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INVESTIGATING THE RELATIONSHIPBETWEEN SOCIAL PERFORMANCE AND EARNINGS MANAGEMENT: A CASE STUDY IN IRAN BANKING INDUSTRY

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Abstract: *The present research aims to provide a model for investigating the relationshipamong Social Performance and Earnings Management in the banking Industry of Iran in addition to literature and scientific explanation. This study was done based on descriptive and correlational methods, according to its practical objectives. In this study, two models were used in which the first model was evaluated by regression analysis and the second model was tested by using structural equations.In the first model, the impact of four indicators related to social functioning is examined, including the ratio of ATM, the ratio of online branches, the ratio of facilities of the agriculture and ratio of facilities of industry and mining sector on bank's earnings management.that the results indicated that the ratio of ATM, online branches, facilities of agriculture and facilities of industry and mining sectorhave reverse significant impact on bank's earnings management of Iran . The result of the second model indicates that earnings management has reverse and significant impact on electronic services and economic services in the banking industry of Iran.*

Keyword: *social performance, earnings management, bank size, bank ownership, risk*

INTRODUCTION

Among the factors that could cause fundamental changes in the economic environment, we can refer to publicity of ownership of business, financing through public participation, and privatization of the public sector and businesses. In such circumstance, transparency and high quality of financial information which can be regarded as the foundation of optimal economic decisions of investors, creditors and users of financial information have particular importance. In most cases, managers are placed in situations that not only their decisions are not in favor of shareholders, but also they cause a loss in financial reports. Indeed, earnings management occurs when managers record their judgments in financial reporting and their registrations. It should be noted that this issue may change in the content of financial reports and mislead the shareholders about the company's economic performance. On the other hand, basically in a business since the relationship

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between social, political, environmental and economic roles in business has been on the rise, all organizations arefaced with new dynamics. The main challenge that organizations are struggling with, is that they must achieve two outcomes through increasing profitability and meeting the social expectations and then simultaneously managing these two seemingly contradictory outcomes need to develop practical strategies, also they have positive impact both on society and on the organization. The implementation of corporate social responsibility in the organization can be considered as the effective strategy in this regard. Generally, nowadays organizations in addition to their traditional tasks have been obliged to carry out other activities that the purpose of these activities is to meet the expectation of society which can be regarded as the corporate social responsibility (CSR). During this period, effective management refers to the management released from the thought of the organization and thinks about society and wider community, because not only organizations cannot isolate themselves from society, but also society cannot continue without organization.

Corporate Social Responsibility has been considerable controversy subject in the United States during the past few decades. On one side are those who argue that the goal of business is profits and enhancement of stock value and the improvement of welfare. Moreover, community health can be considered as the duty of religious, social and governmental factors. On the other side of the debate are those who argue that business is a social, civil and ethical religion for carrying out social activities in order to improve public welfare through its interests. Proponents of this view do not deny the importance of profits for traders. Benefit is considered to be important for issues, including creating jobs, fair wages, useful products, local tax and other important social cooperation. Optional actions of Administrators through management can provide the basis to hide the real value of the assets and financial situation of the company and has negative consequences for beneficiaries, especially shareholders, staff, society, celebrity of managers and job security. On the other hand, social responsibility deals with the ethical issues concerning behavior and decision- making of organization about topics, including Human Source Management, Environmental Protection, Health Work, Community relations, and relations between customers and suppliers. Therefore, what is seen as the main problem of this study is interaction between social performance and earnings management. Whereas, one of the requirements for banks to survive in the global era and achieve a high market share and competitive advantage, in particular the move towards a competitive economy, is concerned as careful attention to corporate social responsibility in the businesses. This is particularly needed in developing countries to create incumbent fields, including raising awareness, checking the necessary stimulus and removing obstacles and challenges. Considering the importance of corporate social responsibility and alignment ideological and humanitarian motives with the country's business interests, it is sought to investigate the interaction between social performance and earnings management in Iranian banking industry.

