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The Effect of Corporate Governance on Earnings Quality

Quantitative Study

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ABSTRACT :

Purpose: The intention of the study is to explore the effect of corporate governance on earnings quality on Finnish active companies listed on Nasdaq Helsinki Stock Exchange.

Design/ Methodology/ Approach: The study analyses the independence of the audit committee, size of the board, and CEO duality as a measure of the corporate governance on total accruals as an estimation for earnings quality. The sample of the research constitutes 91 active Finnish companies listed on Nasdaq Helsinki Stock Exchange over the period of 7 years from 2017 to 2023. The data obtained from the secondary sources include the annual reports of the respective companies.

Findings: The results of the thesis reveal that there is a positive relationship between independence of the audit committee, size of the board, and CEO duality over the earnings quality which is statistically insignificant.

Although there is a positive association between corporate governance and earnings quality, P value of the regression analysis suggests that the relationship is insignificant, hence rejecting the first hypothesis of corporate governance has a significant positive effect on earnings quality and accepts null hypothesis.

Research Implications: Research shows that globally held assumptions like, strong governance structures enhance the earnings quality may not be compatible with the Finnish contexts, shows traditional variables of corporate governance may not capture the influence on earnings quality in highly regulated and transparent market in Finland which may refine the existing commonly accepted assumptions in Nordic settings.

Findings may lead to policymakers and regulators shifting their focus to evaluate the effectiveness of governance bodies rather than expand governance requirements.

Practical Implication: When conducting research, use at least more than three independent variables to get a good result, which may help to run the dataset to a standard level by eliminating the variables which are not fit for the analysis.

Originality/ Value: The research on the influence of corporate governance on earnings quality conduct for Finnish market for the most recent research period of 2017 to 2023. It contributes new insights by exploring an area that has limited scholarly attention in Finland. Moreover, this study helps to understand the global findings on this topic, also true in the Finnish contexts.

KEYWORDS: Corporate Governance, Earnings Quality, Independence of the Audit Committee, Size of the Board, CEO Duality, Total Accruals

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Abbreviations

CG = Corporate Governance

EQ = Earnings Quality

CEO = Chief Executive Officer

OECD = Organization for Economic Cooperation and Development

GAAP = Generally Accepted Accounting Principles

CFO = Chief Financial Officer

TA = Total Accruals

IAC = Independence of the Audit Committee

SBOARD = Size of the Board

CEOD = Chief Executive Officer Duality

1 Introduction

Understanding corporate governance is a vital area of interest to academics, practitioners, and regulators. Corporate Governance (CG) includes a collection of principles, procedures, and operational structures through organizations that are guided and overseen which encompasses the interactions among leadership teams, governing bodies, investors, and various interested (OECD, n.d.). Effective corporate governance mechanisms improve investor's perception of an organization's reputation, trustworthiness, and reliability (Silva, 2019). The linkage between governance framework and reliability of financial disclosures became a complex and frequently debated topic among accounting researchers (Rezaee & Safarzadeh, 2023). The primary notion is that strong corporate governance oversight methods will increase the earnings quality by effectively monitoring managerial actions and promoting financial reporting integrity (Rezaee & Safarzadeh, 2023) & (Jiang, et al., 2008).

Managers are the stewards of the shareholders' funds; hence they are responsible for providing financial statements to show the real firm's performance. In preparing these financial statements management may try to manipulate them by using different methods to gain personal benefits. Therefore, earnings quality is a vital indicator of the reliability and transparency of financial reporting as earnings comprise a leading source of company related data for investors and stakeholders (Ebaid, 2011). Also, "poor corporate governance and greater earnings management may cause poor earning quality" (Jiang, et al., 2008).

Limited research exists on studies examining the connection between corporate governance and earnings quality in the Finnish context, despite its advanced economy and well-established corporate governance framework. This research will investigate how corporate governance influences on earnings quality of actively traded Finnish organizations in Finland.

1.1 Purpose of the Study

The purpose of the study is to explore the effects of corporate governance on earnings quality in active Finnish organizations that have been publicly traded on Nasdaq Helsinki Stock exchange, spanning seven years from 2017 to 2023. It is essential to investigate the link between corporate governance and earnings quality in order to realize whether we can use corporate governance to serve as a means to reduce or eliminate the issues related to earnings management.

1.2 Research Problem

The absence of corporate governance practices or an inadequate level of corporate governance provides managers with an opportunity to mislead investors and other parties by employing disputed earnings. As an example, the inherent characteristic of accounting accruals provides managers a considerable discretion in shaping the reported earnings an entity publishes in any given period largely because of information imbalance that exist between management and shareholders (García-Meca & Sánchez-Ballesta, 2009). “Managers may manipulate earnings with the intention of reducing corporate tax obligations” (Mulyadi & Anwar, 2014).

Due to the persistent challenge of earnings manipulation, where financial statements may be deliberately adjusted to portray a more positive view regarding the financial well-being of the entity, it becomes increasingly important to explore the corporate governance influence in safeguarding the earnings integrity.

1.3 Research Question

This thesis is focused on evaluating the corporate governance on the earnings quality of active Finnish companies listed on the Helsinki stock exchange. The study tackles the

issue connected to the research question below that arose within the scope of the research problem.

How does corporate governance, particularly audit committee independence, board size, and CEO duality, influence the earnings quality of active Finnish firms publicly traded on Helsinki stock exchange?

These governance factors are extensively recognized in corporate governance literature due to their potential to shape the transparency and trustworthiness of reported financial disclosures. Independence of the audit committee is often linked to enhance oversight and reduce earnings manipulation as their responsibilities extend beyond supervising the financial reporting to oversight of accounting policy selection, evaluation to adherence to regulatory requirements and ethical practices, and oversight of appointment, performance, and independence of external auditors (Hamdan, 2020). The number of directors on an organization's board may influence how effectively decisions are made and how well the organization is supervised. CEO duality can compromise board independence and reduce transparency. Exploring how these elements relate to accuracy of reported earnings can offer meaningful understanding of whether strong corporate governance leads to earnings quality in publicly traded companies in Finland.

1.4 Significance of the study

Over the past years, investor concern has been increasing regarding earnings quality, particularly following numerous disclosures by international companies about non-genuine and transient earnings in their quarterly reports (Hamdan, 2020). "Corporate governance plays a pivotal role in this context because it is crucial for overseeing a company's financial reporting process" (Salehi & Asgari, 2013). It is about ensuring the integrity of the financial data that is shared to investors and the general public. Corporate governance mechanisms can help reduce competing of interests between management and owners, which potentially enhance the earnings quality (Salehi & Asgari, 2013).

Finland has a high emphasis on corporate governance as it values transparency and accountability. This study could provide insight into how corporate governance mechanisms influence the quality of financial reporting, which is critical for maintaining investor confidence. The thesis on the impact of corporate governance on earnings quality in Finland is significant for several reasons. First, the study is conducted by researching the Finnish market and by providing a more recent research period from 2018- 2024. Secondly, there is lack of extensive research on this subject in Finland, which would fill the critical gap in academic literature and provide a regional perspective that complements existing global studies. Thirdly, previous similar studies have demonstrated that strong corporate governance can lower discretionary accruals, which is an important indicator of earnings management. Research in the Finnish context could reveal that these global findings hold true in the Finnish regulatory and cultural environment. Finally, the study could help regulators, and policymakers, to use the findings of this thesis to strengthen financial system integrity and Finnish companies to implement effective governance practices to boost earnings quality.

1.5 Hypotheses of the Study

Better corporate governance structures lead to reduce manipulation of reported earnings, enhanced predictability and consistency in financial outcomes, as well as improve timeliness, cautiousness and information relevance of accounting data (Rezaee & Safarzadeh, 2022). Their research on oversight structures and financial reporting reliability, performed using information derived from organizations listed on the Tehran Stock Exchange, revealed a statistically and economically meaningful connection across all evaluated models (Rezaee & Safarzadeh, 2022).

Salehi & Asgari, (2013) found a substantial link between earnings quality and several determinants including board size, the ratio of non executive directors, and the audit committee's size. Also, the outcomes demonstrate that forming of audit committee

significantly impact in improving the quality of reported earnings among the firms listed on Tehran stock exchange during 2006 to 2010 period (Salehi & Asgari, 2013).

The findings from the thesis examining the impact of governance structures on Earnings Quality (EQ) in spanish listed organizations which are outside of the financial sectors reveal that EQ positively associated by the scope and intensity of the board's activities and variables related to audit committee has a significant association with earnings quality (Mayoral & Sánchez-Segura, 2008).

On the basis of research problem and the guiding from revelations of the previous research following hypotheses can be suggest to analyse the connection between corporate governance and earnings quality of active public traded organizations in Nasdaq Helsinki Stock Exchange in Finland.

H1: Corporate governance has a significant positive effect on earnings quality in listed companies in Finland.

And based on this consideration null hypothesis proposed in this research is as follows,

H0: Corporate governance has no significant effect on earnings quality in listed companies in Finland.

1.6 Limitations

The research predominantly depends on the secondary data sources including databases and annual reports, hence limited use of primary data sources. As a result, study is more inclined towards secondary data and carries risk related to reliability and completeness of the information. Also, the data collected from financial statements can be subject to manipulation and not comparable due to differing accounting policies and assumptions applied by individual companies.

