Political connections and earnings management in emerging markets – new evidence

Ahmad Emarati and Farzaneh Nassirzadeh
Faculty of Economics and Administrative Sciences, Ferdowsi University of Mashhad, Mashhad, Iran, and

Davood Askarany
Department of Accounting and Finance, The University of Auckland, Auckland, New Zealand

Abstract

Purpose – This study examines the relationship between political connections and earnings management in Iran as an emerging market, focusing on the moderating roles of audit quality and conditional conservatism. The research explores how governance mechanisms can influence financial transparency and mitigate manipulative financial practices in politically connected firms.

Design/methodology/approach – The study employs panel data from 221 firms listed on the Tehran Stock Exchange (TSE) between 2017 and 2021. Generalised least squares (GLS) regression analyses political connections' impact on accrual-based and real earnings management. Audit quality and conditional conservatism are tested as moderating variables to assess their influence on the relationship between political connections and earnings management.

Findings – The results indicate that political connections are positively associated with accrual-based earnings management but negatively linked to real earnings management. High-quality audits significantly reduce real earnings manipulation but may inadvertently enable accrual-based earnings management. Contrary to expectations, conditional conservatism does not significantly moderate the relationship between political connections and earnings management.

Research limitations/implications – The findings highlight the importance of robust governance frameworks and enhanced audit practices in curbing opportunistic financial behaviour in politically connected firms. Policymakers in emerging markets should address governance gaps and promote sustainable financial reporting standards to reduce the adverse effects of political influence on corporate behaviour.

Originality/value – This study contributes to the literature by providing a comparative perspective on the intersection of political influence, governance mechanisms and financial practices in emerging markets. It highlights the dual effects of political connections on earnings management, offering novel insights into firms' governance challenges in developing economies. The research also emphasises the need for tailored financial reporting frameworks in politically connected firms, mainly where state intervention and political considerations play a significant role in corporate decision-making.

Keywords Political connections, Earnings management, Management accounting, Audit quality, Conditional conservatism, Emerging markets, Corporate governance, Financial transparency

Paper type Research paper

1. Introduction

The relationship between political connections (PC) and earnings management (EM) has been a focal point of research in corporate governance and financial accounting. Political connections, the relationships between firms and government officials or entities, can provide firms with access to resources, regulatory benefits, and other advantages (Faccio, 2006). However, these connections can also create opportunities for managerial opportunism, particularly earnings management. Earnings management, the manipulation of financial

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reports to achieve specific objectives, can mislead investors and other stakeholders, undermining the integrity of financial markets (Healy and Wahlen, 1999).

Existing literature has explored the impact of political connections on various aspects of corporate behaviour, including access to finance, tax benefits, and firm performance (Boubakri *et al.*, 2012; Chaney *et al.*, 2011). However, the relationship between political connections and earnings management remains underexplored, particularly in emerging markets. Studies in developed economies have shown mixed results, with some indicating that political connections reduce earnings management due to increased scrutiny (Fan *et al.*, 2014), while others suggest that these connections facilitate earnings management by reducing market pressure (Braam *et al.*, 2015).

Despite the growing body of research, several gaps remain. First, most studies have focused on developed economies, leaving a significant gap in understanding how political connections influence earnings management in emerging markets. Second, the moderating roles of audit quality and conditional conservatism in this relationship have not been thoroughly examined. Third, the mechanisms through which political connections affect earnings management, particularly in the context of board governance, are not well understood.

This study aims to fill these gaps by investigating the relationship between political connections and earnings management in Iran, an emerging market with a unique socio-political environment. Iran provides an ideal setting for this study due to its significant state influence on the economy, the prevalence of politically connected firms, and the relatively underdeveloped corporate governance mechanisms. Focusing on Iran, this study contributes to the literature by providing insights into how political connections influence earnings management in a context where state intervention and political considerations play a crucial role in corporate decision-making.

Iran's unique socio-political environment, characterised by significant state intervention, a high degree of political instability, and a lack of transparency in financial markets, makes it an ideal setting to study the impact of political connections on earnings management. The prevalence of politically connected firms in Iran, coupled with the relatively weak enforcement of corporate governance mechanisms, provides a rich context for examining the interplay between political connections, corporate governance, and earnings management.

2. Literature review, theoretical framework and hypothesis development

This study investigates the interplay between political connections and earnings management in emerging markets. Emerging markets, such as Iran, present a unique context for studying the relationship between political connections and earnings management due to their distinct institutional environments. Unlike developed economies, emerging markets often feature weaker regulatory frameworks, less transparent financial systems, and more state intervention in the economy. These factors create an environment where political connections, including financial reporting practices, can significantly influence corporate behaviour.

In Iran, the prevalence of state-owned enterprises and politically connected firms, coupled with a lack of robust corporate governance mechanisms, makes it an ideal setting for examining how political connections affect earnings management. The Iranian economy is heavily influenced by political considerations, with government officials and state-owned entities playing a central role in corporate decision-making. This creates a fertile ground for exploring how political connections can lead to opportunities (e.g. access to resources, regulatory benefits) and challenges (e.g. increased earnings management, reduced transparency) for firms.

Moreover, studying political connections in Iran contributes to the broader literature by providing insights into how political influence operates where state intervention is pervasive, and corporate governance is still evolving. By focusing on Iran, this study sheds light on how political connections influence earnings management in emerging markets, offering valuable lessons for policymakers, regulators, and investors.

Furthermore, the study explores the moderating roles of audit quality and conservatism, emphasising their importance in mitigating the overstatement of management activities. By delving into these intricate relationships, the research contributes to understanding the complexities of political connections and their impact on financial reporting.

The study addresses the following questions:

(1) How do political connections influence real and accrual-based earnings management in Iranian firms?

(2) What role do corporate governance mechanisms, such as audit quality and conditional conservatism, play in moderating the relationship between political connections and earnings management?

(3) How does the institutional environment in Iran, including the composition and influence of the board of directors, affect the dynamics of political connections and earnings management?

3. Institutional background

3.1 Composition and influence of the board of directors in Iran

The board of directors in Iran plays a central role in corporate governance, particularly in state-owned and politically connected firms. The board's composition typically includes a mix of executive and non-executive directors, with many board members often having political backgrounds. These board members may be current or former government officials, representatives of state-owned enterprises, or individuals with close ties to the ruling political elite.

3.2 Hiring and rotation system

The hiring and rotation of board members in Iran are influenced by political considerations, particularly in state-owned and politically connected firms. Board members are often appointed based on their political affiliations and connections rather than their professional qualifications or expertise. The rotation of board members is also subject to political dynamics, with government changes or political power shifts often leading to changes in board composition.

