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EARNINGS MANAGEMENT: ANALYSIS OF POWERFUL CEOs IN THE PRESENCE OF SOCIAL TIES

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ABSTRACT

This study aimed to analyze the influence of powerful CEOs on earnings management (EM), considering the presence of social ties between the CEO and members of the board of directors (BD). The sample consisted of 183 Brazilian companies listed in [B]³ from 2011 to 2017, totaling 881 observations. EM was measured by the Jones (1991) and Modified Jones (1995) models and considered the dependent variable, under which the effect of (i) a CEO power metric developed by principal component analysis was analyzed from a multidimensional perspective of power (structural power, ownership power, power of specialization and power of prestige), (ii) an index that measures the level of social ties between the CEO and the Board members based on indicators already reviewed by the literature (educational, professional, and family relationships background), and (iii) the interaction between these variables. The results of 6 linear regression estimates (OLS) with cross-section pools and robust errors indicate that powerful CEOs are related to higher levels of discretionary accruals, while social ties mitigate EM. When the interaction between these variables is included, both CEO power and social ties may fail to engage in EM practices. This result contributes to the discussion about the interference of social factors on economic decisions, drawing attention to the impact of social factors on the quality of profits and the CG of companies.

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1 INTRODUCTION

In a context of separation between management and ownership, where managers have different incentives at the time of decision-making, the personal characteristics of these managers can offer a guide to *stakeholders* about the quality of the entity's corporate governance. This assessment is even more relevant in relation to the *Chief Executive Officer (CEO*), as they can act in favor of their personal interests to the detriment of shareholders. The CEO is the most influential agent in the organization, and this influence can come from observable characteristics, such as remuneration and duality, or unobservable characteristics, such as power.

The literature calls powerful CEOs as those agents with greater power to influence decisions (Adams, Almeida & Ferreira, 2005). In this regard, the role of the Board of Directors (BD) is even more relevant, as the BD can be "captured" by a powerful CEO, becoming entrenched (Bebchuk & Fried, 2004; Dow, 2013). In another aspect, the members of the BD have individual incentives to exercise the monitoring of the CEO (Hermalin & Weisbach, 1998), making the personal alignment between the agents gain relevance. In this environment of apparent tension, social ties can be beneficial for the company, as the literature has pointed these out as a factor for mitigating information asymmetry (Adams & Ferreira, 2007).

Previous studies report mixed results for companies led by powerful CEOs. In the same vein, are the results presented regarding the social ties between BD and CEO. In this way, it is pertinent to evaluate the consequences when, in addition to being powerful, this CEO is also socially connected with the BD since previous studies have not exhausted the theme. Thus, to seek a greater understanding of this interaction, this study focuses on analyzing the implications of this management profile on Earnings Management (EM).

The analysis decision involving EM among the list of possible corporate consequences considers that EM is discretionary. It should be noted that discretion is inherent to accounting processes. However, even though it is a practice that is part of the administration's routine, it deserves attention because, when combined with the existence of conflicting interests, it can encourage the use of freedom of judgment for purposes other than providing a true and appropriate view (Sprenger, Kronbauer & Costa, 2017). Thus, managers can use discretion aimed at EM to obtain some particular benefit (Schipper, 1989). Given the above, this study has its guiding question *"What is the effect of the CEO's power in earnings management in the presence of social ties?"* and aims to analyze the influence of CEO power on EM considering the presence of social ties.

To achieve the research's objective, we used the Jones (1991) and Modified Jones model as proxies for earnings management (Dechow et al., 1995). To measure the CEO power, a metric was constructed that considered eight variables that express the four dimensions of power proposed by Finkelstein (1992). The exploratory factor analysis technique was used with the principal components extraction method to measure this variable. As for the measurement of the level of social ties, a social tie index was constructed, consisting of 5 indicators characterizing elements of social tie based on the educational and professional *background* and the CEO's family relationship with the directors. From the results of econometric tests, we identified that powerful CEOs tend to be more involved in earnings management practices. However, in the presence of social ties, powerful CEOs may fail to engage in EM practices.

It is understood that this research contributes by offering empirical evidence on the management profile composed of powerful CEOs socially tied to the BD members. It contributes to complementing the previous literature, such as the studies by Göx and Hemmer (2020) and Caton et al. (2015). The research also presents a methodological contribution by employing its own measures of power and social ties that bring together different indicators already listed in the

literature in a single proxy. It also advances by demonstrating the interaction between such *proxies* on the EM since no studies have been identified that have addressed this same approach.

Empirically, this study is relevant for investors, regulatory bodies, and governance agents, as it draws attention to unobservable aspects that influence the quality of CG. The results can be useful to regulatory bodies, as they can be used to discuss normative actions and deliberations on governance mechanisms to mitigate the perverse effects of powerful CEOs and social ties. Governance agents can use the results to establish institutional policies and strategies to ensure the efficiency of governance mechanisms in the presence of powerful CEOs. For investors, the study contributes to the elucidation and discussion of social factors that can influence decisions and economic results, and thus, should also be observed during an investment decision process.

