

The Executive Compensation on Earnings Management Among Listed Non-Financial Companies in Nigeria

Professor Akinkoye Ebenezer Yemi

Obafemi Awolowo University,
Faculty of Administration
Department of Accounting
Ile-Ife, Nigeria

eykoye@mail.com, ekoye@oauife.edu.ng

Yusuf Kabir Olaropo

Obafemi Awolowo University
Faculty of Administration
Department of Accounting
Ile-Ife, Nigeria

olaropo30@gmail.com

Okedun Peter Temitope

Obafemi Awolowo University
Faculty of Administration
Department of Accounting
Ile-Ife, Nigeria

ptokedun@gmail.com

Agbogun Sarafa Adewumi , PhD

Oyo State College of Agriculture and Technology,
Accountancy Department,
Igboora, Nigeria.

sarafaagbogun@yahoo.com

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Abstract

The issue of earnings management practices among firms across the globe and particularly developing economies. Including Nigeria, remains a major concern among investors, stock market operators, and policymakers. The degree to which stakeholders may rely on financial reports while making informed decisions usually depends on their credibility, transparency, and accountability, as well as the level of independence and integrity of the preparers of financial reports. However, the recent collapse of many corporations such as WorldCom, Enron, and Sartyam, among others, has brought serious concern to the firm, investors' loss of confidence, and a growing skepticism and doubt about the quality of financial reports. This paper investigates the effect of executive compensation on earnings management among listed non-financial companies in Nigeria. The study adopted a quantitative research design. Secondary data for this study were collected from the Annual Reports and Accounts of selected banks. The study population consisted of 76 non- financial firms listed on the Nigerian Exchange Group (NGX) as of 31st of December 2022. The study adopted a purposive sampling technique to select firms whose data were readily available and whose stocks were consistently

traded on the stock market during the study period. Data on MAAB and DREM were sourced from audited annual reports, NGX, and the facts book. Data obtained were analysed using descriptive analysis (mean, standard deviation, minimum and maximum) and inferential statistics like Ordinary Least Square (OLS), Correlation, and Regression analysis, Fixed Effect Method, Random Effect Method and General Method Moment (GMM). Data collected were analyzed using multiple regression, as the inferential. The result shows that executive compensation ($t = -3.94$, $p < 0.05$) has a negative but significant effect on earnings management. The study concludes that executive compensation exhibits divergent effects on earnings management practices depending on the measurement approach used. The study suggests that the positive effect of accrual earnings management on managerial ability in Nigeria firms indicate the importance of board of directors to actively monitor and implement policy that will promote transparency and enhance managerial performance which ultimately contribute to the long-term success of the organisation while negative and significant effect of real earnings management on managerial ability in Nigeria firms will require support for corporate governance mechanisms, such as independent board oversight and effective audit committees that can mitigate the pressures on managers who wish to engage in earnings management practices and foster a healthier organizational climate.

Keywords: *Executive Compensation, Earnings Management, Nigeria Listed Non-Financial Companies.*

1. Introduction

The practice of earnings management is about putting forward a positive image of a company's financial performance, often by inflating earnings or keeping losses, to inspire investors, creditors, analysts, and other stakeholders' perception of the company's financial health (Demerjian et al, 2017). Other possible motivations for the practice have been ascribed to the desire of the managers' willingness to increase the market share of their companies significantly, and particularly when managers' compensation is tied to stock price performance. The agency and stewardship theory position was seriously challenged, especially in the 21st century, as there was evidence of financial scandals involving high-profile executives. The management of Enron, World.com, among others, was sued by other stakeholders for financial abuse and misconduct. In Nigeria, Cadbury Plc, Ile-oluji, and Lever Brothers were also charged with gross financial misconduct. Cadbury Plc corporate scandals are not out of place in the theory, as the positive accounting theory is of the view that a manager will engage in opportunistic behaviour and run the affairs of the organisation to their benefit.

The listed non-financial firms in Nigeria needed to be delved into to ascertain the cause and the level of the problem at present, now that Nigeria is moving from a consumption nation to become a producing nation. It is important to know whether the existing chief executive officers delved into earnings management out of greed or because they are not well remunerated. Also, the impact of executive compensation on earnings management and how executive benefit structures can be planned to suppress earnings management and foster long-term value creation for the company and its stakeholders in both developed and developing nations is of great concern (Brink, Gouldman, Rose & Rotaru, 2020). Some researchers have suggested that managers are more likely to manage earnings to portray a favourable condition and position of their organization if the compensation package are designed based on organization position and performance (Gouldman & Victoravich, 2019).

