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EXPLORING THE RELATIONSHIP BETWEEN EARNINGS MANAGEMENT AND CORPORATE SOCIAL RESPONSIBILITY REPORTING IN NIGERIAN COMPANIES

Confidence Joel Ihenyen Ph.D[1], Samson Milton NA'AGI[2]
Chinaemezu Evangelina OJIAKU[3]
Department of Accountancy, Faculty of Management Sciences, Niger Delta University, PMB 71, Wilberforce Island, Bayelsa State, Nigeria.

ABSTRACT

This study specifically was examined to interrogate the connection among earnings management and corporate social responsibility in Nigerian corporations. Thus, in order to conduct this study, real earnings management, abnormal production costs, abnormal cash flows and abnormal discretionary expenses were used as the proxies of earnings management while corporate social responsibility score was the measure of CSR reporting. Using cross – sectional quasi – experimental research design, as well as ordinary least square regression analysis to analyse data obtained from the annual reports of 30 manufacturing companies listed on the Nigerian Stock Exchange between 2012-2021, results indicated a significantly positive association among the two variables. Therefore, it was suggested, as one of the recommendations, that since earnings management practice has become a norm in the accounting world, it is also suggested that in order to curb this practice among manufacturing companies in Nigeria, the internal control system should be strengthened and the content of accounting ethics should also be used to build an ethical environment so as to enhance the ethical perception of management and employees.

KEYWORDS: *Corporate, Earnings, Discretionary, Management, Responsibility, Social*

1. INTRODUCTION

Earnings are regarded as the single most important figure in the financial statements of any organization, hence they are one of the performance statistics often referred to as a point of interest to critical stakeholders such as providers of funds, creditors, investors, suppliers, employees, management, customers, as well as the communities hosting these organisations. Earnings are said to be important because they show the real profitability of the organisation, hence they are an indication of the progression, or otherwise, of any entity towards the achievement of their objectives (Iyobosa, 2021). Therefore, the reported earnings in the financial statements of a company goes a long way in influencing the decisions of concerned stakeholders. It is not far-fetched that financial reporting helps a firm which is performing optimally to be distinguishable from a company whose performance is sub-par. It is in view of the apparent importance of reported earnings in the financial statements of companies that managers/ directors always look for ways and means to give a picture of their economic performance over time. One of such ways employed by management of a company to show the public that they are performing at optimum is by strategically manipulating the financial statements, often within the boundaries of the rules and regulations of accounting, with the aim of influencing the reported earnings figures in order to achieve a specific financial objective or to depict a desired image of the financial performance of the company, thereby potentially influencing stock prices, stakeholders' perception or confidence, according to Huanzhen (2022) . This strategic manipulation of the company's financial statement is referred to as earnings management.

In the opinion of Iyobosa (2021), all over the world, the issue of earnings management has become a topical and global phenomenon with perceived negative impacts on companies, thereby creating so much uproar in the academic world (that is, among academics, scholars, and industry professionals). It has been argued that earnings management has led to the fall of globally acclaimed corporations such as such as Enron, WorldCom, Xerox. As a matter of fact, come Nigerian companies have equally been badly hit by this accounting technique, chief among them are Cadbury Nigeria

Plc and Intercontinental Bank Plc. A number of studies have been carried out in order to investigate the global increase of managers and firms fabricating or falsifying financial records (Harris, et al., 2019). The intentional manipulation of financial statements by management reduces the reliability and authenticity of the accounts, which essentially affects how the firm's stakeholders make decisions (Kurawa & Ahmed, 2020). Additionally, Kurawa and Ahmed (2020) point out that a variety of circumstances might encourage directors to control profitability. Increasing stock market prices, accepting performance-based incentives in advance, avoiding taxes, and influencing the terms of contracts are a few of these issues. Managers have the ability to manipulate or influence profits in order to further their own agendas or to divulge confidential information, which may affect earnings data (Chen et al., 2018). Although there is no guarantee that earnings management complies with all financial reporting laws and regulations, such as GAAP or the International Financial Reporting Standard (IFRS), it has become so prevalent in recent years that many people have become aware of it (Huanzhen, 2022).

