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The Influence of Shareholding Mechanisms on Earning Management Practices: The Case of Listed Moroccan Companies

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ABSTRACT

Introduction: Shareholding mechanisms, in particular the concentration of capital and the type of shareholder, have a considerable influence on the production of accounting information. More specifically, we seek to verify whether the shareholder category and the degree of capital concentration have an impact on accounting earnings management practices.

Objectives: Our objective is to implement an analytical framework that would best explain the best choice of governance mode and enable the process of producing financial information to be steered.

Methods: Being interested in the mutual interaction between shareholder structure and the quality of financial statements, the main objective of this paper is to examine the influence of shareholder structure on the quality of financial statements in the Moroccan context, a context that is differentiated by its specific legal framework and typical governance traditions. It is in the context of these issues that this research is situated. Specifically, it attempts to find answers that correspond to the following summary questions

- Firstly: What is the relationship between the typology of the company's shareholders and the improvement in the quality of the financial statements?

- Secondly: is there a relationship between the degree of shareholder concentration and improvements in the quality of financial statements?

Results: The results obtained from a sample of all Moroccan companies listed between 2014 and 2018 indicate that these mechanisms act differently and sometimes antagonistically depending on several variables. The assessment of the quality of results was studied using discretionary models based on accruals. The main results seem to indicate that the concentration of capital in the hands of a controlling coalition contributes to improving the quality of the information produced by the company. The contribution of institutional and family shareholders to the earnings management system is open to question. The presence of these partners in the capital of Moroccan companies increases accounting data management practices. Furthermore, the results indicate that the control exercised by industrial and managerial shareholders is more effective. Finally, the presence of employees in the capital contributes to the effectiveness of the control exercised in the production of accounting information. Nevertheless, the risks of loss of confidentiality associated with such a presence limit the contribution of this mechanism to the system of governance as a whole.

Conclusions: The results of the assessments carried out can be summarised as follows:

- The concentration of capital in the hands of controlling shareholders improves the quality of information produced by the company. However, the reference shareholder may opt for earnings management practices in order to gain private profits.

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- The contribution of institutional and family shareholders to the system of governance is open to question, and also increases the management of accounting results.

- Employee and management shareholders appear to be more vigilant and more effective. The latter make it possible to curb the management of the accounting result. Finally, no relationship between state ownership and the quality of the information produced by the company has been verified.

Keywords: Earnings Management, Shareholder Structure, Discretionary Accruals, Corporate Governance.

INTRODUCTION

The financial scandals that have hit the headlines in many countries may have reinforced accounting's reputation for arbitrariness. "Worse still, they have shown that companies' accounting results can be misleading, and they have cast doubt on the sincerity of accounting statements and the ethics of those who produce them and those responsible for verifying them" (Colasse, 2010). Colasse adds that these cases prove that we must admit that "accounting is an ambivalent instrument that can successively and simultaneously inform and misinform, show and hide". However, the issue of the quality of financial statements has not been completely resolved following the considerable developments and efforts made by countries in the areas of corporate governance and financial transparency. "It should be remembered that most of the world's high-profile scandals - Enron, Vivendi Universal, the US Treasury, the European Commission and the European Commission - have had a major impact on the quality of financial statements: Enron, Vivendi Universal, Crédit Lyonnais, WorldCom stem from companies that had adopted the rules of corporate governance. Moreover, before Jean-Marie Messier's departure, thirteen of Vivendi's nineteen directors were independent, including Marc Viénot, a director of Société Générale. In this context, while it is obviously relevant to identify the sources of failure in existing structures, we believe, as Bessire et al (2008) do, that "it is high time to explore other avenues if we are to move towards good governance". One form of control that has often been put forward by agency theorists is shareholding, the concentration and composition of which can have a strong influence on the balance of power within a company. It should be noted that the financial literature admits that the shareholding structure is an effective mechanism of corporate governance and a determinant of its value (Berle and Means, 1932; Jensen and Meckling, 1976; Fama and Jensen, 1983, Shleifer and Vishny, 1997; Faccio and Lang 2002).

