

# EARNINGS MANIPULATIONS IN POLITICALLY INFLUENCED FIRMS

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## Abstract

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This paper investigates the relationship between political influences and earnings manipulations because little has been known about the relationship between both variables using multiple proxies. The authors measure earnings manipulation using models developed by Bhattacharya et al. (2003) and McNichols (2002), for a large sample of 129 listed firms in Pakistan Stock Exchange over the period 2009–2013. This study finds that politically influenced firms are involved in accruals earnings management and lack transparency, implying lower earnings quality. Our findings are consistent with prior studies, which show the positive relationship between political influences and earnings manipulations. However, the authors add contribution by using three proxies of political influences. The findings are useful for regulators to monitor earnings manipulations activities among public listed companies. In addition, the findings add to the growing literature in the field of corporate governance.

**Keywords:** Political Influences, Earnings Manipulations, Accruals Quality, Earnings Aggressiveness, Corporate Governance

## 1. INTRODUCTION

Bleibtreu & Königsgruber (2015), who studied political connections, corporate governance and financial reporting, opined that corporate political connections are a global phenomenon and that it creates complex economic consequences. Some scholars also pointed the trend of political connections and financial reporting occurred both in emerging markets and developed economies. Cheema, Munir & Su (2016) and Chen, Ding & Kim (2010) for example, inferred that political connections affect corporate performance, thus developed economic consequence.

There is also empirical evidence that confers similar observation, i.e. political connections influenced corporate performance. Studies assert that politically influenced firms were more involved in accruals earnings management (Al-dhamari & Ismail, 2015; Chaney, Faccio & Parsley, 2011; and Balkaoui, 2004) hence, affect firm performance. Faccio (2006), for example, concluded that there is a positive relationship between the two, political connection and firm value. Like Faccio, other researchers also found similar outcome (Wu, Wu, Zhou & Wu, 2012; and Li, Meng, Wang & Zhou, 2008), where they found politically influenced firms involved in managing earnings and producing less transparent earnings to hide their political rents which they get from their connections (Braam et al., 2015; and Chaney et al., 2011). Some even associated

political connections to business practices (Faccio, Masulis and McConnell, 2006).

Pakistan is not excluded from the above-mentioned phenomenon. Some even view that the corruption in Pakistan escalates that political connections influenced on earnings management (Saeed, Belghitar & Clark, 2015). This paper argues based on the theory of political connection, which precept that there is interdependence between corporate political connectedness and financial reporting. The theory builds on the assertion that corporate political connections affect the government's roles, which are: the power to affect corporate well-being and mediates conflict between corporate actors (Bleibtreu & Königsgruber, 2015). The theory provides predictions that inform the effect between political connections and reporting quality. The theory suggests that political connection leads to reporting manipulation.

Grounded by the said theory, this paper argued that it is highly likely that there is a relationship between political influences and earnings management. This paper examines the relationship between the politically influenced firms and earnings quality (measured as earnings opacity and accruals earnings management). Specifically, this paper investigates whether accruals earnings management and earnings opacity differ between politically influenced firms and non-politically influenced firms. The paper contributes to the growing literature on earnings quality.

The remainder of this paper is structured as follows. First, synthesise previous studies, followed by the construct of accruals earnings management (accruals quality). Next methodology was deliberated. Subsequently, the paper discussed the finding which was later followed by the concluding remark and contribution of the study.

## 2. LITERATURE REVIEW

### 2.1. Pakistan Political Environment

The Index of Economic Freedom had rank Pakistan amongst the corrupt countries in the world (Saeed et al., 2015). In the last 25 years, three national assemblies and their elected prime ministers have been dismissed on the charges of political patronage and corruption (Saeed et al., 2015). In fact, the current Prime Minister (Mr Nawaz Sharif), the current opposition leader (Mr Syed Khurshid Shah), the current Finance Minister (Mr Ishaq Dar) and numerous other prominent politicians and their close relatives are facing multiple corruption cases in National Accountability Bureau (NAB) and Supreme Court of Pakistan.

