An appraisal of corporate governance and earnings management practices in Nigeria

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Abstract: This study examined corporate governance and earnings management practices in Nigeria. Descriptive survey was adopted. Primary data was used for the study through structured questionnaire and was tested with Z-test statistical tool. The findings of this study revealed that there was a negative relation between outside directors and earnings management as corporate boards dominated by outside directors makes manipulative accounting difficult, constrain the fraud tendencies of manager and reduces the likelihood of earnings management while boards that are dominated by inside directors increase transfer of wealth to managers at the expense of the stakeholders and increase the tendencies of fraudulent reporting. Based on the study findings it is recommended that the audit committee members should be encouraged to possess a certain level of financial competencies in order to decrease the likelihood of earnings management and; that corporate organizations should provide formal orientation programs for their new and existing directors and support the development of external courses on issues of corporate governance and earnings management.

Keywords: Corporate Governance, Earning management and financial efficiency.

INTRODUCTION

There has been a considerable debate concerning the impact of corporate governance in enhancing the reliability of earnings in Nigeria[1-4]. Bergstresser et al [5] posited that it will be difficult to eliminate the manipulation of earnings report as most organizations adopt accrual accounting methods. Bergstresser et al [5] accruals are a particularly important tool for manipulative accounting because they are components of earnings that are not reflected in current cash flows, and a great deal of managerial discretion goes into their construction. Cornett et al [6] in view reiterated that since financial statements reflect performance as well as managerial competence, it is not unlikely that managers will engage in manipulating earnings within the regulatory framework to insinuate that they are good managers. This aggressive accounting practice may even become more prominent when managerial compensation, such as option and stocks, is tied to firm performance.

Notwithstanding the foregoing arguments, it is important to stress that financial reports serve as a mirror through which a firm’s performance is viewed by all its stakeholders. The quality of these reports is contingent upon its reliability in making investment decisions by investors and other interested parties to the firm, therefore there is the need to seek for means of enhancing the corporate reporting standards of organizations. Unfortunately, studies that explored the relationship between corporate governance and firms’ earnings management are contradictory. Also, the relationship between governance mechanisms and financial reporting quality or opportunistic accounting has been less discussed. Only a few studies concluded that good governance mechanisms can impact on the discretionary behaviour of managers [7-8]. Other studies indicated that the relationship presents a rather complex situation that needs further investigation[8].

In Nigeria, most managers of organizations are involved in manipulative accounting in a bid to either mislead some stakeholders about the underlying economic performance of the company or to influence contractual outcomes that depend on reported accounting numbers. This has however been shown to impact negatively on performance of organization as they result in business failure and consequently business close down. In recent business practices, managers of organizations still engage in earnings management to woe investor and insinuate that they are good managers notwithstanding they undermine the confidence of stakeholders and sometime constitute a source of conflict between managers and stakeholder[9-10]. Therefore, in Nigeria, if these practices of manipulative accounting continue, definitely it will undermine the reliability and confidence of foreign investors on indigenous companies’ reports and of...
course, these will cut down on business transaction. Hence, there is a need to look out for means of enhancing the corporate reporting standards of organizations. In this study corporate governance is viewed as one of such means of limiting manipulative accounting which in recent studies have received little attention. The main objective of the study is to examine corporate governance and earnings management practices in Nigeria. Specifically, this study aimed to examine the extent to which the proportion of independent directors affects earnings management in corporate organization; to ascertain the extent to which possession of certain level of financial competencies by audit committee members affect earnings management in Nigerian corporate organization.

CONCEPTUAL FRAMEWORK

1. The Concept of Corporate Governance

Corporate governance has been looked at and defined variably by different scholars and practitioners. However they all have pointed to the same end, hence giving more of a consensus in the definition. Coleman and Nicholas-Biekpe [11] defined corporate governance as the relationship of the enterprise to shareholders or in the wider sense as the relationship of the enterprise to society as a whole. However, Mayer [12] offers a definition with a wider outlook and contends that it means the sum of the processes, structures and information used for directing and overseeing the management of an organization. The Organization for Economic Corporation and Development [13] has also defined corporate governance as a system on the basis of which companies are directed and managed. It is upon this system that specifications are given for the division of competencies and responsibilities between the parties included (board of directors, the supervisory board, the management and shareholders) and formulate rules and procedures for adopting decisions on corporate matters.