There are some other factors which may enhance the earnings quality other than the factors relating to corporate governance. Additionally, there may be timeframe limitations which may not reflect long term trends.

1.7 Structure of the Study

The thesis constitutes five chapters, in which chapter two contains the literature review, which includes an introduction that constitutes mainly the definitions of corporate governance and earnings quality, theoretical review that explain main theories relevant to this research, and empirical literature review that provides previous research related to this study and their findings. Chapter three contains methodology which covers research design, research approach, population, sample, method of data collection, calculation methods, measurements of the variables, conceptual framework, and method of analysis. Chapter four provides data analysis and their results, which includes subheadings of introduction, descriptive statistics, correlation matrix, test of multicollinearity, regression results, and research question and hypothesis testing. Finally, chapter five contains discussion about results, conclusion, implications and recommendation and direction for further research.

2 Literature Review

2.1 Introduction

This part provides a comprehensive examination of corporate governance and earnings quality by delving into their definitions, fundamental principles, and factors affecting different governance systems. A particular focus is given to the corporate governance landscape in Finland, discussing the regulatory framework and best practices.

2.1.1 Corporate Governance

Corporate governance (CG) may be interpreted in many ways depending on different perspectives on the role of corporations and their relationship with various stakeholders. Corporate governance guides how business corporations are directed and controlled and their relationships with their shareholders and stakeholders (OECD, n.d.). CG is viewed as a system of guiding values and standards that influence the corporations, shareholders, and management. This sets of guidelines reflects both firm specific features and elements that promote sound governance practices to support ethical and effective corporate oversight such as patterns of ownership, stakeholder relationships, transparency of financial reporting, information disclosure, and board configuration (Cornelius, 2005). Corporate governance encompasses the system of interactions among company leadership, shareholders, board of directors, and other stakeholders while establishing organizational structure and mechanisms by which the company is governed, sets its goals and outlines the ways of accomplish set objectives and tracked (OECD, 2023). These definitions show that understanding corporate governance involves considering core principles, practical applications, and the wider institutional environment in which it functions.

Corporate governance principles may differ across countries and regions, yet certain fundamental elements form the foundation of effective governance globally. To illustrate,

the 2002 South African King Report outlines 7 key elements defining corporate governance, emphasizing its core aspects and similarly in 2003, the Australian Stock Exchange (ASX) developed set of ten guiding principles through its Corporate Governance Council, offering a comprehensive framework for good corporate governance practices (Wajeeh & Muneeza, 2012). These examples highlight the importance of establishing clear guidelines to ensure accountability, transparency, and fairness in organizational management.

Transparency and Disclosure: Open and timely communication of relevant data and information to shareholders and other stakeholders is crucial for accountability and informed decision-making. This includes clear financial reporting, disclosure of potential conflicts of interest, and transparent board processes (Halla, 1999).

Accountability: The board of directors' task to ensure accountability to the shareholders by overseeing the organization's performance and adherence to legal and ethical standards. These provide investors to evaluate and query the decisions made by the board and its sub committees (King Committee on Corporate Governance, 2002).

Responsibility: Responsibility encompasses behavior that supports remediation and penalizes poor oversight. Effective and responsible management implements measures to guide the company toward corrective action. The board holds accountability and must demonstrate both responsive and a strong sense of responsibility toward all stakeholders (King Committee on Corporate Governance, 2002).

Fairness: Internal systems within the organization must strike a balance by considering the interests of all parties who have participated in their operations and their future. It is essential to recognize and respect the rights of different groups. For instance, the interests of minority shareholders should be given the same level of consideration as those of the majority shareholders (King Committee on Corporate Governance, 2002).

The globalization of business has led to debates on whether corporate governance practices are becoming more uniform worldwide or diverging due to cultural and regional distinctions (Rossouw, 2009). Various factors shape the evolution and application of corporate governance systems on an international scale. These include Ownership patterns which include insider and outsider systems, the dominant perception of the firm's role within the society, along with cultural and societal norms, and socio-political priorities.

Ownership Patterns: Insider systems of corporate governance have heavily concentrations among families or government entities or both, and owners directly intervene in how the company is run and they depend more on borrowing than on issuing shares, offering smaller investors minimal safeguard and tending to favor stakeholder-oriented ethics of corporate governance (Rossouw, 2009). While outsider systems have broadly distributed ownership, prioritize the rights of all shareholders both major and minor, which depends on equity rather than debt, and align more with shareholder focused principles of corporate conduct (Rossouw, 2009).

View of the Firm: The prevailing view within society or region regarding what role a company is expected to play significantly influences the ethical approach to overseeing the business operations. When the dominants perspective sees firms primarily as a profit generating tools for investors(Mono-purpose conceptions of the firm), resulting governance tends to prioritize shareholder interests, while the enterprises are viewed as multi purposes within the social and economic fabric (Multi-purpose conception of the firm), governance systems evolve to reflect broader responsibilities to various interests groups (Rossouw, 2009).

Cultural and Societal Norms: For a corporate governance framework to work efficiently, it must be embraced for the local business environment and the broader public contexts. The norms, beliefs, and cultural principles present in the surrounding community in the company functions shape both the corporate governance practices and their underlying ethics (Rossouw, 2009).

Socio-political Priorities: In regions undergoing economic transformation or structural change, businesses are anticipated to actively engage in the development or transition processes which lead to stakeholder oriented approach in corporate governance, and in contrast to these economies, developed economies have less pressure for companies to be involved in socio-political processes (Rossouw, 2009).

Legal system: Countries whose legal system is rooted in common law, which prevailed in the UK and US, tend to favor shareholder-oriented governance regimes, and countries whose legal framework follows civil law which is more common in Continental Europe, may find greater acceptance of stakeholder-oriented approaches (Cornelius, 2005).

According to these, it is crucial to emphasize that effective corporate governance can take many forms. The best approach will vary according to the specific circumstances of the company and the country in which it operates.

The G20/OECD guidelines for corporate governance serve as the main global standard for good governance practices. They aim to support policymakers in evaluating and improving the legal, regulatory, and institutional structures that shape corporate governance and thereby promoting market trust, boosting economic performance, and ensuring financial system stability (OECD, 2023). These principles are not legally binding and do not intend to offer an exhaustive description of national laws, instead they aim to highlight the objectives and suggest various means to accomplish them (OECD, 2023). However, OECD principles of Corporate Governance signify a substantial effort to foster a shared understanding of effective corporate governance practices on a global scale.

The company's' corporate governance standard can be assessed using different measures. Few of them can be categorized as follows,

Size of the board: The board members serve as an essential function in an organization by carrying out the duties within the organization in the favorable interests of the people

who appoint them. Organizations board of directors play a crucial role in safeguarding reliability of financial statement information and are charged with ensuring oversight of the senior management to confirm that their activities in line with the interest of key parties such as investors, creditors, shareholders, and other stakeholders (Dimitropoulos & Asteriou, 2010). Researchers contend that larger board decreases overall efficiency and the one who is favorable to smaller board argues that smaller board size has a likelihood of getting full consensus in a decision and genuine communication and greater interaction (Salehi & Asgari, 2013).

Independence of the audit committee: Recently the duties of the audit committee have increased from auditing the firm's financial reporting and disclosure process, because they serve as the tool for evaluating good corporate governance (Hamdan, 2020). Committees overseeing financials of the company that operate separately from executive leadership play a key role in supporting the board of directors' oversight function and help to mitigate low quality reporting (Siagian & Tresnaningsih, 2011).

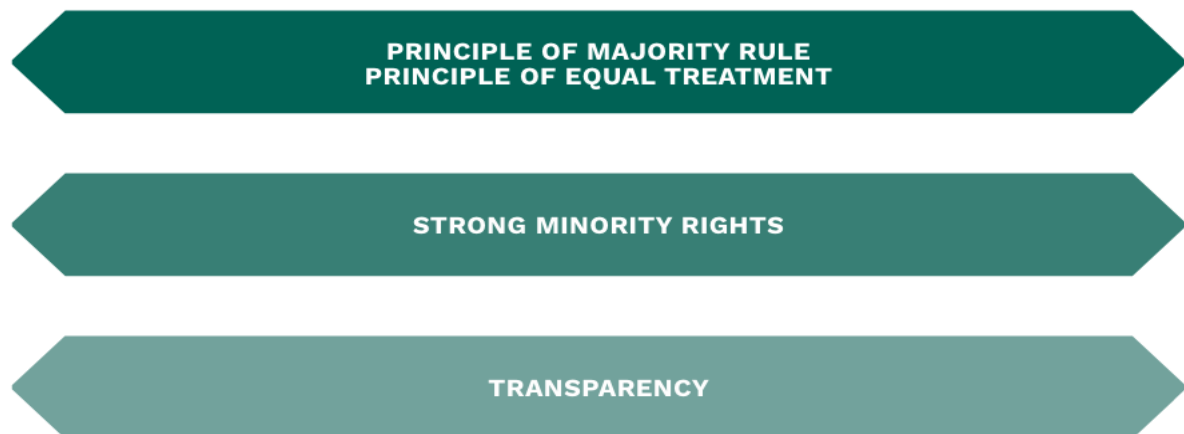
CEO duality: CEO duality describes a governance arrangement where a single individual simultaneously occupies the positions of chief executive officer and chairperson of the board. The existence of a CEO also serves as the chair of the board can undermine the boards, and audit committee's ability to properly oversee the quality of financial reporting (Kamarudin, et al., 2012). Agency theorists suggest that CEOs with too much power may act in their personal interest rather than acting in favor of the general investors and the organization's monetary targets (Arif, et al., 2023).

