CORPORATE GOVERNANCE AND EARNINGS MANAGEMENT
IN SAUDI LISTED FIRMS

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IN SAUDI LISTED FIRMS

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Abstract

The system of corporate governance is designed for the effective and efficient operation of corporations on behalf of stakeholders as a mean of enabling various stakeholders to monitor managers effectively against opportunistic behavior. The corporate governance mechanisms have shown in other context of different organizations to affect firms’ behavior particularly the earnings management practices. The issue has been tested worldwide and it was shown that earnings management could be affected by the structure of corporate governance of the firms. Therefore, this study aims to investigate the impact of corporate governance mechanisms (i.e. independent director, Board size, board meetings and audit committee characteristics) on earnings management activities in Saudi listed firms for the year 2008. The study is significant due to the lack of empirical studies in the field of corporate governance and earnings management since the Saudi code of corporate governance has been enacted in the late 2006. More interesting this study will be of significant since it tests the period following the financial crisis in order to show whether the earnings management activities have experienced a change during this period compares to the past period as well as whether the corporate governance enhance the earnings quality and help in curbing earnings management in such critical period. The results of the study show that earnings management activities do not experienced any change post enactment of corporate governance code for Saudi listed firms. Furthermore, the corporate governance mechanisms have shown to have no impact on earnings management except for the board meetings which show negative relationship with earnings management. The impactions of the study for regulations are to help them in assessing whether the corporate governance achieved its objectives in order for them to take the corrective actions wherever necessary.
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Alshammari Ahmad Jassim H.

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CHAPTER ONE

INTRODUCTION

1.0 Background of the study

The chapter provides an introduction of the study. In the first section 1.1 of the chapter, an overview of the study is provided. In Section 1.2 the problem statement is presented. The motivation of the study is highlighted in section 1.3. The objectives of the study are highlighted in the section 1.4. It follows by section 1.5 which discusses the contribution of the study. Finally section 1.6 proposes the organization of the report.

1.1 Overview

Corporate governance has become a popular issue in the last few decades. It started in 1992 with the Cadbury report in the UK. Cadbury committee for corporate governance was the result of several high profile company collapses is concerned primarily with protecting weak and widely dispersed shareholders against self-interested Directors and managers. In response to the corporate scandals, congress enacted the Sarbanes-Oxley (SOX) Act on July 30, 2002. The act specifically targets corporate governance reform and has created a reporting system that now makes corporate governance more transparent to the public. In addition, the development of rating schemes for corporate governance has added to its transparency.

While previous research suggests a relation between good governance practices and less fraudulent financial reporting (Beasley, 1996). Corporate governance issues are sparse and no definitive relationship has been determined. Most other developed and emerging market countries have adopted best practices Codes e.g. Combined Code in the UK, Cromme Code in
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