



An empirical study: The relationship between Internal Mechanisms of Corporate Governance and Accounting Conservatism

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ABSTRACT

Corporate governance corporate governance is known as one of the effective mechanisms. This group of capital market participants with regard to knowledge and the necessary expertise, access to effective communication channels can play a fundamental role in promoting corporate governance system and thus increase efficiency and productivity. The purpose of this study is investigating the Relationship between Internal Mechanisms of Corporate Governance and Accounting Conservatism in Corporations of Accepted in Tehran Stock Exchange in period of time between 2010- 2014. This current research in terms of purpose is applied research and in terms of method is descriptive-correlational research. This study consists of five hypotheses, to test the hypothesis multivariate linear regression tests combined (firm-year) is used. The Research Findings show that there is no significant relationship between Internal Mechanisms of Corporate Governance and Accounting Conservatism in Corporations of Accepted in Tehran Stock Exchange. The results also show that there is no significant relationship between board independence, concentration of ownership, board size and the dual duties of Director and Accounting Conservatism.

Keywords: Board size, Corporate Governance, Accounting Conservatism, Tehran Stock Exchange



1. INTRODUCTION

Conservatism is post-events related to the balance sheet or independent news and reflects the book value of net assets is underestimated that is not related to changes in future cash flows. Conservatism after the events, related to income and costs related to the news and early detection means more bad news than good news in earnings (Kanagartenam et al, 2013).

Later in the century, conservatism was an integral part of accounting. One of the applications related to contracts divided opinion among the contenders efficiency of different companies. English as trustees in bankruptcy were the first public audit institutions. Accountant's bankruptcies in clearings and all loss before profit distribution were identified. In order to ensure this was the case and the first settlement paid to people who have priority in liquidation. Predicting all future losses will reduce the possibility of payment in cash of the capital. All appropriate accounting profit if the distribution is taken into account, the fact that the results presented today provide less benefit more could be considered related topics. Nowadays, the increasing needs of customers and the public, sometimes the demands of different stakeholders, the complexity of regulations and technology and provide more attention to corporate governance structure and it was set up through corporate goals and ways to achieve those objectives and monitoring performance are determined. The corporate governance system to set rules, regulations, institutions and procedures applied which determine how companies are run efficiently and in the interests of the people, the aim of applying corporate governance framework to ensure there is an appropriate balance between freedoms to manage, the company provides accountability and interests of different stakeholders (Navazi, 2009).

Therefore, the current research has considered to investigate of the Relationship between Internal Mechanisms of Corporate Governance and Accounting Conservatism in Corporations of Accepted in Tehran Stock Exchange and try this question to be answered whether internal mechanisms of corporate governance and accounting conservatism are effective or not? If yes, what is the effect of relationship?

2. STATEMENT OF PROBLEM:



Stakeholder theory in 1984 by (Porter) was introduced in this theory, he says large companies and their impact on society is so deep that should be considered in addition to stakeholders in different parts of the community and companies should be held accountable for all these sectors (Karami et al., 2009). One of the important consequences of asymmetric behavior conservatism gains and losses on net asset value is less than the insistence on offer. Legislator's capital markets, standard setters and academics, because of this conservatism criticized the offer less than the current period can lead to future periods less than the costs and thus results in future periods to overstate earnings. The accounting principles of conservatism Board as a covenant moderating the Financial Accounting Statement No. 4 has listed accountants and thus respond with appropriate caution. Chat field conservative tracks in the middle ages. As large current property owners entrust their affairs steward underneath.

Finally, whether accounting conservatism is one of the desirable characteristics of financial statements or not, is an accounting research issue has long been debated. Many studies have been done in a conservative report. Kam Lai (2010) argues that conservatism in financial reporting arise as a result of some economic reasons. He explained the factors under four contracts based on the explanation, the explanation of lawsuits, explaining the tax and accounting rules and regulations of the explanation. The necessity of this research is to analyze and study fundamental factors that can play a special role in the decision-making process.