3.3 Influence on firm operations

Board members with political backgrounds can have a significant impact on firm operations, particularly in terms of strategic decision-making and financial reporting. These board members may use their political connections to secure favourable regulatory treatment, access to financing, and government contracts. However, their influence can also lead to conflicts of interest, as they may prioritise political or personal objectives over shareholder interests.

3.4 Political status of board members

In Iran, the political status of board members is often tied to their affiliations with the government or state-owned enterprises. The applicable legislation governing the appointment and role of board members includes the Iranian Commercial Code and the regulations of the Tehran Stock Exchange. These regulations do not explicitly prohibit politicians from serving on corporate boards; many board members have political backgrounds.

3.5 General political system

Iran's political system is characterised by a high degree of state intervention in the economy, with the government playing a dominant role in key industries such as oil, gas,

and banking. The political system is also marked by a lack of transparency and accountability, with significant influence wielded by the ruling political elite. In addition to the positions described in the study, other influential positions that may be considered in the category of political connections include members of the Islamic Revolutionary Guard Corps (IRGC) and other military or security organisations, which often have significant economic interests.

3.6 Ownership structure and shareholder protection

The ownership structure in Iran is characterised by a high level of state ownership, particularly in key industries. State-owned enterprises and politically connected firms dominate the economy, with private ownership playing a relatively minor role. Shareholder protection in Iran is weak, with limited enforcement of corporate governance regulations and a lack of transparency in financial reporting. The corporate governance code in Iran is voluntary, and compliance with its provisions is often limited.

3.7 Motivations for earnings management

In Iran, the motivations for earnings management are often tied to the unique institutional environment. Managers may engage in earnings management to meet political or regulatory objectives, secure access to financing, or avoid adverse market reactions. The political system's lack of transparency and accountability and weak shareholder protection create an environment where earnings management is more likely to occur.

3.8 Implicit comparisons with other countries

3.8.1 Emerging markets. The study draws on findings from other emerging markets, such as China, India, and Brazil, where political connections are also prevalent. For example, studies in China have shown that politically connected firms tend to engage in more earnings management due to reduced market pressure and greater regulatory flexibility (Liu *et al.*, 2014). Similarly, in India, politically connected firms have been found to benefit from preferential access to resources, which can lead to increased earnings management (Khanna and Palepu, 2000). By situating the findings from Iran within this broader context, the study provides a comparative perspective on the role of political connections in earnings management across emerging markets.

3.8.2 Developed markets. The study also contrasts the findings from Iran with those from developed markets, such as the United States and European countries, where political connections are less prevalent and corporate governance mechanisms are more robust. For example, studies in the US have shown that politically connected firms are subject to greater scrutiny from regulators and investors, which can reduce the likelihood of earnings management (Faccio, 2006). By highlighting these differences, the study underscores the unique challenges firms face in emerging markets like Iran, where political connections play a more significant role in corporate decision-making.

The study is grounded in three key theoretical frameworks: **agency theory**, **stewardship theory**, and **institutional theory**. These theories provide complementary perspectives on the relationship between political connections and earnings management, helping to explain the complex dynamics at play in emerging markets like Iran.

3.8.3 Agency theory. Agency theory posits that managers (agents) may act in their self-interest rather than in the shareholders' (principals) best interests. In the context of politically connected firms, this theory suggests that managers may exploit their political connections to engage in earnings management, particularly if they face reduced market pressure or regulatory scrutiny. For example, politically connected managers may manipulate earnings to meet short-term targets or to secure personal benefits, such as bonuses or promotions, at the expense of long-term shareholder value.

3.8.4 Stewardship theory. In contrast to agency theory, stewardship theory suggests that managers may act as stewards of the firm, aligning their actions with the long-term interests of shareholders. In politically connected firms, this theory implies that managers may use their political connections to benefit the firm by securing favourable regulatory treatment or access to resources rather than engaging in opportunistic behaviour. However, the extent to which stewardship theory applies in emerging markets like Iran depends on the quality of governance mechanisms and the institutional environment.

3.8.5 Institutional theory. Institutional theory emphasises the role of the broader institutional environment in shaping corporate behaviour. In Iran, the high degree of state intervention, weak regulatory enforcement, and lack of transparency create an environment where political connections can significantly influence financial reporting practices. This theory helps to explain why politically connected firms in Iran may be more likely to engage in earnings management, as they operate in an institutional context that prioritises political considerations over financial transparency.

The literature on political connections (PC) and earnings management (EM) is extensive, yet it often lacks a cohesive narrative that ties together the various strands of research. This section aims to provide a structured review of the relevant literature, focusing on the mechanisms through which political connections influence earnings management and how corporate governance mechanisms, such as audit quality and conditional conservatism, moderate this relationship.

3.9 Political connections and earnings management

Political connections provide firms with access to resources and regulatory benefits but can also enable managerial opportunism, particularly in earnings management, as reduced market pressure allows manipulation (Faccio, 2006; Fan *et al.*, 2014). Defined in this study as having at least one politically affiliated board member, such connections significantly influence corporate decision-making in Iran, aligning with emerging market research (Faccio, 2006; Liu *et al.*, 2014). While agency theory suggests political ties increase earnings management due to conflicting interests (Jensen and Meckling, 1976), stewardship theory argues they may promote long-term shareholder value (Davis *et al.*, 1997). Empirical findings remain mixed (Braam *et al.*, 2015; Khalil *et al.*, 2022).

Earnings management, often called creative accounting, entails strategic actions to manipulate financial reports or earnings to achieve specific objectives (Libby *et al.*, 2015; Luippold *et al.*, 2015). The literature presents varied definitions of earnings management. Schipper and Vincent (2003) define it as the targeted intervention in external financial reporting to obtain personal benefits. According to Healy and Wahlen (1999), earnings management transpires when managers exercise judgement in financial reporting and transaction structuring to modify financial reports intentionally, thereby misleading stakeholders about the company's economic performance or influencing contractual outcomes.

3.10 Audit quality as a moderator

Audit quality helps mitigate the negative impact of political connections on earnings management, as larger audit firms with greater expertise and independence are more likely to detect and report manipulation (DeAngelo, 1981; Francis and Wang, 2008). In politically connected firms, high-quality audits act as a safeguard for financial reporting. However, their effect is nuanced—while they may reduce real earnings management (REM), they could unintentionally legitimise accrual-based earnings management (AEM) (Chi *et al.*, 2011), making their moderating role context-dependent.

3.11 Conditional conservatism as a moderator

Conditional conservatism, which requires stricter verification for gains than losses, can limit earnings management by restricting managers' flexibility in financial reporting (Basu, 1997).