On the other hand, over the past few decades, corporate social responsibility (CSR) has gained more recognition in the business world, which has resulted in a greater sense of conscientiousness regarding the strategies used to generate and allocate profits. Presently, enterprises exhibit a heightened preoccupation with their ethical and moral comportment, as well as their interconnectedness with pertinent factions of societal interest (Ahmed, 2017). It is widely acknowledged that companies can attain various benefits by cultivating a favourable perception among their stakeholders and fostering strong connections with employees and the surrounding community. This, in turn, leads to the acquisition of a positive reputation (Gras-Gil et al., 2016). In practical application, it is observed that enterprises that undertake corporate social responsibility initiatives and disseminate corresponding reports to the general public are inherently obligated to furnish transparent and dependable financial data while simultaneously showcasing a steadfast dedication to ethical conduct and responsible governance. Nevertheless, it can be contended that corporate social responsibility (CSR) may serve as a mechanism for managers to solidify their own interests by manipulating earnings information, as posited by Kouaib and Almulhim in their 2019 study.

Scholars generally think of earnings management (EM) as an ethical dilemma, which is why Iyobosa (2021) says it's important to look into the possible link between EM and corporate social responsibility. Numerous studies have endeavoured to shed light on this association. Nevertheless, the findings derived from these numerous studies conducted over a period of time have exhibited a notable lack of consistency, to put it mildly. In light of the persistently inconclusive empirical findings, it is imperative to undertake further research in order to delve into the intricate relationship between earnings management and corporate social responsibility reporting within corporate entities. Consequently, this scholarly investigation endeavours to bridge this lacuna by elucidating the matter further. Furthermore, it is imperative to note that there exists a dearth of comprehensive research pertaining to the Nigerian context in relation to this particular study, as per the discernment of these esteemed researchers. Given the conspicuous voids in the existing body of literature, this study aims to scrutinise the intricate correlation between earnings management (as gauged by total real earnings management, abnormal production, abnormal discretionary expenses, and abnormal cash flows) and corporate social responsibility reporting within a carefully chosen cohort of publicly traded manufacturing enterprises in Nigeria. Consequently, hypotheses are formulated in light of these objectives.

2. LITERATURE REVIEW

Theoretical Framework

Stakeholder Theory

The foundation of this study is rooted in the stakeholder theory, as espoused by Edward Freeman in 1984, which stands as a prominent framework within the realms of social, environmental, and managerial research. According to Grougiou et al. (2014), this theory provides a beneficial framework for studies into the association between earnings management (EM) and corporate social responsibility (CSR). It posits that CSR is an obligation for any organization, and it is necessary for the firm to carry out a broader range of accountability, not only to the primary users of the financial information, but also to every other stakeholder, the host community inclusive. The stakeholder theory posits that organisations bear a fiduciary responsibility towards a diverse array of stakeholders, distinct from shareholders. These stakeholders encompass creditors, customers, suppliers, employees, government entities, the community, the environment, and future generations. Consequently, the theory revolves around the collective of groups, organisations, and individuals who possess the capacity to exert influence upon or be influenced by the entity in question and how said entity can effectively navigate and oversee these various entities. Furthermore, it is imperative to acknowledge that the aforementioned theory places significant emphasis on the notion that organisations bear a responsibility and moral obligation towards a broader spectrum of stakeholders. Consequently, it becomes essential for managers to integrate the interests of all stakeholders into their reports (Grougiou et al., 2014). This notwithstanding, this theory makes a provision for the way and manner the agents of an entity can carry out some strategies that can be used to relate with stakeholders, which does not impact directly on the practical behavior of managers. According to Grougiou et al. (2014), because the company is a multilateral network of connections between stakeholders, and managers always tend to act in their own self-interest, the expectation gap between information needed by stakeholders and the information provided by managers is always on the high side, which gives managers the room to practice earnings management. Going further, Grougiou et al. (2014) opine that earnings management becomes a norm for companies that have to relate with several stakeholders' interests. Therefore, the stakeholder framework asserts that there is an affirmative association among earnings management and corporate social responsibility.