Oladimeji [14], opined that corporate governance could be conceptualized in the manner in which power is exercised in the management of economic and social resources for sustainable human development. It addresses the institutional framework. It is view corporate governance as the manner in which the power of a corporation is exercised in accounting for corporation’s total portfolio of assets and resources with the objectives of maintaining and increasing shareholder’s value and the satisfaction of other stakeholders while attaining the corporate mission. In other words, corporate governance refers to the establishment of an appropriate legal, economic and institutional environment that allows companies to thrive as institutions for advancing long-term, shareholders value and maximum human centered development. The corporation has to achieve this while remaining conscious of its responsibilities to other stakeholders, the environment and the society at large.

Corporate governance is also concerned with creation of balance between economic and social goals and between individual and communal goals. To achieve this, there is the need to encourage efficient use of resources, accountability is the use of power, and the alignment of the interest of the version stakeholders, such as individuals, corporations and the society.

In his view, Smith [15] sees corporate government as a “culture that has a common understanding of the roles of management and the board”. To him “corporate governance is a culture of continuous open dialogue and communication. In rounding up his views on corporate governance, smith noted that it is about people. “People doing not just where the rules say but about doing what is right”.

According to Cornett [16] corporate governance is an internal system encompassing policies, processes and people, which serves the needs of shareholders by directing and controlling management activities with good business savvy, objectivity and integrity. Sound corporate governance is therefore independent on external market place commitment and legislation plus a healthy board culture that safeguards policies and processes.

In another perspective, Arun and Turner [17] contend that there exists a narrow approach to corporate governance, which views the subject as the mechanism through which shareholders are assured that managers will act in their interests. However, it was[18] observed that there is a broader approach which views the subject as the methods by which suppliers of finance control managers in order to ensure that their capital cannot be expropriated and that they can earn a return on their investment.

2 Earnings Management

According to Healy and Wahlen [19] earnings management is the deliberate altering of financial information to either mislead investors on the underlying economic status of a firm or to gain some contractual benefits that depend largely on accounting numbers. In their view [20] conceptualized earnings management as the active manipulation of earnings toward a predetermined target. In the same vein, the Assurance Handbook [20] defined earnings management to include the recording of accounting entries, without any event to justify the accounting or the failure to record or correctly record transactions for the purpose of altering results. From the definitions above, it can be said that the common subject is one of altering results.

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To Bergstresser and Phillippon[5] accruals are the most important earnings management instruments that are used by managers to either increases or decrease reported income. This is because they are components of earnings that are not reflected in current cash flows, and a great deal of managerial discretion goes into their construction.

THEORETICAL FRAMEWORK

The study will be based on some basic theories. The theories to be applied to this study include the bureaucracy and decision theory.

1 The Bureaucracy Theory

The major propounded of this theory is Weber[21]. According to the theory, for an efficient definition of task and responsibility within an organization there must be permanent administration and standardization of work procedures. Such standardization of work procedures include allocation of task according to duties, a clear cut division of labour and a high level of specialization, and a hierarchical authority. Weber[21] believed that such standardization will bring about effective leadership in organization and performance.

The bureaucracy theory applies to this study, since corporate governance is expected to improve coordination of task and responsibilities within organization and reduce manipulative accounting practices just as theorized in the bureaucratic theory by Weber [21].

2 The Decision Theory

Barnard [22] is one of the proponents of this theory. The theory states that an organization is an information processing network with numerous decision points of which understanding how these decisions are made helps in understanding behavior in the organization. This theory further stressed that for effective coordination of activity within an organization there must cooperative decision making.

This study is based on decision theory in the sense that corporate governance is hoped to enhance decision making and reduce earning management tendencies within the organization

Corporate Governance and Earnings Management

The importance of effective corporate governance to corporate and economic performance cannot be overemphasized in today’s global market place. According to Shehu and Abu-Bakr [23] companies perceived as adopting international best corporate governance practices are more likely to attract international investors than those whose practices are perceived to be below international standards. Olayinka [24] noted that Corporate Governance has succeeded in attracting a good deal of public interest because of its apparent importance for the economic health of corporations and society in general. Corporate governance specifies the distribution of rights and responsibilities among different participants in the corporation, such as the board, managers, shareholders and other stakeholders, and spell out the rules and procedures for making decisions on corporate affairs. By doing this, it provides the structure that makes manipulative accounting difficult. The role of corporate governance in limiting accounting difficult. The role of corporate governance in limiting earning management will be discussed in the subheading below:

Composition of the board and earnings management

Among the set of corporate governance mechanisms, the board of directors is often considered the primary internal control mechanism to monitor top management and protect the shareholders’ interest. For example, Fama [25] argues that board of directors is a “market-induced institution, the ultimate internal monitor of the set of contracts called a firm, whose most important role is to scrutinize the highest decision makers within the firm”. It has been argued that it is the responsibility of the directors to ensure that financial statements are prepared according to approved accounting standards [26]. Since the applicability of accounting standards is very flexible, management may choose an acceptable accounting method or estimate that is appropriate for the need of the organization. In this respect, the compliance with the accounting standards may not necessarily mean that financial statements are free from manipulation. Thus, the compliance with accounting standards as required in the Companies and Allied Matters Act (CAMA), 1990 may reduce the propensity to manage earnings but may not eliminate the entire practice of earnings management. Therefore, it is important that the board of directors carry out its monitoring role effectively in order to ensure that financial reporting provides quality information to users by reflecting proper underlying economic substance of the company transactions.

The components within the board are essential ingredients for effective monitoring. The appointment of managers as directors (i.e. insiders) is important because they have more information about the organization compared to outside directors. However, domination by insiders may lead to transfer of wealth to managers at the expense of the stockholders[27-28]. Therefore, outside directors are appointed on the board mainly to obtain independent monitoring mechanism over the board process thereby reducing agency conflicts and improve performance[29]. Consistent with this theory, results in prior studies suggest that outside directors are positively related to abnormal stock
return[30] and performance and negatively related to fraudulent reporting. Similarly, there is a negative relation between outside directors and earnings management[7].

However, there are critics on the role of non-executive directors on the board. Some believe that they perform little role in monitoring the board because lack of real independence, time, as well as enough information[31-32]. To be effective, independent non-executive directors should have both, strong incentives to monitor the board, and the capabilities to identify earnings management[33]. Boards dominated by outsiders are arguably in a better position to monitor and control managers [34]. Outside directors are independent of the firm’s managers, and in addition bring a greater breadth of experience to the firm[35-36]. A number of studies have linked the proportion of outside directors to financial performance and shareholders’ wealth [37-39]. Sakar et al. [40] posit that firms with high quality governance mechanisms, such as independent board of directors are associated with low levels of earnings management.

The relation between between board composition and firm performance has been explored in the literature. Most of these studies are the extension of Weisbach [41] who investigated the efficiency of CEO monitoring mechanism between inside and outside directors. The work documents that outside directors play a significant role in monitoring CEO; This means that boards that are dominated by outside directors can significantly constrain the opportunistic tendencies of managers and act in a manner that is consistent with the value maximization objective of the firm.

Audit committee and earnings management

An audit committee is an operating committee of the Board of Directors charged with oversight of financial reporting and disclosure. Committee members are drawn from members of the company’s board of directors, with a Chairperson selected from among the committee members. The Companies and Allied Matters Act (CAMA), 1990 states that a public limited liability company should have an audit committee (maximum of six members of equal representation of three members each representing the management/directors and shareholders) in place. The members are expected to be conversant with basic financial statements.

The audit committee’s function has evolved over the years. The primary objective of an Audit Committee is to increase the credibility of annual financial statements, assist directors in meeting their responsibilities and enhance audit independence [42]. Audit Committees have been involved in monitoring and protecting the interests of shareholders[43-45]. Researchers have also argued that financial reporting is more reliable and questionable corporate practices are reduced where an audit committee exists[46-48].

Due to their responsibility for oversight of internal control and financial reporting, good governance dictates that audit committee members should possess a certain level of financial competencies. Thus, the Blue Ribbon Committee [49] recommends that each member of the audit committee should be or become financially literate and that at least one member should have accounting or related financial management expertise, where ‘experience’ is defined as ‘past employment experience in finance or accounting, requisite professional certification in accounting, or any other comparable experience or background which results in the individual’s financial sophistication, including being or having been a CEO or other senior officer with financial oversight responsibilities’. This recommendation is supported. They observe that the accounting experience of audit committee members as well as their knowledge of auditing is positively associated with the likelihood that they will support the auditor in an auditor-corporate management dispute. These recommended best practices and research findings suggest that the financial competencies of audit committee members decrease the likelihood of earnings management.

