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Research paper

The Effect of Integration of Coroprate Governance Mechanisms and Audit Quality in Earning Management: An Empirical Analysis of Listed Banks in Iraqi Stock Exchange

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Abstract

The aim of this study is to examine the effects of board of directors, audit committee and concentration ownership as corporate governance mechanisms on earning management. The study aims also to investigate the role of audit quality on the association between corporate governance and earning management of listed banks in Iraqi stock exchange for the year 2015. The number of meetings and directors are other factors to be examined. The size of audit committee members and the audit committee presence that are professionally certified are the factors to be considered in audit committee. In another word, the concentration of ownership included both managerial ownership, block shareholders and foreign ownership. The findings showed that external audit has effect on the fiveparameters considered under the effects of corporate governance on earning management. Therefore, the numbers of meetings, the audit committee knowledge, audit committee existence, managerial ownership and foreign ownership significantly have impact on earning management. Conversely, external audit has no impact on the association between block shareholder, size of the board of directors and earning management. In lieu of the study's outcome, corporate governance proves to be a huge impact on reducing earnings management while the intervention of audit quality equally contributes to the reduction of earnings management practices.

Keywords: *external audit, corporate governance, earnings management, banks, Iraq.*

1. Introduction

In the last two decades, there were witnesses of scandals surrounding corporate accounting across the East Asian, Europe and United States such as Xeros, HealthSouth, Enron, WorldCom and Tyco. These manipulative scandals in accounting have led to critical awareness that calls for investigations on financial report quality. In this manner, more credibility and transparency are achieved for protection over stakeholders and shareholders via the power of legislation or disclosure-related standards [39]. According to Goncharov , earnings management is the central issue of those scandals [15]. In financial economics researches on earning management become the main issue of numerous studies [23]. Notably, Ali Shah stated that earning management is receiving significant attention in the literatures of accounting and has been consistently a great concern to practitioner and regulators [1].
According to agency theory, the mechanisms of monitoring are meant to unite the motives of both shareholders and managers and reduce the bone of contention between them [22]. In addition, practices of fraudulent earning management produces less reliable accounting earnings which can never lead to positive financial performance of firms. By wrongful selection of treatments that protect the interests of the managers only and selection of inappropriate methods of accounting rather than methods that reflect the truthful financial position of the firm, earning management will probably minimize the quality of its application for investment decisions andearning reporting. Therefore, this can reduce the confidence of the investor in the financial report and obscure information that are meant to be known by the stakeholders [31].
In the early 1990s, corporate governance was first introduced; and since then, it has been widely employed till recent years especially among those who are working in regional, local and international organizations. The challenge is that there is no corporate governance law that enforces companies to comply effectively. However, these practices are considered or applied with different mechanisms from one company to another despite the existence of practices of governance on the Iraqi environment as presented by the Central Bank and Laws of banks. Meanwhile, a weak control system is part of the problems that are facing the implementation of these mechanisms since the systems are designed by the management of the companies. Thus, this can be replaced by some parts of the mechanisms of corporate governance and can be replaced by the involvement of the auditor. The work of the auditor must be of high quality in order to have an effective reduction in misleading earnings management practices. Hence, no study has examined the relationship between external audit quality as corporate governance mechanism on earning management in Iraq to the researcher's best knowledge.
Earnings management is one of the most serious problems facing an effective performance of companies [41]. Mismanagement of earnings misleads the users of the financial statement of the company [3]. This therefore results to decline in the confidence of the stakeholders to accept the credibility of the financial statement. This study aimed to demonstrate the integrative roles of quality of audit and corporate governance in an attempt to reduce earnings

management practices taking a group of banks listed in the Iraqi market of securities as a case study. In line with the statement, the research problem is to find out whethercorporate governance alone contributes to the reduction of earnings management or earnings management will be better if audit quality is integrated into the framework. Therefore, to investigate the effect of corporate governance as represented by the audit committee, board of directors and concentration of ownership in the management of profits and then investigate the role of audit quality in addition to the dimensions of governance in the management of profits in Iraqi banks listed in the Iraq Stock Exchange for the year 2015 is the general aim of this study.

