Financial reporting quality during and after the pandemic

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FINANCIAL REPORTING QUALITY DURING AND AFTER THE PANDEMIC

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List of Abbreviations

APC: Abnormal Production Costs

ADE: Abnormal Discretionary Expenditures

AM: Accruals Manipulation

BM: Basic Materials

COGS: Cost of Goods Sold

COVID: Coronavirus Disease 2019

DA: Discretionary Accruals

EBIT: Earnings Before Interest and Taxes

ESG: Environmental, Social, and Governance

FR: Financial Reporting

GDP: Gross Domestic Product

PPE: Property, Plant, and Equipment

RAM: Real Activities Manipulation

RE: Retained Earnings

RMDISX: Abnormal Discretionary Expenditures (Real Manipulation)

RM: Real Manipulation

ROA: Return on Assets

SG&A: Selling, General, and Administrative Expenses

TA: Total Accruals

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Introduction

The COVID-19 pandemic has supplied unprecedented demanding situations to businesses globally, disrupting economic activities and causing substantial monetary uncertainty. In reaction to this crisis, firms have needed to navigate through turbulent instances, often resorting to various strategies to hold monetary balance and meet stakeholder expectations. Among these strategies, profits control has drawn good sized attention as corporations might be incentivized to manipulate monetary statements to give a more favorable picture throughout uncertain instances.

Earnings management refers to the planned manipulation of economic reporting to reap positive financial results, whether through accrual-primarily based practices or real sports manipulation. Accrual-primarily based earnings control (AEM) involves changing accounting estimates and judgments, whilst real activities manipulation (RAM) entails changing the actual business operations, including overproduction of stock or cutting discretionary costs. Both kinds of earnings control can extensively distort the authentic economic fitness of a organization, raising issues about the satisfactory and reliability of monetary reporting, especially for the duration of durations of economic turmoil.

This look at investigates the quantity and nature of profits control practices during and after the COVID-19 pandemic, that specialize in each accrual-based totally and real sports manipulation across special industries. By analyzing the behavior of corporations throughout this era, this research pursuits to make a contribution to the information of ways economic crises influence financial reporting practices. Moreover, the have a look at explores whether or not the effect of COVID-19 on income control various across industries, thinking about that exclusive sectors confronted specific demanding situations and possibilities in the course of the pandemic.

Given the significance of accurate economic reporting for traders, regulators, and different stakeholders, this studies sheds light at the implications of earnings management in the course of crises. It additionally gives insights into the wider results of the pandemic on corporate conduct, presenting treasured training for destiny economic disruptions.

Literature Review

I. Financial Reporting: Basics and Objectives

1. Financial Reporting Basics

Reporting stands out as one of the fundamental tasks in an accounting information system. This system begins by recording information and concludes with reporting, which involves sharing relevant financial details. The accounting information system generates data that is communicated to users of financial statements through reporting and disclosures. Essentially, any useful and important information gathered from an entity's accounting system can be shared with both internal and external users via reporting.

The financial reporting process is crucial for reducing information asymmetry between management and shareholders (Penno, 1985). However, it is imperfect and can be influenced by market conditions and institutional settings (Stephen, 2012). The process involves both representations by management and verifications by owners, such as external audits (Mark, 1985).

The primary objective of reporting is to convey financial details from organizations to users of financial statements. These users, ranging from owners and managers to investors, employees, creditors, and government entities, are keen on understanding various aspects of an organization's financial information. This includes details about the volume, structure, and liquidity of assets, the financial structure of the entity, and the risks it undertakes (Pantazi & Vasile, 2021). The information presented through reporting can encompass both financial and non-financial data to cater to the diverse needs of these users. While "reporting" might initially suggest at first thought financial aspects, contemporary practices extend beyond financial reporting to encompass non-financial information. This expansion highlights the growing significance of non-financial reporting for entities in recent times. Moreover, the reporting process is divided into two categories: internal reporting and external reporting. This division is determined by the target audience, specifically the financial statement users mentioned earlier.

This exhaustiveness of information to be reported is due to efforts to reduce the conflicts in the principal and the agent relationship.

This relationship is a foundational concept in agency theory, extensively studied by scholars such as Joseph, (1989) and Spremann & Gunter, (1987), This relationship examines how a principal, typically an owner or a shareholder, can design a compensation system to incentivize an agent, usually a manager, to act in the principal's best interests. The complexity of this relationship is further explored by Pratt & Zeckhauser, (1990) and Makin & Tirole, (1992) who address the difficulties in monitoring the agent's performance and designing effective incentives. These studies underscore the intricate dynamics and potential conflicts that arise due to divergent interests and asymmetric information between the principal and the agent.

The inherent tension that exists between managers and shareholders is explained by the theory mentioned above. The reason for the conflict is that managers make decisions based on how best to serve themselves. The information asymmetry between managers and outside capital providers is what leads to the conflict. A lack of information sharing between managers and shareholders can lead to imperfections like moral hazard and adverse selection, which can lower the efficiency of capital investments. (Youngtae, Lim, & Jinho, 2013). This problem is addressed through public oversight of the agent's finances, which is seen as an indicator of public interest and value (Bryce, 2012). The demand for a high Financial reporting quality and auditing in this context is driven by the need to bridge the information gap between principals and agents, ensuring the credibility and reliability of financial statements (Asein, Owolabu, & Soetan, 2020).

2. Financial Reporting Objectives

Financial statements should consistently offer dependable information that aids users in making informed decisions. These statements ought to reveal pertinent, trustworthy, comparable, and comprehensible financial data. (Kamaruzaman, Mazlifa, & Maisarah A, 2009)

Financial Reporting is an aspect that is always present in any business or organization, as it provides stakeholders with important information about the entity's financial health and performance. According to Andrain, Evita, and Erlane, (2018) in their study on "The effect of accounting methods on financial reporting quality," the choice of accounting methods can have a significant impact on the quality and reliability of financial reporting. As such, it is essential for businesses and organizations to carefully consider their financial reporting practices and ensure that they are compliant with relevant accounting standards and regulations. The accounting practices undertaken and upheld by a company serve as the bedrock for financial reporting. These practices encompass the identification, collection, and evaluation of all the financial transactions within the business. (Wahyuni, Puspitasari, & Purspitasari, 2020), Financial reporting can, in the best-case scenario, lead to first-best investment levels. Moreover, financial reporting can lessen adverse selection concerns by enhancing enterprises' access to finance, resulting in less disinvestment. Moreover, financial reporting might limit enterprises' access to capital in cases when firm managers tend to overinvest (empire-building). Blehi, Bleibtreu, & Stefani, (2023).

FR is valuable when the information within the reports aids in making unbiased and well-informed decisions. Such reports are considered beneficial if they meet stakeholders' expectations or assist in adjusting analyst assessments. (Baalouch, Ayadi, & Hussainey, 2019).

Financial Accounting Frameworks

Every nation maintains its distinct accounting system, tailored to its unique requirements. In a concerted effort to enhance the global comparability and quality of financial statements, the International Accounting Standards Board (IASB) introduced the International Financial Reporting Standards (IFRS). The primary aim of IFRS is to reduce the disparity in reporting regulations across countries, lower the financial reporting costs for multinational corporations, and streamline the process of financial statement analysis. (IASB, IAS 41, 2000)

IFRS represents a comprehensive set of accounting standards, interpretations, and a framework for the preparation and presentation of financial statements. It operates on the premise of principle-based standards rather than rule-based standards. This principle-based approach offers companies greater flexibility in selecting accounting policies and estimates that align with their specific business needs. However, it is worth noting that reliance on principle-based standards may introduce certain risks, including the potential for errors in management estimates and distortions in business practices. (Elad, 2004)

Every transaction conducted by the business is handled in accordance with the prevailing accounting standards and regulations (Bhasin, 2015). Financial reporting's main purpose is to provide useful financial information about companies, especially related to money, to assist in making economic decisions. (IASB, International Accounting Standard Setting: A Vision for the Future, 1999). Accounting standards serve as the fundamental principles of the accounting system, and they establish the most effective methods in accounting and reporting. (Briloff, 1972), 00Simply put, if accounting information includes inconsistent measurements, unreliable estimates, or fake transactions, it's sure to be wrong, incomplete, and misleading. There have been claims that people were deceived for a long time by financial reports that didn't provide accurate, useful, and practical information about the company. (Mamo, 2014)

The Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) collaborate to resolve disparities and disputes related to their individual guidelines. This cooperative initiative aims to establish a comprehensive framework, which is expected to enhance the quality and usefulness of financial reporting standards. (Bini & Francesco Dainelli, 2016)

In this context, it can be stated that accounting conventions have guided professionals in establishing accounting standards. The standards established in these conventions aid in recognizing financial reports in cases where companies use creative accounting or earnings management techniques. (Karda, Salehi, & Abdollahi, 2016)

Among the interesting topics for creditors, owners, governments, and even managers are separating ownership and management, creating a conflict of interest between them, providing financial statements for external financial reporting purposes, and assessing the quality of the intended statements. The financial statements will be of the necessary caliber if they actually accomplish these goals. (Kardan, Salehi, & Abdollahi, The relationship between the outside financing and the quality of financial reporting : Evidence from Iran, 2016). Basically, if there's a conflict of interest and not everyone has the same info, managers might mess with the numbers in financial statements. (Rajgopal & Venkatachalam, 2011)

3. The financial reporting components

Financial statements and reports serve as documents that offer an overview of an entity's financial status. Typically, there exist four important categories of financial statements:

The Balance sheet

Which is an important tool in accounting, serving as both a historical record and a predictor of future performance (Frunze, 2023). It is divided into assets, liabilities, and stockholders' equity, providing a snapshot of an organization's financial position. This information is vital for financial diagnosis, helping to assess a company's financial health and predict future cash flows (Ciuhureanu, 2012). However, the balance sheet has its limitations, as it may not fully capture a company's true value (Warren, 1926).

The profit and loss statement

The profit and loss statement are a key financial document that provides a snapshot of a company's financial performance over a specific period (Donaldson, 1983). It is influenced by various factors, including operational, financial, and investment incomes and expenses (Khajimuratov, Ismoilova, & Sayfullayev, 2023). The structure and preparation of this statement have evolved over time, with the new format incorporating additional categories of income and expenses (Nederiṭa, 2021). Despite the emergence of the comprehensive income statement, the profit and loss account remain the preferred financial statement for investors (Ionel, Iulia, & Ionela, 2012).

Cash flows

Cash flows are a critical aspect of a company's financial health, representing the movement of cash in and out of the business. They are essential for maintaining financial stability and maximizing profits. Effective cash flow management is crucial, particularly in unstable economic conditions. Also, the analysis of cash flows is a key tool for assessing a company's liquidity and solvency and should not be overlooked in favor of balance sheets and income statements.

Notes to the financial statements.

The notes to the financial statements play an indispensable role in providing additional information for decision-making and risk assessment (Kerezsi, T, & Fenyves, 2018). The specific content of these notes can vary based on the financial position of the company. It is also important to consider the basis of the presentation, as different countries may have different requirements.