Since the establishment of Pakistan, Pakistan has been ruling by industrialist; Ahmad Dawood (founding owner of Dawood group), Yusuf Haroon, a leading industrialist, was the first Chief Minister of Sindh province, and Rafiq Saigol (founding owner of Saigol group) held main posts in the governments and ruling parties (Saeed et al., 2015). In general elections of 2002, 2008, and 2013, the major political parties that participated were led by politicians representing some of the country's main business family. The majority of the prominent politicians belong to large business conglomerates coming from families that owned big businesses, such as Ittefaq Group (of current Prime Minister of Pakistan and current Chief Minister of Punjab), Air Blue (of Khaqaan Abbasi, current Federal Minister for Petroleum), Saifullah Group (of Anwar Saifullah, Former Federal Minister, and Usman Saifullah, current Senator), Service Industries (of Ahmad Mukhtar, Former Defense Minister), JWD Group (of Jahangir Khan Tareen, Former Federal Minister, and Ahmed Mahmood, Former Governor of Punjab). In a country, where politicians have their own business interests; it is difficult to sustain a distinction between 'interests of the state' and 'business interests'. Therefore, the common perception is that politicians systematically misuse resources through the abuse of state power.

For the above-mentioned reasons, Noorani (2015) opined that the powerful bureaucrats and politicians obtain personal benefits because the conflict of interest law is weak in Pakistan. Moreover, the inefficient monitoring by the security exchange commission of Pakistan (SECP) and weak governance and legal system, resulting in the poor implementation of good corporate governance practices in Pakistan (Cheema et al., 2016). Therefore, it is expected that politically influenced firms are more likely to employ accrual-based earnings management strategy and earnings aggressiveness compare to non-politically influenced firms in order to hide their political rants. This paper hypothesized that politically influenced firms disclosed lower quality accounting information.

### 2.2. Empirical Evidence

Synthesizing the literature, the current study found that there is growing interest in examining political influences and firm performance. Interestingly, the literature delineates various criteria used to define political influences. Some used proxy such as board member or large shareholder is member of parliament or of government (Chaney et al., 2011); firms headquartered in a politician's hometown (Faccio & Parsley, 2009); monetary contributions to politicians and lobbying expenditures (Correia, 2014); a firm as politically connected if it has a CEO who formerly served in government or the military. Other examples could be enumerated (Wu et al., 2012). The list goes on where some used proxy such as senior managers or board of directors are members of provincial or national assembly, are closely related to politicians, former Bureaucrat or army officer, and significantly owned by government (Cheema et al., 2016; Bushman & Piotroski, 2006; Faccio, 2006; Khwaja & Mian, 2005; Belkaoui, 2004).

What matter is that studies showed that politically influenced firms get preferential treatment and gained from their political connections (Pastor & Veronesi, 2013; Faccio, 2010). Nonetheless, there were drawbacks when one is politically connected as well. There is also a risk that the politically influenced firms have to consider, which are the opposition parties and media. Both are a threat to the politically influenced firms, because if the firms are known to be politically involved in manipulating earnings then probably the firms could lose all the benefits (Braam et al., 2015; and Faccio, 2006). Since firms' reputation and integrity are likely at stake, which may increase political costs for connected politicians (Kothari, Mizik & Roychowdhury, 2012; and Faccio, 2006).

### 2.3. Politically Influenced Firms

According to (Saeed et al., 2015), politically influenced firms' means firms' connections with government officials or politicians and have influenced on firms decision making. Influenced in this respect means cronyism (political appointments in firms) or shareholding or political board of directors (Cheema et al., 2016; Saeed et al., 2015; and Chaney et al., 2011).

Another perspective of political influenced is through connections with individuals who have position(s) in the government (Faccio, 2006; Johnson & Mitton, 2003; Fisman, 2001), through state ownership of firms (Capalbo, Frino, Mollica & Palumbo, 2014), the presence of politician(s) or their close relatives on the board of director (BOD) or in senior management (Cheema et al., 2016; and Saeed et al., 2015), the presence of former Bureaucrat or army officer on the BOD or in senior management (Cheema et al., 2016; and Narayanaswamy, 2013). Due to its influence by the government official or politicians, there is empirical evidence that politically influenced firms impacted the firms' earnings quality.

Prior studies identify political influences as rent-seeking activities where firms use resources in bribing or lobbying to get preferential treatment and privileges from government officials. Khan and Jomo (2000) explained the rent-seeking activities; activities that involve bribing, lobbying or through political connections.

Based on the above, the current study adopted three proxies that represent political influences. They are: 1) a presence of politician's on the board of directors; one of the shareholders (control at least 10 percent of votes) or senior managers (such as President, Vice-President, Chairman, CEO or Secretary) are a member of provincial assembly or parliament, a head of state or a minister (Faccio, 2006) or a senior managers or large shareholders are closely related (friends and family) to top officials, which is known as indirect political connection (Asquer & Calderoni, 2011; Goldman, 2009); 2) percentage of government ownership in a firm (Capalbo, Frino, Mollica & Palumbo, 2014); and 3) if one of the senior management is either former or present civil/military bureaucrat (Cheema et al., 2016; and Narayanaswamy, 2013).