OBJECTIVES

Our objective is to implement an analytical framework that would best explain the best choice of governance mode and make it possible to steer the process of producing financial information. Being interested in the mutual interaction between shareholder structure and the quality of financial statements, the main objective of this paper is to examine the influence of shareholder structure on the quality of financial statements in the Moroccan context, a context that is differentiated by its specific legal framework and typical governance traditions.

It is in the context of these issues that this research is situated. Specifically, it attempts to find answers that correspond to the following synthesis questions:

- **Firstly**: What is the relationship between the typology of the company's shareholders and the improvement in thequality of the financial statements?

- **Secondly**: is there a relationship between the degree of shareholder concentration and improvements in the quality of financial statements?

1. LITERATURE REVIEW :

METHODS

1.1. RESULTS MANAGEMENT: THE REAL VS. THE ACCOUNTING APPROACH

By remaining within the bounds of the law, company directors are able to influence the presentation and, above all, the content of the financial statements. In fact, they have the latitude to make decisions that enable them to shape accounting information in accordance with the legal framework. In particular, the profit and loss account forms a

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lever on which managers can easily act. This is what is known as results management. In this sense, Schipper (1989) demonstrates that there is such a thing as strategic results management. This is a deliberate intervention in the process of presenting financial information, the aim of which is to appropriate personal gains. Explained by numerous incentives, earnings management remains a practice that alters the quality of financial statements. Recourse to this practice not only leads to unreliable accounting figures, but can also cause considerable harm to all users of this information system. Type of results management: Research and studies distinguish between two types of results management (e.g. Cohen et al. 2008): results management based on accounting choices and results management based on actual activities. The types of Results Management therefore represent the two varieties of RBM as defined by Cohen et al. (2008): RBM and RBM.

1.1.1. MANAGING RESULTS THROUGH ACTUAL ACTIVITIES (GRA)

The financial literature has defined ARM in several ways: "Executive actions that deviate from normal business practices" (Cohen and Zarowin 2010, p. 2);" Actions [by management] that change the timing or structuring of transactions, investments and/or financing of transactions in order to influence reported accounting figures" (Gunny 2010, p. 855). These two definitions show that the ARM corresponds to a choice made by the manager with the aim of modifying the published accounting figures.

1.1.2. MANAGING RESULTS THROUGH ACCOUNTING CHOICES (GRC)

GRC "is achieved by changing the accounting policies or estimates used in preparing the financial statements" (Zang [2012, p. 676]. CRM therefore corresponds to the accounting choices made by management when preparing the financial statements. This type of RGM has no impact on cash flows. This is noted by Roychowdhury [2006, p. 336], who defines CRM as "earnings management that does not lead to changes in cash flows".

1.2. EARNINGS MANAGEMENT AND SHAREHOLDER CONCENTRATION

Agency theory has advocated a form of control which has a very strong impact, namely shareholding, the concentration and composition of which can strongly influence the power relationships between shareholders and managers. These two elements (concentration of capital and nature of shareholders) condition shareholders' incentives to invest in controlling the management of the firm. Several studies have been devoted to the relationship between capital concentration and the quality of accounting information. Warfield et al (1995), using a sample of 1,618 US firms from 1988 to 1990, concluded that the information content of accounting profits increased with the percentage of capital held by directors, managers and principal owners. Consistent with these results, Ebrahim (2007) finds a negative association between capital concentration and accounting data management in the US context. However, Zhong et al (2007) do not confirm these results by further refining the analytical framework. More

specifically, these authors consider the percentage of capital held by major shareholders other than directors and managers and distinguish between two samples of companies according to whether the change in earnings compared with the previous year is positive or not. In Great Britain, the results of the study conducted by Donnelly and Lynch (2002) show a negative relationship between the relevance of accounting profits and capital dilution. In a different institutional context, that of Chile, Iturriaga-Lopez and Saona (2005) find a negative and significant relationship between the percentage of capital held by the largest shareholder and the value of discretionary accruals. Finally, and in contrast to the previous results, two studies have failed to verify the negative impact of capital concentration on the quality of accounting information in the Asian context. Yeo et al (2002) observed, on the basis of a sample of companies listed on the Singapore stock exchange, that the information content of the accounting result increases with the ownership of control blocks.

