	-.0049592	.0084758	-0.59	0.560	-.0217562	.0118379
lev	-.0000136	.0000267	-0.51	0.613	-.0000665	.0000394
_cons	-.0698215	.1951226	-0.36	0.721	-.4565087	.3168657
sigma_u	.15656892					
sigma_e	.12165123					
rho	.62355766	(fraction of variance due to u_i)				

F test that all u_i=0: F(22, 110) = 4.04 Prob > F = 0.0000

. est store fe

. xtreg emgt intown manown owncon ta lev, re

Random-effects GLS regression
 Group variable: id
 Number of obs = 138
 Number of groups = 23
 R-sq: within = 0.1163
 between = 0.0001
 overall = 0.0211
 Obs per group: min = 6
 avg = 6.0
 max = 6
 corr(u_i, X) = 0 (assumed)
 Wald chi2(5) = 8.72
 Prob > chi2 = 0.1209

emgt	Coef.	Std. Err.	z	P> z	[95% Conf. Interval]	
intown	.1039577	.1005222	1.03	0.301	-.0930622	.3009776
manown	.1765063	.0718726	2.46	0.014	.0356386	.317374
owncon	.013994	.0715526	0.20	0.845	-.1262465	.1542345
ta	.0025852	.0078804	0.33	0.743	-.0128601	.0180305
lev	-.0000209	.0000265	-0.79	0.429	-.0000729	.000031
_cons	-.0366712	.187679	-0.20	0.845	-.4045153	.331173
sigma_u	.08748038					
sigma_e	.12165123					
rho	.3408548	(fraction of variance due to u_i)				

. est store re

. hausman fe re

Note: the rank of the differenced variance matrix (4) does not equal the number of coefficients being tested (5); be sure this is what you expect, or there may be problems computing the test. Examine the output of your estimators for anything unexpected and possibly consider scaling your variables so that the coefficients are on a similar scale.

	Coefficients		(b-B) Difference	sqrt(diag(V_b-V_B)) S.E.
	(b) fe	(B) re		
intown	.5330163	.1039577	.4290587	.1799362
manown	.2224336	.1765063	.0459273	.0675704
owncon	.0669328	.013994	.0529389	.0373467
ta	-.0049592	.0025852	-.0075444	.0031207
lev	-.0000136	-.0000209	7.38e-06	3.28e-06

b = consistent under Ho and Ha; obtained from xtreg
B = inconsistent under Ha, efficient under Ho; obtained from xtreg

Test: Ho: difference in coefficients not systematic

chi2(4) = (b-B)'[(V_b-V_B)^(-1)](b-B)
= 12.16
Prob>chi2 = 0.0162
(V_b-V_B is not positive definite)

Appendix H: Names of Listed Insurance Companies Used in the Study

- | | |
|-------------------------------|---------------------|
| 1. AIICO | 13. Mutual Benefit |
| 2. Consolidated Insurance | 14. Niger Insurance |
| 3. Continental Reinsurance | 15. Oasis |
| 4. Cornerstone | 16. Prestige |
| 5. Crusader | 17. Regency |
| 6. Custodian | 18. Sovereign |
| 7. Equity Assurance | 19. NEM |
| 8. Guaranteed Trust Assurance | 20. Standard |
| 9. Guinea Insurance | 21. Unity Kapital |
| 10. Lasako | 22. Universal |
| 11. Law Union and Rock | 23. Royal |
| 12. Linkages | |