Non-Executive in the Boards: Empirical evidence suggests that greater extent to which the boards consists of independent, non-management members, are significantly contribute to safeguard the objectives of the owners, improve overall board effectiveness and non-executive members have an vital role in addressing the agency problems (Salehi & Asgari, 2013).

Reward of board: Beyond overseeing the CEO's action, shareholder protection can be strengthened by rewarding the CEO based on the achievement of the goals which are align with of the shareholders' and ensuring that the incentives are performance based (Salehi & Asgari, 2013).

2.1.1.1 Corporate Governance in Finland

Finland, a member of the European Union has an efficient and flexible corporate governance model that is grounded in the principle of majority rule, which allows shareholders to have a significant ownership influence. However, to prevent abuse, this principle is counterbalanced by the principle of equal treatment, qualified majority requirement, and the rights of minority shareholders (Finnish Corporate Governance Code, 2025). The foundation of good corporate governance in Finland is based on a combination of laws, decrees issued based on them, regulations, and best practices (cgfinland.fi, n.d.). Key legal provisions underpinning this framework include the Limited Liability Companies Act, the Securities Market Act, the Auditing Act, and the Accounting Act, also Finnish listed companies must follow EU-level regulations and rules of the Helsinki Stock Exchange, which include the Corporate Governance Code and its reporting requirements, and regulations and guidelines of the Financial Supervisory Authority (Finnish Corporate Governance Code, 2025).



Picture 1. Key Features of Finnish Corporate Governance Model (Source: Finnish Corporate Governance Code)

2.1.2 Earnings Quality

A key intention of engaging in financial analysis is to assess the company's overall performance comprehensively. This evaluation involves analyzing various financial metrics, ratios, and trends to gain a clear insight into the operational effectiveness of the organization, profitability, and strength of the financial standing. To ensure an accurate assessment of the organization's true performance, it is vital to assess the consistency and integrity of its earnings.

Earnings quality is a crucial concept in accounting and finance that offers valuable insights into an organization's financial performance and its capacity to produce sustainable and reliable profits. It reflects the magnitude of reported earnings accurately representing the economic performance of the company (Krishan & Persons, 2008). While it appears a simple concept, earnings quality is multifaceted and lacks a universally accepted definition. Different financial statement users hold different views on what defines high quality earnings. As an example, auditors often interpret fraudulent reporting as stemming from earnings quality issues, driven by atypical items and insufficient clarity

in the reported earnings even if these earnings comply with Generally Accepted Accounting Principles (GAAP). Regulators primarily assess high-quality earnings based on adherence to GAAP guidelines and creditors assess earnings quality by how readily earnings can be transformed into cash flow, which ensure liquidity and repayment capacity whereas compensation committee considers earnings to be reliable if they genuinely reflect executives' actual performance and are minimally influenced by external factors beyond managerial control (Islam, et al., 2022). Therefore, it depends on the information needs and decision contexts. The complexity arises because the reported earnings are impacted not only by a organization's fundamental performance but also by the accounting choices and estimates made in the measurement process (Dichev, et al., 2013).

There are several ways of defining earnings quality and each emphasizes different aspects of decision usefulness. Many Chief Financial Officers (CFOs) believe that high-quality earnings can be maintained and replicated over time and they emphasize specific characteristics such as consistent reporting practices over time, alignment with real cash flows, and the exclusion of non-recurring items and long-term estimates, factors essential to ensuring earnings sustainability (Dichev, et al., 2013). Also, this perspective focuses on the long-term profit-generating ability of a firm, suggesting that current earnings reflect strong quality if they provide a reliable indicator of the future profitability (Dichev, et al., 2013). One way to understand earnings quality is as how well the disclosed earnings reflect accurate, trustworthy, and meaningful insight about an organization's underlying financial performance (Nasution & Jonnergård, 2017). This indicates the importance of transparency and the absence of manipulation or bias in the reported numbers. Higher the quality of earnings offers greater insight into the company's financial aspects that matter most for particular decision making (Dechow, et al., 2010). This definition emphasizes the conditional nature of earnings quality, acknowledging that varying decision-making contexts may necessitate emphasizing different attributes of earnings. Schipper & Vincent, 2003 define high-quality earnings as those that fully represent the Hicksian income, which is the change of total wealth. In another way, the quality of

earnings increases, when accounting income is more closer to the economic income (Rezaee & Safarzadeh, 2022).

Measuring earnings quality presents significant challenges, as it involves a complex analysis of various financial and operational factors. There is no universally accepted metric or standardized approach for assessing earnings quality. Instead, researchers have developed numerous proxies, each targeting different aspects of earnings quality.

Table 1. Earnings Quality Proxies (Measurements)

Category	Indicators
Properties of earnings	<ul style="list-style-type: none"> • Earnings persistence • Abnormal accrual and modeling the accrual process • Earnings smoothness • Asymmetric timelines and timely loss recognition • Target beating
Investor responsiveness to earnings	<ul style="list-style-type: none"> • Direct evidence on Earning Response Coefficient (ERC) as a proxy for earnings quality
External indicators of earnings mis-statements	<ul style="list-style-type: none"> • Firms subject to SEC enforcements (Accounting and Auditing Enforcement Releases (AAERs)) • Restatements • Internal control deficiencies

Source: (Dechow, et al., 2010), P.346

Properties of earnings examine the nature of financial results to determine their overall quality.

Earnings persistence: This metric assesses how likely current earnings are to continue over time. Higher persistence generally indicates higher earnings quality, suggesting greater sustainability and profits (Kalembe, et al., 2024). This can be calculated by regressing future earnings on current earnings, often controlling other factors such as operational cash movements and adjustments through accruals (Dechow, et al., 2010).

Accruals Quality: Accruals, defined as the portion of earnings not represented by cash transactions, can be used to assess the earning quality. Accrual reliability indicates that accruals are informative about future cash flows and less likely to be manipulated. Common measures of accrual quality include discretionary accruals and accrual estimation errors. Discretionary accruals are portion accruals considered to be managed by managers for opportunistic purposes. Lower discretionary accruals indicate a greater earnings integrity (Dechow, et al., 2010). The discretionary accruals can be estimated using different models, including the modified Jones model, which involves regressing total accruals against variables such as changes in revenues and fixed assets (Saona, et al., 2023). Accruals estimation errors reflect the difference between estimated accruals and the actual cash flows realized in subsequent periods and lower estimation errors suggest higher accruals quality.

Earnings Smoothness: This metric assesses the degree to which earnings are smoothed over time, potentially masking underlying volatility in performance. While some smoothing can be informative, excessive smoothing can be indicative of earnings manipulation and lower earnings quality (Rezaee & Safarzadeh, 2023). This can be determined by taking the ratio of variability in operating income to the variability in sales revenue. A lower ratio indicates greater smoothness (Rezaee & Safarzadeh, 2023).

Asymmetric Timeliness: This measure examines whether positive and negative news are incorporated into earnings with equal timeliness. Asymmetric timeliness where negative news is recognized more slowly than positive news may indicate practices of manipulating financial results and a diminishing earnings reliability (Kalembe, et al., 2024).

Timeliness can be assessed by examining the speed with which earnings respond to positive and negative changes in underlying economic performance.

Target Beating: This approach focuses on the tendency of firms to control earnings to match or surpass forecasts of analyst or other performance targets. Frequent target beating, especially by narrow margins, may serve as a warning sign of potential earnings manipulation and lower earnings quality (Thesing & Velte, 2021). This can be measured by examining the distribution of earnings relative to the analyst forecast.

Investor responsiveness to earnings assesses the informativeness of earnings by examining how investors react to earnings announcements. The Earnings Response Coefficient (ERC) captures the sensitivity of stock prices to unexpected earnings. A higher ERC suggests that earnings are more informative and high-quality (Kalembe, et al., 2024).

Signs of earnings manipulation, such as regulatory actions and financial restatements, are key indicators of potential issues with earnings quality. Financial statement restatements, for instance, are widely recognized as a strong indication of prior earnings quality problems. (Bazrafshan, et al., 2021). These restatements are typically measured by binary variables where the assigned value is one if a firm restates its earnings and zero otherwise. Another important indicator is the issuance of Accounting and Auditing Enforcement Releases (AAERs) by the Securities and Exchange Commission (SEC), which highlights accounting irregularities and signals of accounting misconduct (Dechow, et al., 2010). Additionally, significant flaws in internal controls over financial reporting are considered indicators of an increased risk of earnings misstatements and leading to decrease overall financial integrity of the reporting (Dechow, et al., 2010).

2.2 Theoretical Review

How CG practices influence the integrity of reported earnings has been the subject of extensive research, with various theoretical frameworks providing insights into this

complex interplay. This section provides key theoretical foundation that support the research. It begins with a discussion of agency theory and then explores stewardship theory, stakeholder theory, sociological theory, resource dependency theory, and finally transaction cost theory. This structured review establishes the theoretical foundation for examining the interplay between corporate governance and earnings quality.