3. RESEARCH BACKGROUND

Atmaja et al (2014) effect on earnings management board size and independence were examined. They include a set of family and nonfamily firms listed in the Australian Stock Exchange during the period from 2009 to 2013, respectively. The results show that there are more discretionary accruals in family firms than nonfamily firms. Ali Shah et al (2014) study entitled "Corporate governance and earnings management in listed companies Pakistanis" has done. One reason for this result, disclosure of corporate governance practices provided by the companies mentioned.



Tariq H. Ismail and Rasha M. Elbok (2011) examined the effect of conditional and unconditional conservatism on earnings quality and stock prices in Egypt. Their findings showed that

- (1) Conditional conservatism negatively affects the quality of earnings and stock prices Egyptian firms,
- (2) Unconditional conservatism does not impact on earnings quality the negative impact on stock prices Egyptian firms.

Penman and Zhang (2014) Effect of changes in the relationship between conservatism and investment earnings quality looked on. They found that when a company makes use of conservative accounting and changes in its temporary investments reduce or increase current profits, therefore, it cannot be a good indicator of future earnings. Conservative accounting operations may not be conducive to high-quality earnings. Xia, D. Zhu (2009) examined the relationship between conservatism with their corporate governance. For this purpose, the relevant data from 2001 to 2006 began. According to their findings, the high degree of leverage, low levels of low-level controls shareholder and property management is more conservative accounting. The government's concern and political pressure on the owners and non-owners be more conservative. They also concluded that the most important factor accounting conservatism in China, debt and ownership and the board has little effect. Pour theoretical and Nazari Pour and Fatehi (2016) considered to a study entitled "The Role of Corporate Governance on bankruptcy (financial distress) in Corporations of Accepted in Tehran Stock Exchange. In other words, because the increase in institutional ownership, managerial ownership, board independence and concentration of ownership in the company, incentives for managers of financial distress do not decrease.

Mo'ayyeri and Amini (2016) in a study entitled "The relationship between accounting conservatism, monetary and credit policy of the business in Corporations of Accepted in Tehran Stock Exchange.

The results of research, evidence of the absurdity and lack of trade credit coefficients of conservative accounting policies and the results showed that the coefficient of monetary policy significantly and adversely impact conservatism.



Khezdozi and Javaheri (2015) in a study entitled the relationship between accounting conservatism quality's profits and stock prices in Corporations of Accepted in Tehran Stock Exchange. The findings show that there is a significant relationship between conditional and unconditional conservatism and earnings quality. As well as between conditional and unconditional conservatism and stock price have a significant relationship. In other words, increasing the amount of conservatism in events (unconditional) quality is less profit (negative relationship between conservatism and unconditional quality profits and stock prices) and also to increase the conservatism of the events (provided) by increasing the quality of earnings (positive relationship between conservatism high profits and stock prices) is associated.

Nazari Pour and Ezzati (2015) in a study entitled the relationship between earnings management, corporate governance and cohesion spending in Corporations of Accepted in Tehran Stock Exchange. In addition, the results show that the adjusted coefficient of determination and the entire period of study cost stickiness changes affecting corporate governance criteria (concentration of ownership, managerial ownership and institutional shareholders), earnings management and control variables research.

Akhgar and Rahimzada (2015) in a study entitled the relationship between institutional investors and managing their profits with accounting conservatism in Corporations of Accepted in Tehran Stock Exchange. The findings show the first statistical society, for the first hypothesis and the relationship between institutional investors and accounting conservatism is negative. For the second hypothesis results indicate a positive relationship between earnings management and accounting conservatism. The population loss is secondary to that of companies, three hypotheses were tested and the same results were obtained in a non-loss companies had achieved.

Ismail Zadeh (2014) examines the impact of corporate governance on earnings quality is examined in Corporations of Accepted in Tehran Stock Exchange. Construction of corporate governance that is examined in this study, the percentage of institutional ownership, number of blocks major shareholders, the percentage of non-executive directors in the board, the absence of the CEO as Chairman or Vice Chairman and independent auditor size. Hypothesis to a panel analysis and using data from 94



companies of Accepted in Tehran Stock Exchange through a combination of time-series data is done. The results show that a positive relationship between the percentage of institutional ownership, block number of major shareholders, the percentage of non-executive directors on the Board, the absence of CEO as Chairman or Vice Chairman of the Board of Directors and auditor size and quality of earnings.