II. Financial Reporting Quality

1. The importance of FRQ:

Firm value is a hot topic for both company leaders and researchers. They explore what factors influence a firm's value. Various studies, like those by Varaiya, Kerin, & Weeks, (1987), Liow, (2010), Hermuningsih, (2014), Kodongo, Mokoaleli-Mokoteli, & Maina, (2015), and Nam, (2019) have delved into the impact of financial statement information on firm value. However, these studies sometimes agree or disagree due to using different methods and measurements. In the realm of financial statements, Earnings Quality is an important indicator that grabs the attention of many stakeholders. Inaccurate or misleading financial reporting can have serious consequences, including loss of investor confidence, legal penalties, and

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reputational damage. In contrast, High-quality financial reporting is of key importance for many users, as it influences the perception of the latter on the issuing company. Providing high-quality and useful financial reporting is a prerequisite for the efficiency of the enterprise. The usefulness of financial reporting is connected with the extent to which this information corresponds to the particular needs at any given time and how the information contributes to the solution of a particular problem. Usefulness is determined by the quality of financial reporting. (Tsoncheva, 2014),

Monitoring systems play a crucial role in mitigating the potential opportunism in managerial investment decisions, particularly in situations marked by information asymmetry between managers and external capital providers. (Jensen, 1994) underscores the significance of such systems in preventing managerial tendencies to overinvest. (Watts & Zimmerman, 1983), as well as (Ball, 1989), view accounting as an integral component of a firm's control mechanism. Furthermore (Bushman & Smith, 2001) offer a comprehensive overview of literature highlighting financial accounting reporting as a vital source of information employed by shareholders and others for managerial monitoring. Recent studies also indicate that the quality of financial reporting can impact investment efficiency, underscoring the role of monitoring in addressing information asymmetry between managers and shareholders.

The relationship between reporting quality and firm-level capital investment efficiency is examined by (Biddle & Hilary, 2006). They offer proof that High reporting quality improves investment efficiency by lessening the information asymmetry that exists between managers and outside capital providers. This effect is more pronounced in stock market-dominated economies than in creditor-dominated ones.

Low levels of overinvestment and underinvestment are positively correlated with high-quality financial reporting, according to Biddle, Hilary, & Verdi, (2009). They contend that through lowering adverse selection and generating projects with positive net present value, improved financial reporting can raise capital. On the other hand, in companies with large capital, improved financial reporting can reduce managerial incentives to partake in value-destroying practices like empire building, Additionally, it can improve investors' capacity to keep an eye on managerial investment choices. According to McNichols & Stubben, (2008) research, companies that discredit their financial status tend to make investments that are significantly larger than what is considered optimal. This result implies that internal decision-making may be impacted by the quality of financial reporting.

2. Measuring FRQ and the different measurement techniques and methods

Despite emphasizing the significance of producing high-quality financial reports, both the FASB and IASB face a notable challenge highlighted in previous literature: the operationalization and measurement of this quality. Evaluating financial reporting quality empirically becomes intricate due to its context-specific nature, introducing a multitude of preferences among various stakeholders (Dechow & Dichev, 2002; Schipper & Vincent, 2003; Botosan, 2004; Daske & Gebhardt, 2006). Given the diverse preferences within different user groups, the perceived quality of financial reports may vary. Moreover, even within a specific user group, individuals may interpret the usefulness of similar information differently

depending on the context. This inherent context and user-specificity make direct measurement of quality problematic (Botosan, 2004). Consequently, numerous researchers opt for an indirect approach to gauge the quality of financial reporting, focusing on attributes believed to impact it, such as earnings management, financial restatements, and timeliness e.g., (Barth, Landsman, & Lang, 2008; Schipper & Vincent, 2003; Cohen, Krishnamorthy, & Wright, 2004)

The value relevance model assesses the quality of financial statements by looking at stock market reactions and accounting indicators (Rashid M. M., 2020). A company's stock price indicates its market worth, and accounting data derived from accounting procedures also show a company's value (Kardan, Mahdi, & Rahimeh, 2016). Although the model's applicability is good, its drawbacks include its inability to reliably anticipate market value and stock price. The International Accounting Standard Board (IASB) qualitative framework is the method that was utilized to operationalize the qualitative parts of the report. Accordingly, the two components of qualitative features are enhancements and fundamental characteristics (Hadiyanto, Evita, & Erlane, 2018)

The two key elements required to determine the quality of financial reporting are relevance and faithful representation. However, in order to generate high-quality financial statements, a few additional qualities are added to the basic ones, such comparability and understandability. When these assertions give people the ability to precisely evaluate and comprehend past and present events and make educated economic decisions, they are deemed relevant and helpful (Rashid M. M., 2020).

The core principle of faithful representation is to record economic activities truthfully, avoiding any manipulation. Comparability, as an augmenting factor, ensures that similar events are portrayed using consistent accounting methods, while distinct economic events are represented with varying figures and indicators, allowing for clear and objective differentiation for easy comparison and interpretation (Rashid M. M., 2020) Users often desire to compare financial statements across different periods or between companies; comparability is the trait that facilitates such comparisons. To meet the standard of high-quality financial reporting, statements should be easily comprehensible, ensuring clear and effective information dissemination.

It is deemed crucial that government systems and disclosure procedures accurately reflect accounts and budgets (Dabbicco, 2015). Additionally, according to, (Yasser, Abdullah, & Irfan, 2016) reporting is the formal procedure utilized by organizations to inform their stakeholders of financial and operational information.

Furthermore, the IASB qualitative uses the following characteristics framework to identify the elements of financial reporting quality (Salehi, Nasrin, & Ali, 2018).

A-) Relevance:

The AASB Framework attributes a "predictive and confirmatory role" to relevance, emphasizing that information should serve decision-makers and other users. In essence, information is deemed relevant if it aids users in making sound economic decisions (Akpanuko, Essien, & Ntiedo, 2018). The significance and nature of information are highlighted as factors

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influencing its relevance. Moreover, information is considered material when its misrepresentation or omission can impact the decisions of users relying on financial reports (Saleem, et al., 2020). This definition aligns with others proposed during the review period, maintaining consistency (Kewo & Cecilia, 2017). Authors have employed various attributes to characterize relevance, with usefulness and materiality being pivotal in defining relevance from the 1960s to the 2000s. The concept of usefulness later evolved into decision-usefulness, incorporating the element of timeliness.

The most significant aspect of relevance is its predictive value, as it directly influences decision usefulness. This can be measured through three constructs. The first construct evaluates the extent to which annual reports provide insights into future business scenarios. Forward-looking financial statements articulate the management's vision for the organization's future, leveraging information that enables them to anticipate upcoming business conditions—information not typically available to shareholders and other stakeholders. Consequently, investors and capital providers find such information valuable when included in annual reports. The second construct focuses on the extent of information disclosure regarding business risks and opportunities (Kruglyak, Zinaida, Olga, & Shvyreva, 2018). Non-financial information complements financial data by contributing to its predictive value. Insights into business risks and opportunities are essential for understanding potential future business scenarios (Cheung, Esther, Elaine, & Sue, 2010)

The third pillar evaluates the business's application of the fair value idea. The extant literature generally suggests that the predictive importance of financial reporting information is determined using fair value and historical cost (Cohen, Sandra, & Sotirios, 2017)

B-) Faithful Representation:

The accuracy of information is paramount in financial reports. These reports should be detailed, correct, and unbiased to represent the data truthfully. Standards in accounting outline what should be included in these reports—things like financial events, resources, and obligations. It's tough to solely judge how accurate a report is just by looking at it; real-world data is essential to ensure the information is true, as noted by (Muraina & Kabiru, 2020). (Botosan, 2004) says it's hard to measure accurate representation just by looking at annual reports. She suggests you need real economic info to make sure things are represented faithfully. On the other hand, (Maines, 2006) believe that making educated guesses and using assumptions that match the economic ideas standards aim for can help with accurate representation. So, we focus on specific parts in the annual report that make it more likely to be accurate. These parts might not always follow local GAAP or IFRS directly, but they indirectly show how well financial reports stick to certain accounting standards.

According to the ED[1], faithful representation is the second essential quality feature. Annual reports must be comprehensive, impartial, and free from material inaccuracy in order to accurately depict economic phenomena that information is intended to represent (IASB, 2008). Five items that pertain to neutrality, completeness, freedom from material error, and verifiability are used to measure faithful representation in accordance with previous research (

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[1] Exposure Draft

(Dechow, Sloan, & Sweeney, 1996; McMullen, 1996; Beasley, 1996; Rezaee, 2003; Cohen, Krishnamorthy, & Wright, 2004; Sloan, 2001; Jonas & Blanchet, 2000; Maines, 2006)

(Cernusca, Lucian, Delia, Cristina, & Bogdan, 2016) suggest that accurate estimates and assumptions about economic factors are important for showing the real economic situation in reports. This study focuses on what makes an annual report more accurate. These factors don't always follow specific accounting rules like IFRS or local GAAP, but they help in presenting financial information correctly according to certain accounting standards. One key aspect is being 'free of bias'. It's hard for reports to be completely unbiased because they're based on uncertain conditions and include various guesses. While completely removing bias isn't possible, it's essential to have reasonably accurate financial information for making meaningful decisions.

An unqualified auditor's report is essential for ensuring reliable and faithful financial information reporting, as highlighted by (Bean, Anne, & Helen, 2015). Neutrality in reporting is about whether the preparer attempts to present events objectively or focuses solely on positive aspects while neglecting the negatives. Several researchers, including Esra & Engin, (2020), have studied how audits and their reports impact a company's economic value. They've concluded that these reports provide added value by assuring the accuracy of annual reports, establishing trust in the faithful representation of information.

Lastly, in annual reports, a big part of showing information accurately is the corporate governance statements. Many researchers have looked at how well financial reports match with corporate governance, internal control, fraud, and getting earnings wrong. What they found is that when internal control and governance aren't good, the quality of financial reporting drops (Bimo, Irenius, Sylvia, Ancella, & Wardhani, 2019). It's clear that info about corporate governance is valuable for people putting in money. This type of information makes it more likely that the reports represent things accurately (Tassadaq, Fizza, & Qaisar, 2015)

C-) Understandability

The Australian Accounting Standards Board (AASB) defines understandability as an essential feature of financial report information. The material should be easy to grasp and pleasant to read (Habib, Md Borhan Uddin, & Mostafa Monzur, 2019). It is believed that users are familiar with economic operations and other business components such as accountancy. Furthermore, users are required to be diligent in their evaluation of this information (Bini, Francesco, & Francesco, Business model disclosure in the Strategic Report: Entangling intellectual capital in value creation process, 2016). Understandability was formerly defined as "sufficient wording in a 'narrative' or 'vertical' form of financial statements to make them explanatory" (Cheung, Esther, Elaine, & Sue, 2010). Since then, understandability has been linked to communication. Two major advances have been highlighted: who or what was the focus of establishing understandability, and whether technical or non-technical terminology should be used to report Financial Information.