The audit committee has a very important role to play regarding fraud and overseeing fraud risk management. In this regard, audit committees play an important role in preventing, detecting and investigating fraud and earnings management. As far as fraud and earnings management is concerned, the audit committee should have zero tolerance, and all instances of such should be taken with all seriousness.

Empirical Studies

Olayinka [24] conducted a study on earnings management and corporate Governance in Nigeria. The descriptive survey research was adopted. The population of the study comprised of business organizations quoted on the Nigeria Security Exchange (NSE). The sample consisted of one hundred respondents in Lagos. Primary data was obtained from the targeted respondents through a carefully constructed questionnaire. The hypotheses formulated were tested with the pearson chi-square statistics. The findings of the study indicated that board dominated by outside directors brings a greater breadth of experience to the firm and are in a better position to monitor and control managers, thereby reducing earnings management. It was also observed that audit committee whose members possess certain level of financial competencies would reduce the likelihood of earnings management. The
study recommended that board composition should include greater proportion of independent outside directors with corporate experience and that audit committee members should be encouraged to possess a certain level of financial competencies in order to decrease the likelihood of earnings management.

Similarly, Shehu and Abu-Bakr [23] conducted a study on corporate governance, earnings management and financial performance: A case of Nigerian manufacturing firms. The correlational descriptive design was adopted for the study. The sample consisted of ten manufacturing firms in Lagos. Secondary data were the main sources of data collection and these were extracted from annual reports of the sample firms for the period between 2008 to 2010 and univariate OLS multiple regression was used as a tool for data analysis. The study documented that corporate governance significantly impact on both the adjusted and unadjusted firm performance in different magnitudes and directions. Specifically, the study empirically established that board composition is inversely related with earnings management.

Also, Cornet et al. [16] examined the impact of corporate governance and pay-for-performance on earnings management. Using 100 largest firms in the U.S. as ranked by S&P between 1994-2003, they find that the presence of independent outside directors reduce earnings management. Similarly, Cornet et al. ([6] investigate how corporate governance mechanism affects earnings and earnings management at large publicly traded U.S. companies for the period between 1994-2002. The study finds that largely independent boards constrain managers’ discretionery behaviour. In the same vein, the research conducted by Roodposhti and Chashmi [50] for the period between 2004-2008 in Iran, using 196 firms listed on Tehran Stock Exchange, revealed a negative association between board independence and earnings management.

On the contrary, Hashim and Devi [51] examined the relationship between board independence, CEO duality and accrual management in Malaysia. Using 200 top non-financial companies listed on Malysian Stock Exchange, they find that large proportion of independent executive directors is associated with higher income-increasing earnings management. Also, Moreso, Shah et a [53] investigated the relationship between board composition and earnings management in Pakistani listed companies for the period between 2003 and 2007. They find no significant relationship between board composition and earnings management.

Gap in the literature

The literature reviewed covered the conceptual framework, theoretical framework, theoretical studies and empirical studies. Most of the authors viewed corporate governance as sum of the processes, structures and information used for directing and overseeing the management of an organization. Most of the concern over corporate governance stems from the fact that sound governance practices by organizations result in lower tendencies towards earning management. However, the researcher observed from the reviewed that only little attention was given on the influence of corporate governance practices such as board composition and audit committee. In this study effort will be made to fill this gap in literature and highlight the role of board composition and audit committee in reducing earnings management.

RESEARCH METHODOLOGY

The design adopted for this study was the descriptive survey. According to Nworgu, this design involves the gathering of data through questions. This design was selected for this study because the study seeks to sample the opinion of respondents and draw inferences based on their views. The target population of the study consisted of forty four (44) management staff of Nigeria Bottling Company, Onitsha.

Method of Data Analysis

Data generated from the study was analyzed using weighted mean statistics and Z-test. The weighed mean statistics was used to answer the research question of the study while the Z-test was used in testing the hypotheses of the study. The decision rule for the weighed mean statistics was fixed at 3.0

Hypotheses

H0: Greater proportions of independent directors in organization board of directors do not reduce the likelihood of earnings management in Nigerian corporate organizations.

H1: Greater proportion of independent directors in organization board of directors reduce the likelihood of earnings management in Nigerian corporate organizations.

H0: Possession of certain level of financial competencies by audit committee members does not reduce the likelihood of earnings management in Nigerian corporate organizations.