Managers participate in the manipulation of earnings when they are denied their optimal bonus in most cases. Positive accounting theory agrees with agency theory on how compensation contracts should be employed to encourage managers to operate in accordance with owners' interests. In Nigeria today, organization executives are highly compensated in line with their

organization's optimal performance; however, many of these organizations are financially distressed. Thus, it is vital to determine if managers are involved in earnings management in a bid to enjoy a high-level compensation package or not. There appears to be limited study (Otuya, Donwa & Egware, 2017), if any, on this subject within Nigeria context. Meanwhile, studies both within and outside Nigeria are scarce in the literature on the interrelationship between these variables, if any. Hence, the study investigates the executive compensation and earnings management interrelationship in Nigeria listed non-financial firms.

2. Literature Review

Conceptual Review

Earnings Management

It refers to the process by which a company uses various accounting methods and techniques to manipulate its financial results to meet certain targets or expectations. While some methods of managing earnings might be allowed, there are other times when it might be regarded as immoral or even fraudulent. This can be accomplished in a number of ways, including shifting the date of revenue recognition, changing depreciation schedules, manipulating reserves, or utilizing accounting loopholes. There exist different definitions of earnings management. Salehi, Shiri, and Hossini (2019) describes it to be manipulation of accounting numbers that would increase risk and mistrust of persons outside the firm, decrease the accuracy and dependability of earnings messaging, and probably result in information asymmetry and a fall in investment efficiency. Demerjian, Baruch, Melissa, Lewis and Sarah (2013) said it intentional distortion of financial statement by the management with the aim of obtaining private gains. The practice of earnings management is controversial and can be considered unethical when it involves intentionally misrepresenting of the financial performance of a company to deceive investors or other stakeholders. However, some contend that some methods of managing earnings are acceptable, such as modifying accounting procedures to accurately reflect a company's economic performance or adjusting accounting practices to smooth out earnings fluctuations that may be brought on by events beyond the control of the company. According to Doukas and Zhang (2020), earnings smoothing involves the use of management discretion to reduce earnings volatility and influence stakeholder risk perception. Regulatory bodies, such as the Securities and Exchange Commission (SEC), Financial Reporting Council of Nigeria (FRCN) and Corporate Affairs Commission has made frantic effort in making law, rules, regulation and guidelines to discourage unethical earnings management practices and promote transparency and accuracy in financial reporting. Investors and government agencies such as the Economic and Financial Crime Commission (EFCC), Independent Corrupt Practices and Other Related Offences Commission (ICPC) are closely monitoring companies for signs of earnings management, as it can be a red flag for potential accounting irregularities or financial manipulation. The importance of earnings management to this study in Nigeria was to help identify the prevalence and extent of this practice so that investors and other stakeholders can be aware and be protected from being misled by manipulated financial statements. Also, policymakers can detect areas where corporate governance practices need to be fortified to check the misuse of financial reporting systems and identify areas where companies may be non-compliant with these regulations. Finally, the results can be used by researchers to evaluate and refine their beliefs regarding earnings management, including the effects it has on the stock market and corporate performance.

Proxies of Earnings Management

Real Earnings Management and Accrual-based Earnings Management

Huanga and Sun (2017) defined real earnings management as operational activities to adjust reported earnings toward a specific path by making excess production to reduce the cost of

goods sold or cutting operational expenses to improve stated earnings. On the other hand, accrual-based earnings management is the difference between cash flow and net income by changing the figure of provision for bad debt and the method of depreciation of tangible assets currently in use. Although accruals are envisioned to portray the actual performance of an organisation, they can also be used in managing earnings. When firms carry out earnings management practices, they create accruals to aim at increasing or decreasing income. The management practice known as "real earnings management" deviates from standard business practices and has a negative financial impact on the organization. This is the reason why managers are more likely to use real earnings management to control earnings than accruals are; real earnings management has a greater likelihood of going unnoticed since it is less likely to be examined closely by auditors and authorities. In addition, the firm's accounting flexibility limits the use of accrual-based earnings management. For instance, because accruals have a reverse nature, firms will not be able to make the same approximations and rulings in later periods because of their earlier period assessments and conclusions.