THEORETICAL FOUNDATIONS

Accounting is an information system which is regarded as the most important sub-task of management information system. It is responsible for collecting management information system, classifying, summarizing and reporting of economic and financial events of an organization, as well. Reporting profit can be defined as one of the items of financial statements which has been entitled as criterion for educating the performance and profitability of nonprofit unit. Net profit is calculated by methods and accounting estimations. Managers' authority in the application of the principles and compliance, anticipating and also several practices, including changing the methods of evaluating Inventory, Depreciation, Goodwill, Current price as the research costs and development and the cost of doubtful receivables, such as those cases that managers can benefit through applying changes. On the one hand, because of greater awareness of managers of the company, it is expected that information provided and presented in such best way possible that reflects the company's status. On the other hand, the management of nonprofit unit indicates the company's status much desirable by manipulating the company's earnings for reasons like retention of the company, receiving bonuses, etc. Under these circumstances, the real benefit has been in conflict with profit reported in the financial statement and events occurred as earnings management.

Corporate Social Responsibility (CSR) has different meanings, but not always the same for everyone. Some people believethat it is definedas significant legal liability or responsibility, while for others it means social responsible behavior in terms of compliance with ethical issues. Furthermore, for other groups of people, it can be defined as being responsible, whereas most of people regard it as charity gifts and charitable contributions. Along with such cases, there are other groups of people consider it as social awareness and those who have embraced this concept, regard it in the sense of legitimacy. In this meantime, the small number of people still sees it as an assigned task to impose higher standards of conduction on businesses and businessmen, and also merchants and industrialists, but not citizens.

BACKGROUND OF THE STUDY

Senobar *et al.*, (2010) have explored the relationship between social responsibility and financial performance of companies engaged in pharmaceutical industry. This analysis will yield result that there is no relationship among corporate social responsibility and its five components and financial performance variable. Besides, there is a positive relationship between the size and risk of financial performance. JabbarzadehKangarlouei and Bayazidi (2012) have investigated the relationship between corporate social responsibility and commitment to conservatism in financial reporting of companies listed on Tehran Stock exchange. They also have used Gioli's model and *et al*, in order to measure corporate social responsibility through Singapakdi's standards questionnaires (1996).

In one study which has been conducted by Briyan *et al,*(2007) in Australia, statistically significant relationship has not been found between corporate social responsibility and financial performance. RhimMcney *et al.*, (2009) have discovered the causal relationship between corporate social performance and financial performance of Canadian companies during 2004 and 2005. Therefore, the results showed that there is no significant relationship between two variables, including social performance and financial performance. Apart from this, Vasiliki*et al*, (2014) have examined the relationship between corporate social responsibility and earnings management in the US banks. The results indicated that there is no significant relationship between two variables, such as corporate social responsibility and earnings management in American banks.

RESEARCH QUESTION

The question that arises in this study is as follow:

Is there any significant relationship between social performance and earnings management in the banking industry?

To investigate this question, the mutual influence on each social performance and earnings management on each individual mode have been tested. The following hypothesis is experimented to answer the research question:

RESEARCH HYPOTHESIS

H1: Social performance has significant impact on earnings management in Iran banking industry.

H2: Earnings management has significant impact on social performance in banking industry of Iran.

METHODOLOGY

The present study is an applied research by using descriptive and correlational analysis. Statistical datawere collected by organizational documents, and also the interaction between social performance and earnings management have been explored in banking industry of Iran. This research is an applied research according to its objectives and has been performed to test hypothesis by Regression, statistical data analysis and statistical analysis. Moreover, based on the data collected and the type of procedure, the relationship between variables was examined to answer research hypotheses using the application of *Excell.Stat*, *SPSS*, and *EviewsSoftwares and* regression model.

POPULATION AND SAMPLE

In this study, all banks in Iran's banking industry were applied.The research sample consistedof allbanks, includingstate-ownedand privatebanks. Therefore, the total population is selected as samples which have served in the level of countryduring 2008-2012.