2.2.1 Agency Theory

Agency perspective addresses challenges that exist in an organization due to the division of the organization's ownership and managerial control. It focuses on the reduction of this problem. An agency relationship refers to a contractual agreement in which one or multiple parties (referred to as principals) who designate a separate party (the agent) to perform tasks in place of them, thereby permitting the agent a certain level of decision-making authority. However, when both parties are driven by the goal of maximizing their personal benefits, there is a likelihood that the agent's action may not fully reflect the goals of the principal (Jensen & Meckling, 1976). This problem exists in large organizations where the owners assign tasks to managers to manage the firm with the hope that managers act for the benefit of the owners. This can be mitigated by creating proper incentives for the agent and bearing monitoring expenses to restrict the agent's undesirable behavior, while in some cases, the agent may also bear costs (known as bonding cost) to assure the principal that harmful actions will be avoided or compensated if they occurs (Jensen & Meckling, 1976). Formal oversight structures, including independent board members and audit committees, are seen as tools to mitigate such agency problems and enhance earnings quality (Rezaee & Safarzadeh, 2022).

2.2.2 Stewardship Theory

According to stewardship theory, managers are viewed as stewards of the shareholders' funds in the business, and they behave collectively because they are trying to accomplish

the organizational goals as a whole. As per the stewardship theory, managers and top-level executives focus on their roles with a higher purpose, acting not as greedy individuals and prioritizing the interest of the organization and its investors over personal gains (Davis, et al., 2000). According to Davis, Schoorman, Mayer, & Tan, (2000), Stewards or managers exhibit a deep sense of commitment to the organization and its objectives, and they are intrinsically motivated to contribute to the well-being of the company and the broader community. Their long-term vision and commitment can drive innovative efforts that enhance organizational capabilities and deliver superior returns on investments (Jasir, et al., 2023).

Overall, stewardship theory provides an insightful framework for understanding managerial behavior in environments where intrinsic motivation and shared sense of purpose drive actions. By recognizing the motivations and potential challenges faced by stewards, organizations can develop governance structures that effectively leverage the strengths of this approach while addressing potential drawbacks.

2.2.3 Stakeholder Theory

The stakeholder theory posits that an organization's success is influenced by a wide range of individuals and groups, both internal, such as owners, employees, and customers, and external, such as competitors, governments, and the media to the organization. This theory challenges the conventional shareholder focused perspective of corporate governance because the theory proposes that managers must account for the interest of all stakeholders and not solely those of the shareholders (Stoelhorst & Vishwanathan, 2024). This theory highlights the interconnectedness between an organization and its stakeholders, recognizing that each group can both affect and be affected by the organization's performance. The theory argues for a shift in focus from maximizing shareholder value to creating value for all stakeholders (Stoelhorst & Vishwanathan, 2024). Therefore, stakeholder theory suggests that top management is bound to maintain a

connection covering multiple parties, including employees, suppliers, environmental and political groups, and other third parties rather than focusing solely on shareholders.

2.2.4 Sociological Theory

The corporate governance perspective grounded in sociological theory primarily discusses the Board of Directors structure and composition, which also focuses on how power and wealth distribution in society can be affected. This theory discusses how “director interlocking” could lead to an oligopoly of power, which is a scenario where decision-making power concentrated on a few privileged business groups could challenge the social equity and economic progress of society. The interlocking director network, which emerges from directors’ holding positions across multiple companies, plays a pivotal role in shaping the governance dynamics (Feng, et al., 2024).

The good corporate governance framework must address these risks by ensuring transparency, accountability, and diversity in board compositions. By mitigating excessive concentration of power, a governance framework can promote fair decision-making processes that align with the interests of all stakeholders and support sustainable societal and economic growth.

2.2.5 Resource Dependency Theory

Resource Dependency Theory (RDT) emphasizes how organizations rely on external resources, including financial, physical, and informational assets (Bolton, et al., 2024). RDT recognizes the inherent uncertainty of the commercial environment and emphasizes the necessity for entity to actively manage their interdependencies with external resources to mitigate this uncertainty. This theory suggests that a companies with a larger and more heterogeneous board is beneficial for a company due to broader range of expertise

and improved access to valuable resources and theory posits that women on board is believed to bring a unique perspective and strategic advantageous (Kyei, et al., 2022).

According to the RDT theory, organizations are not self-sufficient, and they must actively manage their relationship with the external environment to acquire the necessary resources for survival and success. This involves strategic actions such as forming diverse boards, engaging in mergers, and leveraging social networks. Therefore, in terms of corporate governance, RDT suggests that an entity's board serves a vital function in securing access to external resources.

2.3 Empirical Literature Review

2.3.1 CEO duality and earnings quality

Chief Executive Officer (CEO) duality occurs when CEO also hold the position of the board's chairman, which is a significant issue in corporate governance as it impacts the balance of power and the effectiveness of board monitoring. This arises from the fact that the CEO is both making decisions and monitoring those decisions, which compromises corporate governance and creates the likelihood of manipulating earnings. Therefore, it is important to explore the connection between CEO duality and earnings quality.

The research conducted to assess the interaction of CEO duality with quality of earnings revealed that the coexistence of CEO and chairperson duties in one individual has an adverse impact on the quality of reported earnings (Alves, 2021). This research draws its information from the annual reports and corporate governance reports of Portuguese publicly traded non-financial organizations spanning the years 2002 through 2016. This study employs a regression model to investigate the relationship between CEO duality and earnings quality. CEO duality was captured using dummy variable, where a value of 1 was assigned if the same person held both the CEO and board chairperson, and 0 if the roles were separated. Earning quality is measured through discretionary accruals,

calculated using modified Jones model with a cross-section estimation approach, as commonly used in accounting research (Alves, 2011). According to Alves,(2021), the key insights derived from the research revealed that Portugues regulatory framework did not mandate CEO and chairman role separation. This lack of seperation may create conditions that favor the strategic presentation or alteration of financial information. Consequently, the results provide empirical support for recommendations against CEO duality by demonstrating that concentrated leadership power can adversely impact credibility of reported data (Alves, 2021).

The research investigated the influence of CEO power dynamics on a Financial Reporting Earnings Quality (FREQ) utilizing the data from Egyptian publicly traded firms from 2012 to 2021, suggested that dimentions of CEO influence, including dual role occupancy, ownership stakes, length of tenure, and CEO's network connections, negatively impact FREQ (Hemdan, et al., 2023). This suggests that powerful CEOs have higher probability to engage in earnings manipulation. The study used a modified Johns model to measure discretionary accruals, which is used to assess the earnings quality and the investigation highlights the importance of corporate governance mechanisms such as board independence and gender diversity as ways to constrain CEO power and mitigate the negative impact on FREQ (Hemdan, et al., 2023).

The study on how powerful CEOs affect earnings quality in Bangladesh revealed that powerful CEOs have a significant adverse impact on quality of earnings (Arif, et al., 2023). This suggested that CEOs who hold greater authority tends to enagage in both accounting and operational manipulations to influence earnings. This study identified four sources of CEO power. Ownership power which measures the CEO's share ownership and that of their family, and is shown a detrimental effect on the reliability earnings, structural power which is hierarchical influence stemming from the chief executive officer seat on the board and their influence on decision-making, shown to possess a negative correlation with earnings quality, expert power which related to CEO's tenure and professional experience is shown an inverse relationship with qulity of earnings, and

prestige power which is related to the CEO's educational background have an insignificant effect on earnings quality (Arif, et al., 2023). The study used non-financial organizations traded on the Dhaka Stock Exchange in Bangladesh throughout the decade beginning in 2010 and ending in 2019 and used two proxies to indicate quality of earnings, which are discretionary total current accrual which is derived from the modified Johns model, and discretionary total accruals (Arif, et al., 2023).

The study explored on how audit committee independence relates to earnings quality and the influence of CEO duality on this relationship investigated by Kamarudin, Ismail, & Samsuddin, (2012) revealed that audit committee independence is positively link with higher earnings quality, however this link is weakned when the CEO simultaneously serves as the board chairman. This indicates that when a CEO has too much control, the overseeing duty performed by the audit committee becomes less effective. The study used data from non-financial companies listed in Malaysia from 2005 to 2010 and used an ordinary least squares (OLS) regression model to test the hypotheses. Earnings quality was measured using McNichols' (2002) cross sectional model of accrual quality and independence of the audit committee and CEO duality were operationalized as a binary variable, coded "1" when present and "0" when not. The study supported the recommendations of the Malaysian Code of Corporate Governance 2012, which emphasizes the noteworthy of an independent audit committee and separation of roles between CEO and chairman of the Board (Kamarudin, et al., 2012).

Drawing from existing empirical studies examining the relationship between CEO duality and earnings quality, the evidence suggests that the combining decision-making and oversight responsibilities within a single individual (CEO) can undermine the strength of corporate governance.

2.3.2 Independence of the audit committee and earnings quality

The independence of the audit committee plays a influential role in ensuring the integrity and transparency of financial reporting processes. As an essential governance mechanism, the audit committee oversees financial reporting, internal control, and the external audit process, making its effectiveness a cornerstone of sound corporate governance. Major factor affecting a committee's performance is its level of independence, as independent members are assumed to prioritize shareholder interest over managerial influence. Considerable research has explored how independence of the audit committee influences earnings quality in contexts outside of Finland.