The study is organized into five sections, initially presenting the introduction. The second consists of a review of the theoretical and empirical literature, followed by methodological procedures. The fourth section presents the analysis and interpretation of the results. Finally, final considerations and suggestions for future studies are presented.

2 THEORETICAL FRAMEWORK AND HYPOTHESIS DEVELOPMENT

Among the elements reported through the financial statements, profit can be understood as one of the main elements with informational load, as it can induce the behavior of users of accounting information, to establish expectations about the organization's earnings, and to provide relevant information about the organization's performance that impacts specific decision making (Beaver, 1968; Dechow et al., 2010). In this spectrum comes earnings management, which occurs when managers use judgment to make accounting choices or structure transactions to intentionally intervene in the modification of financial statements (Healy & Wahlen, 1999; Kothari, 2001; Schipper, 1989). The occurrence of earnings management is due to the managers' discretion to influence the reported earnings.

The motivating factors for earnings management can be divided into three groups: (i) those linked to the capital market, which aims to manipulate accounting information to influence the risk perception of the company's investors; (ii) the factors linked to contractual relationships, related to the compensation of managers, the relationship with investors and creditors, and finally, (iii) regulatory factors and political costs, focused on avoiding political friction with other companies of the same and other sectors to avoid any possibility of regulatory intervention (Martinez, 2001). According to Ball (2006), political and economic aspects of the institutional environment in which the company is inserted can also interfere in the decisions of practices, standards, and norms to be adopted by the agents involved in the process of preparing the financial statements, which consequently can affect the quality of reported accounting information. The attention and importance given to profit can be an incentive for managers to use earnings management not to disappoint investors and, consequently, not affect the evaluation of their performance (Chan et al., 2016), thus denoting a private benefit. For Healy and Wahlen (1999), managers would not be interested in managing earnings in the absence of potential benefits. From the above, it is possible to argue that the opportunistic behavior of managers may be linked to the practice of earnings management, be it for the benefit of the entity and shareholders or for their own benefit.

Although EM is already widely discussed and investigated, academia has paid little attention to social aspects that can shape the behaviors of agents involved in the governance system of organizations, such as the board and the CEO, and how this can influence EM. Besides, previous investigations indicate that the social dynamics and behaviors of governance actors also need to be taken into account, as economic decisions and the efficient exercise of their functions are directly linked to the psychosocial processes of the actors involved (Nicholson et al., 2017; Ogunseyin, 2017; Pugliese et al., 2015). And within these social aspects that can affect decisions

to manage earnings, there is the CEO power and the social ties between them and the members of the Board of Directors.

The CEO represents the most influential agent in an organization and, probably, the driver of strategic choices as well as organizational results (Child, 1972, Daily & Johnson, 1997, Bigley & Wiersema, 2002, Lewellyn & Muller-Kahle, 2012), and their power to influence decisions must be considered by *stakeholders*. Those senior executives with greater power to consistently influence decisions are referred to in the literature as powerful CEOs (Adams, Almeida & Ferreira, 2005). Therefore, powerful CEOs are endowed with the ability to make decisions without the need to build consensus on it (Gupta et al., 2018).

From the perspective of Agency Theory, in an environment of separation between control and ownership, a powerful CEO could benefit from the ease of making decisions to obtain advantages for themselves at the expense of shareholders, giving rise to a conflict of interest. The presence of a powerful CEO can even inhibit the effectiveness of CG controls (Rickling & Sharma, 2017). Thus, a powerful CEO would maintain substantial control over the company, despite opposition from other executives or board members (Francoeur et al., 2021). Additionally, to internal decisions, the CEO power can influence the company's performance and, consequently, their compensation (Amedu & Dulewicz, 2018). This risk can be exacerbated in a shareholding context such as the Brazilian one, where there is weak legal protection for shareholders and a high shareholding concentration.

Several conditions, observable or not, can give a CEO greater power within an organization. The duality of the CEO, shareholding, remuneration, and the fact that the CEO is the founder of the company, for example, have already been observed separately in the literature, which assumed these characteristics as a *proxy* for the CEO's power (Vo & Canil, 2019; Rickling & Sharma, 2017; Adams, Almeida & Ferreira, 2005; Amedu & Dulewicz, 2018). In this light, identifying a powerful CEO is a cautious task, as power can come from many sources. This identification can be made from the proposition of Finkelstein (1992), which presents four dimensions of power: structural power, property power, specialized power, and prestige power. The first dimension refers to the hierarchical position assumed by the executive, the second is linked to their ownership in the company, their control, as well as their ties with the founder, the third dimension refers to the executive's knowledge and experience, and the fourth represents their reputation or *status*.