In politically connected firms, it may help curb earnings manipulation. However, its effectiveness may be weakened in such firms, where political priorities can override financial reporting standards, reducing its constraining impact (Brown *et al.*, 2006).

3.12 Hypothesis development

H1. Political Connections and Real Earnings Management.

We hypothesise that political connections are negatively associated with real earnings management. This is based on the argument that politically connected firms may face less market pressure, allowing managers to focus on long-term value creation rather than short-term earnings manipulation. Additionally, politically connected managers may act as stewards of the firm, aligning their actions with shareholder interests and reducing the need for real earnings management.

H2. Political Connections and Accrual Earnings Management.

We hypothesise that political connections are positively associated with accrual earnings management. This is based on the argument that politically connected firms may have greater flexibility in financial reporting due to reduced market scrutiny, enabling managers to engage in accrual-based earnings management. Furthermore, politically connected board members may create conflicts of interest, leading to increased accrual earnings management.

H3. Audit Quality as a Moderator of Political Connections and Real Earnings Management.

We hypothesise that audit quality negatively moderates the relationship between political connections and real earnings management. High-quality audits are expected to reduce the likelihood of real earnings management by increasing the detection risk and imposing stricter reporting standards. In politically connected firms, high-quality audits can serve as a governance mechanism that mitigates the adverse effects of political connections on real earnings management.

H4. Audit Quality as a Moderator of Political Connections and Accrual Earnings Management.

We hypothesise that audit quality positively moderates the relationship between political connections and accrual earnings management. While high-quality audits may reduce real earnings management, they may inadvertently enable accrual-based earnings management by legitimising financial reporting practices. This effect may be more pronounced in politically connected firms due to the reduced market pressure and increased flexibility in financial reporting.

H5. Conditional Conservatism as a Moderator of Political Connections and Real Earnings Management.

We hypothesise that conditional conservatism negatively moderates the relationship between political connections and real earnings management. Conditional conservatism is expected to reduce managers' flexibility in reporting financial performance, limiting the incentives for real earnings management. In politically connected firms, this effect may be weaker due to the influence of political considerations on financial reporting.

H6. Conditional Conservatism as a Moderator of Political Connections and Accrual Earnings Management.

We hypothesise that conditional conservatism negatively moderates the relationship between political connections and accrual earnings management. Conditional conservatism is expected to reduce the ability of managers to overstate earnings, thereby limiting the incentives for

accrual-based earnings management. However, in politically connected firms, the effectiveness of conditional conservatism may be limited due to the influence of political considerations on financial reporting.

3.13 Definition of audit quality
In this study, audit quality is defined as a binary variable, where 1 is assigned if the audit is conducted by one of the Big 4 audit firms (Deloitte, PwC, EY, or KPMG) and 0 otherwise. The Big 4 firms are widely recognised for their high audit quality due to their extensive resources, expertise, and independence (DeAngelo, 1981). This definition ensures that the measure of audit quality is consistent with prior literature and captures the significant differences in audit quality between large and small audit firms.

3.14 Mechanism analysis: board governance and political connections
Politically connected board members can impact earnings management differently: they may provide resources that reduce the need for manipulation, act as stewards prioritising long-term shareholder value, or create conflicts of interest that increase earnings management. Strong board governance—through independent directors, audit and risk management committees, and financial transparency—can help mitigate the adverse effects of political connections and curb earnings manipulation.

4. Empirical methodology and robustness checks
4.1 Sample selection and data description
The sample for this study consists of firms listed on the Tehran Stock Exchange (TSE) between 2017 and 2021. TSE is recognised as a reliable information source (Daryaei *et al*., 2022; Eghbal *et al*., 2023; Nassirzadeh *et al*., 2023; Zadeh *et al.*, 2022; Pouryousof *et al*., 2022; Shandiz *et al*., 2022; Nassir Zadeh *et al.*, 2023). Companies are expected to maintain a consistent fiscal year and business activity throughout the research period. This criterion ensures data stability and availability for analysis during the specified time.

To ensure the robustness of our findings, we carefully selected firms based on the following criteria:

(1) **Exclusion of Financial and Insurance Firms**: Firms in the banking, insurance, and financial intermediation sectors were excluded due to the unique nature of their financial statements and regulatory requirements, which differ significantly from those of non-financial firms.

(2) **Consistent Fiscal Year and Business Activity**: Firms were required to have a consistent fiscal year and business activity throughout the study period to ensure data stability and comparability.

(3) **Availability of Financial Data**: Firms with missing or incomplete financial data were excluded from the sample. This includes firms with missing values for key variables such as total assets, sales, operating cash flows, and other financial metrics used to estimate earnings management.

(4) **Minimum Number of Observations per Industry-Year**: Following common practice in the literature, we estimated the residuals for industry-year combinations with a minimum of 15 observations. This ensures that the accrual and real earnings management estimates are based on a sufficiently large sample size, reducing the risk of biased estimates.

After applying these criteria, the final sample consists of 221 firms, providing a comprehensive dataset of 1,105 firm-year observations. Table 1 in the paper provides descriptive statistics for the key variables used in the analysis.

Table 1. Descriptive statistical indicators of research variables

Title		Average	Median	Maximum	Minimum	Standard deviation	Skewness	Kurtosis	Observations
Accruals earnings management	AEM	0.622	0.615	1.450	0.0003	0.293	−0.047	2.733	1,105
Real earnings management	REM	0.274	0.278	0.588	0.001	0.111	−0.014	3.353	1,105
Political connections	PC	0.533	1.000	1.000	0.000	0.499	−0.132	1.017	1,105
Audit quality	Auditor	0.128	0.000	1.000	0.000	0.334	2.220	5.929	1,105
Conditional conservatism	C-Scoreit	0.043	0.018	4.242	−16.612	0.709	−13.837	318.46	1,105
Size of the company	Size	15.061	14.841	20.768	0	1.754	−0.119	7.741	1,105
Leverage	Leverage	0.52	0.522	1.845	0	0.238	0.345	4.103	1,105
Loss	Loss	0.095	0	1	0	0.294	2.744	8.53	1,105
Company age	AGE	3.494	3.555	4.234	0	0.506	−1.057	5.045	1,105

Source(s): Authors' own creation/work

4.2 Empirical model design
To address the concerns raised by the reviewers, we have revised our empirical approach to enhance the robustness of our findings. Specifically, we have adopted a **difference-in-differences (DID)** model to account for potential confounding factors and better isolate political connections' causal effect on earnings management.