Variables

Following hypotheses have been tested using regression models. Testing of the research is fitted based on two following models:

$$\beta_0 + \beta_1 E_1 + \beta_2 E_2 + \beta_3 CS_1 + \beta_4 CS_2 + \beta_5 SIZE + \beta_6 CR + \beta_7 OWNER + \beta_8 ROE + \varepsilon_{it} EM_{it=} \quad (1)$$

$$BSP_{it=}\beta_{0+}\beta_1 EM_{it+}\beta_2 SIZE_{it+}\beta_3 CR_{it+}\beta_4 OWNER_{it+}\beta_5 ROE_{it+}\varepsilon_{it} \quad (2)$$

In theregression model(1)

Dependent variable: Earnings Management (EM)

Independent variable: Bank Social Performance (BSP)

Control variables: Bank Size (SIZE), Credit Risk (CR), Ownership (OWNER), Return on Equity (ROE)

Regressionmodel (2)

Dependent variable: Bank Social Performance (BSP)

Independent variable: Earnings Management (EM)

Control variables: Bank Size (SIZE), Credit Risk (CR), Ownership (OWNER), Return On Equity (ROE)

Size: The natural logarithm oftotal assets

Credit Risk: Forthispurpose, theriskindexis used *Z-SCORE*that is to divide the natural logarithm of the return on assets and return on assets ratio of capital to assets of the Bank by the standard deviation.

Riskis calculatedas follows:

CR: Credit Risk = Z-SCORE

$Z = Ln (ROA + CAP) / \sigma_{ROA}$

ROA:Return OnAssetsbeforetax

CAP :Ratio of capital toassets

σ_{ROA} : The standard deviation ofreturn on assets

Owner: It can be defined as the different identity of banks. In this study, the type of ownership will be divided into public and private banks. If the mentioned bank is state, it takes the value of 1, otherwise zero.

Return on Equity (ROE): The ratio of net profit to equity

Earnings Management (EM): This part has been used by the methodology of Ahmad *et al.* (1999), and Kanagartman *et al.* (2004) (7). The researchers said that in accordance with the following model of localization are some variables.

$$EM_{i,t=\rho}\left(\frac{\Delta LLP_{i,t}}{TA_{i,t-1}},\frac{\Delta EBT_{i,t}}{TA_{i,t-1}}\right)$$

Total Assets of the bank

$EBP_{i,t}$: Earnings beforededuction ofthe cost of Payments andbad debtsthe banks

LLP: Savepayments

Bank Social Performance (BSP): It can be examined by the next two Dimensions: Facility Servicesbusiness are analyzed from the perspective of Clients with our Society (C.S):

CS_1 : Facilitiesofthe agricultural sectortototalloans

CS_2 : Facilitiesforthe convenienceofindustry and mine sector.

From the perspective of the Environment (E): Retail banking, as is discussed below:

E_1 : ATMs of any bank in all branches of that bank ATMs of all banks in total bank branches

E_2 : Online branches of each bank in total bank branches in total online branches of the bank branches.

FINDINGS OF THE STUDY

Analysis of variables and assumptions of the model

The first hypothesis testing was done based on research data for the bank –year, which used regression analysis according to the form and purpose of the study of multiple regression analysis. To use this analysis, the assumption sunder lying regressionanalysis would be justifiabletoensurethat theresultscontinue to bethe fundamentalassumptionsofthemodel.

1) Diagnostictests and choosing the appropriate model: In order to choose the regression model in the analysis, a number of tests should be performed just beforepre-estimation to determine the data are able to be combined

or assign a representative for each period. For this study, *Limmer* test was used. Furthermore, it can be seen the calculatedlevel of significance is greater than05/0, which *Pooled*modeldoes not havethepower toreject. Therefore,*Limmer*testformodels of themodelhas supportedpooledfor the period.

Table 1
***Limmer* test results of the research model for pooled or panel model and type effects**

Limmer Test or Chaw						*The Purpose and Test*
Based on theresults of theChi-squaretest			*Fisher Test Results*			
Result	*Error Level*	*Chi- Square*	*Result*	*Error Level*	*StatisticsF*	
Pooled	0.4200	3.897661	Pooled	0.5049	0.840150	Test of Period