Song, (2022) investigated role of audit committee features such as autonomy, professional knowledge, engagement level, and authority in shaping the association between corporate social responsibility (CSR) and the quality of earnings among Korean entities publicly traded on the Korean Stock Exchange during the period 2011 to 2015. The study concluded that active audit committees enhance the financial reporting standards of firms, engaging in ethically motivated CSR. Specifically, the greater audit committee engagement was linked to tighter constraints on earnings management via discretionary accruals. The ressearch further investigated that audit committees exhibit higher effectiveness when they include independent members, accounting professionals, demonstrate strong participation, and possess relative power (Song, 2022). The multivariate regression was employed to assess these impacts by researcher.

Hamdan (2020) conducted an empirical study examining how specific characteristics of the audit committee affects the quality of financial earnings reporting. Drawing data from manufacturing firms listed on financial markets of Gulf Cooperation Council(GCC) countries between 2014 to 2018, revealed that audit committees with greater size and independence are connected with a positive impact with higher earnings quality in GCC industrial companies. The analysis used three key audit committee atributes; independence, size, and diligence. The independence of the audit committee independence is characterized by the presence of non-executive members, whereas its

size is determined based on the overall count of its members. The quality of earnings is assessed through the DeAngelo model and accrual accounting, where accruals are determined by the year to year difference between net operating profit after interest and taxes and the corresponding variation in operating cash flows (Hamdan, 2020). Specifically, independent audit committees contribute positively and significantly to the quality of reported earnings and larger audit committees are linked to higher earnings quality, whereas the diligence of the committee measured by how often it meets, did not show meaningful effect (Hamdan, 2020).

The thesis explore the role of independent board members and leadership structure within oversight committees in relation to the reliability of financial reporting, concluded that having independent board members and oversight committees contributes positively to the credibility of reported earnings (Siagian & Tresnaningsih, 2011). The analysis excluded companies operating in sectors such as banking, finance, insurance, real estate, property, and telecommunication industries and explored the impact of meeting Jakarta Stock Exchange (JSX) requirements, which mandate at least 30% independent members and oversight committees to include a minimum of three independent individuals (Siagian & Tresnaningsih, 2011). Reliability of reported earnings evaluated through two indicators, discretionary accruals and the earnings response measure and Multivariate regression was applied to assess changes in reporting credibility following firms' adherence to JSX governance standards (Siagian & Tresnaningsih, 2011). The study highlighted the value of appointing board members with no executive affiliations and establishing oversight committees led by independent individuals.

Empirical research indicate that supervisory panels comprised largely or exclusively of non-executive members, is better positioned to fulfill its oversight responsibilities, thereby enhancing the credibility of reported financial information.

2.3.3 Board size and earnings quality

The number of directors on an organization's board serves as a pivotal role in shaping governance mechanisms and influencing the standard of financial disclosures. Corporate boards have the duty to supervise the reliability of financial informations, ensuring that senior executives acts in alignment with the goals and expectations of stakeholders, including creditors, investors, shareholders, and other related parties of the organization (Dimitropoulos & Asteriou, 2010). Numerous researchs have explored the connection between the number of board members and quality of earnings.

The research examined how board composition, including board size, influences the informativeness and reliability of annual earnings in publicly traded Greek firms between 2000 and 2004, found that a positive correlation between the proportion of independent directors on the board and the informativeness of annual financial reports (Dimitropoulos & Asteriou, 2010). This suggests that a board composed of a higher proportion of independent directors can improve both the reliability and decision usefulness of financial disclosures. However, Dimitropoulos & Asteriou, (2010) found that there is no significant relationship between board size and the informativeness of earnings.

Salehi & Asgari (2013) investigated the impact of corporate governance factors on earnings quality by examining 94 entities traded on the Tehran Stock Exchange over the years 2006 to 2010. The study used variables such as board size, audit committee structure, the proportion of stockholding and non-executive directors, and overall management effectiveness. Earnings quality (EQ) was assessed using discretionary accruals, which is calculated using the balance sheet approach and the modified Jones model. The study found board size, the number of non-executive directors, and the audit committee's scale were significantly associated with EQ suggesting these governance mechanisms contributes credibility of financial reportings (Salehi & Asgari, 2013).

According to these findings larger board brings broader range of skills, knowledge, and viewpoints which strengthen their ability to supervise and evaluate the financial reporting activities effectively.

Numerous scholars have examined how corporate governance influences earnings quality, primarily focusing on regions outside of Finland. Prior researchers have utilized a range of governance related factors to analyze their samples and applied diverse techniques to assess the earnings quality in their respective fields. Their findings have provided differing perspectives on the corporate governance effect on earnings quality. Hence it would be valuable to investigate how the corporate governance influences on earnings quality within the context active listed companies in Finland. Such research could help Finnish companies mitigate earnings manipulation activities by management and improve openness and integrity in financial reporting.

3 Methodology

3.1 Research Design

Multiple approaches to research designs used by researchers to allow the results to be interpreted with a minimum degree of ambiguity. Such designs include descriptive or exploratory, correlational, quasi-experimental, experimental, review, and meta-analytic (Byrne, 2017). This particular study adopts descriptive research design, as it aids in answering questions related to the who, what, when, where, and how of a given research problem. However, it does not aim to conclusively determine the reason behind the phenomena. Descriptive research is used to collect data reflecting how things presently are and to outline the characteristics or relationships among elements within a defined context.

3.2 Research Approach

Two research approaches are used by researchers: inductive and deductive. In inductive research, the process starts by examining specific phenomena, which are then used to develop concepts and theories. This approach typically involves qualitative methods such as case studies and ethnographic research (Woiceshyn & Daellenbach, 2018). Deductive research follows a top-down approach, beginning with an existing theoretical framework, from which hypotheses are formulated and empirically tested, and then outcomes are used to refine or adjust the original theory (Woiceshyn & Daellenbach, 2018). This research is related to the deductive approach as it uses quantitative methods to collect data for the thesis.

3.3 Population

The research focused on a population consisting of 202 active Finnish firms based in Finland, all of that were publicly traded on the Helsinki Stock Exchange as recorded on 20th of February 2025.

3.4 Sample

A sample refers to a subset of the broader population, made up of specific elements, rather than the whole group. This study sample includes 91 out of 202 active Finnish firms listed on the Nasdaq Helsinki.

Table 2. Sample

Description	Amount
Number of active Finnish companies listed on Helsinki Stock Exchange	202
Number of companies in the sample	91

3.5 Method of Data Collection

The data consists of two main sources: primary and secondary. Primary sources refer to the original point at which any given information first appears, while secondary sources are documents that interpret or analyze primary source material. This study utilizes secondary data to analyze the selected research sample. The dataset for the thesis is to be obtained through an examination of publicly available financial disclosures issued by the firms selected for analysis.

3.6 Calculation Methods

The objective of this research is to explore how corporate governance influences the quality of reported earnings. To explore the connection between these two factors, discretionary accruals (DAs) can be used as an indicator of the quality of earnings. Accrual accounting elements are components of reported earnings which do not correspond directly with present period cash flows and discretionary accruals are the components of total accruals that are subject to manipulate earnings (Alves, 2021) and (Al-Thuneibat, et al., 2016).

The adjusted Jones framework evaluates accruals by incorporating multiple factors, such as variations in revenue, shifts in accounting receivable, and the amount of gross fixed assets including property, plant, and equipment (PPE) (Alves, 2021). First, we need to calculate the Total Accruals (TA), followed by the computation of the portion considered non-discretionary. This allows for the separation of total accruals into their discretionary and non-discretionary (Al-Thuneibat, et al., 2016).

$$TA_{it}/A_{it-1} = \phi 1_{jt} (1/A_{it-1}) + \phi 2_{jt} [(\Delta REV_{it} - \Delta AR_{it})/A_{it-1}] + \phi 3_{jt} (PPE_{it}/A_{it-1}) + \epsilon_{it} \quad (1)$$

Where,

TA_{it} = For company i in the year t , total accruals are derived by subtracting cash flow from operating activities from net income before extraordinary items ($TA_{it} = NI_{it} - CFO_{it}$)

A_{it-1} = total assets for the previous period

ΔREV_{it} = revenue for company i , in time t less revenues in $t-1$

ΔAR_{it} = accounts receivable in time t less accounts receivable in $t-1$

PPE_{it} = gross property plant and equipment for company i in year t

NI_{it} = net income amount of company i at year t

CFO_{it} = amount of cash flow from operations of company i at year t

After calculating the TA needs to calculate non-discretionary accruals (NAs).

$$NA_{it}/A_{it-1} = \{\phi_1 (1/A_{it-1}) + \phi_2 [(\Delta REV_{it} - \Delta AR_{it})/A_{it-1}] + \phi_3 (PPE_{it}/A_{it-1})\} \quad (2)$$

Once the non-discretionary portion of accruals is determined, the discretionary component is calculated using the below equation,

$$DA_{it} = (TA_{it}/A_{it-1}) - (NA_{i,t}/A_{it-1}) \quad (3)$$

All the relevant data for calculating the DAs, with the adjusted Jones model are sourced from obtained from the companies publicly available annual reports and databases.

To assess the level of company's governance practices, utilize three variables: CEO duality, independence of the audit committee, and total number of board of directors.