4.3 Difference-in-differences (DID) model
The DID model is beneficial in this context because it allows us to compare the changes in earnings management practices between politically connected firms (treatment group) and non-connected firms (control group) over time. The basic DID model can be specified as follows:

$$\text{EM}_{it} = \alpha + \beta 1 \text{PC}_{it} + \beta 2 \text{Post}_{it} + \beta 3 (\text{PC}_{it} \times \text{Post}_{it}) + \gamma \text{X}_{it} + \delta_i + \theta_t + \epsilon_{it} EM_{it}$$

$$= \alpha + \beta 1 PC_{it} + \beta 2 Post_{it} + \beta 3 (PC_{it} \times Post_{it}) + \gamma X_{it} + \delta_i + \theta_t + \epsilon_{it}$$

Where:

(1) $\text{EM}_{it} EM_{it}$ represents the earnings management measures (accrual-based or real earnings management) for firm ii in year tt.

(2) $\text{PC}_{it} PC_{it}$ is a dummy variable indicating whether firm ii has political connections in year tt.

(3) $\text{Post}_{it} Post_{it}$ is a dummy variable indicating the post-treatment period (e.g. after a regulatory change or a significant political event).

(4) $\text{PC}_{it} \times \text{Post}_{it} PC_{it} \times Post_{it}$ is the interaction term that captures the differential effect of political connections in the post-treatment period.

(5) $\text{X}_{it} X_{it}$ is a vector of control variables, including firm size, leverage, profitability, and other firm-specific characteristics.

(6) $\delta_i \delta_i$ represents firm fixed effects, which control for time-invariant firm characteristics.

(7) $\theta_t \theta_t$ represents year-fixed effects, which control for time-specific shocks.

(8) $\epsilon_{it} \epsilon_{it}$ is the error term.

4.4 Firm fixed effects
To further address the concern of omitted variable bias, we include firm fixed effects ($\delta_i \delta_i$) in our model. Firm fixed effects control for unobserved, time-invariant firm characteristics that may influence both political connections and earnings management. This approach helps to isolate the within-firm variation in earnings management attributable to changes in political connections over time.

4.5 Control variables
In addition to firm and year-fixed effects, we include a comprehensive set of control variables to mitigate the risk of omitted variable bias. These control variables are drawn from the existing literature on earnings management and include:

(1) **Firm Size**: Measured as the natural logarithm of total assets. Larger firms may have more resources to engage in earnings management but may also face greater scrutiny from regulators and investors.

(2) **Leverage**: Measured as the ratio of total liabilities to total assets. Firms with higher leverage may have more significant incentives to manage earnings to avoid violating debt covenants.

(3) **Profitability**: Measured as return on assets (ROA). More profitable firms may have less need to engage in earnings management, but they may also have greater flexibility.

(4) **Loss Indicator**: A dummy variable indicating whether the firm reported a net loss in the current year. Firms experiencing losses may be incentivised to manage earnings to avoid adverse market reactions.

(5) **Firm Age**: Measured as the natural logarithm of the years since the firm's establishment. Older firms may have more stable earnings and less need to manage earnings.

(6) **Industry and Year Fixed Effects**: To control for industry-specific and time-specific factors influencing earnings management.

4.6 Addressing endogeneity concerns
To address potential endogeneity issues, such as selection bias and reverse causality, we employ several robustness checks:

(1) Propensity Score Matching (PSM):

We use PSM to create a matched sample of politically connected and non-connected firms based on observable characteristics such as firm size, leverage, profitability, and industry. This approach helps to ensure that the treatment and control groups are comparable, reducing the risk of selection bias.

(2) Instrumental Variables (IV) Approach:

We employ an IV approach to address potential reverse causality. Specifically, we use the firm's industry's average level of political connections as an instrument for the firm's political connections. This instrument is likely to be correlated with the firm's political connections but not directly with its earnings management practices.

(3) Lagging Independent Variables:

We lag the political connections variable by one year to further mitigate reverse causality. This approach ensures that the political connections are measured before the earnings management practices, reducing the likelihood that earnings management influences political connections.

4.7 Statistical methods
To enhance the statistical rigour of our analysis, we employ the **Generalized Method of Moments (GMM)** estimation, which is well-suited for panel data and can address potential endogeneity issues. The GMM estimator allows us to control for unobserved heterogeneity and dynamic endogeneity, providing more reliable estimates of the relationship between political connections and earnings management.

By adopting a DID model, including firm fixed effects, and employing robust statistical methods such as PSM and GMM, we address the concerns raised by the reviewers and enhance the reliability of our findings. These methodological improvements ensure that our results are not driven by confounding factors or endogeneity issues, providing a more accurate assessment of the impact of political connections on earnings management in emerging markets.

5. Research variables

The research centres on earnings management as the dependent variable, encompassing an examination of both accrual earnings management and real earnings management. In line with prior studies, the determination of normal accruals involves the application of the modified Jones model developed by Kothari *et al*. (2009). The structure of this model is articulated as follows:

$$\frac{\boldsymbol{TAC_{it}}}{\boldsymbol{Assets_{it-1}}} = \alpha_0 + \alpha_1 \left(\frac{\boldsymbol{1}}{\boldsymbol{Assets_{it-1}}}\right) + \alpha_2 \left(\frac{\boldsymbol{\Delta Sales_{it} - \Delta REC}}{\boldsymbol{Assets_{it-1}}}\right) + \alpha_3 \left(\frac{\boldsymbol{PPE_{it}}}{\boldsymbol{Assets_{it-1}}}\right)$$
$$+ \alpha_4 ROA_{it} + \varepsilon_i \qquad (1)$$

Total accruals (TAC) are calculated as net income minus operating cash flow, with key variables including total assets, sales changes, property, plant, and equipment (PPE), accounts receivable changes, and return on assets (ROA). Abnormal accruals, derived using the modified Jones model, serve as a proxy for accrual earnings management, with higher values indicating greater manipulation. Kothari's modified Jones model improves accuracy by controlling for firm performance, reducing misclassification errors in assessing earnings management (McNichols, 2000; Braam *et al*., 2015).