4. RESEARCH HYPOTHESES

Main Hypothesis:

There is a significant relationship between the internal mechanisms of corporate governance and accounting conservatism in Corporations of Accepted in Tehran Stock Exchange.

Minor Hypotheses:

- 1- There is a significant relationship between board independence and Accounting Conservatism of company.
- 2- There is a significant relationship between concentration of ownership and Accounting Conservatism of company.
- 3- There is a significant relationship between board size and Accounting Conservatism of company.
- 4- There is a significant relationship between dual duties of Director and Accounting Conservatism of company.

Test period, population and sample:

The study tested a five-year period the period the period 1389 to 2014 based on the financial statements of the companies is preferred. However, due to the need to test research hypotheses year changes calculated (t) compared to the year (t-1); also requires information 2009 to calculate some variables as well. So population numbers rose to 102 companies that had these characteristics.

5. RESEARCH FINDINGS

Testing Research Hypotheses

Testing First Minor Hypothesis:

There is a significant relationship between board independence and Accounting Conservatism of company.



Fixed effects regression model the impact of board independence on conservatism (0.098) and with a significant level (0.108) was not significant.

This indicates that the independence of the board of directors does not have a significant effect on conservatism. The impact of changing livestock industry working positive (0.039) and the significance level (0.009) is significant. The types of variable composition and independence of the board, (0.091) and with a significant level (0.085) were not significant. This finding is contrary to the findings of Lara and colleagues (2006), Jing Li (2009). The test control variables firm size (SIZE), leverage (Lev) has a significant impact on conservatism and statistically significant at the 95% confidence level. But the asset growth rate (AINT) does not have an impact on accounting conservatism.

Table 1: Fixed effects regression model the impact of board independence on accounting conservatism

VIF statistics	probability statistic t	t-statistic	Regression coefficients	Symbol
-	0.065	2.01	0.087	Constant
1.5847	0.009	3.19	0.039	DUM
1.2838	0.108	1.24	0.098	IBD
1.6483	0.012	2.96	0.043	SIZE
1.2429	0.093	1.14	0.145	AINT
1.3381	0.027	2.71	0.062	Lev
Durbin-Watson statistic	Statistic F	Probability statistic F	Adjusted determination coefficient	Coefficient of determination
1.98	25.67	0.0018	0.17	0.19

Second Minor Hypothesis:

There is a significant relationship between concentration of ownership and Accounting Conservatism of company.



Random effects regression model the impact of concentration of ownership on accounting conservatism (0.121) and according to a significant level (0.113), it is not significant.

This indicates that the concentration of ownership does not have a significant effect on accounting conservatism. The impact of changing livestock industry working positive (0.045) and the significance level (0.015) is significant. But the variables of industry composition and concentration of ownership, (0.101), according to significant level (0.093) is not significant. Combine this with regard to concentration of ownership, types of returns (DUM * RET * CO), (0.087) and with a significant level (0.065) was not significant. This suggests that the combined effect of these three variables on accounting conservatism is not meaningful. This means the hypothesis is at 95%.

Also, the testing the control variables (firm size (SIZE), Financial leverage (Lev) has a significant impact on conservatism and it is statistically significant at the 95% confidence level. But the asset growth rate (AINT) does not have an impact on accounting conservatism.

Table 2: Random effects regression model the impact of concentration of ownership on accounting conservatism

VIF statistics	probability statistic t	t-statistic	Regression coefficients	Symbol
-	0.065	2.01	0.087	Constant
1.5847	0.009	3.19	0.039	DUM
1.2838	0.108	1.24	0.098	IBD
1.6483	0.012	2.96	0.043	SIZE
1.2429	0.093	1.14	0.145	AINT
1.3381	0.027	2.71	0.062	Lev
Durbin-Watson statistic	Statistic F	Probability statistic F	Adjusted determination coefficient	Coefficient of determination
2.07	43.16	0.0047	0.14	0.17

The Third Minor Hypothesis:



There is a significant relationship between board size and Accounting Conservatism of company.