Based on the abovementioned, the current study adopted the following criteria:

- 1) A politician's full name match to a firm senior management or large shareholder if their names match exactly.
- 2) Review of a list of parliament or assembly members at provincial and federal level.
- 3) Review of a list of committee members of each political party on their website.
- 4) Follow the book of Rehman (2006) who identified the list of politically influenced firms in Pakistan.
- 5) Review the list of listed firms where government holding significant shareholding.
- 6) Review the website of firms who have former bureaucrats/former army officer as senior management.

$$TCA_{j,t} = \partial_0 + \partial_1 CFO_{j,t-1} + \partial_2 CFO_{j,t} + \partial_3 CFO_{j,t+1} + \partial_4 AREV_{j,t} + \partial_5 PPE_{j,t} + \varepsilon_{j,t}$$

Where:

- $TCA_{j,t}$  is a total current accrual of firm j in year t;
- $CFO$  is cash flows from operations of firm j in year t;
- $AREV$  is revenue of firm j in year t; and
- $PPE$  is gross property, plant, and equipment of firm j in year t. All the variables are scaled by lagged total assets. The variance of  $\varepsilon$  is an inverse measure of earnings quality.

Subsequently, the current study adopted Bhattacharya et al. (2003) to examine earnings opacity of firms. Specifically, the current study used earnings aggressiveness model to detect earnings opacity. Earnings aggressiveness is the propensity to speed the realization of gains and delay the

$$ACC_{kt} = (\Delta CA_{kt} - \Delta CL_{kt} - \Delta CASH_{kt} + \Delta STD_{kt} - DEP_{kt} + \Delta TP_{kt}) / TA_{kt-1}$$

Where:

- $ACC_{kt}$  are the total accruals of firm k in year t;
- $\Delta CA_{kt}$  is Change in current assets of firm k in year t;
- $\Delta CL_{kt}$  is the change in current liabilities of firm k in year t;
- $\Delta CASH_{kt}$  is the change in cash of firm k in year t;

### 3. MEASUREMENTS OF EARNINGS MANIPULATIONS

Studies showed that accruals quality is a measure of earnings quality (Dechow & Dichev, 2002; McNichols, 2002) Earnings consist of accruals and cash flows, however, accruals are discretionary and based on estimates thus cash flows are considered more consistent than accruals (Dechow, 1994). Earnings are mostly manipulated through accruals (Dechow, 2011) and numerous measures view that high accruals reduce earnings quality (Francis et al., 2006; Bhattacharya et al., 2003). As accruals give the discretion to use judgments, it provides an opportunity for earnings management (Dechow & Schrand, 2004).

To investigate the involvement of firm in accruals earnings management, the current study employed accruals quality as a measure of earnings quality, which was introduced by Dechow & Dichev (2002). Hence, the current study measures accruals quality by matching operating cash flows and working capital accruals; where a poor match indicates poor accruals quality. The current study regress change in working capital for last year, present, and next year's cash flow. Dechow-Dichev (DD) Model was further modified and enhanced by McNichols (2002) after including additional explanatory variables i.e. revenue, and Property, Plant & Equipment (PP&E). Kent, Routledge & Stewart (2010) found that the DD model and modified DD model perform equally well whereas; Francis et al. (2005) found that the modified concept or model has better explanatory power:

realization of losses, which would eventually result in more positive or high accruals (Bhattacharya, 2003). The model delineates the magnitude of accruals as a measure of earnings quality. Bhattacharya (2003) stated that the opportunistic overstatement of earnings increases the level of total accruals. Earnings aggressiveness reduces earnings quality because it increases total accruals, and high accruals represent less persistent earnings (Dechow et al., 2010). The current study hypothesized that the firms have high total accruals when they get involved in earnings manipulations. Leuz, Nanda, & Wysocki (2003) used the magnitude of accruals as a measure for earnings management. Whereas, Bhattacharya (2003) measured earnings aggressiveness as the magnitude of accruals:

- $\Delta STD_{kt}$  is the change in long-term debt included in total current liabilities for firm k in year t;
- $DEP_{kt}$  is the amortization and depreciation expenses of firm k in year t;
- $\Delta TP_{kt}$  is the change in tax payables of firm k in year t; and
- $TA_{kt-1}$  is the total assets of firm k in year t-1.