1.3. EARNINGS MANAGEMENT AND SHAREHOLDER STRUCTURE

The presence of institutional investors, whose volume of assets under management has grown considerably, can influence the agency relationship between shareholders and management, and even between majority shareholders and minority shareholders. This is all the more true given that, as shown by the study conducted by Finet (2009) on the distribution of the capital of newly listed companies in France for the period 2005-2007, the proportion of institutional investors on average exceeds that in public hands (31% versus 28.2%). Finet (2009, p. 143) concludes that "institutional investors would therefore seem to constitute a counterweight to the power of management" or even "a buffer zone, a relay between the management team on the one hand and the market on the other".

The financial literature has shown the existence of a high level of activity in terms of accounting policy in managerial firms, theoretically The shareholding of the manager makes it possible to align the interests of managers with those of shareholders and thus to reduce principal-agent type I agency conflicts (Jensen and Meckling 1976). According to this theory, the greater the shareholding of managers, the less they deviate from the objective of maximising value. However, when the managerial shareholding becomes large, this may lead the manager to allocate private profits to

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himself or to adopt a strategy of entrenchment aimed at retaining power within the firm (Mork et al. 1988). In another thesis and from a tax perspective (Dhaliwal, Salomon and Smith, 1982) explain that the interest of managers in managing earnings upwards differs according to their shares in the firm's capital, since managing earnings upwards will automatically generate an increase in tax payable which will have a negative impact on the value of the firm, and consequently the increase in the shares held by the management team will prevent them from managing earnings upwards. The family shareholding structure remains one of the most widespread (LaPorta et al, 1999), and can dominate any type of company, large or small, operating in a variety of sectors. According to Allouche and Amann (2002, p. 111), "the importance of family businesses remains relatively unexplored. It is estimated that 63% of companies with sales of between €50 million and €2 billion are controlled by families".

The financial literature has analysed the relationship between earnings management and family shareholding from two main angles derived from agency theory: principal-agent alignment, and the management entrenchment effect: In a family firm, principal-agent alignment consists of a divergence of interests between managers and shareholders. Wang (2006) explains that this alignment is reflected in transparent, high-quality earnings reports. The management team and family shareholders have an interest in cooperating and favouring a long-term partnership for two reasons:

- Passing on the company's heritage to future generations
- Protecting the family's image and reputation.

The result of this alignment will be to minimise opportunistic accounting practices (Wang 2006). Industrial shareholding can take two extreme forms: a minority stake or a majority stake (in the case of a subsidiary of an industrial group). Industrial shareholding is highly developed in certain Asian countries, such as Japan and South Korea, through what are known as Keiretsu. This type of shareholding is spreading more and more in Europe (France and Sweden) through the development of industrial groups and the penetration of financial markets by these giant groups. Hundley and Jacobson (1998) explain that industrial shareholding can lead to a loss of flexibility and can disrupt governance mechanisms, In Japan, for example, Keretsu members have a poorer export performance than other forms of ownership. The growth of industrial shareholding stems from the strategic choices made by companies seeking to form alliances with other companies and groups with competitive advantages and industrial know-how, which will make these collaborations a real catalyst for growth and high profitability in the long term; several studies have confirmed the existence of a positive effect of this type of shareholding on performance (Estrin et al., 2009; Yu et al., 2009; Bamiatzi et al, 2014). In Morocco, this type of shareholding is beginning to spread and penetrate the Moroccan economic and industrial fabric, for two main reasons:

-Industrial development in Morocco requires the experience and expertise of foreign companies, which make the transfer of their technologies to Moroccan firms conditional on access to capital as the main shareholder. If we take the example of SONASID (Société Nationale de Sidérurgie), 64% of the company's capital is held by ArcelorMittal, a global steel group with considerable expertise and know-how, and one of the largest steel producers in the world.

-Another case in point is Cosumar, whose main shareholder is the Singaporean company Wilmar International, which currently holds 30% of the capital. Cosumar is a food company specialising in the production of palm oil and sugar.