Random effects regression model the impact of board size on accounting conservatism (0.116) and according to a significant level (0.109), it is not significant. This indicates that the board size does not have a significant effect on accounting conservatism. Also, the testing the control variables (firm size (SIZE), Financial leverage (Lev) have a significant impact on conservatism and it is statistically significant at the 95% confidence level. But the asset growth rate (AINT) does not have an impact on accounting conservatism.

Table 3: Random effects regression model the impact of board size on accounting conservatism

VIF statistics	probability statistic t	t-statistic	Regression coefficients	Symbol
-	0.065	2.01	0.087	Constant
1.5847	0.009	3.19	0.039	DUM
1.2838	0.108	1.24	0.098	IBD
1.6483	0.012	2.96	0.043	SIZE
1.2429	0.093	1.14	0.145	AINT
1.3381	0.027	2.71	0.062	Lev
Durbin-Watson statistic	Statistic F	Probability statistic F	Adjusted determination coefficient	Coefficient of determination
2.01	35.38	0.0025	0.15	0.18

The Fourth Minor Hypothesis:

There is a significant relationship between dual duties of Director and Accounting Conservatism of company.

Pooled regression fixed effects model the impact of the duties of CEO duality of accounting conservatism (0.145) and due to the significant level (0.137) was not



significant. This shows that the duties of CEO duality no significant effect on accounting conservatism. The impact of changing livestock industry on a positive and significant accounting conservatism (0.045) and considering the significance level (0.015) is significant. This means the hypothesis is at 95%.

Also, the testing the control variables (firm size (SIZE), Financial leverage (Lev) have a significant impact on conservatism and it is statistically significant at the 95% confidence level. But the asset growth rate (AINT) does not have an impact on accounting conservatism.

Table 4: Pooled regression fixed effects model the impact of dual duties of Director on accounting conservatism

VIF statistics	probability statistic t	t-statistic	Regression coefficients	Symbol
-	0.065	2.01	0.087	Constant
1.5847	0.009	3.19	0.039	DUM
1.2838	0.108	1.24	0.098	IBD
1.6483	0.012	2.96	0.043	SIZE
1.2429	0.093	1.14	0.145	AINT
1.3381	0.027	2.71	0.062	Lev
Durbin-Watson statistic	Statistic F	Probability statistic F	Adjusted determination coefficient	Coefficient of determination
2.13	51.14	0.0069	0.09	0.12

The Main Hypothesis:

There is a significant relationship between the internal mechanisms of corporate governance and accounting conservatism in Corporations of Accepted in Tehran Stock Exchange.

Due to the lack of effective corporate governance components (board independence, concentration of ownership, board size and the dual duties of Director) on accounting



conservatism main hypothesis will be rejected. The effect of combining components of corporate governance (board independence, concentration of ownership, size of the Board and CEO duality tasks) with varying types of accounting conservatism on the relationship between corporate governance with respect to the variable types, there is no conservative. Finally, in order to accurately test the relationship between accounting conservatism and corporate governance (board independence, concentration of ownership, board size and the dual duties of Director), benchmark returns Basu's model was added to the model to test hypotheses and this conclusion that the corporate governance, types of returns and accounting conservatism there is no significant relationship.

6. CONCLUSION

The study, conservative accounting on two floors divided the conservatism of the events (unconditional) and the conservatism of the events (provided). Conservatism is post-events related to the balance sheet or independent news and reflects the book value of net assets is underestimated that is not related to changes in future cash flows. Conservatism after the events, related to income and costs related to the news and early detection means more bad news than good news in earnings. The use of estimates in the financial statements, profit affected and may lead to different profit is the result of actual performance. That's why earnings are taken with real profit; the objective will not be enough. Therefore, such a benefit, profit, and investors perceived quality difference between the estimated profit and therefore the actual performance, increase the risk of their investment in the company as a result of increased risk, demand higher yields to invest their resources. Hence the conditional conservatism, based on the estimate (guess occurrence of bad news), added benefit is the quality. Test the hypothesis in this study was supported by the same subjects. On the other hand, unconditional conservatism has been reduced due to the predictive power of data and information risk is high. As a result, the expected rate of return on investment by ultimately affects the price of securities and the effect of economic measures is conservative on pricing securities.



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