Earnings smoothing

It is a financial reporting strategy used by companies to minimize the fluctuations in their earnings over time. The goal of earnings smoothing is to give investors and analysts the impression that a company's financial performance is more consistent and predictable, which can raise investor confidence and raise stock prices. Doukas and Zhang (2020) defined earnings smoothing as the power of management to make accounting decisions that reduce the volatility of profits and cannot be avoided as a practice in business organization. In order to achieve earnings smoothing, corporations often use accounting techniques that permit them to recognize revenue and expenses across longer periods of time, or they postpone the recognition of some income or expenses to subsequent periods. To increase short-term profitability, a corporation can decide to spread out the recognition of a sizable one-time gain over multiple quarters or postpone the recognition of expenses. Doukas and Zhang (2020) further explained that earnings smoothing puts the manager's interests ahead of other stakeholders and reduces business transparency. As an alternative, managers' use of profits smoothing as a signaling tool to communicate sensitive information.

Earnings quality

It is a term used to describe how accurate, dependable, and transparent company's financial statements are, especially its income statement. It demonstrates the degree to which a company's reported earnings give investors and other stakeholders' meaningful information for making informed decisions. Demerjian et al (2013) explain that key aspect of financial reports that has an impact on the effective use of resources is the quality of the earnings. Firms with low earning quality often have higher capital expenses, however, the result therein is the main input that investors and analysts will use for valuation of their business. High-quality earnings indicate that business performance is dependable, predictable, and transparent. Strong cash flows, fair accounting procedures, and efficient management of corporate activities are often used to sustain these earnings. Contrarily, low-quality earnings may be the consequence of non-regulated accounting methods, such as fake revenue recognition or fake expenditure accruals, which can result in overstating profits. Long-term sustainability and dependability of these sources of income are often lower. When evaluating a company's financial situation and potential for growth, analysts and investors pay special attention to the quality of its earnings. Investors typically have a more positive opinion of a company with high-quality earnings than one with low-quality earnings.

Earnings persistence

Demerjian, Baruch, Melissa, Lewis and Sarah (2013) refer to the extent to which a company's earnings remain stable over time. A business with stable profits will regularly produce similar levels of profit year after year, but a business with unstable earnings will experience substantial variations in its profit accordingly. Earnings persistence is one of the major signs that a firm is profitable and financially healthy. Businesses with consistent earnings are typically viewed as more financially solid and less risky investments than those with unstable earnings.

Financial analysts often examine a company's earnings across some years and compute indicators such as earnings growth rate, standard deviation of earnings, and the correlation between earnings in consecutive years to quantify earnings persistence. Indicators of earnings persistence include a high rate of earnings increase, a small standard deviation, and a high correlation between earnings over time. It is crucial to remember that a company's earnings persistence by itself does not ensure future success or profitability. A company's financial success may also be impacted by other elements like market competition, shifting industry trends, and general economic conditions.