Additionally, detailed disclosures in the balance sheet and income statement comments can offer valuable insights into earnings, as suggested by (Cheung, Elaine, & Wright, 2010).

Using narrative forms can significantly improve the understandability of the information. Incorporating graphics and tables is expected to make relationships clearer, as noted by (Rashid & Mamunur, 2020). Moreover, employing easily understandable language and clear sentence structures, as recommended by (Kardan, Mahdi, & Rahimeh, 2016), can enhance a reader's comprehension. In cases where technical terms are unavoidable, a glossary section, as proposed by (Cheung, Elaine, & Wright, 2010) can provide additional information to aid in understanding complex terms.

D-) Comparability

Comparability means that similar situations should be described using the same accounting facts and figures, as mentioned by (Cheung, Elaine, & Wright, 2010). On the other hand, different situations are expected to involve distinct accounting methods, making the differences understandable and easy to interpret. This is why businesses in comparable situations tend to use similar accounting techniques, according (Kardan, Mahdi, & Rahimeh, The Relationship between the Outside Financing and the Quality of Financial Reporting: Evidence From iran, 2016) Any differences between the figures in annual reports that aren't due to performance should ideally be eliminated, as noted by (Rashid M. M., 2020). The terms "uniformity" and "consistency," which gained popularity in the 2000s, are used to describe comparability. Consistency means that all reporting periods should use the same methods or explicitly mention any variations, as explained by (Carlin & Nigel, 2011).

Companies are advised to prioritize consistency to achieve comparability. Achieving consistency involves demonstrating the capacity to manage uncertainty and change (Kardan, Mahdi, & Rahimeh, 2016) Businesses often revise estimates, accounting procedures, and judgments in response to updated rules, regulations, or new information. For instance, an update in the expected lifetime of an asset may necessitate revising estimates. Concerning consistency, it's essential for businesses to disclose the effects of such changes on past results. This disclosure is crucial for obtaining comparable earnings estimates, allowing for a precise evaluation of business performance. Modifications in accounting policies, judgments, or estimates might alter the earnings figures from previous years, enabling a visual assessment of these changes.

Consistency demands that accounting principles remain unchanged, ensuring that revised figures align with those from previous years. Presenting a comparison of financial results over multiple years, even without alterations in judgments, estimates, or accounting procedures, heightens the comparability of financial information. Comparability extends beyond the consistent use of accounting methods within a single firm; it encompasses the comparability of financial reports across firms. Therefore, when assessing the comparability of annual reports from different organizations, it's crucial to focus on the annual report structure, accounting policies, transaction descriptions, and other developments (Kardan, Mahdi, & Rahimeh, 2016)

The Exposure Draft underscores the importance of companies striving for comparability through consistency. (Jonas & Blanchet, 2000) interpret consistency as the ability to adapt to change and uncertainty. Changes in information, rules, or regulations often prompt companies to adjust their estimates, judgments, and accounting policies. For instance, if new information

prompts a reevaluation of the expected lifespan of an asset, this might lead to an estimate change. Moreover, many EU-listed companies shifted from local GAAP to IFRS in 2005 due to new regulations and rules. In terms of consistency, it's crucial for these companies to articulate how such changes impact previous results. Comparability of earnings figures is vital in evaluating a firm's performance over time (Cole, Branson, & Breesch, 2007). When a company modifies its estimates, judgments, or accounting policies, it might revise previous years' earnings figures to illustrate the impact of these changes on past results.

E-) timeliness:

Accounting standard-setting bodies throughout the world have identified timeliness of reporting as one of the most significant features of financial information. Because decision-making delays frequently incur some cost to the decision-maker or those affected by the choice, the timeliness of information used in the decision-making process is critical. In awareness of this fact, securities authorities set time limitations on publicly traded corporations' disclosure of financial information while allowing ample time for the creation of credible information. (Brown & Glen W. Dobbi, 2011)

The International Accounting Standards Board (IASB) emphasizes timeliness as a fundamental aspect of financial reporting. In the United States, the Accounting Principles Board (APB) articulated timeliness as one of the qualitative objectives of financial reporting disclosure in (APB, 1970). Although this statement was later replaced, the Financial Accounting Standards Board continued to acknowledge the significance of timeliness in its Statement of Financial Accounting Concepts (FASB, 1980). The U.S. Securities and Exchange Commission also underscores the importance of timeliness, mandating that listed companies file their annual 10-K reports within specific deadlines. Additionally, (OECD, 2004) identifies timeliness as a principle of good corporate governance.

The issue of timeliness presents various dimensions. There exists an inverse relationship between the quality of financial information and the speed at which it's reported (Kenley & Staubus, 1974). Over time, accounting information tends to lose relevance (Hendriksen & van Breda, 1992); (Lawrence & Glover, 1998) (Atiase, Bamber, & Tse, 1989)

Evidence suggests that there's a tendency for companies to take longer to report bad news compared to good news ((Bates, 1968; Beaver, 1968). This delay in reporting negative information occurs because companies often hesitate to disclose unfavorable news and might spend more time adjusting the figures or employing creative accounting methods when faced with such situations (Givoli & Palmon, 1982; Trueman, 1990; Chai & Tung, 2002). In contrast, there's a pattern where positive news, like earnings beating expectations, tends to be swiftly released, while the reporting of negative or below-expectation results gets delayed. (Chambers & Penman, 1984; Kross & Schroeder, 1984; Dwyer & Wilson, 1989) observed this trend among municipalities. Similarly, (Haw, Qi, & Wu, 2000)) noted this behavior in Chinese companies, and (Leventis & Weetman, 2004) found a similar pattern in Greek firms.

However, research by Jan, Marc, Ruud, & Geert, (2003) discovered that this trend didn't hold true for Belgian companies. Han and Wang (1998) similarly found exceptions, noting that petroleum refining companies delayed reporting exceptionally high profits during the 1990s

Gulf crisis, possibly due to political repercussions outweighing the potentially positive market reaction.

On the other hand, Rees & Giner, (2001) found that companies in France, Germany, and the UK tended to report bad news sooner than good news. (Basu, 1997)'s study also observed that companies tend to report bad news more promptly than good news, attributing this trend to conservatism. (Gigler & Hemmer, 2001) supported this point, noting that firms with more conservative accounting systems were less likely to make timely voluntary disclosures compared to those with less conservative systems.

Expanding on Basu's study, (Pope & Walker, 1999) revealed cross-jurisdictional effects when handling extraordinary items, comparing US and UK firms. (Jerry & John, 2003) delved into the potential relationship between earnings timeliness and the share price reactions of competing firms. However, (Jindrichovska & Mcleay, 2005) found no evidence of conservatism in the Czech accounting system regarding reporting bad news earlier than good news, potentially due to the Czech tax system offering little incentive to do so. (Ball, Kothari, & Robin, The effect of international institutional factors on properties of accounting earnings, 2000) found that companies in jurisdictions with a strong shareholder orientation tend to disclose earnings information sooner than those operating under a legal code system.

3. Manipulation of Financial Numbers: Motivations and Strategies

- Research has consistently shown that bonus schemes can significantly influence a manager's intention to engage in earnings management. (Purwaningsih & al., 2019), (Marantika & al., 2021) suggests that this is particularly true when the bonus is linked to firm performance, as it can lead to income-increasing decisions when current earnings are below analysts' forecasts (Achilles & al., 2013). However, the impact of bonus schemes on earnings management can also be influenced by other factors, such as the manager's level of Machiavellianism (Purwaningsih & al., 2019) and their motivation, with those possessing strong extrinsic motivation being more likely to engage in earnings management (Achilles & al., 2013)

- Moreover, research consistently demonstrates a strong connection between debt covenants and firms' inclination to resort to earnings management strategies. Notable contributions to this understanding include (Franz, 2014) who established that firms in close proximity to violating their debt covenants exhibit a higher likelihood of employing both accounting and real earnings management techniques. (Kim, Lei, & Pevzner, 2011) further substantiates this by revealing that firms with more restrictive net worth debt covenant slack tend to engage more frequently in real earnings management practices. Additionally, (Nikolaev, 2010) identifies a positive correlation between the inclusion of covenants in public debt contracts and the timely recognition of economic losses in accounting earnings. Collectively, these findings underscore the role of debt covenants as a significant motivator for firms to manipulate their earnings.

- Also, other researches consistently show that investor and analyst expectations can serve as a strong motivation for earnings management. Callao & Jarne, (2015) found that analyst forecasts can incentivize earnings management, particularly as the publication of

earnings approaches. This is further supported by (Kwag & al., 2010) who found that investors tend to under-adjust for analyst optimism in the case of income-decreasing firms, leading to market mispricing. (Athanasakou & al., 2010) and (Lianjing & al., 2011) both found that firms use various methods of earnings management, such as earnings forecast guidance and classification shifting, to meet analyst expectations. However, the market does not necessarily reward firms that achieve expectations through these methods, and the use of earnings management to meet analyst forecasts can raise concerns about earnings quality.

- Stock offerings also can serve as a motivation for earnings management, with firms using discretionary accruals to report higher earnings before the offering (Pastor-LLorca, 2006). This can lead to overvaluation of issuing firms and subsequent declines in earnings (Rangan, 1998). The need for subsequent equity issuances can also influence earnings management, with firms less in need more likely to engage in income-increasing earnings management (Hagige & Wang, 2018). Additionally, the issuance of subsidiary stock can be used as an earnings management strategy, particularly when earnings fail to meet expectations (Williams & Williams, 2005).

- Further research has consistently shown that firms have strong incentives to avoid negative earnings surprises. This is particularly true for firms with higher transient institutional ownership, greater reliance on implicit claims with stakeholders, and higher value-relevance of earnings (Matsumoto, 2002). To achieve this, firms may engage in upward management of reported earnings and downward management of analysts' forecasts (Burgstaler & Eames, 2006). Additionally, firms with negative returns may be more likely to undertake earnings management to avoid losses, particularly if they have a higher need for debt (Moreira, 2007).

In addition to the previously explored motivations, it's crucial to acknowledge that financial reports may also be subject to manipulation for other strategic reasons where companies might manipulate financial statements to present a bleaker financial picture. This tactic, commonly referred to as 'taking a bath' with profits, is employed not to make the company appear better, but intentionally worse. Another practice is driven by the desire of management to retain their positions and boost their income. However, this manipulation introduces inaccuracies into financial statements, creating challenges in making sound decisions based on reliable information. Consequently, the overall integrity of financial reporting is undermined. (Habib, Hussain, & Jiang, 2011). An increasing body of accounting research suggests that enhanced financial reporting quality can alleviate the adverse impacts of financing constraints on investment. This is achieved by minimizing information asymmetry. (Biddle, Hilary, & Verdi, 2009), (Biddle & Hilary, 2006)

III. Financial Crises and Financial Reporting Quality

III.1. The impact of previous financial crises on financial reporting quality.