3.7 Measurements of variables in the study

The study incorporates multiple factors, with the quality of earnings serving as the dependent variable, which is qualifying through total accruals. The independent variables are CEO duality, independence of the audit committee, and board size. Measurements methods for these variables are summarized below.

Table 3. Measurements of the variables

Variable	Measurement
Dependent Variable	
Total Accruals	(Net Income-Cash flow from operation)/Total Assets
Independent Variables	
CEO duality	Coded "1" if CEO also hold the position of chairman.

Independence of the audit committee	Percentage of independent directors in the audit committee.
Size of the board	Number of board of directors exist in the company.

3.8 Conceptual Framework

The conceptual framework developed for this research is shown below.

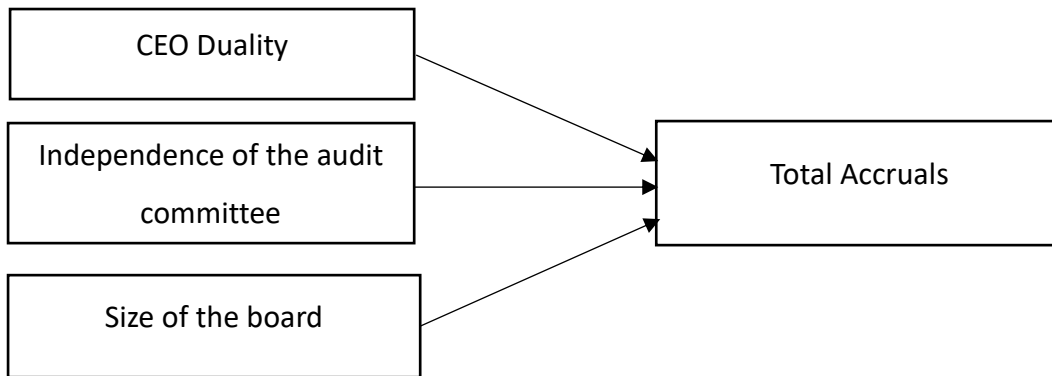


Figure 1: Conceptual Framework

3.9 Method of Analysis

After calculating the Discretionary Accruals (DAs) and determining the level of corporate governance associated with the respective companies, a panel regression model was employed to examine the relationship between corporate governance and earnings quality.

$$TA_{it} = \beta_0 + \beta_1 IAC_{it} + \beta_2 SBOARD_{it} + \beta_3 CEOD_{it} + \epsilon_{it} \quad (4)$$

TA_{it} = Level of TAs for a company i at time t

IAC_{it} = Compliance with audit committee requirement by company i at time t

$Sboard_{it}$ = Compliance with board of directors' requirement by company i at time t

$CEOD_{it}$ = Compliance with CEO duality by company i at time t

4 Data Analysis and Results

4.1 Introduction

This chapter contains statistical and econometric regression outcomes which helps to determine the impact of corporate governance on earnings quality of active listed companies in Finland during the time period of 2017 – 2023 by carrying out panel data regression model using EViews software. EViews have been used to find descriptive statistics, variables correlations and the results of regression models that assess the explanatory variables on the outcome variable. Additionally, to descriptive statistics, correlation and regression results, this chapter contains an interpretation of the thesis findings to determine whether the research objectives outlined in Chapter one have been successfully met.

4.2 Descriptive Statistics

Table 4. Descriptive Statistics (EViews Output)

	TACC	IAC	SBOARD	CEOD
Mean	-0.048536	84.24553	7.447410	0.131868
Median	-0.044350	100.0000	7.000000	0.000000
Maximum	0.420934	100.0000	17.00000	1.000000
Minimum	-0.437399	0.000000	3.000000	0.000000
Std. Dev.	0.055804	21.06331	2.111472	0.338613
Skewness	-0.374766	-1.672535	1.367702	2.176059
Kurtosis	19.10368	5.919295	5.819281	5.735232
Jarque-Bera	6897.921	523.1835	409.5585	701.2951
Probability	0.000000	0.000000	0.000000	0.000000
Sum	-30.91712	53664.40	4744.000	84.00000
Sum Sq. Dev.	1.980529	282169.6	2835.488	72.92308
Observations	637	637	637	637

The table outlines a key statistical details of the dataset's descriptive statistics, covering the chosen sample of operating Finnish organizations traded on Nasdaq Helsinki during the period spanning from 2017 to 2023. It summarized the key characteristics of the variables used in the study, including central values and distribution patterns. Central tendency is presented by metrics such as the mean and median, while dispersion is captured using standard deviation, range (minimum and maximum), skewness and kurtosis.

According to the above table, the dataset includes of a total of 637 firm year observations, representing 91 active Finnish firms publicly traded on the Nasdaq Helsinki Stock Exchange across the seven-year span from 2017 to 2023. Each observation reflects to a single company in a specific year, thereby includes the annual financial and accounting data relevant to evaluate the link between corporate governance on earnings quality. The variable includes Total Accruals (TACC), Independence of the Audit Committee (IAC), Size of the Board (SBOARD), and CEO Duality (CEOD). Total accruals (TACC) serve as the dependent variable of the study and proxy for the earnings quality and independence of the audit committee (IAC), size of the board (SBORAD), and CEO duality represent the independent variables of the study and proxy for corporate governance. As per the analysis, using the statistical software of EViews there are not any missing variables in the sample as shown in the above table.

The mean value of the TACC is -0.0485 and standard deviation is 0.0558 indicate moderate variation in accrual levels across firms and years. The negative mean implies that the general trend of income decreasing accruals across the sample organizations. the median or the middle value after sorting the observations is -0.0443 . The upper and lower value of the total accruals range from 0.4209 to -0.4373 which shows a considerable dispersion. Moreover, the distribution of the TACC is negatively skewed (-0.37) and leptokurtic which indicates a positive kurtosis of 19.10 . And Jarque Bera test confirms that the non-normal distribution.

IAC shows the mean value of 84.25% and standard deviation of 21.06 which reflects how far the observations are from the mean value. The maximum and minimum value range from 100 to 0 show that the varying levels of independence of the audit committee across the sample firms. IAC is negatively skewed with -1.67 and non-normally distributed as per the Jarque Bera statistic because the P value of 0.

The size of the Board (SBOARD) mean value indicates 7.45 members, which indicates the average value of the sample firm represents 7 members on the board. The Median or Middle Value of SBOARD shows 7 members with a maximum of 17 members and minimum of 3 members. The positive skewness of 1.36 and leptokurtic or high value kurtosis indicates a right tailed distribution.

CEO duality (CEOD), which indicate 1 and 0 values for the sample reflects cases where the CEO simultaneously serves the chairperson of the board, which has a mean value of 0.13, which shows that roughly 13% of the observations, CEO also hold both the roles. The distribution demonstrates a pronounced rightward skew, indicated by a skewness value of 2.17 and kurtosis of 5.73, which suggest most firms opting for role separation.

4.3 Correlation Matrix

Table 5. Correlation Matrix (EViews Output)

	TACC	IAC	SBOARD	CEOD
TACC	1.000000			
IAC	0.048767	1.000000		
SBOARD	0.093723	0.067127	1.000000	
CEOD	0.041115	-0.199033	-0.060658	1.000000

A correlation coefficient quantifies the association between two data points, which reflects how changes in one variable are expected to change against the value of another variable. In positive correlation, when one variable increase or decreases, another variable also increases or decreases in the same direction. And when one variable negatively

correlates with one variable, it causes an increase in one is typically associated with a decrease in the other and vice versa.

Values of correlation coefficients lie within the range of -1 to +1. The correlation coefficient of +1 indicates perfect positive relationship, where an increase in one variable consistently corresponds to an increase in another. Conversely, a coefficient of -1 represents a perfect negative relationship, meaning that as one variable increases, the other decreases. And the correlation coefficient value equal to 0 implies no linear association between the variables.

According to the above EViews output, total accruals show mildly positive association with audit committee independence, as it indicates the correlation coefficient of 0.05 which is between the range of 0 to 0.3. The correlation coefficient of 0.093 indicates the correlation with size of the board and total accruals and it indicates a positive weak relationship with the total accruals. The correlation between CEO duality and total accruals also specified a weak positive relationship as its coefficient is 0.041. These results show how much independence of the audit committee, size of the board, and CEO duality are related with total accruals of the selected companies which are listed on Nasdaq Helsinki stock exchange.

4.4 VIF Values to Test Multicollinearity

Table 6. VIF Values (EViews Output)

Variance Inflation Factors
Sample: 2017 2023
Included observations: 637

Variable	Coefficient Variance	Uncentered VIF	Centered VIF
C	0.000143	29.58363	NA
IAC	1.14E-08	17.78069	1.044557
SBOARD	1.10E-06	13.55275	1.006882

CEOD	4.42E-05	1.202225	1.043690
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Generally, if a variable exhibits a VIF value exceeding 10, it may merit additional investigation as there is an existence of the multicollinearity or independent variables are heavily correlated with each other. According to the above table centered VIF values for independence of the audit committee, size of the board, and CEO duality are less than 10. Therefore, it can be inferred that the variables do not exhibit perfect multicollinearity.