Larcker and Tayan (2012) state that it is still unclear to what extent having a powerful CEO is beneficial for an organization and its shareholders. Among the topics that have received attention from researchers for this analysis, there is the EM. For Schipper (1989), EM comprises a purposeful intervention in preparing financial statements to obtain some particular benefit. It is understood that this practice directly affects the company's earnings and, consequently, the CEO, either through the bonuses that will be received or through their reputation and ability to manage the company.

Thus, Zhou, Wang, Zhang, and An (2018) indicate that powerful CEOs are more likely to undertake EM to increase their compensation. One can also cite as motivations: the maintenance of their *status*, the report of a favorable performance for the shareholders, the protection of discrepancies of the earnings in relation to the market forecasts, the mitigation of risks involving the oscillations of the earning and, consequently, the stock volatility, among others (Ali & Zhang, 2015, Klein, 2002, Lin, 2014, Malmendier & Tate, 2009, O'Connor Jr, Priem, Coombs, & Gilley, 2006, Petrou & Procopiou, 2016, Zhou et al., 2018). Given this circumstance, it is conjectured that:

H_1: CEO power is positively related to EM.

As well as the CEO power, other unobservable aspects can influence the quality of an organization's CG. Although the literature focuses on formal aspects of the BD configuration to classify a BD as independent, the existence of social factors that bring the members of the BD and the CEO together also affect the roles played by the BD in an organization. Thus, the social ties between CEO and BD, understood as a factor of approximation between individuals, can influence corporate decisions, including the discretion of sharing information between the agents involved. In this aspect, the degree of monitoring of the BD may vary according to its composition, given that its members exhibit different levels of alignment of preferences with the CEO or with the shareholders, as well as having different individual incentives to monitor the CEO (Göx & Hemmer, 2020, Hermalin & Weisbach, 1998). The alignment of preferences, as well as individual incentives, may result from common backgrounds between the CEO and the members of the BD (social ties), which would generate a sense of belonging, favoring the personal interaction of agents, reducing information asymmetry (McPherson et al., 2001; Holmström, 2006; Westphal, 1999).

Previous studies on social ties between CEOs and BD were ambiguous regarding the quality of accounting information. Krishnan et al. (2011) suggest a positive relationship between the social ties of the CFO/CEO with the board and the EM of the analyzed entities. Hoitash (2011) identified that the quality of statements and internal controls are better in organizations with social ties between CEOs and BD, indicating that these ties can add value to shareholders. Dimitrova (2017) found no relationship between the social tie of CEOs and board members with EM in the US market. The study by Kuang et al. (2020) shows that social ties between CFOs and directors decrease the likelihood of resubmission of financial statements. When evaluating from the perspective of accounting conservatism, Zhang et al. (2020) identified a negative relationship between the social ties CEO x board and accounting conservatism.

Considering that the existence of social ties between CEO and BD members can mitigate information asymmetry and, consequently, reduce the CEO's pressure to present short-term earnings, reducing the incentive for the CEO to engage in practices of EM (Ge & Kim, 2014), the second hypothesis is proposed:

H_2: The social ties between the CEO and the BD members are negatively related to the EM.

In this regard, the effectiveness of the BD's advisory function can be related to the closeness between the CEO and the BD members. For the BD to provide good advice, the CEO needs to share their information with the BD. Therefore, a BD closer to a powerful CEO can optimize the quality and usefulness of the BD's functions (Caton et al., 2015). In this sense, Göx and Hemmer (2020) studied how a "friendly" BD would affect the CEO's incentives to manage earnings, pointing out that in these cases, there is a lower level of EM. Caton et al. (2015) indicate that the negative influence of CEO power on company value is limited to companies with independent BD. In this aspect, the presence of social ties between the CEO and the BD members would increase the sharing of information, reducing the CEO entrenchment.

From this perspective, it is conjectured that companies with social ties between the CEO and the BD, even led by a powerful CEO, may have a lower level of EM. Based on previous studies and predicting that an environment of greater trust between CEO and BD (Holmströn, 2004) would allow the CEO to feel more comfortable sharing information (Westphal, 1999), in addition to suffering less pressure in relation to performance (Ge & Kim, 2014), the third hypothesis is elaborated:

H_3: In the presence of social ties, CEO power is negatively related to EM.

The relationships object of the study can be summarized as shown in Figure 1.