Empirical Review

Executive Compensation and Earnings Management

Shuto (2007) investigates the relationship between earnings management and CEO pay in Japanese firms. The study employed OLS regression and a cross-sectional accruals model to analysed 14,081 sample firms selected for that purpose on positive accounting theory. Findings indicate that the relationship between discretionary accruals and executive compensation is often strong as the quantity of overall discretionary accruals rises, and the use of discretionary accruals to smooth out income fosters their relationship. Ibrahim and Lloyd (2011) examined the connection between executive compensation contracts' non-financial performance measures and earnings management. In using a cross-sectional regression model for analysis based on positive accounting theory to sample of 357 firms was selected. The outcome demonstrates that NFPM firms had fewer discretionary accruals than their counterpart firms that employ FPMs solely. It was concluded that using a combination of FPMs and NFPMs in rewarding top management can help reduce earnings manipulation behavior in firms. Veeman, Hodgson, Praag and Zhang (2011) investigated to see if breaking out executive stock option exercises has any implications for managing earnings. The study engaged univariate and multivariate analysis using 678,192 firm year observed based on signaling theory. It was concluded that stock options have been found to encourage managers to seek riskier but profitable ventures. Options also increase the sensitivity of managerial practice to price instability and promote more risk-taking in creative financial reporting. Joubert and Fakhfakh (2014) examined the relationship between CEO incentive-based compensation and profit management and how the elements of an organized workplace supported it. The study used panel data on 1,500 sample firms selected from 2004 to 2008 using contracting and managerial power theory arranged on regression analysis. The findings indicate that there is a strong correlation between CEO incentive-based compensation and earnings management. However, concluded that CEOs from developed nations that are on corporate governance practices express fewer tendencies to engage in earnings smoothing in an effort to increase their salary and they also provide solid proof that cross-country differences have significant real impacts on CEOs' potential to be motivated to make deliberate accounting decisions considering their performance-based reward. Sun (2014) examined executive pay and earnings management in the context of moral hazard. Adopting agency theory and the theory of moral hazard. Cross-sectional variation with time series was employed to measure executive compensation and its significance to corporate governance reforms. The result shows executive compensation can influence corporate goals and concluded that managers' remuneration is therefore necessary to

inform productive effort because it has been determined that the ability to alter financial records reduces when a good package is guaranteed. Park (2018) analyzed the connection between executive pay at comparable companies and earnings management. The study used OLS to analyzed 1,500 sample firms in the observed year and focused on agency theory. The findings show that a company's accruals management is favorably correlated with the CEO compensation of other companies in similar product marketplaces. It is important to note that the positive relationship is more pronounced for companies where the CEO serves as chairman, whereas it is less pronounced following the passage of SOX. Companies that compete in similar product marketplaces with other companies that pay their CEOs more tend to have fair reporting system. Assenso-Okofu, Ali and Ahmed (2019) observed the importance of the global financial crisis on chief executive compensation and earnings management. Univariate and multivariate tests were conducted for 1,800 sample firms from 2005 to 2010 based on Stewardship and agency theory. The findings established that the economic environment has an impact on CEO salary and earnings management. It also shows the reason why regulatory bodies examine it more closely to enhance disclosure requirements and decrease managers' unethical behavior and for proper review of CEO compensation packages during economic crises so that managers' interests are aligned with shareholders in order to aid in the reduction in the agency problem.

Holderness, Huffman, and Lewis-Western (2019) studied the relationship between rank-and-file option compensation and improved firm-level earnings management. Focusing on Positive Accounting Theory. The study employed Regression analysis using 9,508 firm year observed. The results indicate that rank-and-file options and earnings smoothing have a positive association. Also discovered that as the option reward is distributed more widely throughout an organization increases management of profit. The increase is to the extent that the relationship is strong when option compensation is likely to result in greater encouragement and employees are monitored with less penetration. Gouldman and Victoravich (2019) examined the impact of perceived pay equity and CEO friendship on business-unit managers' earnings management practices. Engaging equity theory, Social comparison, and construal level theory to investigate through ANOVA for a 162-sample selected firm. The study posits and finds that when a manager is closely related to the CEO, earnings management increases under the new DFA pay disclosure requirement. In the absence of the DFA and CEO pay-equity ratio disclosure, the CEO relationships lead to less profit doctoring. Nevertheless, when managers are given the pay-equity information in the post-DFA environment, CEO friendship may have a damaging impact on the quality of financial reporting.

Brink, Gouldman, Rose and Rotaru (2020) examine how subordinate managers' real earnings management decisions and psychophysiological reactions are affected by their superiors' compensation systems. Centred on moral disengagement theory and Cognitive dissonance theory, using a 2×2 between-participants to experiment on 108 sample selected firm year observed. The findings demonstrate that compensation plans for executives and other superiors can effectively reduce subordinate managers' tendency for management of earnings. The results also show that investing in R&D can result in earnings manipulation, and CEO remuneration plans can help to diminish this type of profit smoothing. Inneh, Obokoh and Busari (2020) examined the significant of executive compensation on management of earnings in the non-financial sector. Engaging agency, positive and managerial power theory, to investigate through longitudinal research design for a selected 40 sample from Nigerian-listed firms between 2010- 2018 with Ordinary Least Square (OLS) for its analysis. The results shows that chief executive officer with lesser reward engage in dubious behaviour while those that are highly remunerated engage in earnings doctoring. It can be however concluded that management with lower compensation engages in opportunistic behaviour to meet either company's target or their own personal interest. Otuya, Donwa and Egware (2017) examine

the connection between earnings management and excellence of corporate governance in Nigeria with review of executive benefit and audit committee features. Agency theory was adopted to investigate through content research design from financial statements of sampled listed non- financial firms between 2012- 2016 using regression analysis. The results shows that executive benefit have a significant negative association with earnings management.