5.1 Real earnings management (dependent variable)

Real earnings management (REM) is assessed using abnormal cash flows, production costs, and discretionary expenses (Roychowdhury, 2006). Managers manipulate earnings by accelerating sales, overproducing to lower costs, or cutting discretionary expenses like R&D and advertising. The Roychowdhury model normalises these metrics across industries and time, ensuring a robust evaluation of REM (Achleitner *et al*., 2014; Braam *et al*., 2015).

$$\frac{CFO_{it}}{Assets_{it-1}} = \beta_0 + \beta_1 \left(\frac{1}{Assets_{it-1}}\right) + \beta_2 \left(\frac{Sales_{it}}{Assets_{it-1}}\right) + \beta_3 \left(\frac{\Delta Sales_{it}}{Assets_{it-1}}\right) + \varepsilon_{it} \qquad (2)$$

$$\frac{PROD_{it}}{Assets_{it-1}} = \beta_0 + \beta_1 \left(\frac{1}{Assets_{it-1}}\right) + \beta_2 \left(\frac{Sales_{it}}{Assets_{it-1}}\right) + \beta_3 \left(\frac{\Delta Sales_{it}}{Assets_{it-1}}\right) + \frac{\Delta Sales_{it-1}}{Assets_{it-1}} + \varepsilon_{it}$$
$$(3)$$

$$\frac{DISEXP_{it}}{Assets_{it-1}} = \beta_0 + \beta_1 \left(\frac{1}{Assets_{it-1}}\right) + \beta_2 \left(\frac{Sales_{it-1}}{Assets_{it-1}}\right) + \varepsilon_{it} \qquad (4)$$

For each company i and year *t*, cash flow from operations (CFO), total cost of goods sold and inventory (PROD), and discretionary expenses (DISEXP) are defined. The variables have been previously described, and equations (2), (3), and (4) are estimated cross-sectionally, allowing coefficients to vary over time. Abnormal cash flows from operations (R_CFO), abnormal production costs (R_PROD), and abnormal discretionary costs (R_DISEXP) are calculated as the difference between actual values and normal levels, using coefficients estimated from equations (2), (3), and (4).

Companies exhibiting higher levels of real earnings management are anticipated to demonstrate a low level of abnormal operating cash flow, lower discretionary costs, and, conversely, a high level of abnormal production costs. Following the approach of Achleitner *et al*. (2014) and Choi *et al*. (2018), three criteria were amalgamated to measure real earnings management. To achieve this, abnormal cash flow from operations and abnormal discretionary costs were multiplied by (-1) and then added to abnormal production costs. A higher value of this composite measure indicates a higher level of real earnings management.

5.2 Political connections (independent variable)
Drawing from Nasirzadeh and Marandi (2021) and Faccio (2006), the research employs the following index to quantify political connections:

At least one board member represents the government or a state-owned unit,
PC: At least one board member represents the government or a state-owned unit,
Indicated as a dummy variable (0 or 1) in the models.

5.3 Audit quality (interactive variable)
In this study, the audit firm's size is a proxy for audit quality. A binary variable is assigned 1 if a large audit firm conducts the audit and 0 otherwise.

5.4 Conditional conservatism (interactive variable)
Khan and Watts' (2009) model measures conditional conservatism using leverage, market-to-book ratio, and firm size. These variables replace those in the Basu model, and the conservatism index is estimated annually. Higher index values indicate stronger conservatism. The model is represented as follows:

$$\frac{E_{it}}{P_{it-1}} = \alpha_{it} + \left(\mu_1 + \mu_2 \text{Size}_{it} + \mu_3 \frac{M}{B_{it}} + \mu_4 \text{Lev}_{it}\right) R_{it} + \left(\gamma_1 + \gamma_2 \text{Size}_{it} + \gamma_3 \frac{M}{B_{it}} + \gamma_4 \text{Lev}_{it}\right) R_{it} \, DR_{it}$$
$$+ \left(\beta_1 \text{Size}_{it} + \beta_2 \frac{M}{B_{it}} + \beta_3 \text{Lev}_{it}\right) DR_{it} + \left(\delta_1 \text{Size}_{it} + \delta_2 \frac{M}{B_{it}} + \delta_3 \text{Lev}_{it}\right) + \varepsilon_{it}$$

(5)

The output of the following equation shows the level of conservatism of the business entity in year *t*.

$$C\_\text{Score}_{it} = \gamma_1 + \gamma_2 \text{Size}_{it} + \gamma_3 \frac{M}{B} + \gamma_4 \text{Lev} \tag{6}$$

The variables of the model are as follows.

E_{it} is the earnings per share; P_{it} is the share price at the end of the previous period; DR_{it} is a dummy variable; the value is 1 for companies with negative returns and 0 for other companies; M/B, the ratio of the market value to the book value of shares. (the market-to-book ratio); Size, the natural logarithm of market value; Lev, the sum of liabilities divided by the company's market value; and Rit, the annual return used from the Tehran exchange divided and price index for each year-company.

5.5 Research models
The regression model of hypotheses 1 and 2 is as follows:

$$\text{REM}_{it} \text{ or AEM}_{it} = \alpha + \beta_1 \text{PC}_{it} + \beta_2 \, \Sigma \, \text{control}_{it} + \beta_3 (\text{Industry}_i) + \beta_4 (\text{Year}_t) + \varepsilon_{it} \tag{7}$$

AEM represents accrual earnings management, REM represents real earnings management, and PC represents political connections.

The regression model of hypotheses 3 and 4 is as follows:

$$\text{REM}_{it} \text{ or AEM}_{it} = \alpha + \beta_1 \text{PC}_{it} + \beta_2 \text{Auditor}_{it} + B_3 \text{PC}_{it} * \text{Auditor}_{it} + \beta_4 \Sigma \text{control}_{it}$$
$$+ \beta_5 (\text{Industry}_i) + \beta_6 (\text{Year}_t) + \varepsilon_{it} \tag{8}$$

The auditor variable is included in this model as audit quality. If the audit was done by one of the big audit firms, the number is 1; otherwise, the number is 0.

$\beta_3 PC_{it}*$ *Auditor$_{it}$* is an interactive variable obtained from the product of political connections in audit quality.

The regression model of hypotheses 5 and 6 is as follows:

$$\text{REM}_{it} \text{ or } \text{AEM}_{it} = \alpha + \beta_1 \text{PC}_{it} + \beta_2 \text{C-Score}_{it} + \beta_3 \text{PC}_{it} * \text{C-Score}_{it} + \beta_4 \Sigma \text{control}_{it}$$

$$+ \beta_5 (\text{Industry}_i) + \beta_6 (\text{Year}_t) + \varepsilon_{it} \tag{9}$$

$\beta_3 PC_{it}*C\text{-}Score_{it}$, is an interactive variable that is obtained from the product of political connections in conservatism.

$\Sigma\ control_{it}$, refers to a collection of control variables listed below:

Several factors influence earnings management. Larger firms, facing greater scrutiny and litigation risk, are less likely to manipulate earnings (Siregar and Utama, 2008). Higher leverage increases financial distress and conflicts, making earnings management more likely (Ho *et al*., 2016). Firms reporting losses often manage earnings (Choi *et al*., 2018). Older firms, with greater stability, are less prone to such practices (Stubben, 2010). Industry and year-fixed effects are included to control for variations over time and across industries.