Table 2
The results ofnormal distribution based on three different tests

Jarque–Bera test		*Shapiro-Wilk test*		*Kolmogorov–Smirnov test*		*N*	*Variable*
Error Level	*Statistics*	*Error Level*	*Statistics*	*Error Level*	*Statistics*		
0.000000	95.23897	.000	.703	.000	.246	75	Earnings Management
0.000000	59.45107	.000	.841	.000	.186	75	ATM
0.000000	159.5873	.000	.642	.000	.334	75	Online Branches
0.000000	2507.928	.000	.385	.000	.363	75	Facilities in agriculture
0.000000	627.0791	.000	.585	.000	.274	75	Facilitiesindustry and mine sector
0.166345	3.587381	.045	.967	.034	.107	75	Bank Size
0.001472	13.04199	.000	.884	.000	.197	75	Risk
0.147064	3.833780	.002	.942	.015	.115	75	Return on equity

Table 3
Results of linear regression, residual distribution and Durbin-Watson

The residual distribution		*Durbin Watson*		*Testlinear relationship*	
The significance level	*Jarque–Bera testStatistics*	*Lack ofcorrelation*	*Durbin-Watsonmodel*	*The significance level*	*Statistics F*
0.001136	13.56059	1.5-2.5	1.971795	0.000000	11.19805

The results ofthe first model and social performance impact on earnings management model

To evaluate the first hypothesis and the role of social performance variable on earnings management, an equation was used, in addition to the four control variables, including the type ofownership ofthe bank, the bank size and risk.

First Main Hypothesis: Social performance management of profitsin the banking industry has a significant effect.

The main hypothesis included four sub-hypotheses as follows:

Hypothesis 1: ATM machinesofother banks have significant effecton earnings managementin the banking industryofIran.

Hypothesis 2: Online branches of banks have significant effect on earnings managements in the banking industry of Iran.

Hypothesis 3: Facilitiesofthe agricultural sectorin the banking industryhas a significant effecton earnings management.

Hypothesis 4: Facilitiesofthe agricultural sectorin the banking industryhas a significant effecton earnings management.

The above table shows that social performance variables including the proportion of ATM machines and online branches and the facilities of the branches of the agricultural sector have negative impact on earnings managementat 99% confidence and the effect of the ratio of loans at 90% confidence for this sector is significantly negative.

Analysis of variables and assumptions for the second model

In the second model, the dependent variableis the social function having four variables. Each of the four variables is associated with one of the two main factors. The structural equation model is used with partial leasts quares method. In this

Table 4
The effect of social performance management andcontrol variables on profit

Dependent variable: Earnings management, Number of the period: 5, Number of school: 15, Total amount: 75						
The significance Level	*Statistics T*	*Standard Error (SE)*	*Coefficient*	*Name of Variable*		
0.8986	0.127964	1.561308	0.199792	Constant Coefficient	C	β_0
0.0011	-3.424836	0.101374	-0.347188	ATM	E1	β_1
0.0007	-3.542947	0.982184	-3.479826	Online Branches	E2	β_2
0.0004	-3.739219	0.144033	-0.538572	Facilities in agriculture	CS1	β_3
0.0711	-1.833749	0.652424	-1.196381	Facilitiesindustry and mine sector	CS2	β_4
0.0016	-3.282160	0.221023	-0.725432	Ownership	OW	β_5
0.0000	4.423188	0.101394	0.448483	Bank Size	SIZE	β_6
0.1975	-1.301555	0.000898	-0.001169	Credit risk	CR	β_7
-0.222055	The mean ofthe dependent variable		0.539159	Coefficient of determination		
1.776361	Deviation ofthe dependent variable		0.491011	Correctedcoefficient of determination		
106.3724	Totalsquareunexplainedde viations		1.260019	Standard deviation ofregression		
1.971795	Durbin-Watson		11.19805	F Statistics		

study, Socialperformancemeasurementis usedfor reflectivestructure and combined measurement were usedfor theindependent variables.Moreover, CL and inferential statistics were used to determine the path used from Bootstrapre-sampling, in which Re-insertion of thesamplingmethodused intheoriginal sample. The second model is considered in the equation as follows:

$$BSP_{it} = \beta_0+\beta_1\ EM_{it} + SIZE_{it} + \beta_3\ CR_{it} + \beta_4\ OWNER_{it} + \beta_5\ ROE_{it} + \varepsilon_{it} \qquad (2)$$

$$\begin{cases} CS = \beta_0 + \beta_1\ EM_{it} + \beta_2\ SIZE_{it} + \beta_3\ CR_{it} + \beta_4\ OWNER_{it} + \beta_5\ ROE_{it} + \varepsilon_{it} \\ EM - \beta_0 + \beta_1\ EM_{it} + \beta_2\ SIZE_{it} + \beta_3\ CR_{it} + \beta_4\ OWNER_{it} + \beta_5\ ROE_{it} + \varepsilon_{it} \end{cases}$$