Crises exert a profound influence on financial reporting quality, (Amitav, 2022) Investigation's reveal the multifaceted impact of crises on financial reporting, unraveling a complex narrative across some central themes:

the determination of earnings quality

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Alqam, (2022) found that financial ratios and governance strategies significantly impact earnings quality, suggesting that managers should have more control over these ratios. Persakis & Iartridis (2015) reported a decrease in earnings quality during the 2008 Global Financial Crisis, particularly in countries with weaker shareholder protection. Kousenidis, Ladas, & Negakis (2013) observed an improvement in earnings quality during the European debt crisis, but noted a decrease in quality for firms with high discretionary accruals. Valdiansyah & Murwaningsari, (2022) identified pre-managed earnings, liquidity, and efficiency as key determinants of earnings quality, with governance mechanisms moderating these factors.

the scrutiny of audit quality

Johl, Jubb, & Houghton, (2003) found that audit quality, as measured by the level of earnings management, was associated with abnormal accruals, with greater constraint evident post-crisis. Similarly, Persakis & Iatridis, (2016) reported that audit quality was lower during the 2008 financial crisis, but higher for firms with strong investor protection and legal enforcement. However, Kyriakou, (2022) found that the proportion of non-financial firms with lower audit quality was higher during the crisis, and that auditors were less likely to provide higher audit quality. These findings suggest that while audit quality may be influenced by financial crises, the specific nature of this influence is complex and may vary across different contexts.

the interplay of conservatism,

Conservatism in the face of financial crises can take various forms. Companies adopting financially conservative strategies before a crisis tend to be more effective in securing debt funds and supporting investments, as noted by Zeng, (2011). This cautious approach may also emerge as a response to a debt crisis, where factors like social conflict and adjustment costs contribute to delayed inflation stabilization, as suggested by Labán & Sturzenegger, (1994). In the context of international debt crises, maintaining fiscal conservatism, which involves maintaining low debt/GDP ratios and employing flexible exchange rate regimes, becomes pivotal for both preventing and managing such crises, as highlighted by Rogoff (2005)

valuation effects,

Bin, Blenman, & Chen, (2004) found that the outbreak of a currency crisis leads to a significant negative impact on American depository receipts (ADR) performance. This is further supported by Yamani & Swanson, (2014) who found that equity markets become more integrated after global financial crises, leading to a decrease in the global value premium. Sundram & Mathur, (1997) observed significant wealth effects and changes in risk for banks during the Mexican debt crisis, indicating a broader impact on the financial sector. Finally, Persuad, (2008) highlighted the pro-cyclical nature of fair value accounting rules, which can exacerbate the systemic disappearance of liquidity during crises. These studies collectively underscore the complex and far-reaching effects of financial crises on asset valuation.

corporate governance,

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Erkens, Hung, & Matos, (2012) found that firms with more independent boards and higher institutional ownership experienced worse stock returns during the 2007-2008 crisis, while Ezzine & Olivero, (2013) observed significant changes in corporate governance scores in French firms during the same period. On the other hand, Nguyen, & Yin (2014) and Gupta, Krishnamurti, & Tourani-rad, (2013) found that better governance can mitigate the adverse effects of a credit supply shock on firms' financing and investment activities, and that well-governed firms do not necessarily outperform poorly governed ones during a crisis. These studies highlight the complex and multifaceted nature of the relationship between corporate governance and firm performance during financial crises.

the underpinning influence of financial stability and regulations.

Schuetz, (2010) highlights the need for more rigorous regulation on financial institutions and the use of early warning systems to predict crises. Goyal, (2010) emphasizes the importance of creating correct incentives for market participants through a combination of micro and macro prudential regulation, as well as better national and global coordination of regulators. Dobravolskas & Seiranov, (2011) underscores the role of post-crisis regulatory reforms in rebuilding financial stability, particularly in addressing the inadequacy of national micro-prudential regulators. Hamdaoui & Maktouf, (2020) adds to this discussion by showing that the link between financial liberalization and banking crisis depends on the number of years since the last regulatory reforms, and that the regulatory environment is more important in developed countries.

The findings, although inconclusive in many instances, collectively signify the nascent stage of research in this area, suggesting abundant opportunities for theoretical refinement. Notably, the implications extend beyond academic discourse, resonating profoundly with stakeholders—managers, standard setters, regulators, and policymakers. This review serves as a crucial lens through which shifts in firms' reporting practices during crises are elucidated, offering a vital framework to comprehend the current and potential influence of events like the COVID-19 pandemic on financial reporting practices. It highlights unexplored research territories, paving the way for direct implications for financial reporting practices and emphasizing the ethical quandaries that firms might face amid crises, as they navigate the pressures to optimize profits.

The financial crisis of 2008, originating from defaults on sub-prime mortgages in the United States, set off a domino effect that rippled globally. Triggered by significant economic downturns and the collapse of the housing market, the crisis rapidly engulfed the banking sector and reverberated worldwide in just a few years. This crisis spurred extensive discussions, theories, and regulatory changes in finance, necessitating a long-term restoration of confidence. The transition from a stable to an unstable global economy demanded improved risk management and operational efficiency. Amid this upheaval, financial reporting played a pivotal role, catalyzing a reevaluation of established financial theories and emphasizing the importance of transparency and fair valuation. The crisis underscored the critical need for accurate financial information to prevent future collapses and malpractices. It highlighted the significance of standardized reporting aligned with regulations and underscored the vital role of financial information for global regulators, entities, financial institutions, and civil society.

(Rotariu & Tak, 2011). In addition, the presence of debt covenants serves as another influencing factor. Given that these covenants often hinge on financial metrics such as earnings (Dichev & Skinner, 2002), an increase in income is likely to reduce the risk of covenant breaches (DeFond & Jiambalvo, 1994; Iatridis & Kadorinis, 2009; Saleh & Ahmed, 2005)

The impact of financial crises on financial reporting quality has been a focal point in various studies. (Iatridis & Augustinos, 2013) revealed that companies in Portugal, Italy, and Greece were prone to engaging in increased earnings management during such crises, contrasting with Irish, Italian, and Spanish companies that tended to disclose more value-relevant financial figures. (Ng & Tjomme, 2011)research underscored a significant correlation between lower reporting quality preceding a crisis and subsequent higher rates of non-performing loans and reduced profitability during the crisis. Additionally, banks with inferior reporting quality were at a heightened risk of regulatory intervention and facing failures during tumultuous financial periods.

2. Covid 19 and It's Financial Side effects:

On March 11, 2020, the world was awoken to a frightening reality when the World Health Organization (WHO) proclaimed new coronavirus (COVID-19) a pandemic. (Catrin, et al., 2020). Cases began in Wuhan, China, and quickly spread to Japan, South Korea, Europe, and the United States, reaching worldwide proportions. Prior to the formal pandemic proclamation, significant economic indications from several channels had suggested that the globe was on the verge of an exclusive crisis in our lifetime, if not in human history.

As a result, accounting and auditing activities were disrupted. Auditors faced challenges in conducting audits due to limited access and travel restrictions. This situation hindered auditors from gathering all the necessary evidence, presenting a difficulty for them (Badawy, 2021). Audit evidence, essentially data needed by auditors to draw audit conclusions, became crucial. Accurate and capable audit evidence is what helped auditors identify discrepancies in financial statements, ensuring the quality of the audit. The COVID-19 pandemic harmed the internal control environment, making it weaker. A weaker control environment created circumstances where businesses, supply networks, and customers faced financial pressures, making them more susceptible to fraud. For example, as falsifying financial statements or misappropriating assets (Deloitte, 2020), Although fraud is not a new threat, the COVID-19 pandemic has caused major operational and financial disruptions, putting additional strain on businesses and important stakeholders.

The corona virus significantly disrupted the global economy by leading to widespread lockdowns in towns and nations. These lockdowns and restrictions on migration, imposed by governments to curb the virus spread, have had a direct impact on the earnings and production of commercial firms. Consequently, business performance has suffered because COVID-19 has negatively affected firm performance, as highlighted by (Shen, Fu, Pan, Yu, & Chen, 2020)

The pandemic has caused a significant increase in uncertainty. Almost every aspect is plagued with uncertainty, including the virus's infectiousness, prevalence, and lethality; the availability and deployment of antigen and antibody tests; healthcare systems' ability to meet

an extraordinary challenge; how long it will take to develop and deploy safe, effective vaccines; the ultimate size of the mortality shock; and the duration and effectiveness of social distancing, market lockdowns, and other mitigation and containment strategies.

The COVID-19 pandemic's severity has transformed the reporting and disclosure landscape. Because the prolonged suspension of business operations will have an impact on the different estimations and measurement techniques of various financial report items. Furthermore, this negative impact will create an ambiguous scenario for numerous agreements and contracts established before by corporate companies. Given these facts, there has been much debate about potential reporting guidelines for the COVID-19 pandemic period, as there is a great deal of uncertainty about overall economic performance, business operations, future earnings, and a variety of other financial-related issues. However, in this uncertain age, professional accounting standard setters and practicing companies have attempted to provide a relevant guideline for Financial Reporting Disclosure (KPMG, 2020)

The global economy is suffering greatly because of the COVID-19 pandemic. Preventive measures such as locking down commercial operations for an indeterminate length of time, social isolation, travel limitations, and repeated lockdown announcements have had an immediate detrimental impact on the firm. Such economic volatility will undoubtedly have a negative impact on society, as economic downturns affect all parties involved, including investors, creditors, the general public, financial intermediaries, the government, employees, and so on. These stakeholders are now seeking information in order to assess the financial effect of the worldwide pandemic. During this situation, timely and meaningful information will assist them in making critical decisions. According to legitimacy theory, firms prefer to publish socially responsible information in order to legitimate their actions to their stakeholder groups.

The COVID-19 pandemic significantly disrupted financial earnings, as highlighted in recent academic studies. (Jiyun, 2021) research delves into the specific impact of COVID-19 on bank income, offering proposed strategies to counter the decline in earnings. (Huayu, Mengyao, Hongyu, Zhongfu, & Yongquan, 2020) study reveals that the pandemic had adverse effects on firm performance, especially affecting smaller businesses and industries heavily hit by the crisis. Additionally, (Blanco, Mayordomo, Menéndez Pujadas, & Mulino Ríos, 2020) analysis of non-financial corporations emphasizes the substantial negative outcomes of the COVID-19 crisis, showcasing sharp declines in earnings, employment, and overall profitability. These studies collectively furnish empirical evidence that firmly establishes the detrimental correlation between the COVID-19 pandemic and financial earnings. The insights provided by these papers underscore the severity and widespread implications of the pandemic on various sectors, solidifying the urgency for proactive measures and strategic interventions to bolster financial resilience in the face of such crises.