Conceptual Review

Earnings Management

Several definitions have been provided to the concept of earnings management in the academic world. One of such definition, according to Iyobosa (2021) is that it is a strategic manipulation of financial statements, often within the boundaries of accounting rules and regulations, with the aim of influencing reported earnings figures so as to achieve financial goals or to portray a desired image of the financial performance of a company, thereby potentially influencing stock prices or stakeholders' perception and confidence. To Isam et al. (2020), earnings management pertains to the method of deliberately manipulating the financial statements of an organisation, albeit in order to reach the targeted level of reported earnings, while adhering to generally accepted accounting rules. In severe cases, earnings management may look like a plot by management to misinform some concerned stakeholders. Iyobosa (2021), however, argues that the concept of earnings management should not be considered a fraud or any other illegal activities on the part of the management of a company to misrepresent financial figures, although it is synonymous with concepts like window dressing, income smoothing, creative accounting. In the view of Hickman et al. (2021), earnings management can be described as the process of deliberately taking specific and strategic step to accomplish an expeted level of reported earnings within the stipulations of GAAP. Kurawa and Ahmed (2020) emphasise the phenomenon of earnings management, wherein the managerial body of a corporation engages in strategic manoeuvres that adhere to legal boundaries. These manoeuvres are undertaken with the intention of deceiving specific stakeholders regarding the financial performance of the company or to exert influence over contractual consequences that hinge upon the reported accounts.

Corporate Social Responsibility (CSR)

In any society, no organisation can ignore the environment with which they interact because the main reason for their existence, which is the accumulation of capital, can only be achieved through the existence of their societies which otherwise constitute their markets (Iyobosa, 2021). Corporate social responsibility refers to the related duty of every company to assess and take into consideration the effects of its operations on the financial, ecological, and social well-being of its surroundings. It is imperative for businesses to ensure that these effects result in fair and sustainable advantages for all stakeholders involved while avoiding any detrimental consequences (Agwor & Onukogu, 2018). Corporate social responsibility (CSR) is an inherently voluntary endeavour undertaken by organisations with the noble intention of conducting their operations in a manner that is not only socially responsible but also economically viable and environmentally sustainable (Kouaib & Almulhim, 2019). According to Martinez-Ferrero et al. (2016), the concept of corporate social responsibility (CSR) encompasses various synonymous terms, including corporate social responsiveness, corporate citizenship, strategic philanthropy, and global citizenship, among others. Corporate social responsibility (CSR) encompasses a diverse array of concerns, spanning from matters of corporate ethics and the closure of industrial facilities to the protection of human rights, the preservation of the environment, the cultivation of community relationships, and the fostering of positive employee relations. As posited by Iyobosa (2021), the overarching objective of social responsibility lies in the pursuit of elevating societal well-being while concurrently safeguarding the economic viability of the corporate entity.

Historically, corporate social responsibility was not widely regarded as a significant problem from the time of Adam Smith to the period of the great depression. In recent decades, there has been a discernible surge in the recognition of social responsibility, extending beyond the realm of commerce to encompass the domains of legal studies, accounting, and economics. Therefore, CSR has been a growing phenomenon in accounting theory and practice since the 70s. more recently, there has been a tremendous growth in the field of CSR. In the contemporary landscape of intense competition, corporate social responsibility (CSR) assumes a prominent and esteemed position, holding strategic significance for numerous enterprises, including those in the manufacturing sector (Harris et al., 2019). On the strength of this argument, it is therefore imperative for every organization to treat its social responsibility with the appropriate attention it deserves and to make disclosures of such in their annual reports.

Empirical Review

The scholarly investigation undertaken by Honggowati et al. (2020) provided a comprehensive synopsis of the extant body of literature pertaining to the intricate interplay among earnings management and corporate social responsibility across diverse nations. The current study looked at all the previous research that had been done on electromagnetic fields (EM), corporate social responsibility (CSR), and how these two ideas interact with each other. Among a collection of 23 literary works, it has been discovered that 11 studies have yielded evidence supporting a negative correlation between corporate social responsibility (CSR) and environmental management (EM). Conversely, six studies have revealed a positive correlation between these two constructs. Additionally, two studies have identified a nuanced relationship, wherein the correlation between CSR and EM varies depending on the specific circumstances. Lastly, four studies have failed to establish any discernible connection between CSR and EM. The majority of the findings indicate that there is likely a negative correlation between socially responsible organisations and their engagement in environmental management practices. The categorization of relationships is contingent upon various factors such as the cause-effect dynamic, the presence of information asymmetry, the strategic utilisation of resources by an organisation, cognizance of environmental and ethical concerns, proclivity towards tax avoidance, adherence to corporate governance principles, the inherent characteristics of the firm, the prevailing political milieu, the allure of opportunistic incentives, the accumulation of stakeholder capital, and the psychological disposition of managers, among other pertinent considerations. The interplay between electromagnetic (EM) phenomena and corporate social responsibility (CSR) exerts a discernible impact on the quality of earnings, the performance of firms, and the overall value of said firms.