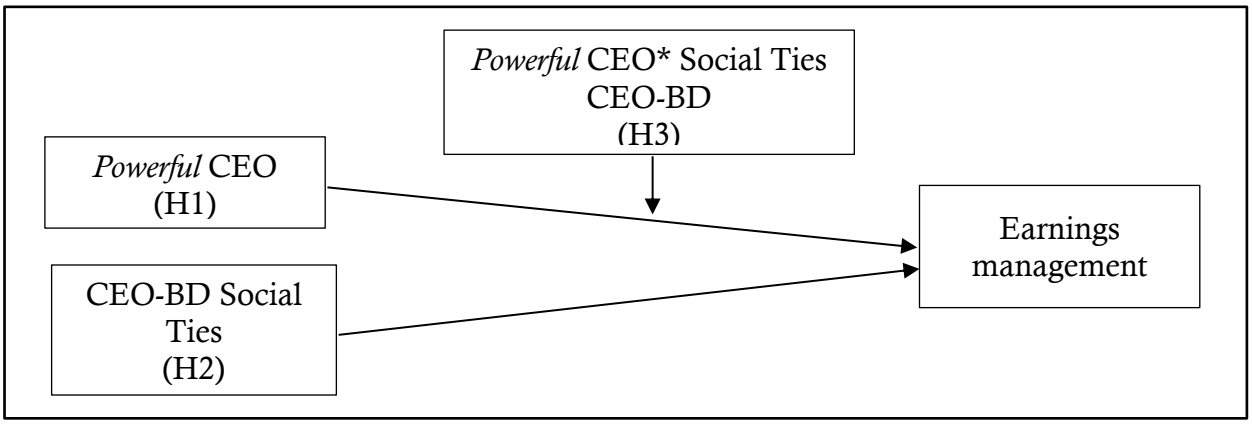

Figure 1. Research hypotheses.

In the following section, we describe the methodological procedures to test the research hypotheses.

3 METHODOLOGICAL PROCEDURES

The study population comprised publicly traded companies listed on [B][3] between 2011 and 2017. To define the sample, the following criteria were established: (i) not being a financial institution; (ii) have data for at least two periods; and (iii) having all the necessary data for the variables under study. A final sample of 818 observations from 183 companies was obtained based on the established criteria.

Three models were established to test the research hypotheses, which were estimated considering two earnings management *proxies* as dependent variables, namely: Jones (1991) and Jones Modified (Dechow et al., 1995). Equation (1) shows the model used to test the effect of CEO power on EM (*PwCEO*) (H_1):

$$ACCRUALS_{it} = \beta_0 + \beta_1 PwCEO_{it} + \sum_k^{22}\{\gamma_k Control_{k,i,t}\} + \varepsilon_{it} (1).$$

To test the effect of the level of social ties between CEO x BD (ICSCA) on EM (H_2), the equational model (2) was used:

$$ACCRUALS_{it} = \beta_0 + \beta_1 PwCEO_{it} + \beta_2 \text{ICSCA}_{it} + \sum_k^{22}\{\gamma_k Control_{k,i,t}\} + \varepsilon_{it} (2).$$

Finally, equation (3) was used to test the effect of the interaction between the CEO power and their level of social ties on the practice of EM (H_3):

$$ACCRUALS_{it} = \beta_0 + \beta_1 PwCEO_{it} + \beta_2 \text{ICSCA}_{it} + \beta_3 PwCEO * ICSCA + \sum_k^{22}\{\gamma_k Control_{k,i,t}\} + \varepsilon_{it} (3).$$

The dependent variable of the three models for the two *proxies* used consisted of the *accruals* obtained through multiple linear regression estimates for each year of observation and with all companies aggregated. This estimation derives from the characteristics of the sample (low number of companies per sector/year). By operationalizing the estimation of *accruals* as reported, concerns regarding the change in general levels of *accruals* that result from events in each year are mitigated, given that the intercepts of each estimation/year already capture these effects (Costa et al., 2018). Consistent with previous studies, the absolute values of the residuals of the *accruals* models were used, disregarding the existence of a positive or negative sign of the measured values (García Lara et al., 2017; Hooghiemstra et al., 2019; Van Linden & Mazza, 2018).

The independent variables considered in this study comprised the CEO power($PwCEO_{it}$) (H1), the social tie index ($ICSCA_{it}$) (H2), and the interaction between them (H3). The $PwCEO_{it}$ variable was constructed from eight variables that express the dimensions of power proposed by Finkelstein (1992), adapted to the Brazilian scenario (Table 1). The calculation of this variable was made possible from the exploratory factor analysis technique with the principal components extraction method. The Kaiser-Meyer-Olkin statistics (KMO statistics) and the Barlett's test of sphericity obtained using the Stata® software indicated the adequacy of the proposal, according to the results presented in Appendix A. Thus, new variables were created to store the rotated factors (Varimax) annually. Subsequently, the criterion of the weighted sum of factors by shared variance was applied, generating a new continuous variable for each CEO in each year analyzed ($PwCEO_{it}$).

Table 1
Variables representing the dimensions of power.

Dimension	Variable	Operationalization
Structural Power	Duality	1 if the CEO is also chairman of the BD and 0 otherwise
	Centrality	ratio between the maximum remuneration and the mean remuneration of the statutory board, this value having been normalized in relation to the highest
Power of Ownership	Shareholder CEO	1 if the CEO is one of the top 5 shareholders and 0 otherwise
	Founding CEO	1 if the CEO is one of the founders and 0 otherwise
Specialization Power	CEO age	number of years
	Consecutive CEO mandates	number of years
Power of Prestige	News involving the CEO	number of news between t_{-5} and t, normalized by the highest value
	CEO awarded as executive of value	1 if the CEO was awarded as an executive of value and 0 otherwise

Source: Prepared by the authors (2021).