COVID-19 is perhaps a one-of-a-kind consequence in terms of its worldwide extent as a pandemic, at least since the 1918 influenza pandemic. However, as previously said, a calamity on the size of COVID-19 was not ruled out. It's intriguing to compare the outcome of COVID-19 (so far) to a hypothetical nuclear confrontation. Nuclear war, unless one considers a highly limited effect, is unsupportable by anybody on Earth. As a result, a nuclear threat, other from indicating economically damaging international tensions, is typically seen as having little effect

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on market pricing. The rationale appears to be that alternative possibilities are unimportant in the case of a non-survivable event, not because of its low frequency.

(Wang & Huang, 2014) reveal that during a recession or time of economic depression, earnings management actions rise in general. They draw attention to the fact that "when firm performance weakens, managers would want to convey a message of recovery and improvement by manipulating earnings."

According to (Rupkey, 2020), even though the collapse in the United States during the 2020 pandemic was officially short, lasting about two months, it had severe consequences. For instance, between February and April 2020, 22 million Americans lost their jobs because of pandemic-related shutdowns. To give you some perspective, the 2001 recession led to the loss of only 2.6 million jobs, and the 2007-2008 recession resulted in the loss of 8.6 million jobs. And it can be summarized that the 2020 recession is unique not only for its brief duration but also for how it unevenly affected different industries. Some, like tourism, restaurants, and air travel, suffered significantly, while others, such as grocery stores, home remodeling, and recreational vehicles, were largely unaffected.

Reinhard Dotzlaw. "KPMG's Global IFRS head" says that COVID-19 seriously endangers a business's survival, and this has big effects on how they report their finances. It affects things like whether a business can keep going, how much money it has, and the value of its assets. The International Organization of Securities Commissions (2020) also recognized that COVID-19 has a major impact on how companies operate. They stressed how important it is for companies to share complete and high-quality financial information. They advised businesses to think about how the COVID-19 situation might affect them now and, in the future, when they're evaluating their operations.

Numerous research studies have explored how companies adjust their earnings during different crises, like oil and financial downturns. However, there's a noticeable scarcity of empirical evidence on earnings management behavior during pandemics. For example, Abdul et al. (2021) examined the potential impact of the COVID-19 lockdown on earnings manipulation for listed Iraqi firms. Additionally, (Xiao & Xi, 2021)looked into how the COVID-19 outbreak influenced earnings management practices in Chinese listed firms. It's worth noting that these studies (Abdul, et al., 2021; Xiao & Xi, 2021) focused on a non-European context at the country level, raising questions about the generalizability of their findings, especially in the European and American context heavily impacted by the 2020 pandemic. This study aims to address this gap by investigating whether European firms engaged in earnings management practices during the COVID-19 pandemic. The choice of a U.S.- and a European sample is motivated by the significant impact of the COVID-19 pandemic on these regions.

Research Design and empirical strategy

I. The research objective

The main objective behind my research is to examine the impact of the COVID-19 pandemic on the Financial Reporting Quality, particularly focusing on earnings management practices, during, and after the pandemic. The core question of this thesis will revolve around the following:

"How has the COVID-19 pandemic influenced earnings management and the overall quality of financial reporting?"

To achieve this, the research will compare the extent and nature of earnings management in two different periods: During the pandemic and post-pandemic period. This comparison will help assess how the pandemic has affected the reliability and transparency of financial statements, or in other words to assess if the managers did manage earning in the covid-19 period or not?

1. Elaboration of hypotheses:

The study of earnings management has gained significant attention in accounting research. Roychowdhury, (2006) explores the concept of real activities manipulation, where firms alter their operational activities to influence reported earnings. This manipulation includes increasing production to reduce the cost of goods sold (COGS) and cutting discretionary expenditures such as R&D, advertising, and selling, general, and administrative (SG&A) expenses. These practices aim to present a more favorable financial position to stakeholders.

Subsequent studies by Cohen, Day, & Lys, (2008) and Cohen & Zarowin, (2010) further validate Roychowdhury's findings, demonstrating that these measures effectively capture real activities manipulation. These studies indicate that firms are likely to engage in earnings management practices, especially during periods of economic uncertainty.

The COVID-19 pandemic has created unprecedented economic disruptions, providing a unique context to examine earnings management practices. The pandemic's impact on financial markets and business operations might incentivize firms to intensify their earnings management efforts to meet financial targets or portray stability.

Moreover, the modified Jones (1991) model has been extensively used to measure accrual-based earnings management (AEM). This model helps estimate discretionary accruals, which represent the difference between a firm's actual accruals and the expected normal level of accruals. Discretionary accruals are a common proxy for AEM, indicating management's use of accounting choices to influence reported earnings.

Given these theoretical foundations and empirical evidence, The following hypotheses are formulated to guide the following Investigation "FRQ During and After the Covid-19 Pandemic"

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Hypothesis 1: Accrual-Based Earnings Management During the COVID-19 Pandemic

H1: *Else being equal, firms engaged in accrual-based earnings management practices more intensively during the COVID-19 pandemic compared to the post-pandemic period.*

Rationale: The economic uncertainty and disruptions caused by the pandemic might incentivize firms to manage earnings more aggressively to meet financial targets or to portray financial stability. This hypothesis will be tested using accrual-based earnings management (AEM) measures.

Hypothesis 2: Real Activities Manipulation During the COVID-19 Pandemic

H2: *Else being equal, firms engaged more intensively in real activities manipulation (RAM) during the COVID-19 pandemic compared to the post-pandemic period.*

Rationale: Following the framework of Roychowdhury, (2006), firms may have manipulated real activities to influence reported earnings during the pandemic. This includes practices like overproducing inventory to reduce the cost of goods sold (COGS) and cutting discretionary expenditures. The abnormal levels of production costs (RMPROD) and discretionary expenditures (RMDISX) will be used to measure this manipulation.

Hypothesis 3: Industry-Specific Differences in the Effect of COVID-19 on Earnings Management

H3: *Else being equal, the impact of the COVID-19 pandemic on earnings management practices varied significantly across different industries.*

Rationale: Different industries experienced varying levels of disruption and economic pressure during the pandemic, leading to diverse motivations and opportunities for earnings management. Prior research suggests that the extent of earnings management can vary significantly across industries due to differences in industry-specific risks, regulatory environments, and economic conditions (Dechow & al., 2010), (Gerakos & Kovrijnykh, 2013). This hypothesis will be tested by including industry dummy variables in the regression analysis to capture the heterogeneity of the COVID-19 impact on earnings management across industries.

II. Research design And Data description

1. Research Approach

This study employs a quantitative approach to examine the changes in financial reporting quality during, and after the COVID-19 pandemic. Quantitative methods are particularly suitable for this type of research because they allow for objective measurement and statistical analysis of financial data. This approach facilitates the identification of patterns and trends over different periods and helps in establishing relationships between variables.

The quantitative analysis in this study focuses on numerical data derived from financial statements, ensuring that the findings are based on empirical evidence rather than subjective judgment. This method involves collecting a large dataset of financial information from publicly listed companies across various sectors in the US market, which provides a comprehensive overview of the impact of the pandemic on financial reporting quality. By employing statistical techniques, the study aims to quantify changes in financial reporting practices and identify significant trends that occurred due to the pandemic.

The choice of a quantitative approach also allows for the application of various statistical models and tests to analyze the data rigorously. We will employ the regression analysis to examine the relationship between financial reporting quality in term of some relevant factors, that will be detailed below. This structured and methodical approach ensures that our analysis will be robust, and our conclusions we will draw will be supported by the data.

2. Data Sources

The data for this study was collected from Refinitiv Eikon Database, focusing on companies Incorporated and headquartered in the United States. The data downloaded is mainly composed of variables from the Balance sheet and Profit and Loss statements. These financial statements provide comprehensive insights into the companies' financial health and reporting practices. The dataset spans a period of 6 years, from 2018 to 2023, which allows for a detailed analysis of financial reporting quality across different stages of the COVID-19 pandemic.

The study covers a diverse range of industries to ensure a comprehensive understanding of the impact of the pandemic on financial reporting quality. The industries included in the analysis are:

- Energy
- Basic Materials
- Utilities
- Consumer non-cyclicals
- Consumer Cyclicals
- Healthcare
- Industrials

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- Real Estate
- Technology
- Hotels, Restaurants & Entertainments

This broad industry coverage helps capture sector-specific variations and provides a holistic view of financial reporting quality during and after the pandemic.

The data were downloaded and segmented into two distinct periods for analysis:

Pandemic (2019-2021): This period covers the height of the COVID-19 pandemic, capturing the immediate and ongoing effects on financial reporting practices.

Post-Pandemic (2022 - 2023): This period reflects the aftermath of the pandemic, allowing for an assessment of how financial reporting quality has evolved as companies and economies began to recover.

By analyzing data from these periods, our study aims to identify significant changes in financial reporting quality that can be attributed to the pandemic and subsequent recovery. This comprehensive dataset, combined with the detailed industry segmentation, provides a robust foundation for the analysis.

3. Metrics and Indicators

Following Roychowdhury (2006), I investigate a specific form of earnings management through the manipulation of real activities. This manipulation involves increasing reported earnings by reducing the cost of goods sold through overproduction of inventory and cutting discretionary expenditures, such as those related to research and development (R&D), advertising, and selling, as well as general and administrative (SG&A) expenses.

To quantify this manipulation, I employ two key metrics. Firstly, I estimate the normal level of production costs using a regression model. The equation used for this estimation includes variables such as the cost of goods sold, changes in inventory, total assets, net sales, and changes in net sales. The abnormal level of production costs is then calculated as the residual from this regression, with a higher residual indicating greater inventory overproduction and a consequent increase in reported earnings.

Secondly, I estimate the normal level of discretionary expenditures, which encompasses R&D, advertising, and SG&A expenses. This estimation is conducted using a similar regression approach, with discretionary expenditures as the dependent variable. The abnormal level of discretionary expenditures is obtained as the residual from this regression, multiplied by (- 1) to signify the reduction in these expenditures aimed at boosting reported earnings.

To combine these two measures into a single proxy for real activities manipulation (RM), I simply sum their respective residuals. This aggregated measure provides insight into the extent of manipulation undertaken by firms to enhance their reported earnings.

III. Sample description and Summary Statistics

1. Sample description

The sample for this study was selected from public companies incorporated and headquartered in the United States. Initially, a total of 146,551 firm-year observations were gathered from Refinitiv Eikon, covering a wide range of industries. This comprehensive initial dataset provided a robust starting point for analyzing financial reporting quality and earnings management practices across different periods: pandemic (2020-2021), and post-pandemic (2022-2023).

To ensure the accuracy and relevance of the analysis, the data underwent a rigorous cleaning process. Missing values in the Research and Development (R&D) variable were replaced with zero. This approach is justified as it reflects the operational reality that many firms, particularly in certain industries, may not engage in R&D activities. Thus, a missing value likely indicates that the firm did not incur any R&D costs during the period, rather than an error or omission in the data.