-The development of the institutional savings of industrial groups, which are mobilising in the financial market and prefer investments in the form of equity securities that give these groups the right to intervene and impose their dictates on the strategic management of companies.

2. RESEARCH METHODOLOGY

2.1 SOURCES AND COLLECTION METHODS

Over the last twenty years, Anglo-Saxon research has been carried out on the most reputable American databases, such as CRSP, Compustat, Value Line and IBES. These are private organisations that offer access to databases containing the financial statements of companies from all over the world on a paying subscription basis. The four main databases are Global (Standard & Poor's), Infinancials, Thomson Financial (Worldscope) and Osiris or Orbis (Bureau Van Dijk). Other databases cover specific countries, for example: Compustat North America (Standard & Poor's) for the United States and Canada, and de Diane for France (Bureau Van Dijk).

2.2 DATA SELECTION

The initial sample is made up of Moroccan non-financial companies listed on the Casablanca Stock Exchange. We did not select any sampling criteria and did not impose any conditions on the sector of activity or size due to the limited number of non-financial companies listed on the Casablanca Stock Exchange. The study period was 2014 to 2018 (5 years). In order to have a cylindrical panel, we only selected companies for which we have at least 5 consecutive accounting periods. In addition, we had to exclude certain companies from this initial population. For

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example, we automatically excluded from our sample companies engaged in financial or similar activities, not only because of the special regulations governing them, but also because of the specific nature of their communications. This concerns banks, insurance companies, holding companies and leasing companies. Table 1 summarises the Moroccan companies engaged in financial or related activities that were excluded from our sample.

Table 1: *Presentation of the sample used to test our model*

Initial sample	**79**
Companies not presented during the 2014-2018 study phase	4
Financial institutions (banks, insurance companies, finance companies)	19
Lack of accounting and financial information	2
Lack of information on shareholder structure	2
Total sample	**52**

2.3 Measuring results management

Research into results management has led to the development of several models for estimating accruals. A study by Dechow et al (1995) compared the effectiveness of five different models, including those of Healy (1985), DeAngelo (1986), Jones (1991), a version modified by Dechow et al in 1995, and the sector model. The results showed that the modified Jones model provides the most reliable estimate of accruals, a conclusion confirmed by Jeter and Shivakumar in 1999. In order to improve on the Dechow et al (1995) model, Kothari et al (2005) developed a new measure of accruals that takes into account the company's past performance. This approach is justified by studies such as that of Beneish (2001), which highlight the importance of performance as a crucial variable not addressed in previous models. The model of Kothari et al (2005) is a significant extension of the initial work of Dechow et al (1995). It establishes a link between the discretionary accruals defined by the original model and the return on assets as an indicator of performance. The results of Kothari et al. show that their performance-based approach has a higher explanatory power than the original model, allowing a more accurate estimation of discretionary accruals. In our study, we apply the model proposed by Kothari et al (2005), which will be described in detail below.

$$\mathbf{ACCTit / Ai\ t\text{-}1 = \alpha1\ (1/Ait\text{-}1) + \alpha2\ ((\Delta CAit - \Delta RECit) / Ait\text{-}1) + \alpha3\ (IMMOit / At\text{-}1) + \alpha4\ ROAit\text{-}1 + \varepsilon it}$$

With :

ACCT: Total Accruals=Net Profit - Operating Cash Flow ;

ΔCA: the change in turnover between two successive financial years (t and t-1);

ΔREC: the change in trade receivables between financial years t and t-1;

FIXED ASSETS: the total amount of the company's gross tangible fixed assets at the end of the financial year t ;

ROA: return on assets ;

Ait-1: total assets of company i at the end of financial year t-1 ;

ε: the error term in this model represents the proportion of discretionary accruals.

2.4 CONTROL VARIABLES

2.4.1 THE SIZE OF THE COMPANY (SIZE)

According to the political-contractual theory, the managers of large firms exploit their own latitude in choosing accounting procedures in order to reduce political costs. The link between firm size and the absolute value of accruals is therefore assumed to be positive. However, the relationship between firm size and discretionary accruals remains ambiguous. As Park et al (2004, p. 443) and Koh (2003) point out, large firms are subject to greater scrutiny from their environment, which is likely to limit managerial discretion. The results of the recent study by Sanchez Ballesta and Garcia-Meca (2007) confirm the hypothesis that managers of large companies manage their results less in view of their visibility. For this reason, the size of the company will be introduced into our model without its sign being rigorously anticipated.