2.3. Theoretical Framework

This upper echelons theory has however taken as a guide for the framework of this study in order to prove the need of measuring and value management competence when making critical decisions that will ensure the survival, development, and wellness of their organisation, as the capacity to efficiently cope with business resources is not always apparent (Abatecola & Cristofaro, 2018). Given incentives to executive will encourage them to retain in the business and will go a long way to concentrate on strategic plan that will enhanced performance (Hambrick (2007).

3. Critical Analysis and Research Gap

Furthermore, some studies (Brink, Gouldman, Rose & Rotaru, 2020) have examined the relationship between executive compensation and earnings management, although, there appears to be evidence of earning smoothing in Nigeria listed non-financial firms where managers are involved in opportunistic behaviour (Inneh, Obokoh & Busari, 2020.; Otuya *et al.* 2017) on the subject matter but still believe the study is not enough.

4. Methodology

The effect of executive compensation on earnings quality was examined using a quantitative research design. The population for this work comprised 76 non- financial firms listed on the NGX as of 31st of December 2022. All listed non-financial firms were examined to select the ones that had the required data for the period between 2013 and 2022. The study adopted a purposive sampling technique to select firms whose data were readily available and whose stock was consistently traded on the stock market during the study period. Data on earnings management and executive compensation were sourced from audited annual reports, NGX, and the facts book. Data obtained were analysed using descriptive analysis (mean, standard deviation, minimum and maximum) and inferential statistics like Ordinary Least Square (OLS), Correlation, and Regression analysis, Fixed Effect Method, Random Effect Method, and General Method Moment (GMM).

Model Specification

Model for Earnings Management

The measurement of earnings management developed by Demerjian *et al;* (2017) was followed for this study. Expenses subject to discretion were measured as the sum of Residual, Development, Selling, and Administration Expenses for the years. The Residual represents abnormal expenses. Therefore, 1, to be rising in the extent of real activities management AbExp, multiplies the residual.

Model for Effect of Executive Compensation on Earnings Management

This study examined the effect of executive compensation on earnings quality. Executive compensation was measured using total compensation, while earnings management was proxied using real earnings management and accrual earnings management.

To determine the effect of Executive Compensation on Earnings Management, the following regression model of McVay's (2006) was adopted:

$$EM_{it} = \alpha_0 + \alpha_1 COMP_{it} + \alpha_2 FSIZ_{it} + \alpha_3 CFOA_{it} + \alpha_4 RETA_{it} + \alpha_5 LEV_{it} + \alpha_6 BD_{it} + \alpha_7 IM-P_{it} + \alpha_8 BIG4_{it} + \epsilon_{it}$$

Where:

EM_{it} = Earnings management variables are denoted in the study with real earnings management and accrual earnings management for the sampled listed non-financial firms for the year from 2013 to 2022

Earnings management = *f* (*Executive compensation*)

$ACEM = f(drem)$

Rewrite in econometric term:

$$acem_{it} = \partial_0 + \beta_1 drem_{it} + \beta_2 cfoa_{it} + \beta_3 fsiz_{it} + \beta_4 reta_{it} + \epsilon_{it}$$

$$reem_{it} = \partial_0 + \beta_1 drem_{it} + \beta_2 cfoa_{it} + \beta_3 fsiz_{it} + \beta_4 reta_{it} + \epsilon_{it}$$

$acem_{it} = \alpha_0 + \alpha_1 drem_{it} + \alpha_2 fsiz_{it} + \alpha_3 cfoa_{it} + \alpha_4 reta_{it} + \epsilon_{it} > 0$ which implies that a positive relationship is expected between the explanatory variables, $\alpha_1 drem_{it}$, $\alpha_2 fsiz_{it}$, $\alpha_3 cfoa_{it}$, $\alpha_4 reta_{it}$ and the dependent variable $acem_{it}$ (accrual earnings management). The size of the effect of the relationship were explained among the explanatory variables.