Further cleaning involved excluding firms operating in the financial sector due to their unique financial reporting practices and regulatory requirements, which could introduce additional variability and complexity. Firms were also required to have complete financial data for at least one year within each of the specified periods. After applying these filtering and cleaning procedures, the final sample comprised 1,209 firm-year observations across various industries, ensuring a reliable and representative dataset for the study's objectives.

Table: Sample Description

Industry	Data Retrieved	Missing Values	Final Observations
Energy	8 067	7 951	116
Basic Materials	14 431	14 278	153
Utilities	4 345	4 333	12
Consumer non-cyclicals	17 972	17 823	149
Consumer Cyclicals	22 402	22 197	205
Healthcare	12 758	12 675	83
Hotels, Restaurants &Entertainments	8 329	8 202	127
Industrials	33 588	33 492	96
Real Estate	9 314	9 308	6
Technology	15 345	15 083	262
Total	146 551	145 342	1 209

Despite utilizing secondary data from Refinitiv Eikon, we conducted random quality tests by comparing selected account numbers with figures from the firms' published reports (We took 2 random companies). These tests revealed no discrepancies, affirming the reliability and trustworthiness of the data. Thus, the dataset derived from Refinitiv Eikon is considered both accurate and dependable for the purposes of this study.

2. Variables selection and Models Definition

For the purpose of this study, we have selected several key variables that are critical for analyzing earnings management and financial reporting quality. The primary variables are categorized into two main groups: dependent variables and independent variables. The dependent variables are those that we aim to explain or predict, while the independent variables are those that we believe influence the dependent variables.

{ Insert Table 1 }

Model's Definition:

Real Activities Manipulation:

To detect earnings management through real activities manipulation, we follow the approach outlined by Roychowdhury (2006). This involves analyzing two main strategies: increasing earnings by reducing the cost of goods sold through overproduction of inventory, and cutting discretionary expenditures, including R&D, advertising, and selling, general, and administrative (SG&A) expenses. The abnormal level of production costs measures the former, while the abnormal level of discretionary expenditures measures the latter. These metrics have been validated by subsequent studies, such as Cohen & al. (2008) and Cohen & Zarowin (2010), to effectively capture real activities manipulation.

I estimate the normal level of production costs following Roychowdhury (2006):

$$\frac{PROD_t}{A_{t-1}} = \alpha_0 + \alpha_1 \left(\frac{1}{A_{t-1}}\right) + \alpha_2 \left(\frac{S_t}{A_{t-1}}\right) + \alpha_3 \left(\frac{\Delta S_t}{A_{t-1}}\right) + \alpha_4 \left(\frac{\Delta S_{t-1}}{A_{t-1}}\right) + \varepsilon_t$$

Equation 1: Overproducing Inventory Model

(1)

Where:

- $PROD_t$: The sum of the costs of goods and services Sold in year t and the change in inventory from t-1 to.
- A_{t-1} : Total assets at the end of year t-1.

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- S_t : Net sales in year t [2].
- ΔS_t : Change in net sales from year t-1 to t.
- ΔS_{t-1} : Change in net sales from t-2 to t-1
- ε_t : Error term

Equation (1) is estimated cross-sectionally for each industry-year with at least 6 observations, following the industry classification by independent variable industry, in which I separated all the data into industries as it is classified in original data base, Refinitiv Eikon. This ensures that the estimated coefficients reflect the impact of industry-wide economic conditions on production costs over time. The abnormal level of production costs (*RMPROD*) is measured as the estimated residual from Equation (1). A higher residual indicates greater inventory overproduction and, consequently, a greater increase in reported earnings through the reduction of the cost of goods sold.

Following Roychowdhury (2006), we also estimate the normal level of discretionary expenditures using the following equation:

$$\frac{DISX_t}{A_{t-1}} = \alpha_0 + \alpha_1 \left(\frac{1}{A_{t-1}}\right) + \alpha_2 \left(\frac{S_{t-1}}{A_{t-1}}\right) + \varepsilon_t$$

Equation 2: Discretionary Expenditures Model

(2)

Where:

- $DISX_t$: are the discretionary expenditures (i.e., the sum of R&D, advertising, and SG&A expenditures) in year t

I conduct a cross-sectional regression analysis for industry-years that have a minimum of 6 observations. The abnormal level of discretionary expenditures is represented by the estimated residual from this regression. To reflect the magnitude of discretionary expenditure cut by firms to boost reported earnings, I follow Zang, (2012). And I multiply these residuals by -1, resulting in a metric denoted as RMDISX. Subsequently, I aggregate the two measures of real activities manipulation into a single proxy, RM, by summing them.

Accrual-Based Earnings Management:

To proxy for accrual-based earnings management, we use discretionary accruals. Discretionary accruals are the difference between a firm's actual accruals and the normal level of accruals. We estimate normal accruals using the modified Jones (1991) model:

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[2] Note: Since sales data was not available, we used EBIT as a proxy for sales

$$\frac{Accruals_t}{A_{t-1}} = \alpha_0 + \alpha_1\left(\frac{1}{A_{t-1}}\right) + \alpha_2\left(\frac{\Delta S_t}{A_{t-1}}\right) + \alpha_3\left(\frac{PPE_t}{A_{t-1}}\right) + \varepsilon_t$$

Equation 3: Accruals Based Earnings Management

(3)

Where:

- $Accruals_t$: are the earnings before extraordinary items and discontinued operations minus the operating cash flows reported in the statement of cash flows in year t
- PPE_t : is the gross property, plant, and equipment.

This regression is estimated cross-sectionally for each industry-year with at least 6 observations. The residuals (AM), which represent discretionary accruals, serve as the proxy for accrual-based earnings management.

By using these models, we can identify the extent to which firms engage in earnings management through both accrual-based methods and real activities manipulation.

Regression Model for Assessing the Impact of Covid-19:

Before detailing the calculations for earnings management proxies, I present the regression model used to assess the impact of the COVID-19 pandemic on financial reporting quality. The analysis focuses on the four most dominant industries in the dataset: Energy, Basic Materials, Consumer Cyclicals, and Consumer Non-Cyclicals. We control for industry effects by including industry-specific dummy variables in the regression.

Regression Model Specification

The regression model used to estimate the effect of COVID-19, along with other control variables, on earnings management is specified as follows:

$$Y = \alpha + \beta_1 Covid_t + \beta_2 ROA_t + \beta_3 Current\ Ratio_t + \beta_4 Assets\ Turnover_t$$
$$+ \beta_5 Sales\ Growth_t + \beta_6 Total\ Assets_t + \sum_{k=1}^{4} \gamma_k\ Industry\ Dummy_k + \varepsilon_t$$

Equation 4: Effect of Covid-19 and Financial Indicators on Earnings Management

Where:

- Y : Represents the dependent variables, which are either RM (Real Activities Manipulation) or AM (Accrual-Based Earnings Management) in $year_t$
- α : is the Intercept
- $Covid_t$: is a binary indicator variable that equals 1 if the observation is during the COVID-19 period (2020-2021), and 0 otherwise.

- ROA_t : Represents the Return on Assets in $year_t$, calculated as EBIT divided by Total Assets.
- $Current\ Ratio_t$: Represents the Return on Assets in $year_t$, calculated as EBIT divided by Total Assets.
- $Asset\ Turnover_t$: is calculated as Sales divided by Current Assets in $year_t$.
- $Sales\ Growth_t$: Represents the year-over-year change in sales in $year_t$.
- $Total\ Assets_t$: Represents the size of the firm in $year_t$.
- $Industry\ Dummy_k$: Represents dummy variables for the four dominant industries: Energy, Basic Materials, Consumer Cyclicals and Consumer Non-Cyclicals.
- ε_t : is the error term.

Purpose and Interpretation

This model allows us to estimate the effect of the COVID-19 pandemic on earnings management practices across the selected industries. By including industry-specific dummy variables, the model controls for industry effects, enabling a more accurate estimation of the impact of COVID-19 and other financial controls on earnings management.

The coefficients β_1 to β_6 provide insights into the relationships between these control variables and the extent of earnings management. The industry dummy coefficients γ_k help account for specific effects associated with each industry.

3. Descriptive statistics

Before proceeding with the estimation of the impact of the COVID-19 pandemic on earnings management practices, it is essential to ensure that the regression model is free from multicollinearity issues, which could distort the interpretation of the results. Multicollinearity occurs when independent variables in a regression model are highly correlated, making it difficult to isolate the individual effect of each variable. To diagnose multicollinearity, I conducted a collinearity diagnostics analysis, which includes the evaluation of the Variance Inflation Factor (VIF), Tolerance levels, and Condition Indices. The results from these diagnostics allow us to determine whether multicollinearity is present and if any corrective measures are necessary. The table below presents the collinearity diagnostics for all independent variables.

Descriptive Statistics

	N	Minimum	Maximum	Mean		Std. Deviation
	Statistic	Statistic	Statistic	Statistic	Std. Error	Statistic
Accruals	3072	-5.69	4.03	0.00	0.01	0.41
Covid	3072	0.00	1.00	0.50	0.01	0.50
Current Ratio	3072	0.00	47.87	2.54	0.05	2.54
Operating Margin	3069	-14.88	6.32	-0.01	0.01	0.47

RM	*3072*	*-8.84*	*11.67*	*-0.05*	*0.02*	*0.98*
ROA	*3072*	*-23.49*	*2.10*	*-0.08*	*0.02*	*0.91*
Sales Growth	*3068*	*-308.47*	*1,411,757.00*	*1761.54*	*880.58*	*48774.70*
Total Assets	*3068*	*41.56*	*97,271,000.00*	*1,363,754.29*	*95,835.07*	*5,308,259.54*
Valid N (listwise)	*3063*					

Table 1: Descriptive statistics for dependent and independent Variables

Regression Analysis and results

I. Introduction to the regression analysis

In this section, I present the results of the regression analysis aimed at evaluating the impact of the COVID-19 pandemic and various financial control variables on financial reporting quality. The analysis was conducted for two key measures of financial reporting quality: Real Activities Manipulation (RM) and Accrual-Based Earnings Management (AM). The RM measure was further broken down into components such as Discretionary Expenditures (RM Disx) and Inventory Overproduction (RM Overproduction). The dependent variables were regressed against the COVID-19 indicator, financial ratios, and industry-specific dummy variables to control for sectoral effects.

II. Results of regression Analysis: Assessing the Impact of COVID-19 on Financial Reporting Quality

1. Accrual Based Earning management

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.379ᵃ	0.144	0.141	0, 3333015285

a. Predictors: (Constant), Total Assets, Sales Growth, Covid, Technology, ROA, Current Ratio, Basic Materials, Operating Margin, Consumer Non-Cyclicals

Table 2: Model Summary for Accrual Based Earnings Management

The regression model for Accruals yielded an R-Squared value of 0.144, indicating that 14.4% of the variation in accruals is explained by the model. The Adjusted R-Squared is 0.141, which corrects for the number of predictors in the model.