H1: Possession of certain level of financial competencies by audit committee members reduce the likelihood of earnings management in Nigerian corporate organizations.
DATA ANALYSIS

Table 1: Data analysis for Hypothesis one

<table>
<thead>
<tr>
<th>S/N</th>
<th>Items</th>
<th>SA</th>
<th>A</th>
<th>U</th>
<th>D</th>
<th>SD</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Boards that are dominated by outside directors provides a structure that makes manipulative accounting difficult</td>
<td>13</td>
<td>13</td>
<td>9</td>
<td>6</td>
<td>3</td>
</tr>
<tr>
<td>2</td>
<td>Boards that are domination by insiders may increase transfer of wealth to managers at the expense of the stakeholders</td>
<td>9</td>
<td>9</td>
<td>11</td>
<td>9</td>
<td>6</td>
</tr>
<tr>
<td>3</td>
<td>Boards that are dominated by inside directors can increase the tendencies of fraudulent reporting</td>
<td>11</td>
<td>10</td>
<td>8</td>
<td>1</td>
<td>0</td>
</tr>
<tr>
<td>4</td>
<td>There is a negative relation between outside directors and earnings management</td>
<td>14</td>
<td>10</td>
<td>7</td>
<td>7</td>
<td>6</td>
</tr>
<tr>
<td>5</td>
<td>Boards that are dominated by outside directors can constrain the opportunistic tendencies of managers.</td>
<td>10</td>
<td>10</td>
<td>7</td>
<td>1</td>
<td>0</td>
</tr>
<tr>
<td>6</td>
<td>Boards with greater proportion of independent directors reduces the likelihood of earnings management</td>
<td>12</td>
<td>10</td>
<td>8</td>
<td>8</td>
<td>6</td>
</tr>
</tbody>
</table>

Table 1 shows the responses on extent the proportion of independent directors will affects earnings management in Nigeria Bottling Company, Enugu. From the table the mean score on all the items (1, 2, 3, 4, 5 and 6) are above the mean cut off of 3.0. This shows that majority of the respondents agree that corporate boards that are dominated by outside directors that makes manipulative accounting difficult, constrain the opportunistic tendencies of manager and reduces the likelihood of earnings management while boards that are dominated by inside directors increase transfer of wealth to managers at the expense of the stakeholders and increase the tendencies of fraudulent reporting.

Table 2: Data analysis for hypothesis two

<table>
<thead>
<tr>
<th>S/N</th>
<th>Items</th>
<th>SA</th>
<th>A</th>
<th>U</th>
<th>D</th>
<th>SD</th>
</tr>
</thead>
<tbody>
<tr>
<td>7</td>
<td>Audit committee increases the credibility of financial statements, and reduces the tendencies of manipulative reporting practices</td>
<td>12</td>
<td>10</td>
<td>8</td>
<td>8</td>
<td>6</td>
</tr>
<tr>
<td>8</td>
<td>Audit committees play an important role in preventing, detecting and investigating earnings management</td>
<td>14</td>
<td>10</td>
<td>7</td>
<td>7</td>
<td>6</td>
</tr>
<tr>
<td>9</td>
<td>Financial reporting is more reliable where an audit committee exists</td>
<td>13</td>
<td>13</td>
<td>9</td>
<td>6</td>
<td>3</td>
</tr>
<tr>
<td>10</td>
<td>Earning management practices are reduced where an audit committee exists</td>
<td>9</td>
<td>9</td>
<td>11</td>
<td>9</td>
<td>6</td>
</tr>
<tr>
<td>11</td>
<td>The financial competencies of audit committee members decrease the likelihood of earnings management</td>
<td>11</td>
<td>10</td>
<td>8</td>
<td>10</td>
<td>5</td>
</tr>
</tbody>
</table>

Table 2 shows the responses on the extent the possession of certain level of financial competencies by audit committee members will affect earnings management in Nigeria Bottling Company, Enugu. From the table the mean score on all the items (7, 8, 9, 10 and 11) are above the mean cut off of 3.0. This shows that majority of the respondents agree that high level of financial competencies by audit committee increases the credibility of financial statements, reduces the tendencies of manipulative reporting practices, makes financial reporting more reliable, play an important role in preventing, detecting and investigating earnings management, and reduce earning management practices.