2. Literature review

2.1 Concept of corporate governance and its mechanisms

Berle and Means were the first to institute corporate governance and discuss separation of ownership from management [7]. Corporate governance mechanisms were created to fill up the void that happens between owners of the company and the managers due to unwarranted practices that can put the industry and the company at risk as a whole According to Tamimi corporate governance is defined as a set of external and internal mechanisms that contribute to the development of a structural framework for the effectiveness of the company's policies, rules and practices that govern the relationships between all authority concerned and enhance its risk management and control capacity to achieve greater value for investments through financial stability and sustained growth. The audit committee, the board of directors and the ownership focus are one of the range of internal and external mechanisms consisted by governance [44].

The motive behind the institution of corporate governance in governing the corporation as a monitoring mechanism is to reduce the fraudulent action by the company's manager. Due to this, corporate governance has several characteristics such as: audit committee, internal auditing, and board of directors to mention few. Previous researches have applied different measures of corporate governance effectiveness. Some of these measures are: board size, board independence, audit committee independence, and ownership concentration [45].

The shareholders of the company elect the board of directors which consists of a group of individuals. The basis of their responsibility is to work for the shareholders' benefit by monitoring the executive management performance. The members of the board consist of internal and external structure of the board of director. The board of director also consists of either one level that oversees executive management or two levels that include an executive and supervisory board; although each country determines the kind of structure that is suitable for its corporate governance. Moreover, there is a general consensus on what type of activities the board should engage in. For example, the board of director must ensure that the qualifications of its members are in consonance with the purpose of the board. Generally, board members must be versatile and experienced in areas such as finance, accounting, marketing and any other related areas that can help the board to execute its duties in the company and take up the responsibilities towards stakeholders and shareholders (42, 32]. According to the Iraqi Banks Law of 2004, the size of the board of directors' members must be between five and nine members.

The board of directors is considered as important and effective factor measured by how the board independence is affected and the size of the members. Increasing the size of the board is considered as part of the practices of corporate governance just like increase in the board independence. However, the increase in size causes more loss of time and profit in decision-making and thus lead to negative effect on earning management [16].

Katmonand Al Farooque opined that an audit committee can be big enough to contain members with distinctive professional expertise and skills but not so large to be uncontrollable [24]. The audit committee assists the board in the overview process of the financial report and consists of members of the board. The board in many cases assigned duty on crucial activities to its present committee. For instance, The audit committee is obliged to overview the company's financial report [29].

Expertise in finance and accounting gives a fundamental knowledge on how to analyse and determine financial information to the members of the audit committee. To ensure that audit committee performs given duties judiciously, information on academic background becomes a paramount feature. Furthermore, Raghunandan mentioned that audit committee with at least single financial expertise have higher interplay with external and internal auditor [36]. From the previous literatures, it is opined that the experience or knowledge or skill of audit committee members is related directly to effective and quality functioning of the audit committees [5, 6].

The financial expertise of the audit committee increases the occurrence possibility of communication to the audit committee, followed by a timely correction [40]. Kusnadi, Leong, Suwardy, and Wang found that a higher financial reporting quality is achieved when there is audit committee with financial expertise [27]. In a team of audit committee, the presence of at least one member with financial expertise has a negative relation with the quality of earning management [10].

Agency theory states that managerial shareholdings encourage managers to improve the firm's value as the managers equally have the same proportion of the financial impact as a shareholder. In line with this, the stock ownership of the CEO leads to bone of contention between the managers and shareholders. Expectedly, the incentives to execute earning manipulations will reduce as there is increase in management ownership; consequently, it is revealed whether the stock ownership of the CEO aligns the managerial interests to the stockholders' or not. Therefore, studies like Ali, Salleh and Hassan, Banderlipe, concluded that low earning management is associated with managerial ownership [2, 4].