The model fit indices: Evaluation Model fitness model with internal and external measures taken. Index external model with the internal model .897 and .845 of the critical statistics are larger and significant which has supported the model in the measurement and structure. In this model, partial least squares index represents the relationship between markers of external model structure and the index indicates the internal model's ability to predict structures endogenous to exogenous factors.

Table 5
The results of Partial Least Squares modelfitindices

Result of Test	*CL*		*Critical Value*	*Criteria Error*	*Values*	*Variable*
	Upper					
Fitness indexExternalmodelis acceptable.	1.000	0.666	7.425	0.121	0.897	External Model
Fitness indexinternalmodelis acceptable.	0.962	0.729	16.030	0.053	0.845	Internal Model

***The results of thestructuralmodel*:** The structural model shows the effect of exogenous variables on the two dimensions of social performance. Critical statistics calculated for independent variable income management on the structure of electronic services is less than the critical value of 96/1's indicating the significance of an adverse effect at confidence level of 95%. Critical statistics calculated for independent variable of interest on loans structures is smaller than the critical value of 64/1 and larger than 961/-1 indicating the significance of its effect at confidence level of 95%, while this effect is negative at 90% confidence level.

The effect of bank ownership structure of electronic services is not significant, However, its effecton the structure of 95%direct and significant facilities. The effectsize of the bankon 90% confidence level for reverse engineering of electronic services is significant, but not significant effecton the structural facilities. The effect of credit risk on the structure of electronic services is significant, but its effect on the structure of facilities in the 90% confidence level is significantly reverse. This model consists of two equations for the coefficient of determination influenced by the structure of electronic services of exogenous variables to influence the structure of .16 and .23 of the facilities of the exogenous variables. Since the coefficients of the importance of bank ownership, the size of the bank's profit exceeded forecasts and management structure of electronic services are larger than. 8, these variables are important to predict the electronic services. The coefficients of the variables of ownership of the bank, risk management and profit exceeded forecasts facilities structureare larger than 0.8, Therefore, this assessment is regarded as an important variable in predicting facilities. The structure of the second model is shown in Table 6.

Table 6

Indices for the relationship betweenthe secondmodelin thesample under study

Sig.	*Coefficient of determinationandtestequation*			*Critical Statistics*	*Estimation Error*	*Estimated Coefficient*	*Structural Bonding*	*Effective Structure*	*Equation*
	Critical Statistics	*Estimation Error*	*Coefficientequation*						
0.811	1.972	0.079	0.155	1.074	0.141	0.151	E- Services	Bank Ownership	First Equation
0.902				-1.854	0.091	-0.168		Bank Size	
0.421				-0.733	0.107	-0.079		Risk	
1.534				-2.371	0.121	-0.286		Earnings Management	
1.108	2.769	0.084	0.232	2.274	0.096	0.217	Facility of Business Services	Bank Ownership	Second Equation
0.776				1.065	0.143	0.152		Bank Size	
0.995				-1.641	0.119	-0.195		Risk	
1.086				-1.905	0.112	-0.213		Earnings Management	
E= 0.151318396641*OW -0.168389527818*SIZ -7.85031013678242E-02*CR -0.286224041002*EM									Equation 1
CS= 0.2172350729*OW +0.152019257128*SIZ -0.195060446141*CR -0.212830215860*EM									Equation 2