The variable $ICSCA_{it}$ was measured from 5 indicators (Table 2) considering educational, professional, and family aspects, based on previous studies (Dimitrova, 2017; Fracassi & Tate, 2012; Kang et al., 2018; Krishnan et al., 2011; McGuinness, 2016; Schmidt, 2015; Wilbanks et al., 2017, Ramos, 2020, Locatelli et al., 2021). The calculated index is established on a scale from 0 to 1, and the closer to 1, the greater the social tie between the CEO and the board. The index was calculated for each year and analyzed company.

Table 2
Social Tie Indicators

ITEM		OPERATIONALIZATION	
Education	Higher Education Institution (Undergraduate course)	1 when the director studied at the same higher education institution at the undergraduate level as the CEO and 0 otherwise.	Each indicator was established based on the proportion of members who are connected to the CEO in relation to the total number of effective members, expressed in decimal notation ranging from 0 to 1. Thus, 0 indicates that no effective Board members are socially connected with the CEO and 1 indicates that all effective Board members are
Professional Experience	Direct tie with the Board	1 when the director is also a member of the Executive Board and 0 otherwise.	
	Previous Professional Experience	1 when the director has previously worked in the same company as the CEO and 0 otherwise.	
	Participation in Boards	1 when the director has already worked on the board of another company where the CEO also worked as a director and 0 otherwise.	

Family	Has a family relationship with the company	1 when the director declares to have a family relationship with the company and 0 otherwise.	socially tied with the CEO.

Source: Prepared by the authors (2021).

Equation 4 presents the formula used to calculate the CEO x BD social tie index per company/year (Locatelli et al., 2021; Ramos, 2020).

$$ICSCA_{it} = \frac{\sum IND_{it}}{5} (4)$$

Where:
ICSCA = CEO x BD Social Tie Index of company *i* in year *t*
∑IND = Sum of proportions of members tied to the CEO considering the 5 indicators calculated from the checklist presented in Figure 2 of company *i* in year *t*
5 = Number of indicators.

The third independent variable (*PwCEO*ICSCA*) (H_3) was operationalized from the interaction between the variables $PwCEO_{it}$ and $ICSCA_{it}$ to allow testing the effect of the relationship between the CEO power and the level of social tie on the earnings management of the analyzed companies.

Control variables were also considered in the study (Table 3), as according to previous investigations, financial and governance elements and organizational and CEO characteristics can influence EM. To reduce the impact of observations with outliers, the financial variables were submitted to the *winsorization* technique, where a lower limit (1%) and an upper limit (99%) were applied.

Table 3
Operationalization of control variables

Variable	Operationalization
Size	Natural logarithm of the total value of the asset.
Leveraging	Ratio of the sum of current and non-current liabilities by total assets.
Return on Assets (ROA)	Ratio of the company's net income in year *t* to total assets in year *t-1*.
Cash Flow	Ratio between operating cash flow and average total assets.
Loss	*Dummy* variable that assumes 1 for when the company has a negative result at t and 0 otherwise.
Gross Margin	Ratio between gross profit and net sales revenue.
Operating cycle	Operational cycle log. Sum between the mean storage period and the mean sales receipt period.
Size of the Board of Directors (BD)	Number of members of the board of directors.
% Women in BD	Proportion of women present on the board over the total number of members of the board of directors.
% BD Independent Members	Proportion of members declared independent by the total number of board members.
% BD Accountant Members	Number of directors trained in accounting sciences.
% Members elected by controllers	Proportion of members elected by controllers.
CEO duality	Assigned 1 for when the CEO is also chairman of the board of directors and 0 otherwise.
Big Four	Assigned 1 for when the audit firm is among the *Big Four*, and 0 otherwise.
Fiscal Council	Assigned 1 for the presence of the fiscal council and 0 otherwise.

New Market	Assigned 1 for when the company is listed in the "Novo Mercado" segment, and 0 otherwise.
Company Age	Established by subtracting the year of observation from the year of incorporation of the company.
Family Business	Assigned 1 for when it is a family business, and 0 otherwise.
CEO gender	Assigned 1 for when the CEO is female and 0 otherwise.
Age	CEO age measured by subtracting the year of observation from the CEO's birth year.
State Control	Assigned 1 when the shareholding is state-owned and 0 otherwise.
Sector	*Dummy* variable created from the sector classification for each sector. Sector classification given based on [B][3].

Source: Prepared by the authors (2021).

For data collection, personal information, and resumes of CEOs and BD, level of corporate governance, size of the auditing firm, and family business were initially obtained from the Reference Form (RF). The documents were extracted from the [B][3] website using RStudio® software using the GetDFPData package (Perlin et al., 2018). Economic and financial data were extracted from the Economática® database. The data for identifying the CEO prestige power were obtained through Google News ® and the "Executive of Value" yearbook published by the Valor Econômico® newspaper. The operationalization of the variables individually considered is presented in Appendix A.