Middle-class shareholders are not interested in management because of the cost attached to the responsibilities but would rather share the benefits in small proportions. At the long run, there are incentives of a free-ride for monitoring management for shareholder with small portion of outstanding shares. Also, shareholders with lager portions of shares receive high incentive in order to effectively influence and monitor the management of the firm and protect the significant part of the investment – this led to hypothesis of efficient monitoring [38]. Therefore, the agency cost might be reduced by concentration of ownership through increase in alleviating and monitoring the free-ride problem [12, 38]. Effective monitor of managerial behavioural actions are expected from bigger shareholders in order to minimize the effect of mismanagement on earning management [20]. In addition, short-term earnings expectations require less pressure on management since shareholders under control focuses more on the long term. Thus, ownership concentration is said to negatively affect earning management according to the efficient monitoring hypothesis. Similarly, discretionary behaviour of the managers is reduced by ownership concentration [21].

The number of share belonging to shareholders determines the mechanism of concentration of the ownership and it is an important mechanism for controlling administrative decisions. From many studies, ownership structures are divided into two: concentrated and fragmented ownership structures. First, concentrated ownership structures indicate ownership concentration among shareholders who own 5% of the shares as issued by the company. On the other hand, distributed ownership structures arecharacterized by large number of shareholder's presence who own small percentages of the shares of the company. Therefore, there is no strong motivation to actively monitor the activities of the company [43].

2.2 Audit quality and earnings management

One of the most important topics in the audit profession is the quality audit. A process of auditing is considered of high quality if an auditor can discover and report errors in material [33]. DeAngelo defined audit quality as the potential of an auditor to detect and report on material misinterpretation and errors in the financial statements of the customer's accounting system [11]. Accordance to generally acceptable auditing standards (GAAS), the quality of the audit is defined as reasonable assurance of audited financial statement and disclosures by complying with generally accepted accounting principles and free from information misinterpretation due to fraud or error [28, 19].

Different interests and concerns are created from the fact that owners of the company are different from the managers of the company [16]. According to the theory of agency, the association between shareholders and managers is always controversial. The property control separation and functions lead to conflicts of agency that result from the fraudulent managers' behaviour in the domain of asymmetric information. Notably, the necessity of managers to be under the control of shareholders has a positive relationship with the complexity of the organization. This is explained through an important number of hierarchical levels which undermine the authority of shareholders to monitor the managers' activities. The complexity of the organization and the decision-making authority assist in increasing the problems of agency and costs associated with it. The firms' owners are responsible to monitor their agents and to control the difficulty. Opportunistic actions can be adopted by the managers against the proprietary interest by making effective use of the asymmetric information while maximizing their own utilities [25].

From the theory, audit quality is the potential ability of an external auditor to detect abnormalities in the financial statements and then disclose it to the eternal agents. The probability to detect is determined by the competence of the auditor while the probability to make disclosure relies on the auditor's independence i.e. curiosity of the auditor to subdue the challenges from the personnel that prepare the financial statement [35].

Hoitash, Hoitash, and Bedard, stated that the external audit makes a provision for new way to protect investors by minimizing the financial risks of the mismanagement [18]. The auditing of financial statement is a monitoring practice that protects the interests of the principals and reduces information asymmetry among the stockholders. This is achieved by provision of reasonable assurance that the financial statements of the managements are free from misappropriation [34]. This is a valuable way of monitoring as applied by many companies to reduce the costs of the agents. In order to provide some assurances that the financial statements of a firm are reliable, the stockholders depend on the outside auditor [22].

Therefore, to investigate the association between external auditing as corporate governance practice and earning management of listed banks in Iraqi stock exchange is the main objective of this study. In different literatures on Iraq, there is no study that investigated the integrative impacts of audit quality, corporate governance on earning management. Thus, it is expected that earning management has negative relationship with audit independence and corporate governance. Also, it is hypothesized that the size of the audit quality and corporate governance will give negative effect with earning management.