4.5 Regression Analysis

4.5.1 Regression Analysis

Table 7. Pooled OLS Regression (EViews Output)

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-0.080245	0.011971	-6.703201	0.0000
IAC	0.000143	0.000107	1.336944	0.1817
SBOARD	0.002474	0.001047	2.362976	0.0184
CEOD	0.009480	0.006646	1.426581	0.1542
R-squared	0.013767	Mean dependent var		-0.048536
Adjusted R-squared	0.009093	S.D. dependent var		0.055804
S.E. of regression	0.055549	Akaike info criterion		-2.936833
Sum squared resid	1.953263	Schwarz criterion		-2.908847
Log likelihood	939.3812	Hannan-Quinn criter.		-2.925967
F-statistic	2.945408	Durbin-Watson stat		1.731291
Prob(F-statistic)	0.032334			

Panel data regression analysis has been used to detect the impact of corporate governance on earnings quality on listed active companies in Nasdaq Helsinki stock exchange. To get the regression results using the statistical software called EViews used 91 actively listed organizations over the period of 2017- 2023 with 637 data points. The sample data can be affected by the time and the firm effect. Therefore, before testing hypotheses

need to investigate the time or firm effect. For that reason, before testing hypotheses, it is necessary to conduct Hausman test.

4.5.2 Fixed Effect and Random Effect

Panel data, which involves observing individuals (such as firms, persons, etc) across several points in time (such as days, years, etc) , is a valuable resource, where researchers are suspect that the outcome variable is influenced by unobservable factors that are constant over time and correlated with observed explanatory variables (Schmidheiny, 2014). The two principal methods for analyzing this panel data are Fixed Effect model (FE) and Random Effect model (RE).

The fundamental distinction between these two models lies in their assumptions about the relationship between unobserved factors and the observed independent variables. In the random effect framework, the individual specific effect is presumed to be no correlation with all explanatory variables across all time periods, whereas fixed effect model assumes that any individual specific effect is linked with the independent variables (Wooldridge, 2001). Fixed effect model is useful when examining how variables within an entity change over time, while accounting for characteristics that do not change over time.

Table 8. Fixed Effect Model (EViews Output)

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-0.101995	0.030423	-3.352569	0.0009
IAC	5.84E-06	0.000227	0.025721	0.9795
SBOARD	0.007000	0.003001	2.332818	0.0200
CEOD	0.006338	0.016206	0.391060	0.6959
Effects Specification				
Cross-section fixed (dummy variables)				
R-squared	0.322358	Mean dependent var		-0.048536
Adjusted R-squared	0.206298	S.D. dependent var		0.055804
S.E. of regression	0.049715	Akaike info criterion		-3.029532
Sum squared resid	1.342089	Schwarz criterion		-2.371861
Log likelihood	1058.906	Hannan-Quinn criter.		-2.774203
F-statistic	2.777510	Durbin-Watson stat		2.513810
Prob(F-statistic)	0.000000			

The table represent above table summarizes the output derived from the regression of the fixed effect model, applied to panel dataset comprising the 91 actively listed Finnish organizations over the period spanning 2017 to 2023.

Table 9. Random Effect Model (EViews Output)

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-0.081920	0.016177	-5.063837	0.0000
IAC	0.000102	0.000139	0.730344	0.4655
SBOARD	0.003177	0.001445	2.199254	0.0282
CEOD	0.008842	0.008908	0.992557	0.3213
Effects Specification				
			S.D.	Rho
Cross-section random			0.025251	0.2051
Idiosyncratic random			0.049715	0.7949
Weighted Statistics				
R-squared	0.009563	Mean dependent var		-0.028975
Adjusted R-squared	0.004869	S.D. dependent var		0.049821
S.E. of regression	0.049700	Sum squared resid		1.563543
F-statistic	2.037175	Durbin-Watson stat		2.161056
Prob(F-statistic)	0.107453			

The table above displays the findings obtained through the random effect regression analysis, utilizing a balanced panel dataset of actively traded Finnish organizations traded on Helsinki market between 2017 to 2023. The estimation relies on data from 637 firm year records.

4.5.3 Hausman Test

Table 10. Hausman Test (EViews Output)

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f	Prob.
Cross -section random	2.598949	3	0.4577

The Hausman test involves two hypotheses, which are outlined below,

Ho (Null): Random effect approach is suitable, indicating no association between the explanatory variables and individual specific effects.

H1(Alternative): Fixed effect model is suitable, suggesting that presence of a correlation between the regressors and the individual effects.

The decision to apply either a fixed effect or random effect model depends on the results of the Hausman test. When the P value exceeds 0.05, there is insufficient evidence to reject the null hypothesis, suggesting that the random effect is suitable. Otherwise, if the P value falls below 0.05, fixed effect model is preferred.

According to the test carried out by EViews, it showed that the probability of the Hausman test indicates 0.4577 which is higher than 0.05. Consequently, it is required to use random effect model for the panel data analysis and fails to reject null hypothesis of the Hausman test, which indicates that the unobserved heterogeneity (variations across firms or entities) is not significantly correlated with independent variables.

4.5.4 Regression Results of the Random Effect Model

Table 11. Regression Results of the Random Effect Model (EViews Output)

Dependent Variable: TACC

Method: Panel EGLS (Cross-section random effects)

Sample: 2017 2023

Periods included: 7

Cross sections included: 91

Total panel (balanced) observations: 637

Swamy and Arora estimator of component variances

White cross-section (period cluster) standard errors & covariance (d.f.corrected)

Standard error and t-statistic probabilities adjusted for clustering

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-0.081920	0.028111	-2.914182	0.0268
IAC	0.000102	0.000214	0.474820	0.6517
SBOARD	0.003177	0.001760	1.805086	0.1211
CEOD	0.008842	0.005028	1.758389	0.1292

Effects Specification				
			S.D.	Rho
Cross-section random			0.025251	0.2051
Idiosyncratic random			0.049715	0.7949

Weighted Statistics				
R-squared	0.009563	Mean dependent var	-0.028975	
Adjusted R-squared	0.004869	S.D. dependent var	0.049821	
S.E. of regression	0.049700	Sum squared resid	1.563543	
F-statistic	2.037175	Durbin-Watson stat	2.161056	
Prob(F-statistic)	0.107453			

Unweighted Statistics				
R-squared	0.012866	Mean dependent var	-0.048536	
Sum squared resid	1.955047	Durbin-Watson stat	1.728298	

The above table represents the panel regression estimated using random effect model with white cross section standard errors which is heteroskedasticity corrected, based on the panel dataset comprising 637 observations across 91 cross sections or firms over the period of 2017 to 2023.

R squared of the given results show that 0.0096 which indicates that approximately 0.96% of the variation in total accruals can be attributed to the predictors used in the model.

Generally, the accepted level of R squared ranges from 0% to 100% and the R squared is higher, the better the model fits the data. The adjusted R squared also slightly lower at 0.0049. Also, the F statistic, which is 2.037 is not statistically significant at 5% level as P value of 0.107(which is less than 0.05) suggests that the model does not significantly explain the relationship between independent and dependent variables.

As per the above regression results show that the coefficient of Independence of the Audit Committee (IAC) is positive (0.000102) with the dependent variable of Total Accruals (TACC), since the p value is 0.6517, which exceeds the 0.05 significance level, the results is not statistically significant. This implies that there is no proof of a significant association between IAC and TACC. There is a positive relationship with the Size of the Board (SBOARD) and TACC because of the positive coefficient of 0.003177. While the sign suggests a positive relationship with TACC, the relationship is statistically insignificant as the P value (0.1211) is higher than 0.05. CEO Duality (CEOD) has a positive coefficient of 0.008842 and the P value of 0.1292, which also shows the statistically insignificant relationship with the TACC.

The Durbin Watson statistics of 2.16 indicate absence of autocorrelation in the residuals as the value is close to the benchmark of 2. This indicates strong support for the validity and consistency of the model's estimates.

4.5.5 Model Summary

Table 12. Model Summary

Variable	Coefficient	Prob.
C	-0.081920	0.0268
Independence of the Audit Committee (IAC)	0.000102	0.6517
Size of the Board (SBOARD)	0.003177	0.1211
CEO Duality (CEOD)	0.008842	0.1292

Proposed model of the research specified in chapter 3 as follows,

$$TA_{it} = \beta_0 + \beta_1 IAC_{it} + \beta_2 SBOARD_{it} + \beta_3 CEOD_{it} + \epsilon_{it}$$

As per the results derived from regression using the EViews, the model can be shown as follows,

$$TA_{it} = -0.081920 + 0.000102IAC + 0.003177SBOARD + 0.008842CEOD + \epsilon_{it}$$

As per the above model, audit committee independence, board size, and CEO duality exhibit positive coefficients of 0.000102, 0.003177, and 0.008842 respectively. This suggests that when independence of the audit committee, size of the board, and CEO duality change by 1 unit, the total accruals also change by the corresponding coefficient value.

Though there is a positive coefficient with the selected independent variables, P values of the regression analysis indicate 0.6517, 0.1211, and 0.1292 for independence of the audit committee, size of the board, and CEO duality respectively, which are higher than the significance level of 0.05. Therefore, it seems that the independence of the audit committee, size of the board, and CEO duality are insignificant to the model.

4.6 Research Question and Hypothesis Testing

Chapter one of the research formulated two hypotheses on the relationship between corporate governance and earnings quality and research question. In this part, the researcher substantiates these propositions through empirical testing, grounded in the results of descriptive and statistical examinations.