These equations were operationalized in 6 estimations, given the gradual inclusion of independent variables in each EM model tested, using a multiple linear regression test with cross-section pools and robust errors.

4 RESULTS AND DISCUSSION

To allow the characterization of the companies in the sample and the variables analyzed, Table 4 presents the descriptive statistics of the data. As reported, it is possible to identify that the *accruals* measured by the absolute value have a mean of 0.0688 when measured by the Jones model (1991) and 0.0611 by the Modified Jones (Dechow et al., 1995). The fact that the *accruals* captured by Jones Modified (accrualJM) are inferior to the Jones model (*accrualJ*) is understandable since it adds variables that can interfere in capturing the EM practice.

Table 4
Descriptive statistics

	Note	Mean	Standard Deviation	Min	Max
Panel A: Dependent variables					
accrualJ	818	0.0688	0.0764	0	0.618
*accrual*JM	818	0.0611	0.0720	0	0.473
Part B: Independent variables					
PwCEO	818	2.81e-10	0.350	-0.777	1.879
ICSCA	818	0.187	0.120	0	0.550
Panel C: Controls					
Size	818	14.90	1.653	9.437	20.44
Leveraging	818	0.672	0.620	0.0847	11.04
ROA	818	0.0239	0.156	-1.595	1.989
Cash Flow	818	0.0650	0.0849	-0.313	0.407
Loss	818	0.302	0.459	0	1
Gross Margin	818	0.316	0.252	-2.762	1

Operating cycle	818	4.844	0.887	1.487	8.711
BD size	818	7.344	2.532	2	17
% Women in BD	818	0.0718	0.116	0	0.667
% BD Independent Members	818	0.254	0.224	0	1
% BD Accountant Members	818	0.0303	0.0645	0	0.400
% Members elected by controllers	818	0.728	0.321	0	1
CEO duality	818	0.112	0.316	0	1
Big four	818	0.813	0.390	0	1
Installed Fiscal Council	818	0.641	0.480	0	1
New Market	818	0.500	0.500	0	1
Company Age	818	32.55	18.90	1	126
Family Business	818	0.472	0.500	0	1
CEO gender	818	0.0293	0.169	0	1
Age	818	54.48	10.30	24	92
State Control	818	0.0868	0.282	0	1

Source: Research data (2021).

Regarding the variable ICSCA, a mean of 0.187 points is observed, which represents a low index of social tie on a scale from 0 to 1. The maximum value reached was 0.550, indicating an organization with a CEO that is highly tied with the BD members. On the other hand, the PwCEO variable presented a variation between -0.777 and 1.879, indicating that for this sample, there are CEOs who have more than one power attribute, contributing to their classification as a powerful CEO.

Regarding the financial variables, a mean of 2.39% (ROA) is identified, with a minimum negative value, corroborated by the Loss variable, indicating that 30.20% of the companies presented losses in the period analyzed. Of the companies that make up the sample, 47.20% are family members, 64.10% have a fiscal council installed, and the Big Four audit 81.3%. Regarding the characteristics of the BDs, it is possible to identify that the mean size is approximately 7 directors, and the mean female participation in the BD is 7.18%. 25.4% of the members of the BDs are formally classified as independent members, and the controller elected 72.8%.

To test the research hypotheses, equations (1), (2), and (3) were operationalized in 6 estimations and are reported in Table 5.

Table 5
Estimation results

	(1) *accrualJ*	(2) *accrualJ*	(3) *accrualJ*	(4) *accrualJM*	(5) *accrualJM*	(6) *accrualJM*
PwCEO	0.0235**	0.0265**	0.0315	0.0295***	0.0291**	0.0189
	(0.0120)	(0.0124)	(0.0221)	(0.0112)	(0.0115)	(0.0187)
ICSCA		-0.0428*	-0.0437*		0.0059	0.00788
		(0.0250)	(0.0258)		(0.0220)	(0.0225)
PwCEO*ICSA			-0.0246			0.0501
			(0.0742)			(0.0690)
Size	-0.0073***	-0.0069***	-0.0068***	-0.0040*	-0.00417*	-0.00417*
	(0.0022)	(0.0022)	(0.0022)	0.0021	0.0021	0.0021
Leveraging	0.0319***	0.0313***	0.0312***	0.0392***	0.0393***	0.0395***
	(0.0095)	(0.0095)	(0.0096)	(0.00947)	(0.0094)	(0.0095)
ROA	-0.0115	-0.0111	-0.0117	-0.0137	-0.0138	-0.0125
	(0.0506)	(0.0505)	(0.0501)	(0.0482)	(0.0482)	(0.0481)
Cash Flow	-0.0435	-0.0395	-0.0405	0.0242	0.0237	0.0257
	(0.0497)	(0.0500)	(0.0500)	(0.0464)	(0.0469)	(0.0469)
Loss	-0.0067	-0.0069	-0.0067	-0.0036	-0.0036	-0.0039
	(0.0077)	(0.0077)	(0.0078)	(0.0070)	(0.0070)	(0.0070)
Gross Margin	-0.0048	-0.0076	-0.0076	-0.0232	-0.0228	-0.0230