### 3.1. Control Variables

The current study controls several variables and used the industry as a dummy to control for sector-specific effects. Congruent with prior studies (Al-dhamari & Ismail, 2015; Zang, 2012; Chaney et al., 2011; Mashayekhi & Bazaz, 2010; Cohen et al., 2008; Cheng & Warfield, 2005) the current study includes firm size (SIZE), profitability (ROA), financial leverage (LEV), growth opportunities (GROWTH), financial loss (LOSS) and audit quality (BIG4).

### 3.2. Sample

The current study selected 129 non-financial listed firms in Pakistan Stock Exchange (PSE), which includes 64 politically influenced and 65 non-politically influenced firms. To cover a complete tenure of elected government in Pakistan, we choose a panel data on Pakistani firms ranging 2009-2013. Additionally, the sample requires 2008 and 2014

data, because one year lagged and lead data is required to represent earnings management attributes. To be included in the sample, each firm must have a data ranging 2008-2014 and firms with missing data of these years to be removed from the sample. After applying these restrictions on approximately non-financial firms, the final sample includes a panel of 129 firms, which includes 64 politically influenced firms and 65 non-politically influenced firms. Thus, current study uses panel data that contains information for a 7-years period.

## 4. RESULTS

Table 1 reports the descriptive statistics for all the variables. Notably, the mean values of accruals earnings management and earnings aggressiveness are consistent with previous studies (Chaney et al., 2011; Balkaoui et al., 2004; Bhattacharya et al., 2003).

**Table 1.** Descriptive statistics of the variables used in the study

Variable	Observations	Mean	Std. Dev.	Min	Max
EA	645	-0.007781	0.2199195	-1.99332	1.984933
AEM	642	0.008401	0.2564954	-1.926478	1.76998
PI	645	0.488372	0.5002527	0	1
PC	645	0.286822	0.4526286	0	1
GOVT	645	0.116279	0.3208081	0	1
BUR	645	0.189147	0.3919295	0	1
ROA	645	7.807891	13.9422	-49.38	61.43
LEV	645	0.628372	0.314634	0.0314643	3.011882
SIZE	645	6.840366	0.6702909	4.729821	8.616926
GROWTH	645	0.166002	0.5022467	-1.459162	7.980104
LOSS	645	0.221705	0.4157163	0	1
BIG4	645	0.443411	0.4971729	0	1

Note: EA is an earnings aggressiveness which is measured by Bhattacharya et al. (2003) model; AEM represents accruals earnings management (accruals quality) which is measured by Modified Dechow & Dichev Model (McNichols, 2002); PI is a dummy variable which is an aggregate measure of political influences, 1 if a firm is politically influenced and 0 otherwise; PC is a dummy variable which represents a proxy of politically influenced firms, 1 in presence of politician(s) on board of directors or senior management and 0 otherwise; GOVT represents a significantly government owned firm, 1 if a firm is significantly owned by government and 0 otherwise; BUR is a dummy variable, which is 1 in presence of current/former civil/military bureaucrat(s) on board of directors or senior management; ROA represents percentage of net income over total assets; LEV is a leverage, which represents the ratio of debt and assets; SIZE is a log of total assets; GROWTH is calculated as the change between current year sales and previous year sales divided by previous sales; LOSS is a dummy variable, 1 if a firm is reporting loss and 0 otherwise; and BIG4 represents top big audit firms, which is a dummy variable and 1 if a firm is audited by top big four audit firms and 0 otherwise.

Table 2 presents the results from Panel Corrected Standard Errors (PCSE), in which the dependent variable is the standard deviation of the variable computed in equation (1) computed over a 5 year period (2009-2013). In the regressions, the dependent variable is converted into an absolute value and then multiplied by negative 1. The explanatory variable is political influences (i.e. political connected BOD, civil or military bureaucrat

as BOD, significant government ownership), the control variables are a loss, firm size, BIG4 auditor, return on assets, leverage, growth, and industry. In the initial cross-sectional tests, we classify a company as connected if political influences are recorded at any time between 2009 and 2013.

To test our hypotheses, we use the following regression:

$$AQ_{j,t} = \delta_0 + \delta_1 PI_{j,t} + \delta_2 SIZE_{j,t} + \delta_3 ROA_{j,t} + \delta_4 LEV_{j,t} + \delta_5 GROWTH_{j,t} + \delta_6 BIG4_{j,t} + LOSS_{j,t} + Industry_{j,t} + \omega_{j,t} \quad (1)$$

Where: accruals quality (AQ) is a proxy for accruals earnings management. All other variables are explained in Table 1. Equation 1 is used to test whether politically influenced (using an aggregate proxy) firms are involved in accruals earnings management. To test the sensitivity of our result, we use all three proxies of political influences as explained earlier.