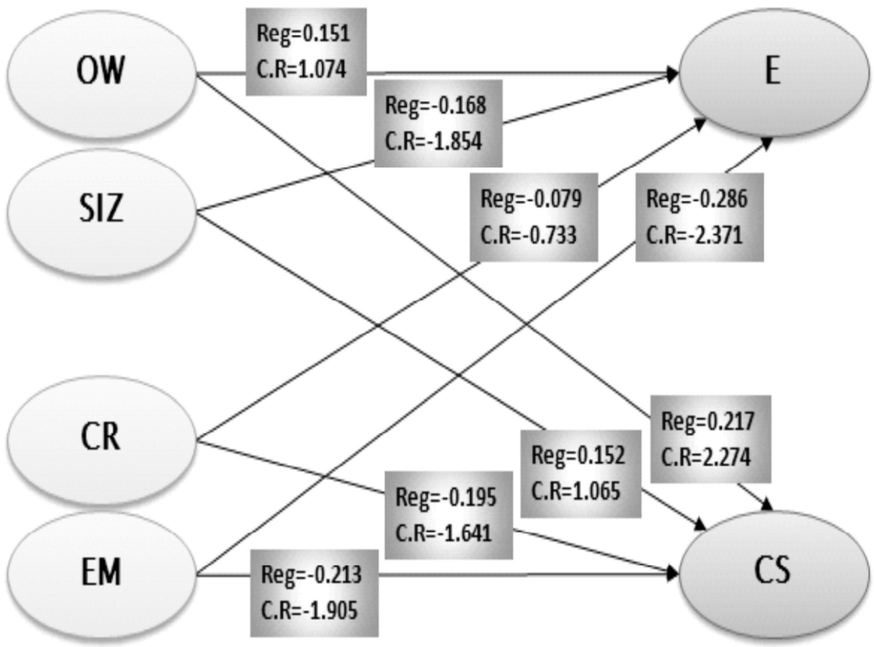

Figure 1: Impact factor variables on endogenous factors and testing statistics

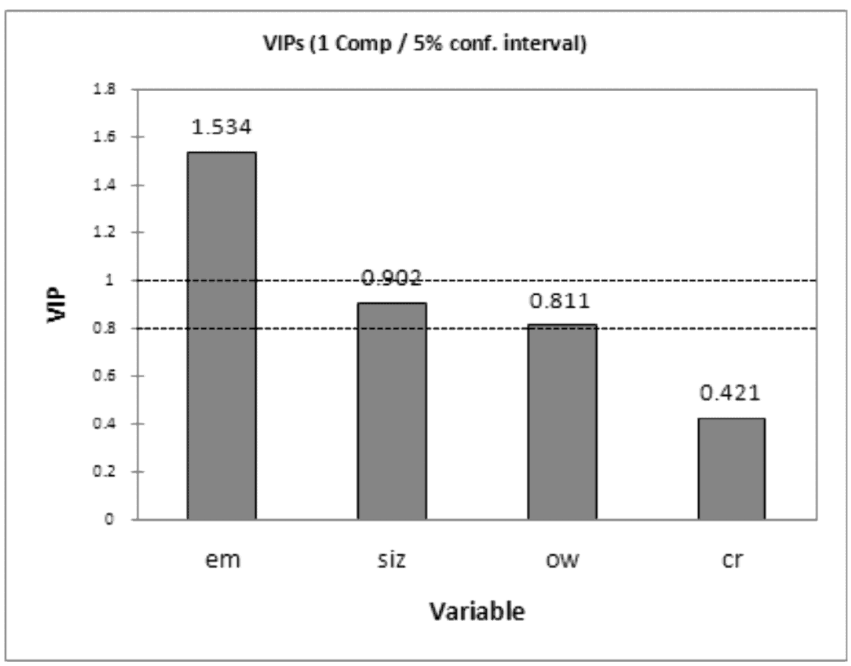

Figure 2: Coefficients of exogenous variables in predicting the structure of electronic services