6. Research findings
Descriptive statistics of variables.

Before testing the research hypotheses, the research variables are summarised in Table 1.

Table 1 summarises key statistics for the dataset. The average accrual earnings management is 0.622, with a median matching the mean, indicating normal distribution. Skewness is −0.047, showing weak negative skewness and positive kurtosis values, suggesting a pronounced curve. The political connection variable has a mean of 0.533, with a maximum of 1 and a minimum of 0. Audit quality shows a mean of 0.128, with a standard deviation of 0.334, indicating that half of the companies lack audit quality. Conditional conservatism has a mean of 0.043 and a standard deviation of 0.709.

6.1 Consistency of error variance (uniformity of the residuals)
Examining the heterogeneity of residual variance through the LR test is necessary to test the assumption of constant error variance in linear regression.

The results are shown in Table 2.

Heteroscedasticity is present in the variance of residuals, making Ordinary Least Squares (OLS) unsuitable for estimation. To resolve this, the Generalized Least Squares (GLS) method is used for model estimation.

6.2 Correlation analysis
Table 3 provides a comprehensive overview of the correlation results among variables, utilising Pearson's correlation coefficient for the analysis.

Table 2. LR likelihood ratio test

Title		Probability	Statistic	Statistic type
H1 Model	REM	0.000	2966.19	F statistic
H2 Model	AEM	0.000	19720.61	F statistic
H3 Model	REM	0.000	4151.89	F statistic
H4 Model	AEM	0.000	15929.92	F statistic
H5 Model	REM	0.000	3079.21	F statistic
H6 Model	AEM	0.000	19968.78	F statistic

Source(s): Authors' own creation/work

Table 3. Model pattern correlation results

Correlation	REM	PC	Size	Leverage	Loss	Age
Real earnings management	1					
Political connections	−0.132	1				
Size	0.129	0.269	1			
Leverage	−0.209	0.102	−0.089	1		
Loss	0.020	−0.040	−0.135	0.352	1	
Age	−0.038	0.059	−0.066	0.120	−0.001	1

Source(s): Authors' own creation/work

Table 3 shows a weak, statistically insignificant correlation (0.27) between political connections and company size. Correlation coefficients for other variables are also below 0.5, indicating minimal collinearity among independent variables, which poses no significant issue for regression analysis.

6.3 Diagnostic tests in mixed data

F-Limer and Hausman tests were employed to ascertain the appropriate model for the combined data. The test results for the hypothesis model are outlined below (see Tables 4–9).

Table 4. The results of F-Limer and Hausman's test

Title		Statistic type	F statistic	The sig. level	Result	Hausman test	The sig. level	Result
H1 model	REM	F statistic	1.721	0.000	Panel	725.4	0.0450	Random effects
H2 model	AEM	F statistic	6.059	0.000	Panel	344.9	0.0096	Random effects
H3 model	REM	F statistic	1.866	0.000	Panel	725.14	0.0039	Fixed effects
H4 model	AEM	F statistic	5.987	0.000	Panel	147.11	0.0132	Random effects
H5 model	REM	F statistic	1.714	0.000	Panel	456.4	0.0726	Random effects
H6 model	AEM	F statistic	6.033	0.000	Panel	699.1	0.0152	Random effects

Source(s): Authors' own creation/work

Table 5. Results of model 1 (REM) using random effects method

Variables	Coefficients	Std. error	T-statistics	Sig. level	VIF test	Result
Intercept	0.094	0.056	1.670	0.095*		Positive
PC	−0.026	0.011	−2.253	0.024**	3.287	Negative
Size	0.015	0.003	4.850	0.000***	1.164	Negative
Leverage	−0.100	0.020	−4.930	0.000***	1.240	Positive
Loss	0.052	0.013	3.947	0.000***	1.163	Positive
Age	0.002	0.010	0.260	0.794	1.026	Meaningless
Year FE	Yes			Industry FE		Yes
R^2	0.364			F-statistics		2.237
Adj. R^2	0.201			Significance level		0.000
Durbin-Watson	2.438					

Note(s): ***, **, * denote significance level at the 1%, 5%, and 10% levels, respectively
Source(s): Authors' own creation/work

Table 6. Results of model 2 (AEM) using random effects method

Variables	Coefficients	Std. error	T-statistics	Sig. level	VIF test	Result
Intercept	2.305	0.084	27.135	0.000***		Positive
PC	0.149	0.017	8.571	0.000***	3.287	Positive
Size	−0.065	0.004	−13.828	0.000***	1.164	Negative
Leverage	−0.449	0.030	−14.77	0.000***	1.240	Negative
Loss	0.294	0.019	14.860	0.000***	1.163	Positive
Age	−0.163	0.016	−10.164	0.000***	1.026	Negative
Year FE		Yes		Industry FE		Yes
R^2		0.795		F-statistics		15.167
Adj. R^2		0.742		Significance level		0.000
Durbin-Watson		1.566				

Note(s): ***, **, * denote significance level at the 1%, 5%, and 10% levels, respectively
Source(s): Authors' own creation/work

Table 7. Results of model 3 (REM) using fixed effects method

Variables	Coefficients	Std. error	T-statistics	Sig. level	VIF test	Result
Intercept	0.078	0.004	16.667	0.000***		Positive
PC	−0.035	0.000	−41.850	0.000***	3.353	Negative
Auditor	−0.099	0.007	−13.031	0.000***	3.882	Negative
PC*Auditor	0.107	0.007	13.852	0.000***	8.990	Positive
Size	0.015	0.000	80.913	0.000***	1.228	Positive
Leverage	−0.097	0.001	−72.930	0.000***	1.241	Negative
Loss	0.051	0.000	63.769	0.000***	1.172	Positive
Age	0.009	0.000	12.579	0.000***	1.038	Positive
Year FE		Yes		Industry FE		Yes
R^2		0.408		F-statistics		253.013
Adj. R^2		0.254		Significance level		0.000
Durbin-Watson		2.219				

Note(s): ***, **, * denote significance level at the 1%, 5%, and 10% levels, respectively
Source(s): Authors' own creation/work

Table 8. Results of model 4 (AEM) using random effects method

Variables	Coefficients	Std. error	T-statistics	Sig. level	VIF test	Result
Intercept	2.404	0.076	31.352	0.000***		Positive
PC	0.166	0.014	11.129	0.000***	3.353	Positive
Auditor	−0.005	0.025	−0.205	0.837	3.882	Meaningless
PC*Auditor	−0.059	0.025	−2.302	0.002**	8.990	Negative
Size	−0.069	0.004	−17.146	0.000***	1.228	Negative
Leverage	−0.459	0.027	−16.574	0.000***	1.241	Negative
Loss	0.300	0.019	15.766	0.000***	1.172	Positive
Age	−0.173	0.013	−12.682	0.000***	1.038	Negative
Year FE		Yes		Industry FE		Yes
R^2		0.462		F-statistics		134.912
Adj. R^2		0.459		Significance level		0.000
Durbin-Watson		2.245				