In Regression (1), we find that political is significantly and positively related to accruals earnings management, implies lower accruals quality (p-value=0.000). The magnitude of the coefficient is

comparatively moderate and signifies that the presence of political influences is related to 3.20% increase in the dependent variable. Moreover, all firm-specific control variables are significant in regression (1). Consistent with prior studies, we find that the residuals of total current accruals are negatively and significantly related to return on assets, BIG4 auditors, leverage, and growth at 1 tale. In addition, size is positively and significantly related to the residuals of total current accruals at 1 tale. However, the loss is positively related, but not significant.

**Table 2.** Linear regression results of accruals earnings management in model 1 and earnings aggressiveness in model 2 as dependent variables, and single proxy of political influences as explanatory variable in both models

Variable	Model 1		Model 2	
	AEM		EA	
	Coefficient	P>z	Coefficient	P>z
PI	0.0319666	0	0.0275975	0.012
ROA	-0.000701	0.191	-0.000438	0.422
LEV	-0.125236	0	-0.081695	0.002
SIZE	0.0285535	0.185	0.0193508	0.338
Growth	-0.044757	0.017	-0.036769	0.042
Loss	0.0198454	0.27	0.007725	0.569
BIG4	-0.031467	0.047	0.0064169	0.791
Industryum1	0.0050567	0.819	0.0458361	0.056
Industryum2	0.0091633	0.8	0.0298325	0.154
Industryum3	0	(omitted)	0	(omitted)
Industryum4	0.0289522	0.175	0.0332967	0.032
Industryum5	-0.169961	0.004	-0.068304	0.026
Industryum6	0.0392374	0.115	0.0508806	0.014
_cons	-0.266259	0.064	-0.233148	0.061
R-Squared	0.1577		0.0723	

In addition, Table 2 presents the results from Panel Corrected Standard Errors (PCSE), in which the dependent variable is the total accruals computed in equation (2) computed over a 5 year period (2009-2013). In the regressions, the dependent variable is

$$EA_{j,t} = \delta_0 + \delta_1 PI_{j,t} + \delta_2 SIZE_{j,t} + \delta_3 ROA_{j,t} + \delta_4 LEV_{j,t} + \delta_5 GROWTH_{j,t} + \delta_6 BIG4_{j,t} + LOSS_{j,t} + Industry_{j,t} + \omega_{j,t} \quad (2)$$

Where: all variables are explained in the previous section and in Table 1. Following (Bhattacharya et al., 2003), Equation 2 is used to test whether politically influenced (using an aggregate proxy) firms are related to earnings aggressiveness. To test the sensitivity of our result, we use all three proxies of political influences as explained earlier.

In Regression (2), we find that political is significantly and positively related to earnings aggressiveness, implies lack transparency (p-value=0.012). The magnitude of the coefficient is comparatively moderate and signifies that the presence of political influences is related to 2.75% increase in the dependent variable. Moreover, consistent with prior studies, we find that the total accruals are negatively and significantly related to leverage and growth. However, return on assets are also negatively related to total accruals, but not significant. In addition, BIG4 auditors, loss, and size

converted into an absolute value and then multiplied by negative 1. All the explanatory variables and control variables are same as above in equation 1.

To test our hypotheses, we use the following regression:

are positively related to total accruals, but not significant.

#### 4.1. Robustness

To check the robustness of our result in Table 3, this study regress residuals of total current accruals with three proxies of political influences instead of combined measure of political influences (i.e. political connections through political board of directors (PC), significant government shareholding (GOVT), and civil or military bureaucracy in board of directors (BUR)). The result of alternative measure is consistent with the main result. We find that all three proxies of political influences are significantly and positively related to accruals earnings management.