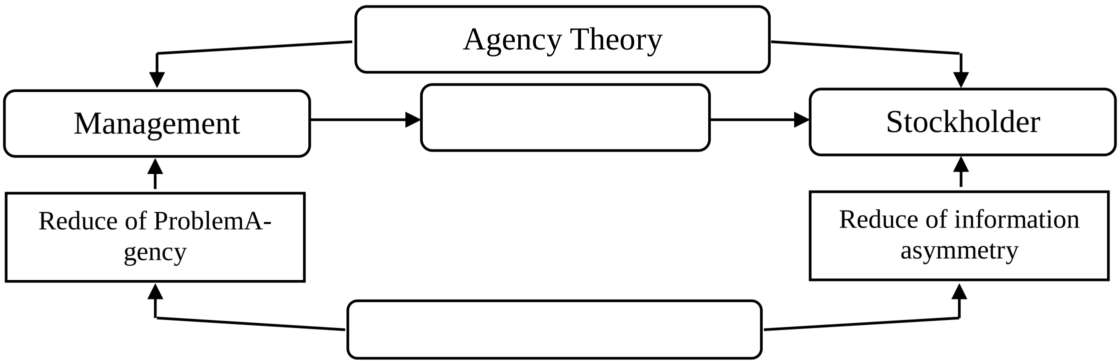

Figure 1: Role audit quality in reducing agency problems.

Figure 1 below presents the emergency of agency theory that led to the separation of ownership from multiple stakeholders. The main challenge is from the emergency of asymmetry on agency. The importance of audit quality is to minimize the level o information asymmetry and agency problems between the management and the stakeholders.

2.3 Corporate governance and earning management

Due to increase in the number of corporate fraud in the recent years, there has been more attention on corporate governance, firm performance and earning management mechanism. Looking at one of the advantages of corporate governance being a tool of monitoring for firm performance, many empirical analyses are performed by scholars in the context of corporate firm in developed countries. The corporate governance practices have influence on manipulation of earning management and overall form performance. Kumari and Pattanayak confirmed the fact that good governance leads tobetter firm performance and controlled earnings management practices [26].

El Mir and Seboui examined the possibility of government mechanisms and earning management to reduce the difference between the market value, accounting value, approximated by created shareholder value (CSV) and economic value added (EVA) [13]. Also, Liu and Lu examined the association between earning management and corporate governance in china by introducing another perspective. It is found that there is low level of earning management for firms with higher corporate governance. The result strongly shows that conflicts of agency between minority investors and controlling shareholders account for a significant portion of earning management of listed firms in China [46].

Moreover, the relationship between corporate governance quality and earning management was examined by Shah, Butt and Hasan [47]. A list of companies for the year 2006 was investigated to analyse the relationship. Analysis showed that there is positive relationship between corporate governance and earnings management. Fallatah and Dickins examined how earning management empowers the casual connection between corporate governance and firm performance. If a firm has a well-established governance system, the earning management decreases. With that earning management can empower the causal relationship as measured by Tobin's Q between corporate governance and firm performance. This study pioneered the fact that earning management that is real activity-based is controlled effectively by a corporate governance system and has direct relationship with corporate governance and firm performance [14].

Another study by Chi, Lisic, and Pevzner stated that firms do consider earning management when their ability to manage accruals is constrained by higher quality auditors. In a firm with strong earning management incentives (i.e. firms that meet earning benchmark and issue seasoned equities), it is found that that city-level auditor industry expertise and audit fees are associated with higher levels of earnings management [9].