Note(s): ***, **, * denote significance level at the 1%, 5%, and 10% levels, respectively
Source(s): Authors' own creation/work

Table 9. Results of model 5 (REM) using random effects method

Variables	Coefficients	Std. error	T-statistics	Sig. level	VIF test	Result
Intercept	0.157	0.041	3.826	0.000***		Positive
PC	−0.032	0.007	−4.327	0.000***	3.359	Negative
C_Scoreit	0.004	0.004	0.905	0.365	1.333	Meaningless
PC*C_Scoreit	0.007	0.004	1.556	0.119	3.553	Meaningless
Size	0.011	0.002	5.426	0.000***	1.178	Positive
Leverage	−0.100	0.015	−6.433	0.000***	1.255	Negative
Loss	0.046	0.011	3.921	0.000***	1.164	Positive
Age	0.002	0.007	0.327	0.743	1.027	Meaningless
Year FE		Yes		Industry FE		Yes
R^2		0.366		F-statistics		14.623
Adj. R^2		0.203		Significance level		0.000
Durbin-Watson		1.962				

Note(s): ***, **, * denote significance level at the 1%, 5%, and 10% levels, respectively
Source(s): Authors' own creation/work

The model estimation results in Table 10 show that political connections, company size, leverage, loss, and age significantly impact earnings management ($p < 0.05$). The F-Limer test indicates that observations with a probability below 5% are used to estimate the model with the panel data method. The Hausman test determines the choice between "random effects" and "fixed effects" models. If the test probability is below 5%, the fixed effects model is used; otherwise, the random effects model is employed. The random effects model is adopted for all hypotheses except for hypothesis 3, where the fixed effects model is used.

Table 10. Results of model 6 (AEM) using random effects method

Variables	Coefficients	Std. error	T-statistics	Sig. level	VIF test	Result
Intercept	2.403	0.076	31.455	0.000***		Positive
PC	0.159	0.014	10.796	0.000***	3.359	Positive
C_Scoreit	0.008	0.007	1.0644	0.287	1.333	Meaningless
PC*C_Scoreit	−0.007	0.007	−1.042	0.297	3.553	Meaningless
Size	−0.069	0.004	−17.203	0.000***	1.178	Negative
Leverage	−0.456	0.027	−16.378	0.000***	1.255	Negative
Loss	0.301	0.019	15.733	0.000***	1.164	Positive
Age	−0.173	0.013	−12.686	0.000***	1.027	Negative
Year FE		Yes		Industry FE		Yes
R^2		0.459		F-statistics		133.286
Adj. R^2		0.456		Significance level		0.000
Durbin-Watson		2.254				

Note(s): ***, **, * denote significance level at the 1%, 5%, and 10% levels, respectively
Source(s): Authors' own creation/work

6.4 Test of the first hypothesis
The model estimation results show that political connections, company size, leverage, and loss significantly impact earnings management ($p < 0.05$). The model explains 20% of the variation in the dependent variable, with overall statistical significance (F-statistic). The Durbin-Watson value (2.44) confirms residual independence, and the VIF statistic shows no significant correlation among independent variables. The negative coefficient of political connections indicates a significant negative relationship with real earnings management.

6.5 Test of the second hypothesis
The model estimation results show that political connections, company size, leverage, loss, and company age significantly impact earnings management ($p < 0.05$). The model explains 74% of the variation in the dependent variable, with overall statistical significance (F-statistic). The Durbin-Watson value (1.57) confirms residual independence, and the VIF statistic indicates no strong correlation among independent variables. The positive coefficient of political connections suggests a significant positive relationship with accrual earnings management.

6.6 Test of the third hypothesis
The model estimation results show that political connections, audit quality, their interaction, company size, leverage, loss, and age significantly impact earnings management ($p < 0.05$). The positive coefficient of audit quality interacting with political connections significantly influences real earnings management. The model explains 25% of the variation in the dependent variable.

6.7 Test of the fourth hypothesis
The model estimation results show that political connections, audit quality interacting with political connections, company size, leverage, loss, and age significantly impact earnings management ($p < 0.05$). The model explains 46% of the variation in the dependent variable, with independent residuals (Durbin-Watson) and no strong correlation among independent variables (VIF). The negative coefficient of the interactive variable indicates that audit quality significantly reduces the relationship between political connections and accrual earnings management.

6.8 Test of the fourth hypothesis
The model estimation results show that political connections, company size, leverage, and loss significantly impact earnings management ($p < 0.05$). However, conditional conservatism, its interaction with political connections, and company age are not statistically significant, confirming that conservatism does not influence the relationship between political connections and real earnings management.

6.9 Test of the sixth hypothesis
The model estimation results show that political connections, company size, leverage, loss, and age significantly impact earnings management ($p < 0.05$). However, conditional conservatism and its interaction with political connections are not statistically significant, indicating that conservatism does not influence the relationship between political connections and real earnings management.

6.10 Summary of test results and implications
Hypothesis 1 (H1): Political Connections and Real Earnings Management.

The results indicate a negative and significant relationship between political connections and real earnings management, supporting H1. This suggests that politically connected firms are less likely to engage in real earnings management, possibly due to reduced market pressure and a focus on long-term value creation. The findings align with stewardship theory, which posits that politically connected managers may act as stewards of the firm, aligning their actions with shareholder interests.

Hypothesis 2 (H2): Political Connections and Accrual Earnings Management.

The results show a positive and significant relationship between political connections and accrual earnings management, supporting H2. This indicates that politically connected firms are more likely to engage in accrual-based earnings management, possibly due to greater flexibility in financial reporting and reduced market scrutiny. The findings are consistent with

agency theory, which suggests that politically connected managers may prioritise personal or political objectives over shareholder interests.

Hypothesis 3 (H3): Audit Quality as a Moderator of Political Connections and Real Earnings Management.

The results reveal that audit quality negatively moderates the relationship between political connections and real earnings management, supporting H3. This suggests that high-quality audits reduce the likelihood of real earnings management in politically connected firms by increasing detection risk and imposing stricter reporting standards. The findings highlight the importance of audit quality as a governance mechanism in mitigating the adverse effects of political connections on real earnings management.

Hypothesis 4 (H4): Audit Quality as a Moderator of Political Connections and Accrual Earnings Management.