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2.4.2 Age of company

The variable Age (AGE) is measured by the number of years between the date of incorporation of the firm and the current year. Ang, Colwm, and Wuh Lin (2000) argue that due to learning curve effects and survivorship bias, older firms are more efficient than younger firms. In addition, they would have had more experience in governance mechanisms; consequently, we would expect a positive relationship between age and the quality of accounting results.

2.4.3 Profitability of the firm :

According to Cormier, Landry and Magnan (2006, p. 157): "[...] The closer a company's performance is to a target, the more likely it is that management will engage in a results management approach to meet or exceed it". Following the example of several studies (Boubakri et al., 2005), we have chosen accounting indicators to measure performance. More specifically, return on equity (ROE) measures the efficiency with which the company uses its equity: - ROE: Earnings before interest and tax (EBIT)/Equity.

Table 2: Variable measurement table

Theme	Variable	Abbreviation	Measure
Share ownership variables	Concentration of shareholders	CONACT	Main shareholder's stake in the capital
	Institutional shareholders	ACTINST	% of shares held by Institutional Investors
	Management shareholding	ACTMAN	% of shares held by management and directors
	Family shareholding	ACTFAM	% of shares held by the family or family group
	Industrial Shareholders	ACTIND	% of shares held by industrial groups
Control variables	Company size	SIZE	The decimal logarithm of sales
	Age of company	AGE	Variable measuring the age of the company since its creation
	Financial performance	ROE	Measured by ROE, the efficiency with which a company uses its equity capital.

We will try to test the relationship between discretionary accruals and shareholding mechanisms. Our research model is as follows:

$$\mathbf{ACCD\ (Y) = \alpha + \beta 1CONACT + \beta 2ACTINST + \beta 3ACTMAN + \beta 4ACTFAM + \beta 5ACTIND + \beta 6TAILLEILLE + \beta 7AGE + \beta 8\ ROE}$$

RESULTS DISCUSSION

The results of our tests have enabled us to identify and characterise the influence of shareholding mechanisms on results management practices. These results are presented in the table below, which details the nature and intensity of this influence.

Variable	Coefficient	Std. Error	T-Statistic	Prob.
C	-1.07E+08	64474410	-1.666352	0.0999
CONC1ACT?	2.56E+08	81699098	3.135417	0.0025
ACTINS?	4791984.	786969.6	6.089161	0.0000
ACTFAM?	7686317.	1403119.	5.478021	0.0000
ACTMAN?	-600267.1	267273.0	-2.245895	0.0277
ACTINDUST?	14989652	1424936.	10.51953	0.0000
LOG(TA?)	13485492	2968208.	4.543310	0.0000
ROEQ?	42957.23	15116.44	2.841755	0.0058

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(ACCDJ?(-1))	0.056715	0.040209	1.410500	0.1626
@TREND	-22777096	5392800.	-4.223612	0.0001
Weighted statistics				
R-squared	0.810096	Mean dependent var	45645120	
Adjusted R-squared	0.732054	S.D. dependent var	87228334	
S.E. of regression	45152479	Sum squared resid	1.49E+17	
F-statistic	10.38017	Durbin-Watson stat	2.104335	
Prob(F-statistic)	0.000000			

The results of our tests indicate a positive and significant association at the 1% level between **institutional** shareholding (ACTINST) and discretionary accruals. The results of our model also indicate that institutional shareholding drives accounting earnings upwards. This result, similar to that found by Hsu and Koh (2005), is consistent with our analysis of the obligations of this category of shareholder. As they themselves are obliged to make their investors' investments profitable, or even to impress them, they may in turn be led to exert pressure on management to post higher earnings. Instead of putting the brakes on the management of accounting data, institutional investors could thus encourage management to improve their accounting results. The involvement of institutional investors in governance depends on their nature. Are they speculative (short-term) or sophisticated (long-term) institutional investors? In this regard, Finet (2009, p. 151) points out that "even if institutional investors clearly have an influence on company management,

Our results, which confirm the existence of a positive link between **family shareholding** and earnings management, support the findings of (Ben Ali[1] , Trabelsi and Gettler Summa, 2008) who explain that for certain firms dominated by family shareholding, the demand for information remains low, family shareholders want to take advantage of private profits to the detriment of other shareholders and therefore engage in earnings management practices.