Also, a weak result is reported in Big 4 auditors. This study therefore suggests that higher quality auditors should be in the position to maintain accrual earnings management. Firms that engage potential and quality auditor reduce costly earning management. It is found that the tenure of longer auditor can be linked with greater real earning management which could prove the advantage of mandating audit firm rotation. Chen and Zhang examined the impact of 2002 Chinese code of corporate governance of listed companies on earning manipulations [8]. It is reported that the CODE of 2002 has positive impact on reducing manipulations related to earning management by introducing independent non-executive directors to the board of audit committee and directors while financial/accounting experts only are introduced to audit committee. When the states are controlling those firms such impacts are minimal but when it is private-owned, it becomes significant.

Generally, regulatory reform of corporate governance plays an important role on regulating the use of earnings management. Shan, investigated how earnings management reduces the level of relevance in value and how effective corporate governance impact earning management [37]. The findings show that companies that engaged in earning management have more negative impact of value relevance than companies that do not engage in earnings management. Moreover, earnings management are more likely to be regulated by companies with good corporate governance practices than other companies. Lin, Liu and Noronha investigated the relationship between corporate governance and informative earning management of Chinese listed firms [30]. The result showed that there is positive impact between corporate governance and possibility of managerial informative in earning management and effectivecorporate governance contributes to improvement in transparent financial report and resourcefulness of the reported earnings. Similarly, Katmon and Farooque investigated the impact of internal corporate governance on the relationship between quality of disclosure and earning management on listed companies in UK. The study revealed that there is negative and significant relationship between quality of disclosure and earning management for all proxies in restraining earning management. Additionally, the variables of the government are mostly insignificant when they are connected with earning management [24].

There are numerous studies on the association between corporate governance and earning management using audit quality as variable of intermediary. However, there are many studies on the relationship between corporate governance and earning management and in the relationship between corporate governance, earning management and audit quality and earning management.

2.4 Earnings management measurement

The measurements employed were based on the study of Talab, Flayyih and Ali which used the model of M-score [41]. The M-score is a mathematical modelthat was devised by Professor Messod Beneish using eight variables related to financial ratio. Earnings manipulators and nonearning manipulators were differentiated by a powerful tool developed by Beneish The model has been widely used in many financial statements of academic researches, certified fraud examiners, investment professionals and articles directed at auditorssince the introduction of the original M-score. Beneish built a set of eight indicators namely DSRI, GMI, AQI, SGI, DEPI, SGAI, LVGI and TATA which enable the identification of possibility of earnings manipulation. Talab, Flayyih and Ali measured the model with the following equation [41]:

M-score= - 4.84 + 0.920 * DSRI + 0.528 * GMI + 0.404 * AQI + 0.892 * SGI + 0.115 * DEPI – 0.172 * SGAI + 4.679 * TATA – 0.327 * LVGI …. Equation 1

Where:

i. Daily Sales in Receivable Index (DSRI)
ii. Gross Margin Index (GMI)
iii. Asset Quality Index (AQI)
iv. Sales Growth Index (SGI)
v. Depreciation Index (DEPI)
vi. Sales General and Administrative Expenses Index (SGAI)
vii. Total Accruals to Total Assets (TATA)
viii. Leverage Index (LVGI)

3. Research methodology

The banks listed in the Iraqi market of securities that duly follow the Banking Law and the Central Bank and their instructions in accordance with corporate governance implementation are selected as the 2015 research sample. This study has two hypotheses to be tested. The first hypothesis states that:"There is a significant and statistical relationship between corporate governance as represented by the board of directors and the audit committee and the concentration of ownership in earnings management".

In order to investigate the joint effect of quality audit and corporate governance roles in earnings management, the following (second) hypothesis was assumed:

“There is significant and statistical correlation between the integration of audit quality and corporate governance in earnings management”.

4. Research framework

The study provides comprehension and understanding on the effect of external audit on the relationship between corporate governance and earnings management. Thus, the proposed conceptual model of this study as presented in Figure 2will be used as a guide for testing the study hypothesis based on agency theory.