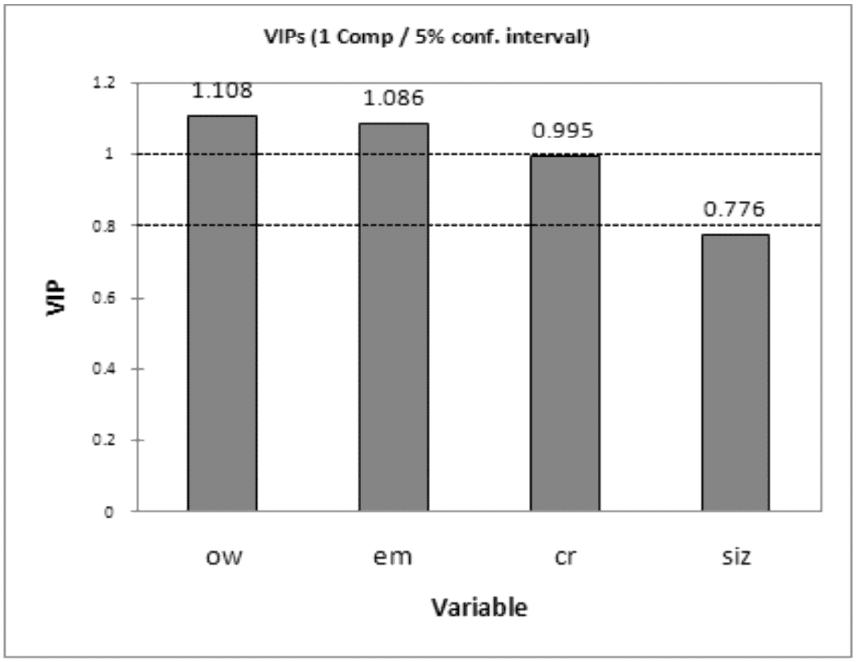

Figure 3: Coefficients of exogenous variables in the prediction of structural facilities services

CONCLUSION

This study investigates theeffect ofearnings managementonsocial functionand effect ofsocial performancemanagementonearnings. Inthe presentstudy, the impacts of three variables including ownership, size of firmandrisk have been controlled. The study sampleincludedbanks inIran. The sampledatawere formedfortheperiod betweenthe years 2008-2012on an annual basis. To achievethe research objectives,twomain hypotheses andsixsecondary hypotheses were proposedand due to the nature ofregression analysis, combination and structuralequation were used. Given thestrongrelationshipbetweenreturn on equityandriskvariablesmay causemulti-linearrelation, the variableof return on equityofmodelswas removed. The resultsshowed theeffect ofsocial performance variables including the proportion of ATM machines, onlinebranches andthe facilitiesofthe branches ofthe agricultural sectoron earnings managementat 99% confidence is significantlynegative, and also the effect ofthe ratio ofindustry and miningfacilitiesat the90% confidence issignificantlynegative. Besides, the effect ofearnings managementon the structureof electronic servicesat 95% confidence wassignificantlynegative. Finally, the effect of profit management on economicfacility services90% was negatively significant at confidencelevel. Itgatheredevidenceofthe effects ofsocialperformance variables onthe impact ofearnings managementandearnings managementhas supportedthesocial function.

Branchesofonline bankingin the banking industryhave a significant effecton earnings management and the effect isreverse. Therefore,withthe increase ofonline bankingbranch, earnings managementin the banking industry of Iran has been reduced. Facilitiesofthe agricultural sectoron earnings managementin the banking industryof Iranhas inverselysignificant effect. Therefore, increasingthe proportion offacilities in agriculture, earnings managementcan be reduced in the banking industry. ATM machineson the earnings management have negatively significant impact in the banking industryofIran. Thus, by increasing the number of ATMs,earnings managementhas been reducedin the banking industryof Iran. Facilitiesofindustry and mining sectorin the banking industry have significant reverse effecton earnings management. Therefore, increasingthe proportion ofindustry and mine sectorfacilities, earnings managementofhas been reducedin the banking industry. Also, Earnings managementin the banking industryoftheelectronic servicesisinverselysignificant effect. In this regard,as the issue of social responsibilitydoes not exceed more than one decade, many companies are not interested in publishingmanydetails of theBank's social responsibility in the financial statements. It was considered as the most important limitations of this study.

The following are offeredas suggestions for future research:

The other dimensions of social responsibilityas well asthe ethical dimension, other dimensions ofeconomic, socialandalternatedimensionsare used inthisstudy. Evaluation ofsocialresponsibilityin various industries,and finallythe need todevelop standards, regulations and doingactionsin the legislative bodies require organizationstopay special attention tosocialresponsibilitytowardsaccountability and transparencywithstakeholdersapproachhas been emphasized here.

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