Hypotheses One

H0: Greater proportion of independent directors in organization board of directors does not reduce the likelihood of earnings management in Nigerian corporate organizations.

H1: Greater proportion of independent directors in organization board of directors reduces the likelihood of earnings management in Nigerian corporate organizations.

Table 3: Testing of Hypotheses One

<table>
<thead>
<tr>
<th>Agree</th>
<th>Disagree</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>n₁ (30)</td>
<td>n₂ (13)</td>
<td>44</td>
</tr>
<tr>
<td>p₁ (0.70)</td>
<td>p₂ (0.30)</td>
<td>1.00</td>
</tr>
<tr>
<td>Z-cal</td>
<td>2.63</td>
<td></td>
</tr>
<tr>
<td>Z-tab (at 5%)</td>
<td>1.96</td>
<td></td>
</tr>
</tbody>
</table>

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From the table 3, p₁ (the proportion of respondent who agree to the research question) is greater than p₂ (the proportion of respondent who disagree to the research question) and Z-calculated value of 2.63 is greater than the tabulated value of 1.96 at 5% level of significance. Hence, the null hypothesis is rejected and therefore concludes that greater proportion of independent directors in organization board of directors reduces the likelihood of earnings management in Nigerian corporate organizations.

**Hypotheses Two**

H₀: Possession of certain level of financial competencies by audit committee members does not reduce the likelihood of earnings management in Nigerian corporate organizations.

H₁: Possession of certain level of financial competencies by audit committee members reduces the likelihood of earnings management in Nigerian corporate organizations.

Table 4: Testing of Hypotheses Two

<table>
<thead>
<tr>
<th></th>
<th>Agree</th>
<th>Disagree</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>n₁</td>
<td>35</td>
<td>n₂</td>
<td>9</td>
</tr>
<tr>
<td>p₁</td>
<td>0.80</td>
<td>p₂</td>
<td>0.20</td>
</tr>
<tr>
<td>Z-cal</td>
<td>3.63</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Z-tab (at 5%)</td>
<td>1.96</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

From the table 4 p₁ (the proportion of respondent who agree to the research question) is greater than p₂ (the proportion of respondent who disagree to the research question) and Z-calculated value of 3.63 is greater than the tabulated value of 1.96 at 5% level of significance. Hence, the null hypothesis is rejected and therefore concludes that the possession of certain level of financial competencies by audit committee members reduces the likelihood of earnings management in Nigerian corporate organizations.

**CONCLUSIONS**

The findings of this study were consistent with previous studies. Olayinka [24] study for instance showed that adoption of good governance codes such as the appointment of independent directors reduces the likelihood of fraudulent financial reporting. Similarly, Adeyemi and Uadiale [2] explain that board dominated by outside directors brings a greater breadth of experience to the firm and are in a better position to monitor and control managers since they have nothing of interest to gain. Also, Dabor and Adeyemi [3] have established that audit committee is capable of increasing the public’s confidence in the credibility and objectivity of published financial statements. They found that audit committee whose members possess certain level of financial competencies would reduce the likelihood of earnings management.

Based on the findings of this study it can concluded that the poor corporate governance structure like appointment of incompetent auditors and constitution of boards with just their personal interest allows for the higher frequency and wider scope of earnings manipulation while the good corporate governance principles, structures and practices forestall and limit the extent and degree of earnings management. Specifically, the study demonstrated that corporate boards that are dominated by outside directors makes manipulative accounting difficult, constrain the fraud tendencies of manager and reduces the likelihood of earnings management while boards that are dominated by inside directors increase transfer of wealth to managers at the expense of the stakeholders and increase the tendencies of fraudulent reporting. The study also revealed that that high level of financial competencies by audit committee increases the credibility of financial statements, reduces the tendencies of manipulative reporting practices, makes financial reporting more reliable, play an important role in preventing, detecting and investigating earnings management, and reduce earning management practices.

**RECOMMENDATIONS**

- Based on the study findings, it is recommended that:
  - Board composition in corporate organizations should include greater proportion of independent outside directors with corporate experience.
  - Executive compensation should be less aggressively linked to performance so that it does not induce managers to manipulate reported earnings to improve their compensation.
  - Audit committee members should be encouraged to possess a certain level of financial competencies in order to decrease the likelihood of earnings management.
  - Corporate organizations should provide formal orientation programs for their new and existing directors and support the development of external courses on issues of corporate governance and earnings management.
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