From the analysis of the research the correlation coefficient of the independence of the audit committee indicates a 0.048767 which is a weak positive relationship as it ranges from 0 to 0.3. Further the regression results of the study indicate a coefficient value of 0.000102 which is positive but not statistically significant as per the P value of the study indicates the 0.6517 which is higher than the 0.05. Hence it can be established that while

there is a weak positive relationship between the independence of the audit committee and the quality of earnings, the relationship is not statistically significant.

As per the correlation test results obtained by EViews indicate positive correlation coefficient for the size of the board of 0.093723 which is a weak positive correlation to the total accruals. Also, regression analysis of the research reveals that the coefficient of 0.003177 is positively related but not statistically significant. Because of the P value of the regression outcome indicates a value of 0.1211 which is higher than 0.05.

Considering the correlation matrix result there is a positive weak correlation coefficient of 0.041115 exist between CEO duality and earnings quality. And as per the regression analysis, coefficient indicates as 0.008842, which is positively related, but the P value of the model showed the value of 0.1292 that is higher than 0.05. Hence, it can be concluded that the findings do not demonstrate a meaningful statistical relationship.

According to the findings from the analysis using correlation and regression tests it can conclude that there is not any significant positive relationship between corporate governance and earnings quality. Hence reject the first hypothesis (H1: Corporate governance has a significant positive effect on the earnings quality of listed companies in Finland) and accept null hypothesis that corporate governance has no significant effect on the earnings quality of listed companies in Finland.

5 Discussion and Conclusion

5.1 Discussion

This research analyzed how corporate governance influences the earnings quality of active organizations traded on Nasdaq Helsinki in Finland. The research sought to address the research question of how elements of corporate governance, specifically audit committee independence, board size, and CEO duality affect the earnings quality of actively traded Finnish organizations in the Nasdaq Helsinki Stock Exchange. Population of the study included 202 actively traded Finnish organizations in Nasdaq Helsinki Stock Exchange as of 20th February 2025. Among them 91 active Finnish companies are selected as sample of the research due to unavailability of the annual report data in some companies in the population. 91 companies are evaluated over a period of 7 years, from 2017 through 2023.

The study investigates how corporate governance relates to earnings quality by incorporating three key indicators of audit committee independence, board size, and CEO duality, which serves as independent variables representing the governance structure of the firm. In addition, the study uses total accruals as a proxy for measuring the dependent variable, earnings quality.

Data for the sample is selected from the secondary sources of data by utilizing databases and annual reports of the respective firms. The information gathered was then processed using the statistical software of EViews. Using the software obtained results for the descriptive statistics, missing variables, multicollinearity, correlation, Hausman test, and finally running the panel data regression to comprehend the connection of corporate governance and earnings quality using the selected variables for the study.

Based on the findings derived from the EViews analysis, the developed hypotheses are ensured by the correlation and panel data regression tests. The conclusion is drawn by

examining the correlation coefficients and regression outputs, including coefficient values and p values. The key outcomes are outlined in the table beneath.

Table 13. Summary Table

Hypothesis	Accepted	Rejected
H1: Corporate governance has a significant positive effect on earnings quality in listed companies in Finland.		Rejected.
H0: Corporate governance has no significant effect on earnings quality in listed companies in Finland.		Accepted.

5.2 Conclusion

The three independent variables examined, namely audit committee independence, board size, and CEO duality have shown a positive coefficient to the dependent variable of total accruals. However, these positive associations were found to be statistically insignificant, as reflected in the p values derived from the regression results. The research findings suggest that there is no statistically significant link between audit committee independence and total accruals, no significant association was found in board size and total accruals, and similarly there is not any statistically meaningful relationship between CEO duality and total accruals.

Overall, variables selected for this research suggest that there is not any statistically significant relationship between corporate governance and earnings quality in the actively

traded organizations in Nasdaq Helsinki Stock Exchange. Nonetheless, beyond the corporate governance factors examined in this analysis, there might be a noteworthy association between corporate governance and earnings quality among Finnish publicly traded entities and further research is necessary to explore this potential relationship.

5.3 Implication and Recommendation

Findings from the study indicate that there is no significant positive association between corporate governance and earnings quality in publicly traded organizations in Finland, which provides several implications.

Theoretically, the study questions the commonly held assumption of agency theory which implies strong governance structures reduce earnings manipulation and enhance reliability of reported profits. The outcome of the research indicate global findings regarding the link between corporate governance and earnings quality may not be true in the Finnish context. And findings also shows that the absence of significant relationships between corporate governance and earnings quality in Finnish context, suggests that traditional variables of corporate governance might fail to reflect the dynamics that influencing earnings quality in highly regulated and transparent market in Finland. This may lead to refining existing theories or commonly accepted assumptions in Nordic settings.

Findings from the study suggest that companies in Finland may adhere to the corporate governance rules and Finnish corporate governance code. Because as an example, most of the Finnish organizations in the sample maintained a separation between the roles of CEO and chairman of the board. Therefore, this may lead policymakers and regulators to shift their focus on evaluating the effectiveness of the governance bodies rather than expanding the governance requirements.

Based on this study it is recommended to get at least more than three independent variables to get a good result for the analysis. Because it can help to run the dataset to a standard level by eliminating the variables which are not fit for the analysis.

5.4 Direction for Further Research

This research has done for the examination of the connection between corporate governance and earnings quality of publicly listed firms in Finland and the study provide no statistically significant positive association between corporate governance and earnings quality. Therefore, further research could broaden the focus to constitute companies across other countries and regions to find whether regulatory and cultural factors can affect the relationship.

This study has explored variables over the period of 7 years; further research can extend the study period depending on data accessibility. Additionally, future studies can explore alternative measures for earnings quality. Also, consider other alternative corporate governance evaluation measures and expand the variables to analyze the level of corporate governance to mitigate the issues.

Moreover, sector or industry specific research can add value for further research to understand whether the relationship varies across industries. Finally, the use of qualitative approaches, including interviews and case studies can be provide good context to the quantitative findings to discover why governance mechanisms might exert a minor role in shaping earnings quality in the Finnish settings.

6 References

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Appendices

Appendix 1. Sample Company List

Number	Company Name
1.	AKTIA BANK ABP
2.	ALANDSBANKEN ABP
3.	ALEXANDRIA GROUP OYJ
4.	ALMA MEDIA OYJ
5.	ANORA GROUP OYJ
6.	ASPO OYJ
7.	ATRIA PLC
8.	BITTIUM OYJ
9.	CARGOTEC CORP
10.	CITYCON OYJ
11.	CONSTI OYJ
12.	DETECTION TECH
13.	DIGIA PLC
14.	EEZY
15.	ELISA CORP
16.	ENDOMINES FINLAND OY
17.	ENENTO GR
18.	ETTEPLAN OYJ
19.	EXEL COMPOSITES OYJ
20.	FINNAIR
21.	FINNAIR CASH 2
22.	FINNAIR NIL PAIL RIGHTS
23.	FINNAIR OYJ
24.	FINNAIR RIGHT 2
25.	FISKARS OYJ

26.	FORTUM OYJ
27.	GLASTON CORPORATION
28.	GOFORE OYJ
29.	HARVIA OYJ
30.	HKFOODS
31.	HUHTAMAKI OYJ
32.	INCAP OYJ
33.	KAMUX OYJ
34.	KEMIRA OYJ
35.	KESKO A
36.	KESKO OYJ
37.	KOJAMO OY
38.	KONE CORPORATION
39.	KONECRANES ABP
40.	LASSILA & TIKANOJA
41.	LEHTO GROUP
42.	LINDEX GROUP OYJ
43.	MARIMEKKO OYJ
44.	MERIAURA GROUP OYJ
45.	METSA BOARD OYJ
46.	METSA BOARD OYJ
47.	METSO OYJ
48.	'MUSTI GROUP
49.	NESTE OYJ
50.	NOHO PARTNERS OYJ
51.	NOKIA OYJ
52.	NOKIAN TYRES PLC
53.	NORDEA BANK ABP
54.	OLVI OYJ

55.	ORIOLA A
56.	ORIOLA OYJ
57.	ORION A
58.	ORION B
59.	OUTOKUMPU OYJ
60.	PIHLAJALINNA OYJ
61.	PONSSE OYJ
62.	QT GROUP OYJ
63.	RAPALA VMC
64.	RAUTE OYJ
65.	REBL GROUP OYJ
66.	SAMPO OYJ
67.	SANOMA- OYJ
68.	SCANFIL PLC
69.	SIILI SOLUTIONS OYJ
70.	SOLTEQ OYJ
71.	SSAB A SVENSKT STAL AB
72.	SSAB B SVENSKT STAL AB
73.	STORA ENSO OYJ
74.	SUOMINEN OYJ
75.	SV. HANDELSBANKEN AB
76.	TALENOM OYJ
77.	TELEFONAKTIEBOLAGET
78.	TELESTE OYJ
79.	TELIA COMPANY AB
80.	TERVEYSTALO OYJ
81.	TIETOEVRY
82.	TOKMANNI GROUP
83.	TORA ENSO OYJ

84.	UPM-KYMMENE OYJ
85.	VAISALA OYJ
86.	VALMET OYJ
87.	VERKKOKA
88.	VIKING LINE ABP
89.	WARTSILA OYJ
90.	WITHSECURE OYJ
91.	YIT OYJ