ANOVAᵃ

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	56.997	9	6.333	57.008	.000b
	Residual	339.602	3057	0.111		
	Total	396.599	3066			

a. Dependent Variable: Accruals

b. Predictors: (Constant), Total Assets, Sales Growth, Covid, Technology, ROA, Current Ratio, Basic Materials, Operating Margin, Consumer Non-Cyclicals

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Indeed, The F-statistic of 57.008 with a significance level of p < 0.001 suggests that the model is statistically significant.

The table below summarizes the key predictors for Accrual-Based Earnings Management

	Coefficients[a]				
Model	**Unstandardized Coefficients**		**Standardized Coefficients**	**t**	**Sig.**
	B	**Std. Error**	**Beta**		
(Constant)	0.084	0.015		5.760	0.000***
Covid	0.037	0.012	0.051	3.055	0.002***
Basic Materials	0.015	0.018	0.016	0.820	0.412
Technology	0.116	0.016	0.153	7.417	0.000***
Consumer non-cyclicals	0.085	0.018	0.093	4.679	0.000***
1 Current Ratio	0.012	0.002	0.083	4.843	0.000***
Operating Margin	-0.107	0.014	-0.139	-7.426	0.000***
ROA	-0.097	0.007	-0.245	-13.236	0.000***
Sales Growth	-5.601E-05	0.000	-0.003	-0.185	0.854
Total Assets	-3.048E-09	0.000	-0.045	-2.667	0.008**

a. Dependent Variable: Accruals

a. Dependent Variable: Accruals

Table 4:Regression Coefficients for Accruals Based Earnings Management

- **Covid**: The coefficient for the COVID-19 variable is 0.037 (p = 0.002), indicating a significant positive effect on accrual-based earnings management. This suggests that during the COVID-19 pandemic, firms were more likely to engage in earnings manipulation using accruals.
- **Technology and Consumer Non-Cyclicals**: Both the Technology (B = 0.116, p = 0.000) and Consumer Non-Cyclicals (B = 0.085, p = 0.000) industries show significant positive coefficients. This implies that firms in these sectors are more prone to engage in accrual-based earnings management compared to firms in other sectors.
- **ROA and Operating Margin**: The Return on Assets (ROA) has a coefficient of -0.097 (p = 0.000), and Operating Margin has a coefficient of -0.107 (p = 0.000), both of which are highly significant. The negative coefficients indicate that higher profitability is associated with less accrual-based earnings management, suggesting that more profitable firms may have less incentive to manipulate earnings through accruals.
- **Basic Materials and Sales Growth:** The Basic Materials industry shows a positive coefficient (B = 0.015) but is not statistically significant (p = 0.412). Similarly, Sales

Growth has a negligible and insignificant impact on accrual-based earnings management (B = -5.601E-05, p = 0.854).

- **Current Ratio:** The Current Ratio has a positive and significant coefficient (B = 0.012, p = 0.000), suggesting that firms with higher liquidity are more likely to engage in accrual-based earnings management.
- **Total Assets**: The coefficient for Total Assets is -3.048E-09 (p = 0.008), which is significant but very close to zero, indicating a minimal negative relationship between firm size and accrual-based earnings management.

2. Real Activities Manipulation (RM): Discretionary Expenditures (RM Disx) – Cutting the COGSS & Overproducing Inventory

Model Summary

The following table summarizes the key statistics of the regression models for Real Activities Manipulation, specifically for Discretionary Expenditures (Model 1) and Overproduction (Model 2):

Model Summary				
Model	**R**	**R Square**	**Adjusted R Square**	**Std. Error of the Estimate**
1	.273a	0.075	0.072	0.39267
2	.164b	0.027	0.024	0.81567

a&b. Predictors: (Constant), Total Assets, Sales Growth, Covid, Technology, Operating Margin, Current Ratio, Basic Materials, Consumer Non-Cyclicals

Table 5:Detailed Model summary for Real Activities Manipulation

- **Model 1 (Discretionary Expenditures).**
- **RSquare**: The R-Square value for Model 1 is 0.075, which means that 7.5% of the variation in earnings management through discretionary expenditures is explained by the independent variables in the model. While this percentage is relatively low, it indicates that the model captures some of the factors influencing discretionary spending practices used to manipulate earnings.
- **Adjusted R-Square**: The Adjusted R-Square value is 0.072, which adjusts for the number of predictors in the model. This slight reduction from the R-Square value suggests that while the model is valid, the inclusion of multiple predictors doesn't significantly improve its explanatory power.
- **Standard Error of the Estimate**: The standard error is 0.39267, indicating the average distance that the observed values fall from the regression line. A lower value would indicate a better fit, so this suggests moderate variance around the fitted regression line.
- **Model 2 (Overproduction).**
- **R-Square**: For Model 2, the R-Square value is 0.027, indicating that only 2.7% of the variance in earnings management through overproduction is explained by the model's predictors. This low R-Square suggests that overproduction as a method of earnings

management is less influenced by the variables included in the model, indicating that other factors might be driving overproduction-based earnings manipulation.

- **Adjusted R-Square**: The Adjusted R-Square for Model 2 is 0.024, reflecting a slight drop from the R-Square value after accounting for the number of predictors. This confirms that the model has limited explanatory power for overproduction.
- **Standard Error of the Estimate**: The standard error here is 0.81567, which is considerably higher than in Model 1, indicating greater variability in the data relative to the regression line. This suggests that the model does not fit the data well and that the observed overproduction practices vary widely.

ANOVA

		Sum of Squares		**df**		**Mean Square**		**F**		**Sig.**	
Model		**(1)[3]**	**(2)[4]**	**(1)**	**(2)**	**(1)**	**(2)**	**(1)**	**(2)**	**(1)**	**(2)**
1 &2	**Regression**	37.931	55.838	8	8	4.741	6.980	30.750	10.491	.000[b]	.000[b]
	Residual	470.897	2031.877	3054	3054	0.154	0.665				
	Total	508.828	2087.715	3062	3062						

a. *Dependent Variable: RMDisx or RMOverproduction*
b. *Predictors: (Constant), Total Assets, Sales Growth, Covid, Technology, Operating Margin, Current Ratio, Basic Materials, Consumer Non-Cyclicals*

Table 6: ANOVA Results for Real Activities Manipulation Models (Discretionary Expenditures and Overproduction)

The ANOVA results for the Real Activities Manipulation models are presented in Table 7. The table summarizes the variance explained by each model, highlighting the significance of the regression coefficients in explaining the variance in Discretionary Expenditures (Model 1) and Overproduction (Model 2).

Key Findings:

- ✓ **Model 1 (Discretionary Expenditures):** With an F-statistic of 30.750 and a significance level of $p < 0.001$, the model is statistically significant, explaining 7.5% of the variance in earnings management through discretionary expenditures.
- ✓ **Model 2 (Overproduction):** The model is also statistically significant, with an F-statistic of 10.491 and a p-value of < 0.001, explaining 2.7% of the variance in earnings management through overproduction.

Coefficients

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[3] Discretionary Expenditures (RM Disx)
[4] Inventory Overproduction (RM Overproduction)

The results from Model 1 and Model 2 in the table below highlight the different factors that influence the two types of real activities manipulation. In both models, Total Assets consistently show a positive and significant relationship, indicating that larger firms are more prone to these practices. Current Ratio is also a significant predictor in both models, suggesting that liquidity plays a key role in determining the extent of real activities manipulation.

Operating Margin stands out as a negative predictor in both models, indicating that more profitable firms are less likely to engage in these manipulative behaviors. However, the impact of Technology and Consumer Non-Cyclicals is only significant in the Discretionary Expenditures model, suggesting sector-specific differences in how firms manage their earnings.

Coefficients[a&b]

Model		Model 1					Model 2				
		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta			B	Std. Error	Beta		
1 & 2	(Constant)	-0.202	0.017		-11.828	0.000	-0.133	0.036		-3.733	0.000
	Covid	-0.012	0.014	-0.015	-0.845	0.398	-0.006	0.030	-0.004	-0.196	0.844
	Technology	0.169	0.018	0.197	9.163	0.000	-0.040	0.038	-0.023	-1.033	0.302
	Consumer non-cyclicals	0.201	0.021	0.195	9.424	0.000	0.031	0.044	0.015	0.702	0.482
	Basic Materials	0.192	0.021	0.187	9.083	0.000	0.000	0.044	0.000	0.000	1.000
	Current Ratio	0.006	0.003	0.036	2.003	0.045	0.049	0.006	0.150	8.189	0.000
	Operating Margin	-0.147	0.015	-0.168	-9.515	0.000	-0.038	0.032	-0.021	-1.180	0.238
	Sales Growth	7.956E-05	0.000	0.004	0.223	0.824	1.325E-03	0.001	0.032	1.784	0.075
	Total Assets	5.044E-09	0.000	0.066	3.747	0.000	1.223E-08	0.000	0.079	4.373	0.000

a. Dependent Variable: RM Disx
b. Dependent Variable: RM InvOverrproduction

Table 7: Regression Coefficients for Real Activities Manipulation Model

III. Discussion of the results

1. Overview of Findings and Comparison with Prior Literature

This section outlines the main findings from the regression analyses conducted above on both Accrual-Based Earnings Management (ABEM) and Real Activities Manipulation (RAM). The primary goal was to assess how the COVID-19 pandemic, along with other financial control factors, influenced the financial reporting quality of firms within selected leading industries.

ം **Accrual-Based Earnings Management (ABEM):**

The analysis revealed that the COVID-19 pandemic significantly boosted accrual-based earnings management. The positive coefficient associated with the COVID-19 variable indicates that firms increased their use of accrual-based strategies during the pandemic. This suggests that companies might have aimed to smooth their earnings, presenting a more stable financial appearance despite the economic challenges. Prior studies, such as Kousenidis, Ladas, & CI, (2013), have documented increased earnings management during economic downturns, particularly through accruals. The current study extends this literature by confirming that similar trends were observed during the COVID-19 pandemic, a unique global crisis.

Figure 1: Trend of Accrual-Based Earnings Management Over Time

Additionally, financial metrics like Return on Assets (ROA) and Operating Margin showed significant negative correlations with accrual-based earnings management. This finding imp   lies that more profitable companies were less likely to engage in these manipulative practices, likely because they didn't need to artificially enhance their earnings.

When examining the impact across different industries, it was observed that firms in the Technology and Consumer Non-Cyclicals sectors were more inclined towards accrual-based earnings management than those in other sectors.
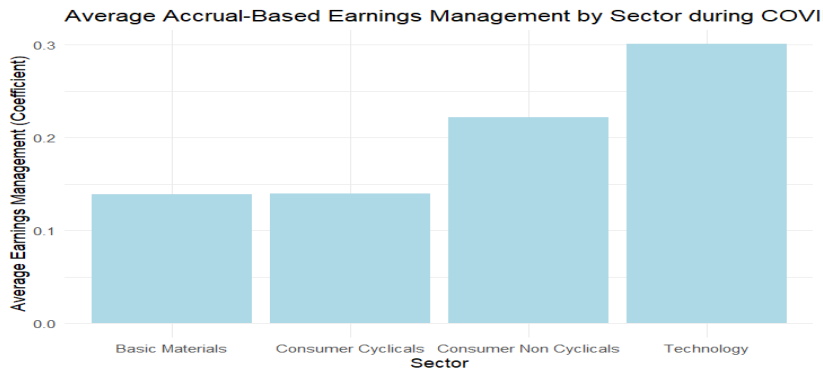
Figure 2: Average Accrual-Based Earnings Management by Sector during COVID-19.