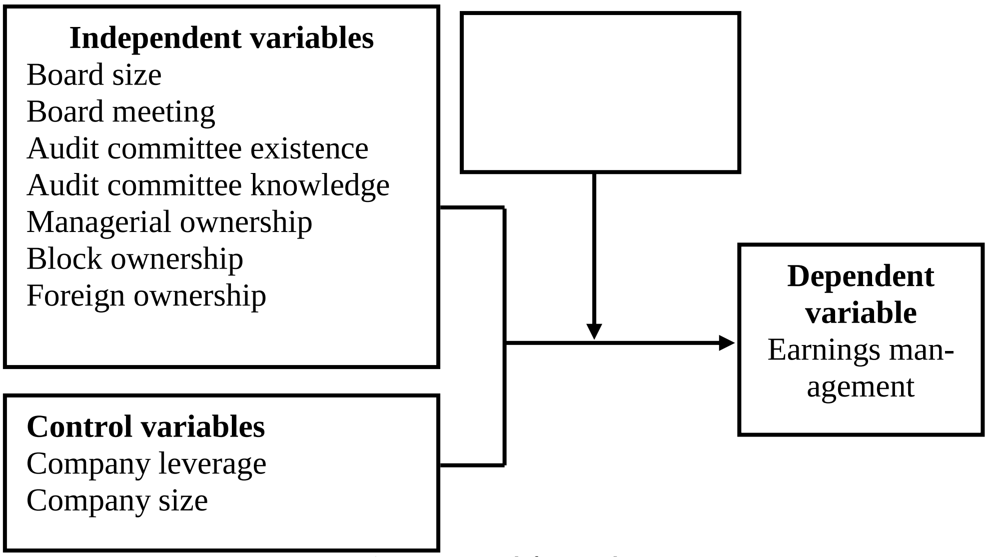

Figure 2: Research framework

5. Research Model and Measurement

Model 1 examine the direct relationship between the independent variables and the dependent variable. The model is tested using panel multiple regression analysis, which is developed to test all the hypotheses raised in the study.
Model 1 is as follows:

$$EM_{it} = \alpha_{it} + \beta_1\ BSIZE_{it} + \beta_2 BMEET_{it} + \beta_3 ACEXIST_{it} + \beta_4 ACKNW_{it} + \beta_5 MGROWN_{it} + \beta_6 OWNCON_{it} + \beta_7 COYSIZE_{it} + \beta_8 COYLEV_{it} + \varepsilon_{it} \ldots \ldots Model\ 2$$

Where**:**
EM: Earnings management
α = Intercept term
β = Regression slope coefficient
BSIZE = Board size
BMEET = Board meeting
ACEXIST = Audit committee existence.
ACKNW = Audit committee knowledge
MGROWN= Managerial ownership
OWNCON = Ownership concentration
COYSIZE = Company size
COYLEV = Company Leverage
ε = Error term

Model 3 examine the moderating effect of audit quality on the relationship between the corporate governance and earnings management. The model is tested using panel multiple regression analysis, which is developed to test hypotheses 2:

$$EM_{it} = \alpha_{it} + \beta_1\ BSIZE_{it} + \beta_2 BSIZE * AQ\ _{it} + \beta_3 BMEET_{it} + +\beta_4 BMEET * AQ\ _{it} + \beta_5 ACEXIST_{it} + \beta_6 ACKNW_{it} + \beta_7 ACEXIST * AQ\ _{it} + \beta_8 ACKNW * AQ\ _{it} + \beta_9 MGROWN_{it} + \beta_{10} OWNCON_{it} + \beta_{11} MGROWN * AQ\ _{it} + \beta_{12} OWNCON * AQ\ _{it} + \beta_{13} COYSIZE_{it} + \beta_{14} COYLEV_{it} + \varepsilon_{it} \ldots \ldots \ldots . Model\ 3$$

Table 1belowcontainthedescriptionofallthevariablesusedadopted in this study model in addition to the source of the variable in past literature.