**Table 3.** Linear regression results of accruals earnings management in model 1 and earnings aggressiveness in model 2 as dependent variables, and multiple proxies of political influences as explanatory variable in both models

Variable	Model 1		Model 2	
	AEM		EA	
	Coefficient	P>z	Coefficient	P>z
PC	0.0231274	0.002	0.0264197	0.024
GOVT	0.0465472	0.023	0.0183573	0.223
BUR	0.0211133	0.072	0.0132109	0.025
ROA	-0.000751	0.171	-0.0004015	0.474
LEV	-0.121958	0.000	-0.08106	0.002
SIZE	0.0235668	0.311	0.0192285	0.34
Growth	-0.045384	0.015	-0.0369815	0.042
Loss	0.0215595	0.232	0.0096518	0.495
BIG4	-0.030857	0.065	0.0062683	0.8
Industryum1	0.0210141	0.377	0.0502519	0.052
Industryum2	0.0192097	0.592	0.0320226	0.126
Industryum3	0	(omitted)	0	(omitted)
Industryum4	0.0412332	0.053	0.0379144	0.018
Industryum5	-0.162956	0.005	-0.0681316	0.025
Industryum6	0.0507675	0.042	0.0515881	0.014
cons	-0.244121	0.108	-0.2340158	0.057
R-Squared	0.1605		0.0722	

In addition, to check the robustness of our result for regression 2 in Table 3, we regress total accruals with three proxies of political influences as explained earlier. The result of alternative measure is largely consistent with the main result. The result shows that the proxy of political influences (i.e. political connections and bureaucracy) is positively and significantly related to earnings aggressiveness. Moreover, significant government ownership is positively related to earnings aggressiveness, but not significant.

## 5. DISCUSSION

The findings indicate that politically influenced firms have lower earnings quality (accruals quality and earnings aggressiveness) comparing to non-politically influenced firms. In addition, the results show that politically influenced firms are significantly and positively related to accruals earnings management and earnings opacity. Therefore, politically influenced firms established in Pakistan with relatively weak regulatory bodies and institutes involve more in accruals earnings management activities and lack transparency. Results from additional analysis also showed that politically influenced firms are related to lower earnings quality. This probably linked to the factors that benefit the politically influenced firms to hide their political rants. In general, the findings are consistent with previous studies (Al-Dhamari & Ismail, 2015; Chaney et al., 2011; Bushman & Piotroski, 2006), implying that there is consistency of results to support the generalization that politically connected firm influenced accruals earning management of firms.

The current study also examined whether politically influenced firms are involved in accruals earnings management and earnings aggressiveness. The current study found that politically influenced are more involved in accruals earnings management, implying lower earnings quality. In addition, compare to non-politically influenced firms, politically influenced (political connected BOD and bureaucracy in BOD) firms are significantly and positively related to earnings aggressiveness. However, government owned firms are positively related to earnings aggressiveness, but not significant.

Additional results show that amongst the politically influenced firms, political connections from ruling party are less involved in real earnings management compare to political connections from the opposition party. However, the results are not significant amongst politically influenced firms when using accruals earnings management measure. Related to earnings management, these findings have numerous important implications for accounting practices. First, the results could be helpful for investors and other stakeholders in assessing the financial reporting quality of the politically influenced firms, which shows that politically influenced firms involved in accruals earnings management and lack transparency. Second, our results show ways to regulatory bodies to improve the quality of financial reporting and existing governance systems. Post implementations of Sarbanes-Oxley Act of 2002, researchers were expecting a reduction in earnings management. However, our results show that politically influenced firms are still involved in accruals earnings

management and lack transparency since they protect their political rants and have more incentives to manipulate earnings.

## 6. CONCLUSION

This paper contributes to the growing literature in the field of corporate governance related to earnings management in many ways. First, the findings add to the existing literature of political influences and earnings management, by providing more detailed investigation between political influences and earnings management. This study gives more insight while using three proxies of political influences and two measures of earnings management. The present study also contributed by testing the difference in effect between ruling party political connections and opposition party political connections on earnings management. Therefore, an important contribution of this study to the existing literature of political influences and earnings management is that it offers more detailed empirical insights using data from a less-studied and less-regulated environment i.e. South Asia (specifically Pakistan).

Secondly, the study contributes theoretically to political influences and earnings management by examining how politically connected people influence firms' management to report manipulated earnings. The findings of the current study also suggest that it does not matter if firms are ruling or opposition; connected firms on any mentioned criteria are reporting manipulated earnings. Thus, the findings of the current study give insights that the political influences through any mean provides incentives to the managers and weaken the earnings quality. This study also enables shareholders to identify which factors should be taken into consideration when evaluating a firms' earnings quality.

Current study possesses potential limitations, which readers must aware when interpreting the findings. Although, this study provides detailed investigation, but did not consider all earnings management (manipulation) models. For example, real earnings management, earnings smoothing, discretionary accruals etc. Future study can do a more longitudinal study by extending the number of years to ten years, and make a comparative study of two elected governments by including two tenure of the elected government instead one tenure of the elected government.

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