However, our results confirm the existence of a negative relationship between **the manager's shareholding** and earnings management, which is in line with the political-contractual theory of accounting (Dhaliwal's hypothesis (1982)). Our results coincide with those of Salomon and Smith (1982), who explain that managers' interest in managing earnings upwards ceases when they hold shares in the firm's capital, since managing earnings upwards will automatically generate an increase in the tax payable, which will have a negative impact on the value of the firm, and consequently the increase in the number of shares held by the management team will prevent them from managing earnings downwards

In a different vein, our results support those of Mard and Schatt, who explain that **the main shareholder** may opt for earnings management practices in the context of public offerings or mergers and acquisitions. This earnings management maximises share value and increases the entry value for new shares.With regard to the control variables, the results of our tests confirm that the relationship between **the size of** the firm and the level of discretionary accruals is positive. This result contradicts the predictions of political-contractual theory and in particular the work of Koh (2003) and Park et al. (2004), which support the hypothesis that large firms are exposed to rigorous control by their environment, given the importance of the contracts that bind them to the various stakeholders. The results of our tests revealed a positive and significant relationship between financial profitability and the level of discretionary accruals. Our results are in line with studies by (Dechow, Sloan and Sweeney, 1995; McNichols, 2000; Beneish, 1997; Thomas and Zhang, 2000). They conclude that companies with extreme financial performance tend to have extreme accruals. Companies with extreme financial performance tend to have extreme accruals (Dechow, Sloan and Sweeney, 1995; McNichols, 2000; Beneish, 1997; Thomas and Zhang, 2000). With regard to the AGE variable, the results of our tests indicate that it is a variable with no impact whatsoever.

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CONCLUSION :

The results of the estimates can be summarised as follows:

The concentration of capital in the hands of controlling shareholders improves the quality of information produced by the company. However, the reference shareholder may opt for earnings management practices in order to gain private profits. The contribution of institutional and family shareholders to the governance system is open to question, as it increases the management of accounting results. Employee and management shareholders, on the other hand, appear to be more vigilant and more effective. The latter make it possible to curb the management of the accounting result. Finally, no relationship between state ownership and the quality of information produced by the company was verified. As far as the control variables are concerned, the size of the firm may constitute a motivating factor for earnings management practices, and financial performance may also encourage these practices. On the other hand, the results of our tests confirmed the traditional role of the audit function in limiting fraudulent manoeuvres, and the fact that the functions of management and chairmanship of the board of directors are held concurrently is a guarantee of the effectiveness and transparency of the quality of the financial statements produced. In conclusion, the results of this work could help to improve the legal, institutional and regulatory frameworks structuring corporate governance mechanisms in Morocco. They are of particular interest to Moroccan companies. The latter need to improve their governance systems. Using the results of this research, they could identify the gaps and weaknesses in their governance systems. This research has certain limitations. While we have tried to remedy some of them, other limitations could be improved in future studies. In the same vein, the operationalisation of certain explanatory variables could be refined. In this respect, we regret that we did not distinguish between two categories of institutional investors: speculative and sophisticated. Still on the subject of ownership structure. Another criticism is that we only looked at companies listed in Casablanca. These companies, which are more closely scrutinised by the media and investors, may not behave in the same way as the other companies that make up the Moroccan industrial fabric. Given this limitation, the generalisation of the results of this research remains open to criticism. A final limitation is that the summary statements on which we have worked have been drawn up in accordance with the general code of accounting standards, law 9-88 instituting Moroccan accounting, ignoring the emergence of international accounting standards and the current trend towards globalisation and the decompartmentalisation of economies and markets, which make these new IAS-IFRS standards an obligation rather than a choice.

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