The primary objective of the study conducted by Almahrog (2014) was to examine the link between earnings management (EM) and corporate social responsibility (CSR) within the United Kingdom. The investigation was conducted utilising a threefold empirical approach, employing data derived from the FTSE 350 Index during the period spanning from 2008 to 2010. The initial phase entailed a comprehensive evaluation of the practice of environmental management (EM) through the utilisation of three distinct EM models to estimate discretionary accruals, which served as a proxy for EM. Subsequently, the subsequent phase involved the examination of corporate social responsibility (CSR) by employing both content analysis and disclosure index methodologies to ascertain the extent of corporate social responsibility disclosure (CSD) as a proxy for CSR. Finally, in light of the research outcomes, it can be inferred that the degree of corporate social responsibility (CSR) has a positive impact on the quality of financial reports. Consequently, it is advisable for organisations to strive towards enhancing their CSR reporting endeavours as a means to mitigate the prevalence of earnings management practices.

Huanzhen (2022) has conducted the current investigation, which explores the complex relationship between corporate social responsibility and earnings management in Chinese companies. Specifically, the study focuses on China's a-share listed companies that have disclosed their corporate social responsibility reports between 2009 and 2019. Through a meticulous analysis of the underlying motives behind earnings management, the investigation aims to ascertain the potential influence of such practices on corporate social responsibility. Moreover, it seeks to shed light on whether Chinese listed companies are genuinely driven by moral considerations when undertaking social responsibility or if they employ it as a strategic tool to safeguard the firm's reputation and management. The empirical findings of the study indicate a positive correlation between earnings management and corporate social responsibility (CSR). Moreover, the robustness of these findings is upheld when employing rigorous statistical techniques such as two-stage least squares (2SLS), Heckman two-step regression, and propensity score matching. By effectively controlling for reverse causality and self-selection bias, the study provides compelling evidence that China's listed companies exhibit a genuine ethical inclination to fulfil their social responsibilities. Henceforth, he espoused the notion

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that corporations ought to prioritise the calibre of earnings data in order to discern the impetus behind corporate social responsibility (CSR) when appraising a company's dedication to CSR.

3. METHODOLOGY

The selection and implementation of the quasi-experimental research design in this study are predicated upon the inherent lack of control that the researcher possesses over the various constituent elements of said design. The utilisation of the cross-sectional quasi-experimental research design is predicated upon its capacity to employ a survey methodology that draws upon a representative subset of the target population. Only listed Nigerian manufacturing companies that disclosed their CSR reports from 2012 to 2021 were selected as the population and sample of this study, and all manufacturing firms with missing data during the period of study were omitted to attain a total of 982 firm-year observations. On this note, according to the official website of the Nigerian Exchange Group (www.nxggroup.com), there were 35 manufacturing companies in the consumer and industrial goods sector, as at September 2022. However, only 30 of them have the relevant data for this study. Therefore, these 30 manufacturing companies comprised the population and sample of the research.

Variables and Model Design

OLS Model

Model 1 is used in this paper to test the hypothesis formulated for the purpose of research.

Null Hypothesis, H_o: There is no significant relationship between earnings management and corporate social responsibility reporting among listed manufacturing companies in Nigeria

$$CSR\_Score_{i,} = \beta_0 + \beta_2 * EM_{i,} + \sum \beta_j + \varepsilon_{i,t} \quad (1)$$

The variable of interest in the model, namely the CSR Score, serves as a proxy for gauging the level of corporate social responsibility (CSR) commitment. Its measurement is conducted through the utilisation of the RKS CSR score. The focal determinant within the model pertains to the concept of earnings management (EM). This study as a result used total real earnings management (REM), abnormal production (A_PROD), abnormal discretionary expenses (A_EXP) and abnormal cash flows (A_CFO) as proxies of earnings management.