	(0.0147)	(0.0148)	(0.0148)	(0.0141)	(0.0142)	(0.0142)
Operating cycle	0.0059	0.0064*	0.0064*	0.0064*	0.0063*	0.0062*
	(0.0038)	(0.0038)	(0.0038)	(0.0038)	(0.0038)	(0.0038)
BD size	0.0001	-0.0001	-0.0001	-0.00174	-0.00173	-0.00172
	(0.0014)	(0.0014)	(0.0014)	(0.0012)	(0.0012)	(0.0012)
% Independent BD Members	-0.0241	-0.0256*	-0.0258*	-0.0186	-0.0184	-0.0181
	(0.0152)	(0.0152)	(0.0153)	(0.0150)	(0.0150)	(0.0151)
% BD Accountants	-0.0551	-0.0553	-0.0564	-0.0136	-0.0136	-0.0113
	(0.0393)	(0.0393)	(0.0394)	(0.0383)	(0.0383)	(0.0382)
CEO duality	0.0044	0.0042	0.0041	-0.0224***	-0.0224***	-0.0222***
	(0.0100)	(0.0099)	(0.0098)	(0.0076)	(0.0076)	(0.0076)
BIG4	-0.0025	-0.0038	-0.0037	-0.0040	-0.0038	-0.0040
	(0.0083)	(0.0083)	(0.0083)	(0.0075)	(0.0076)	(0.0076)
Installed Fiscal Council	0.0087	0.0081	0.0082	0.0065	0.0066	0.0063
	(0.0060)	(0.0060)	(0.0059)	(0.0058)	(0.0057)	(0.0057)
New Market	0.0051	0.0053	0.0053	0.0020	0.0020	0.0019
	(0.0071)	(0.0071)	(0.0071)	(0.0065)	(0.0065)	(0.0065)
% BD Women	-0.0033	-0.002	-0.0018	0.0184	0.0183	0.0162
	(0.0323)	(0.0321)	(0.0317)	(0.0294)	(0.0294)	(0.0297)
Company Age	-0.0004**	-0.0003**	-0.0003**	-0.0003**	-0.0003**	-0.0003**
	(0.0001)	(0.0002)	(0.0002)	(0.0001)	(0.0001)	(0.0001)
State Control	0.0138	0.0128	0.0127	0.0163	0.0165	0.0166
	(0.0115)	(0.0116)	(0.0116)	(0.0110)	(0.0110)	(0.0110)
Family business	-0.00284	-0.0015	-0.0014	0.0031	0.0029	0.0029
	(0.0062)	(0.006548)	(0.0065)	(0.0061)	(0.0062)	(0.0062)
CEO Gender	-0.0391***	-0.0376***	-0.0379***	-0.0410***	-0.0412***	-0.0406***
	(0.0107)	(0.0106)	(0.0105)	(0.0097)	(0.0098)	(0.0098)
CEO Age	-0.0010**	-0.0010**	-0.0009**	-0.0010***	-0.0011***	-0.0011***
	(0.0004)	(0.0004)	(0.0004)	(0.0004)	(0.0004)	(0.0004)
%Members elected by the BD controller	-0.0030	0.0003	0.0003	-0.0072	-0.0076	-0.0078
	(0.0105)	(0.0105)	(0.0105)	(0.0106)	(0.0106)	(0.0106)
Sector	Yes	Yes	Yes	Yes	Yes	Yes
_cons	0.280***	0.277***	0.276***	0.233***	0.233***	0.235***
	(0.0546)	(0.0543)	(0.0545)	(0.0501)	(0.0501)	(0.0504)
Notes	818	818	818	818	818	818
Adjusted R2	0.114	0.117	0.116	0.122	0.121	0.120
F Statistic	3.987***	3878***	3.752***	3.558***	3.483***	3.354***

Standard errors in parentheses * $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$
Source: Research data (2021).

Table 5 shows that the CEO power variable positively affects EM in all estimations, except when the interaction variable between CEO power and social ties is included. The results indicate that the more powerful the CEO, the greater tends to be the practice of EM, culminating in the non-rejection of H_1. In this sense, more powerful CEOs tend to manage earnings more, which may indicate a posture focused on obtaining their own benefits at the expense of shareholders. These results are similar to those found in the reviewed literature, indicating that there may be motivations that lead powerful CEOs to engage in the practice of earnings management. These motivations may be related to remuneration, *status*, bonuses, among others (Ali & Zhang, 2015, Klein, 2002, Lin, 2014, Malmendier & Tate, 2009, O'Connor Jr, Priem, Coombs, & Gilley, 2006), Petrou & Procopiou, 2016, Zhou et al., 2018).