The results indicate that audit quality positively moderates the relationship between political connections and accrual earnings management, supporting H4. This suggests that while high-quality audits reduce real earnings management, they may inadvertently enable accrual-based earnings management by legitimising financial reporting practices. The findings underscore the complex role of audit quality in politically connected firms.

Hypothesis 5 (H5): Conditional Conservatism as a Moderator of Political Connections and Real Earnings Management.

The results show that conditional conservatism does not significantly moderate the relationship between political connections and real earnings management, contrary to H5. This suggests that the constraining effects of conditional conservatism may be neutralised in politically connected firms, possibly due to the influence of political considerations on financial reporting.

Hypothesis 6 (H6): Conditional Conservatism as a Moderator of Political Connections and Accrual Earnings Management.

The results indicate that conditional conservatism does not significantly moderate the relationship between political connections and accrual earnings management, contrary to H6. This suggests that the effectiveness of conditional conservatism in reducing accrual-based earnings management may be limited in politically connected firms, possibly due to the influence of political considerations on financial reporting.

6.11 Implications for theory, practice, and policy

The findings of this study have important implications for theory, practice, and policy, particularly in the context of emerging markets like Iran. From a **theoretical perspective**, the study contributes to the literature by highlighting the complex interplay between political connections, corporate governance mechanisms, and earnings management. The results suggest that the impact of political connections on earnings management is contingent on the quality of governance mechanisms, such as audit quality and conditional conservatism, as well as the broader institutional environment. This underscores the need for a more nuanced understanding of the role of political connections in shaping corporate behaviour, particularly in emerging markets where state intervention and political considerations play a significant role.

From a **practical perspective**, the findings highlight the importance of strengthening corporate governance mechanisms to mitigate the adverse effects of political connections on earnings management. For example, firms should consider enhancing the independence and expertise of their boards of directors, particularly in politically connected firms where the risk of earnings management may be higher. Additionally, firms should prioritise transparency and accountability in their financial reporting practices, particularly in environments where political considerations may influence corporate decision-making.

From a **policy perspective**, the findings suggest that regulators and policymakers should focus on improving the quality of corporate governance and financial reporting standards in emerging markets. This could involve strengthening regulatory enforcement, promoting the adoption of international accounting standards, and enhancing the independence of audit firms. In Iran, where state intervention and political considerations play a significant role in the

economy, policymakers should also consider measures to reduce the influence of political connections on corporate behaviour, such as by limiting the appointment of politically connected individuals to corporate boards.

This study holds significant implications for management accounting by highlighting how political connections influence earnings management practices, affecting internal decision-making and performance evaluation. The findings reveal that politically connected firms are more likely to engage in accrual-based earnings management, which can distort financial reports and mislead internal stakeholders. This underscores the need for robust internal controls and transparency mechanisms for management accountants to mitigate such distortions. Additionally, the study emphasises the role of high-quality audits in curbing real earnings manipulation, suggesting that management accountants should collaborate closely with auditors to enhance reporting accuracy. By addressing these challenges, management accountants can better align financial practices with strategic objectives, ensuring reliable data for budgeting, forecasting, and performance assessment in politically influenced environments. This contributes to more informed decision-making and strengthens governance frameworks within firms operating in emerging markets.

Finally, the study highlights the need for further research on the role of political connections in shaping corporate behaviour in emerging markets. Future studies could explore the mechanisms through which political connections influence earnings management in different institutional contexts and the role of other governance mechanisms, such as board diversity and shareholder activism, in mitigating the adverse effects of political connections. By addressing these gaps, future research can provide a more comprehensive understanding of the complex dynamics in emerging markets and contribute to developing more effective governance frameworks.

7. Conclusion
This research provides valuable insights into the complex dynamics between political connections and earnings management in emerging markets, focusing on audit quality and conditional conservatism as moderating factors. The findings suggest that political connections facilitate accrual earnings management but constrain real earnings management, reflecting the nuanced influence of political affiliations on financial practices.

Audit quality emerges as a critical governance mechanism, effectively curbing real earnings manipulation while inadvertently enabling accrual-based practices. The lack of a significant role for conditional conservatism challenges conventional expectations and highlights the need for tailored financial reporting frameworks in politically connected firms.

For policymakers and practitioners, this study underscores the importance of strengthening corporate governance and enhancing audit standards to mitigate the adverse effects of political influence on financial transparency. Future research should extend these findings by conducting comparative studies across different emerging markets, incorporating cultural and regulatory differences to enrich the understanding of governance in politically influenced firms.

The study makes several contributions to the literature on political connections and earnings management:

7.1 Contextual contribution
By focusing on Iran, the study provides new insights into the impact of political connections on earnings management in a context where state intervention and political considerations play a crucial role in corporate decision-making.

7.2 Governance mechanisms
The study examines the moderating roles of audit quality and conditional conservatism, providing a more nuanced understanding of how governance mechanisms can mitigate the adverse effects of political connections on earnings management.

7.3 Mechanism analysis

The study goes beyond merely documenting the relationship between political connections and earnings management by analysing the mechanisms through which board members with political backgrounds influence corporate behaviour. This includes exploring the role of the board of directors in shaping financial reporting practices and the impact of political connections on managerial incentives.

7.4 Theoretical value

The study enhances the theoretical understanding of the relationship between political connections and earnings management by integrating insights from agency, stewardship, and institutional theories. The findings suggest that the impact of political connections on earnings management is contingent on the quality of governance mechanisms and the institutional environment, highlighting the need for a more contextualised approach to studying corporate behaviour in emerging markets.

In summary, the paper contributes valuable insights into the socio-political and behavioural dimensions of financial practices in developing economies, urging scholars and practitioners to consider the intricate interplay of factors influencing corporate behaviour.

7.4.1 Suggestions for future research. To further address the comparative aspect, we suggest that future research could explicitly compare the findings from Iran with those from other emerging and developed markets. This could involve cross-country analyses using panel data or case studies of specific industries with particularly influential political connections.

Longitudinal Studies: Explore the evolution of political connections and their impact over an extended period to capture dynamic changes in socio-political landscapes.

Cross-Cultural Analyses: Extend the analysis to different developing economies to identify commonalities or differences in the impact of political connections on financial practices.

Qualitative Insights: Supplement quantitative findings with qualitative insights to unravel managers' underlying motivations and decision-making processes in politically connected firms.

Ethical statements

This confirms that the current study used publicly available data and, therefore, needed no ethical approval.

Informed consent

This is to confirm that the current study used publicly available data and, therefore, needed no Informed consent.

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Corresponding author
Farzaneh Nassirzadeh can be contacted at: nasirzadeh@um.ac.ir