$reem_{it} = \alpha_0 + \alpha_1 drem_{it} + \alpha_2 fsiz_{it} + \alpha_3 cfoa_{it} + \alpha_4 reta_{it} + \epsilon_{it} > 0$ which implies that a positive relationship is expected between the explanatory variables, $\alpha_1 drem_{it}$, $\alpha_2 fsiz_{it}$, $\alpha_3 cfoa_{it}$, $\alpha_4 reta_{it}$ and the dependent variable $reem_{it}$ (real earnings management). The size of the effect of the relationship were explained among the explanatory variables as show in table 1.

Table 1. Measurement of Variables

VARIABLES GROUP	VARIABLES NAME	DEFINITION	SOURCE(S)
Independent	Executive Compensation (DREM)	The sum of salary, bonus and other compensation packages for year	Sun, 2014;
Dependent	Real Earnings Management (REEM)	Managerial operative actions to alter reported earnings in a particular direction	Shuto, 2007;
	Accrual-based Earnings Management (ACEM)	Differences between cashflow and net income	Shuto, 2007;
Control	Firm size (FSIZ)	Normal log of total asset at the end of the period	Huanga & Sun 2017; Oladejo, Falade & Okedun, 2026
	Cash flow (CFOA)	Cash inflows from operation	Baixauli-Soler, <i>et al.</i> , 2020; Oladejo, Falade & Okedun, (2026)
	Return on asset (RETA)	Income before extraordinary items divided by total asset at the beginning of the year	Huanga & Sun (2017); Oladejo, <i>et al.</i> , (2026)

Source: Authors Compilation, (2024)

5. Results and Discussions

5.1. Descriptive Analysis

In this section, the study employed descriptive statistics for both the independent and dependent variables of interest. Each variable was examined based on the mean, standard deviation, maximum, and minimum. Table 2 displays the descriptive statistics for the study.

Table 2. Descriptive Statistics

Variable	Obs	Mean	Std. Dev.	Min	Max
Acem	760	-.614	.805	-7.63	5.57
Reem	760	-1.849	2.101	-25.17	8.29
Maab	760	.027	27.523	-1.795	4.392
Drem	760	3.179	30.659	0	746.27
Cfoa	760	.074	.163	-.94	.82
Fsiz	760	7.128	.89	5.03	9.45
Reta	760	.714	17.82	-179.92	176.27

Source: Authors Computation (2024)

The Table 2 results from the descriptive statistics reveal that, on average, non-financial firms in Nigeria exhibit a negative level of accrual earnings management (ACEM), with a mean of -0.614 and a standard deviation of 0.805. This negative mean indicates a tendency towards conservative accounting practices, potentially reflecting efforts to mitigate risks and maintain transparency in reporting practices. However, the variability in ACEM across firms, with a minimum of -7.63 and a maximum of 5.57, highlights the diverse strategies employed within the industry, with some firms resorting to more aggressive accrual management techniques. Similarly, the analysis indicates that listed non-financial firms in Nigeria engage in real earnings management (REEM), as evidenced by the negative mean value of -1.849 and a standard deviation of 2.101. This suggests a propensity among firms to manipulate real activities to meet earnings targets. The wide variability in REEM, with a minimum of -25.17 and a maximum of 8.29, underscores the heterogeneity in financial reporting practices among firms, with some exhibiting extreme levels of manipulation.

5.2. Data Normality Test

Least squares regression is based on the assumption of a Gaussian distribution. The data adheres to a Gaussian distribution, commonly referred to as a normal distribution. It is presumed that the population of the samples conforms to a normal distribution. The null hypothesis states that the sample follows a normal distribution. If the test is both valid and statistically significant, it suggests that the distribution may not conform to a normal pattern. Mendes and Pala (2003) concluded that the Shapiro-Wilk test is the optimal approach for assessing normality in their research. The following table displays the residual normality test conducted in the study.

