

The impact of corporate governance on earnings management of listed companies in Sri Lanka

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Abstract

Earnings management has gained prominence in the financial reporting process of an organization and corporate governance could be recognized as a means of managing that adverse effect. The aim of this study is to examine the impact of corporate governance on earnings management of listed companies in Sri Lanka. One hundred fifty five (155) companies listed in Colombo Stock Exchange were considered as the sample of the study after excluding financial nature companies, companies with the financial year end of 31st December and companies with incomplete data and data from 2017 to 2019 were collected through secondary data sources. Seven corporate governance variables namely, the board size, board activity, board independence, the existence of audit committee, the existence of remuneration committee, the existence of nomination committee and gender diversity are considered as the independent variables of the study. Earnings management measured through modified Jones model (1995) is the dependent variable of the study. Two control variables namely return on asset and leverage are considered and descriptive analysis, correlation analysis and ordinary least square (OLS) and panel regression analysis were performed. Based on the results of OLS regression and panel regression, it was found that the impact of board size, board activity and gender diversity on earnings management are significant in Sri Lankan listed companies. However, it was found that the impact of board independence and existence of nomination committee on earnings management are insignificant. The findings of this study suggest that the existing corporate governance guidelines need to be revisited to mitigate opportunistic management behavior related to earnings manipulations.

Keywords: *Corporate governance, companies listed in Colombo Stock Exchange, earnings management.*