As shown in Figure 1, The Technology sector exhibits the highest level of accrual-based earnings management during the pandemic, followed by the Consumer Non-Cyclicals sector. And as a consequence, we can directly see the variation of Industries behaviors during economic uncertainties.

Real Activities Manipulation (RAM):

The analysis of Real Activities Manipulation (RAM) was divided into two parts: Discretionary Expenditures (RM Disx) and Inventory Overproduction (RM InvOverproduction). Each revealed distinct patterns in earnings management behavior:

- Discretionary Expenditures (RM Disx): The analysis showed that the COVID-19 pandemic did not have a notable effect on earnings management through discretionary expenditures. However, firms in the Technology, Consumer Non-Cyclicals, and Basic Materials sectors exhibited significant positive coefficients, suggesting that these companies were more likely to engage in earnings management by cutting back on discretionary charges.

- Inventory Overproduction (RM InvOverproduction): Similarly, the pandemic did not have a significant impact on earnings management through inventory overproduction. Nevertheless, the data showed that firms with higher Current Ratios and larger Total Assets were more prone to this type of earnings management. This indicates that companies with better liquidity and larger size had the means to manipulate their earnings through production-related strategies.

2. Robustness tests
2.1. *Multicollinearity Testing*

Multicollinearity refers to a situation where two or more predictor variables in a regression model are highly correlated, meaning one can be linearly predicted from the others with a substantial degree of accuracy. High multicollinearity can inflate the variance of the coefficient estimates, making our models unstable. Therefore, testing for multicollinearity is essential to ensure the reliability of the regression results.

The most commonly used diagnostic tool for multicollinearity is the **Variance Inflation Factor (VIF).** A VIF value greater than 10 is often considered indicative of high multicollinearity, although some researchers use a more conservative threshold of 5.

In our study, VIF was calculated for all predictor variables in the regression models for both RM (Real Activities Manipulation) and Accruals as dependent variables. The results, presented in Table 9 below, show that all VIF values are below 5, indicating that multicollinearity is not a concern.

Predictor Variable	VIF
Covid	1.003
ROA	1.225
Current Ratio	1.061
Operating Margin	1.245
Sales Growth	1.002
Total Assets	1.016
Industry (Dummies)	1.062

Table 8: VIF (Variance Inflation Factor) for Independent Variables

Interpretation: All VIF values are below the threshold, suggesting that the coefficients estimated in the regression models are reliable and not significantly affected by multicollinearity.

To further examine potential multicollinearity, we generated a correlation matrix to assess the pairwise relationships between the predictor variables. The correlation matrix is displayed in Figure 3 below.

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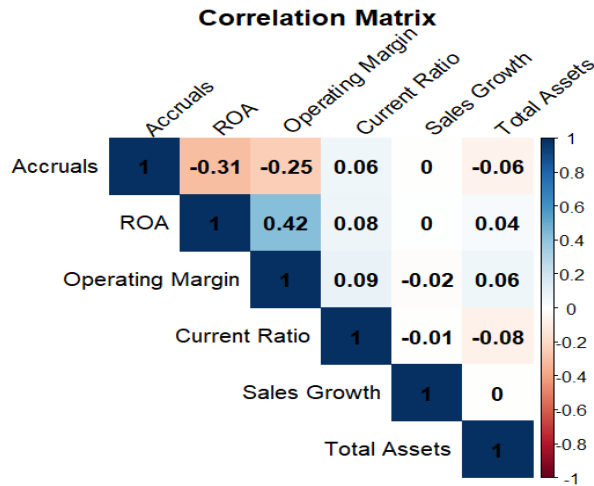
Figure 3: Correlation Matrix for Predictor Variables

3. Theoretical and Practical implications of the study:

This research adds to what we know about how companies manage their earnings during tough economic times. Just like earlier studies, my findings show that companies used both accrual-based methods and real activities manipulation more during the COVID-19 pandemic. This means that during crises, companies tend to manage their earnings more aggressively. Additionally, by looking at different industries, my research shows that not all industries behave the same way during a crisis.

For people working in business or finance, my findings suggest that it's really important to watch out for unusual financial practices during a crisis. Auditors, for example, should be especially careful when reviewing companies' financial reports during times like the COVID-19 pandemic, especially in industries that were hit hard. This research shows that different industries may need different kinds of attention when it comes to managing financial reports during a crisis.

Conclusion

In conclusion, this thesis provides a detailed look at how the COVID-19 pandemic affected Financial Reporting Quality, focusing on both accrual-based earnings management (AEM) and real activities manipulation (RAM) across different industries. The findings show that the pandemic significantly changed how companies managed their earnings, especially in the technology and consumer non-cyclical sectors. These industries were more likely to use accrual-based earnings management during the pandemic, likely due to the increased economic uncertainty and pressure to maintain a strong financial appearance.

The study also highlights that the impact of the pandemic was not the same across all industries. While technology and consumer non-cyclicals saw a notable increase in earnings management, other sectors like basic materials did not show the same effect. This difference suggests that each industry responded to the pandemic in its own way, depending on its unique challenges and opportunities. Additionally, the study found that factors like a company's current ratio and operating margin played a key role in influencing how aggressively earnings were managed, with liquidity and profitability being important considerations during this time of crisis.

This research adds valuable insights to the broader understanding of earnings management by showing how a global crisis like the COVID-19 pandemic can disrupt normal financial reporting practices. It emphasizes that during such times, there is a need for closer monitoring by regulators, auditors, and other stakeholders to ensure that financial reports remain accurate and reliable. The differences seen across industries also suggest that regulatory responses should be tailored to the specific needs of each sector to better address the risks and challenges they face during a crisis.

Practically speaking, the findings of this study suggest that both regulators and auditors should focus more on industries that are prone to increased earnings management during crises. This could help prevent companies from manipulating their earnings in ways that mislead investors and other stakeholders. For the future, having industry-specific guidelines and stronger audit procedures could improve the overall transparency and reliability of financial reporting, especially during periods of economic uncertainty.

However, it's important to acknowledge the limitations of this study. The research was limited to a specific set of industries and a short time frame due to the final data set distribution, we only focused on the most four dominant industries in our final observations which may limit how well the findings apply to other contexts. Future research could explore the longer-term effects of the pandemic on earnings management or look at additional industries and regions to gain a more complete understanding of these dynamics.

In summary, this thesis shows that the COVID-19 pandemic led to significant changes in earnings management practices, with certain industries being more affected than others. The findings offer important lessons for how companies, regulators, and auditors can respond more effectively to financial reporting challenges during times of crisis, ensuring that financial statements remain trustworthy and reflective of a company's true economic position.

Limitations

Despite the valuable insights provided by this study, there are several limitations that must be acknowledged. First, the research focused only on four industries—Technology, Basic Materials, Consumer Non-Cyclicals, and another Consumer Cyclicals—due to the composition of the available sample. While these industries represent the most significant sectors in my sample the exclusion of other industries may limit the generalizability of the findings. The results, therefore, may not fully capture the variability of earnings management practices across the entire market.

Second, the study conducted the regression analysis on the combined dataset rather than running separate regressions for each industry or each year. Ideally, running regressions industry by industry and year by year would have allowed for a more detailed examination of how the COVID-19 pandemic affected earnings management practices in different sectors and time periods.

This approach would have provided more nuanced insights into the industry-specific and temporal dynamics of earnings manipulation during the pandemic. Consequently, the findings should be interpreted with caution, as they reflect aggregate trends that might mask important differences across industries and time periods. Future research could address these limitations by expanding the sample to include a broader range of industries and by conducting a more granular analysis that considers industry-specific and year-specific effects.

List of appendices

Variable	Description
Dependent Variables	
Total Accruals (TA)	The difference between net income and cash flow from operations. This variable is used as a proxy for accrual-based earnings management. However, in our analysis, we specifically focus on Discretionary Accruals (DA), which is part of TA, to measure Accrual-Based Earnings Management.
Discretionary Accruals (DA)	Calculated using the Modified Jones Model. Represents the portion of accruals that management can manipulate. In the regression analysis, DA is used as a dependent variable and is denoted as AM (Accruals Manipulation).
Abnormal Production Costs (APC)	Previously referred to as abnormal production costs, now captured through the RM (Real Activities Manipulation) proxy. Reflects real activities manipulation by overproducing inventory. Calculated as residuals from the regression of inventory-related production costs.
Abnormal Discretionary Expenditures (ADE)	Part of the RM (Real Activities Manipulation) proxy. Calculated based on deviations from expected discretionary expenditures. This represents real activities manipulation by cutting R&D, advertising, and SG&A expenses.
RM (Real Activities Manipulation)	A combined measure that includes both Abnormal Production Costs (APC) and Abnormal Discretionary Expenditures (ADE).
Independent Variables	
Lagged Total Assets	Total assets at the end of the previous year. Used to normalize various financial metrics.
Return on Assets (ROA)	Calculated as EBIT divided by Total Assets. Used as a control variable to measure firm profitability.
Current Ratio	Calculated as Total Current Assets divided by Current Liabilities. Measures liquidity and is used as a control variable.
Industry Dummies	Categorical variables representing different industries, specifically Energy, Basic Materials, Consumer Cyclicals, and Consumer Non-Cyclicals. These dummies control for industry-specific effects in the regression analysis.
Change in Sales (Δ Sales)	Change in sales from the previous year. Can influence both accruals and real activities manipulation.
Asset Turnover	Calculated as Sales divided by Total Assets. Measures the efficiency of asset usage in generating sales. Used as a control variable.
Covid	A binary indicator variable, where 1 represents the period during the Covid pandemic (2020-2021) and 0 otherwise. Used as an independent variable to assess the impact of the pandemic on financial reporting quality.

Table 9: Independent and Dependent Variables

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<u>Executive Summary</u>

This thesis examines the impact of the COVID-19 pandemic on financial reporting quality, focusing on strengthening earnings management practices across sectors. The study examines accrual-based earnings management (AEM) and real activity manipulation (RAM) during and after the pandemic, which found a significant increase in AEM as firms responded to economic uncertainty although evidence of about RAM is less conclusive, findings industry specific Highlighting important differences, with customer cyclicals and industrial companies shown to be more sensitive to these practices These results highlight the importance of monitoring regulation if projects are targeted in times of economic instability.

Key Words: COVID-19, Earnings Management, Financial Reporting, Accrual-Based, Industry Differences

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