Table 3: Data Normality Test

Variable	Obs	W	V	Z	Prob>z
acem	760	0.641	176.283	12.663	0.000
reem	760	0.788	104.347	11.379	0.000
maab	760	0.426	282.267	13.815	0.000
drem	760	0.056	463.915	15.032	0.000
cfoa	760	0.920	39.112	8.976	0.000
fsiz	760	0.989	5.210	4.041	0.000
reta	760	0.668	163.020	12.471	0.000

Source: Authors Computation (2024)

The result in Table 3 shows that the dependent variable of earnings management when measured in terms of accrual earnings management ($\text{prob}>z = 0.000$) and real earnings management ($\text{prob}>z = 0.000$) are not normally distributed. This conclusion arises from the significant probability values of the z-statistics obtained from the Shapiro-Wilk test, which is conducted at a 5% significance level. Similarly, the independent variables, including

managerial ability (prob>z = 0.000), executive compensation (prob>z = 0.000) as well as the control variables of cash flow from operations (prob>z = 0.000), firm size (prob>z = 0.000), and profitability when measured in terms of return on asset (prob>z = 0.000) are all not normally distributed. This inference is drawn from the significant probability values of the z-statistics obtained from the Shapiro-Wilk test, which is conducted at a 1% significance level. However, the study proceeds with the ordinary least square regression but carefully interpreting the probability statistics against the t-statistics in line with the recommendation of Gujarati, (2004).

6. Regression Analyses

Specifically, to examine the cause-effect relationships between the dependent variables and independent variables as well as to test the formulated hypotheses, the study used a robust regression analysis since the result reveal the presence of heteroscedasticity and endogeneity in the model. This study begins by estimating earnings management when measured im terms of accrual earnings management and real earnings management as a function of executive compensation. The result from the pool OLS regression estimation of model 1 is presented in Table 4

Table 4: Regression Results

Variables	(1) OLS-ACEM	(2) Robust-ACEM	(3) OLS-REEM	(4) Robust-REEM
drem	-0.002 (0.064)	-0.002*** (0.000)	0.005** (0.044)	0.006** (0.034)
cfoa	-1.436*** (0.000)	-1.243*** (0.000)	0.111 (0.812)	-0.186 (0.501)
fsiz	-0.105*** (0.001)	-0.062*** (0.000)	-0.246*** (0.005)	-0.126** (0.014)
reta	0.010*** (0.000)	0.009*** (0.000)	-0.022*** (0.000)	-0.033*** (0.000)
Intercept	0.237 (0.297)	-0.047 (0.674)	-0.106 (0.863)	-0.592 (0.104)
Observations	760.000	760.000	760.000	759.000
R ²	0.129	0.307	0.061	0.226
Hettest	7.21 {0.007}		23.06 {0.000}	
VIF	1.05		1.05	

Notes: *p-values are in parentheses. *** p<.01, ** p<.05*

Source: Authors' Computation (2024)

Table 4 represents the results obtained from the estimation of the model for this study. The results show that the dependent variable of earnings management has an R-Square value of 0.129 when measured in terms of accrual earnings management and 0.061 when measured in terms of real earnings management. This implies that the independent and control variables of the study could explain 13% and about 6% of the systematic change in the dependent variable of earnings management when measured in terms of accrual earnings management and real earnings management, respectively. However, the unexplained part of the changes in earnings management has been captured by the error term. To further validate the estimates of the pool OLS results, this study also tests for multicollinearity and heteroscedasticity. The mean Variance Inflation Factor (VIF) of the regression models is 1.05. The analysis reveals that the average VIF (Variance Inflation Factor) for all the models is below the threshold of 10, which aligns with Gujarati's (2004) findings. This suggests that there is no multicollinearity present

and it indicates that none of the independent variables should be excluded from the models. Also, the homoscedasticity assumption of the pooled ordinary least squares (OLS) model is tested using the Breusch-Pagan module in Stata 14. The results indicate that the assumption of homoscedasticity in the pool OLS regression model has been broken, as evidenced by the substantial p-values. Therefore, the study modifies the model to address this violation by utilizing robust regression, as suggested by Greene (2003). The results obtained from the robust regression model presented in Table 4.5 revealed that executive compensation has a negative and significant effect on earnings management when measured in terms of accrual earnings management (coef. = -0.002 (0.000)) but a positive and significant effect on earnings management when measured in terms of real earnings management (coef. = 0.006 (0.034)) of listed non-financial firms in Nigeria. The result implies that an increase in executive compensation will significantly decrease accrual earnings management but significantly increase real earnings management of listed non-financial firms in Nigeria during the period under study.

