

Additional Evidence on Earnings Management and Corporate Governance

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Abstract

The primary purpose of this paper is to analyze the relationship between corporate governance mechanism and earnings management. Specifically, using a sample of 799 large Japanese manufacturing firms from the period 1999 to 2004, we verify the effect of different governance mechanisms, including internal (managerial ownership, ownership concentration and executive stock option) and external (institutional investors ownership, financial institutions and other corporations shareholding), on earnings management. For internal governance mechanisms, this study presents following three results. First, firms with higher managerial ownership are associated with more earnings management. Second, there is a significant U-shaped relationship between ownership concentration and earnings management. Third, executive stock option does not affect the earnings management; the performance-based managerial scheme is not always effective. For external governance mechanisms, this study presents following three results. First, firms with higher institutional investors ownership are associated with less earnings management. Second, there is a significant U-shaped relation between the shareholdings of financial institutions and earnings management. Third, the shareholdings of foreign other corporations have a positive effect on earnings management. Furthermore, the cross-share holdings of other domestic corporations do not affect the earnings management.

Keywords: Earnings management, Corporate governance

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