The ICSCA variable had a negative and significant effect on EM only when considering the Jones model (1991); this result is similar to the study by Hoitash (2011) and Ramos (2020). It

is believed that this relationship occurs because a more tied board can improve the flow of information, thus mitigating information asymmetry, given the establishment of trust between the CEO and BD. Besides, another aspect to be considered is the reputation of the agents, which in a scenario where there is a high density of board networks, such as the Brazilian one (Dal Magro & Klann, 2019), both CEO and directors act in a way not to get involved in scandals or events that could come to harm the personal image and jeopardize the development of future business. Still on reputation, according to Granovetter (1973), subjects tend to be more responsible with those they know than with other individuals who have no ties.

According to the results presented in Table 5, when the CEO power and social ties *proxies* are evaluated in isolation, both are statistically significant in relation to the EM. However, they lose significance when an interaction variable is included between them. Regarding this result, it is believed that in the presence of social ties, powerful CEOs may fail to engage in EM practices, given that an environment of greater trust between CEO and BD (Holmström, 2004) would allow the CEO to feel more comfortable sharing information (Westphal, 1999), in addition to suffering less pressure regarding earnings (Ge & Kim, 2014).

Finally, the control variables showed relationships with EM similar to the results of previous studies, an example of which are the variables Size and Age of the company, which proved to be negative and significant in all specifications, which indicates that larger or more mature companies tend to be less involved in earnings management practices (Chalmers et al., 2019; Shust, 2015). Likewise, the Leverage variable showed significance with a positive coefficient, indicating that more leveraged companies tend to have greater earnings management. According to previous literature, this practice in leveraged companies may be related to reporting positive earnings to obtain better conditions in capital raising (Anagnostopoulou & Tsekrekos, 2017).

The results of the study point to the relevance of the CEO's gender and age when analyzing the practice of earnings management in the presence of powerful CEOs and social ties. In line with previous studies, female CEOs were less likely to engage in earnings management practices (Gull et al., 2018; Liu et al., 2016). On the other hand, when analyzing the age of the CEO, the result of the study is in line with previous studies indicating that older CEOs tend to manage more earnings. This behavior can be justified because older CEOs are less concerned with future earnings, seeking to anticipate profits (Belot & Serve, 2018). The CEO duality is in line with previous studies (Baker et al., 2019), indicating that dual CEOs tend to be more involved in earnings management practices; this result may indicate a greater entrenchment of the BD in the presence of a dual CEO.

5 CONCLUSION

The objective of this study was to analyze the influence of the CEO's power on the EM considering the presence of social ties. From the results, it was possible to verify that the CEO's power contributes to the increase in the levels of discretionary *accruals*, while social ties mitigate EM. When including an interaction variable between power and ties, it was observed that these variables lose their effect on the EM. Thus, in the presence of social ties, powerful CEOs may fail to engage in EM practices because the environment of greater trust could reduce pressure on the CEO about the company's performance and increase information sharing,

This study advances in relation to the existing literature in several respects. Empirically, the results draw attention to the influence of unobservable factors (CEO power and social ties) on earnings quality and, ultimately, on the quality of CG. In this same aspect, the results demonstrate that, in isolation, power is harmful to the company, as it positively impacts the practice of EM. On the other hand, social ties tend to minimize this practice and, in the presence of powerful CEOs, act as a mitigator of EM.

Methodologically, this study contributes by using its own power metric capable of encompassing multidimensional aspects of CEO power, as well as an index of social tie. The use of aggregated data, either through the power metric or through the ICS, allows the comparability of companies.

It is understood that these results are relevant for policymakers to hire CEOs and directors, regulatory bodies, and institutes of corporate governance, aiming at good practices in the composition of boards. In the theoretical field, this study adds to the evidence that elements of social interactions and CEO power can affect the behavior of governance agents and, consequently, the quality of information. The results of this empirical investigation can be useful to boards so that they can discuss and redefine CEO and director selection and recruitment policies, considering elements of social tie and CEO power as criteria to be observed in the selection process. To regulatory bodies and *stakeholders*, the results found are relevant as they indicate opportunities for re-discussion and reformulation of corporate governance guidelines regarding social ties and the CEO power in the Brazilian market.

In this study, the assessment of possible social ties was limited to the relationship between the CEO and the members of the board of directors. Thus, further research can be carried out evaluating the social ties between directors. When discussing social ties in the scope of governance, we seek to reflect on the effect of social aspects as possible influencers of the economic behavior of agents. Thus, it is suggested that further research investigate the isolated effects of each connecting element and others (religion, political ideology, etc.), as well as alternative metrics to measure them. Besides, it is believed that the social ties between CEO and directors and the CEO power can affect various strategic decisions and administrative and accounting aspects, which opens an opportunity for further research to be conducted.

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