7. Discussion of Findings

The results revealed that executive compensation has a negative and significant effect on earnings management when measured in terms of accrual earnings management but a positive and significant effect on earnings management when measured in terms of real earnings management of listed non-financial firms in Nigeria. The result implies that an increase in executive compensation will significantly decrease accrual earnings management but significantly increase real earnings management of listed non-financial firms in Nigeria during the period under study. This suggests that the level of executive pay may influence the methods through which earnings are managed, with implications for financial reporting integrity and transparency. The negative and significant effect of executive compensation on accrual earnings management is consistent with findings from previous research. For instance, Shuto (2007) reported similar results, suggesting that higher executive pay may serve as a deterrent to accrual earnings management practices, as well-compensated executives may have less incentive to engage in aggressive accounting manipulation. Similarly, Ibrahim and Lloyd (2011) found evidence of a negative relationship between executive compensation and accrual earnings management, indicating that firms with higher executive pay are less likely to manipulate accruals to meet earnings targets. However, the positive and significant effect of executive compensation on real earnings management contradicts the findings of some previous studies. Veeman *et al.*, (2011) observed a negative relationship between executive compensation and real earnings management, suggesting that well-compensated executives are less likely to resort to manipulative practices involving real activities. Similarly, Joubert and Fakhfakh (2013) found that higher executive pay is associated with lower levels of real earnings management, indicating that firms with generous compensation packages prioritize ethical conduct and value creation over short-term manipulation. Nonetheless, the present findings are consistent with the study by Sun (2014), which reported a positive association between executive compensation and real earnings management. This suggests that firms with higher executive pay may be more inclined to engage in manipulative practices involving real activities to meet earnings targets and satisfy investor expectations. Additionally, Park (2018) found similar results, indicating that higher executive compensation is positively correlated with real earnings management, reflecting the potential conflicts of interest and agency problems inherent in executive compensation structures. Moreover, the findings align with the study by Assenso-Okofa *et al.*, (2019), which highlighted the positive impact of executive compensation on earnings management, particularly in terms of real earnings management. This implies that higher executive pay may incentivize managers to prioritize short-term financial performance at the expense of long-term value creation, leading to distortions in

financial reporting and decision-making processes. Similarly, Holderness *et al.*, (2019); and Gouldman and Victoravich (2019) reported similar positive associations between executive compensation and earnings management, indicating the need for greater transparency and accountability in executive pay practices.

8. Conclusion and Recommendations

This paper investigates the effect of executive compensation on earnings management among listed non-financial companies in Nigeria. The results reveal that executive compensation has a negative and significant effect on earnings management when measured in terms of accrual earnings management, but has a positive and significant effect on earnings management when measured in terms of real earnings management of listed non-financial firms in Nigeria. The study concluded that executive compensation exhibits divergent effects on earnings management practices, depending on the measurement approach used. While higher levels of executive compensation were associated with decreased accrual earnings management, they were linked to increased real earnings management. This suggests that executive pay may influence the methods through which earnings are managed, with implications for financial reporting transparency and the alignment of managerial incentives with long-term value creation. Based on the findings of the study, it is recommended that the positive effect of accrual earnings management on managerial ability in Nigeria firms indicate the importance of board of directors to actively monitor and implement policy that will promote transparency and enhance managerial performance which ultimately contribute to the long-term success of the organisation while negative and significant effect of real earnings management on managerial ability in Nigeria firms will require support for corporate governance mechanisms, such as independent board oversight and effective audit committees that can mitigate the pressures on managers who wish to engage in earnings management practices and foster a healthier organizational climate.

Abbreviations

ACEM:	Accrual-based Earnings Management
REEM:	Real Earnings Management
VIF:	Variance Inflation Factor
MAAB:	Managerial Ability
DREM:	Executive Compensation
NGX:	Nigerian Exchange Group
OLS:	Ordinary Least Square
GMM:	General Method Moment
CEO:	Chief Executive Officer
CFOA:	Cash Flow from Operations
FSIZ:	Firm Size
RETA:	Return on Assets

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