Earnings Management

As per the scholarly work of Roychowdhury (2006), as cited in Huanzhen (2022), it has been posited that management possesses the ability to partake in the practice of real earnings management. This is achieved through a series of strategic manoeuvres, including but not limited to the reduction of prices for promotional purposes towards the conclusion of a given period, the deliberate overproduction of goods within the current period, and the intentional curtailment of investments in research and development. By amalgamating the aforementioned triad of variables (A_PROD, A_CFO, and A_EXP), a comprehensive representation of the corporation's real earnings management endeavours can be derived and encapsulated within the construct of a REM. The particular model is formulated in the following manner:

$$\frac{CFOi,t}{Assetsi,-1} = \beta_0 + \beta_2\left(\frac{Si,t}{Assetsi,t-1}\right) + \beta_3\left(\frac{\Delta Si,t}{Assetsi,t-1}\right) + \varepsilon_{i,t} \quad (2)$$

$$\frac{PRODi,t}{Assetsi,-1} = \beta_0 + \beta_1\left(\frac{1}{Assetsi,t-1}\right) + \beta_2\left(\frac{Si,t}{Assetsi,t-1}\right) + \beta_3\left(\frac{\Delta Si,t}{Assetsi,t-1}\right) + \beta_4\left(\frac{\Delta Si,t-1}{Assetsi,t-1}\right) + \varepsilon_{i,t} \quad (3)$$

$$\frac{EXPi,}{Assetsi,t-1} = \beta_0 + \beta_1\left(\frac{1}{Assetsi,t-1}\right) + \beta_2\left(\frac{Si,-1}{Assetsi,t-1}\right) + \varepsilon_{i,t} \quad (4)$$

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$CFO_{i,t}$ denotes the net cash flow arising from operational activities at the conclusion of year $_t$. $PROD_{i,t}$ signifies the cost incurred for production, which encompasses both operating expenses and alterations in inventory, at the conclusion of year $_t$. $EXP_{i,t}$ represents the discretionary cost incurred at the conclusion of year $_t$. $S_{i,t}$ denotes the operating income realised at the conclusion of year t, while $\Delta S_{i,t}$ signifies the disparity between the operating income at the conclusion of year $_t$ and the operating income in year $_{t-1}$. The three residual variables resulting from the regressions are denoted as A_CFO, A_PROD, and A_EXP. The comprehensive assessment of real earnings management (REM) is subsequently derived through the utilisation of model 5:

$$REM = A\_PROD - A\_CFO - A\_EXP \quad (5)$$

Table 1: Definition of Variables

Variables	Measurement methods
CSR_Score	CSR scores released by RKS
REM	Total real earnings management
A_CFO	Abnormal cash flows due to price reduction promotions
A_PROD	Abnormal production costs due to overproduction
A_EXP	Abnormal discretionary expenses due to reduced inputs
Voluntary	Voluntary disclosure of CSR Reports by companies takes the value of 1, otherwise it is 0

The table presents the definitions of all the variables using in the model (1).

4.RESULTS

Descriptive Statistics

Table 2 showcases the outcomes of the descriptive statistics pertaining to the fundamental variables. The mean 39.2546 and median 36.7030 of the CSR_Score are relatively small compared to its maximum value of 75.4500, indicating that listed companies generally score low, but there are still a few companies that score high, which suggests that a few companies have taken the initiative to lead the way in corporate social responsibility. The mean values for the three basic indicators of real earnings management are 0.0000, 0.0006 and -0.0006 respectively, indicating that on average the sample corporations are hardly engaged in real earnings management activities in the form of price reduction promotions and have reduced overproduction, but have reduced their current discretionary expenses. The mean and median value of the composite indicator of real earnings management (REM) is 0.0003 and 0.0118, both of which are small compared to its maximum value of 0.5205, suggesting that, only a small number of companies engage in significant real earnings management activities, with most companies engaging in less real earnings manipulation.

Table 2: Descriptive Statistics of Variables

Variable Codes	Observations	Mean	Standard deviation	Median	Minimum value	Maximum value
Score	982	39.2546	12.2079	36.7030	18.6287	75.4500
A_CFO	982	0.0000	0.0719	-0.0012	-0.2274	0.2129
A_PROD	982	-0.0006	0.1039	0.0076	-0.3471	0.2951
A_EXP	982	-0.0006	0.0568	-0.0060	-0.1342	0.2530
REM	982	0.0003	0.1905	0.0118	-0.6514	0.5205

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OLS Regression Analysis

Table 3 presents the OLS regression results of model (1) to test the formulated hypothesis. As can be seen from results (1), (3) and (4) in Table 3, the regression results for REM, A_EXP and A_PROD are both substantially affirmative at the 1% level, indicating that real earnings management is negatively related to the level of social responsibility commitment and that the alternative hypothesis is evidenced, suggesting that management commitment to social responsibility is ethically motivated and likely to be "sincere". In contrast, result (2) in Table 3 shows a positive but insignificant regression result between abnormal cash flows and CSR, which, combined with the analysis of descriptive statistics, may be due to the fact that fewer sample companies used sales manipulation and therefore the management motives embedded in A_CFO could not be demonstrated.

Table 3: Table of OLS Regression Results for Model (1)

	(1)	(2)	(3)	(4)
Variables	REM	A_CFO	A_PROD	A_EXP
EM	-5.321^{***}	2.526	-8.769^{***}	20.52^{***}
	(-3.24)	(0.81)	(-2.79)	(5.46)
Voluntary	1.457^{**}	1.469^{**}	1.466^{**}	1.373^{**}
	(2.41)	(2.38)	(2.42)	(2.27)
Intercept	-76.65^{***}	-77.57^{***}	-77.51^{***}	-75.71^{***}
Industry	Yes	Yes	Yes	Yes
Year	Yes	Yes	Yes	Yes
N	982	982	982	982
Adjusted R^2	0.380	0.375	0.379	0.384

Source: Researchers' Computation

The table presents the results of OLS regression for model (1). The headings in the second row all represent the proxy variables of earnings management used in the model, and the dependent variables for all the columns are CSR_Score. The asterisks, *** P<0.01, ** P<0.05, * P<0.1, describe the significant level of the coefficients (2tailed tests) and the parentheses present the t-value.

Discussion of Findings

The research explored the association between earnings management and corporate social responsibility of listed manufacturing firms in Nigeria. Findings revealed that with respect to the measures used in the study, that real earnings management, abnormal discretionary expenses and abnormal production are both significantly positive at the 1% level, indicating that real earnings management is positively related to the level of social responsibility commitment, hence evidencing the alternative hypothesis, suggesting that management commitment to social responsibility is ethically motivated and likely to be "sincere". In contrast, there is a positive but insignificant regression result between abnormal cash flows and CSR which may be due to the fact that fewer sample companies used sales manipulation and therefore the management motives embedded in abnormal cash flows could not be demonstrated. This discovery aligns with the conclusions drawn by Huanzhen (2022), whose research unveiled a notable and affirmative correlation between the practice of earnings management and the commitment to corporate social responsibility among major corporations listed in China.

5.CONCLUSIONS AND RECOMMENDATIONS

This study sought to investigate the intricate connection between earnings management and the reporting of corporate social responsibility among manufacturing companies listed in Nigeria. By analysing reports spanning from 2012 to 2021, the study aimed to determine whether earnings management practices have the potential to influence the extent of corporate social responsibility undertaken by these companies. Furthermore, the study delved into the underlying motives behind earnings management in order to ascertain whether these companies engage in social responsibility out of obligation, ethical convictions, or simply as a strategic manoeuvre to uphold their reputation and the reputation of their management. The result of the research shows that earnings management and corporate social responsibility are positively correlated, proving that Nigeria's listed manufacturing companies carry out their social responsibility and report same out of ethical persuasions and motivations. In light of the results of this research, it is therefore suggested that:

i. Regulators of the industry should consider the quality of the earnings of companies in order to determine whether the commitment of these companies is ethical motivated or it is as a result of opportunity.
ii. Manufacturing companies in Nigeria should be encouraged to disclose more information about their social responsibility in order to standardize social responsibility reporting to further promote the efficiency of information transfer in the capital market.
iii. Since earnings management practice has become a norm in the accounting world, it is also suggested that in order to curb this practice among manufacturing companies in Nigeria, the internal control system should be strengthened and the content of accounting ethics should also be used to build an ethical environment so as to enhance the ethical perception of management and employees.

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