Table 1: Variable description and Measurement

Variable	Description	Measurement
Earnings management	EM	M-score
BSIZE	Board size	Number of directors sitting in boardroom.
BMEET	Board meeting	Number of times that the directors met in a year.
ACEXIST	Audit committee existence.	Dummy variable 1 for companies that have audit committee and 0 if otherwise.
ACKNW	Audit committee knowledge	Number of audit committee member with financial knowledge.
MGROWN	Managerial ownership	The percentage of companies' shares held by executive directors.
OWNCON	Ownership concentration.	Percentage of company shares held by foreign institutional
		Block shareholders above 5%.
AQ	Audit quality	The log percentage of the amount paid as audit fees.
COYSIZE	Company size	Measured by the log of total asset.
COYLEV	Company Leverage	Shareholders fund divided by total liabilities.

6. Results and Analysis

The descriptive statistics of all the variables used in the study are presented in table (2). Generally, earning management variables proxy by M-score has a mean value of-1.750 derived between the maximum value of 4.404 and minimum value of - 7.77. Similarly, 6.714 and 8.666 are the mean values of board size and board meeting respectively. Also, 85 per cent of the selected banks have audit committee with a mean value of 0.85 between the maximum value of 1.00 andminimum value of 0.00. Likewise, 66 per cent of the selected banks have audit committee knowledge with a mean value of 0.66 between the maximum value of 1.00 and minimum value of 0.00. The sampled banks accounted for 29 per cent in the case of managerial ownership with a mean of 29.113 between maximum value of 88.89 and minimum value of 0.00. Furthermore, the mean of foreign ownership and block ownership of the selected banks are 0.183 and 0.405 respectively. While the company leverage values ranged from 1.333 to 4.771, the company size for all the sampled banks ranges from 11.631 to 12.190.

Table 2: .Descriptive statistics

Variable	Obs	Std. Dev.	Min	Mean	Max
EM	21	2.080	- 7.727	-1.750	4.404
BSIZE	21	1.007	4	6.714	9
BMEET	21	3.623	1	8.666	15
ACEXIST	21	0.358	0	0.857	1
ACKNW	21	0.658	0	0.666	2
MGROWN	21	24.827	0.017	29.113	84.515
BLOCK	21	0.306	0	0.405	0.943
FOREGIN	21	0.301	0	0.183	0.909
AQ	21	2.02e+07	3.65e+07	5.94e+07	9.37e+07
COYSIZE	21	0.641	8.929	11.631	12.190
COYLEV	21	0.972	8.929	1.333	4.771

6.1. Person correlation analysis

Table (3) below presented the research variables included in the earnings management model and their Pearson correlation matrix respectively. The correlation matrix examines the bivariate correlation among independent, dependent and control variables. In general, there are low correlations between all the variables used in the earnings management model. Nevertheless, as the correlation values are below 0.80 thresholds, this means that the multicollinearity is not a serious threat to the multivariate results as approved by Gujarati [17].The Variance Inflation Factor (VIF) further confirmed the correlation result as resented in the table 4 below.

Table 3: Pearson Correlation Matrix

Variables	EM	BSIZE	BMEET	ACEXIST	ACKNW	MGROWN	BLOCK	FOREGIN	AQ	COYSIZE	COYLEV
EM	1										
BSIZE	0.128	1									
BMEET	-0.059	0.095	1								
ACEXIST	0.104	0.158	0.153	1							
ACKNW	-0.069	0.000	0.097	0.423	1						
MGROWN	-0.040	- 0.234	- 0.276	0.202	- 0.169	1					
BLOCK	- 0.095	0.179	- 0.495	- 0.236	- 0.251	- 0.270	1				
FOREGIN	- 0.063	- 0.243	0.141	0.012	0.184	0.597	- 0.765	1			
AQ	- 0.155	0.097	0.150	0.164	0.383	- 0.162	0.015	- 0.085	1		
COYSIZE	0.570	0.139	- 0.016	-0.076	- 0.012	0.109	- 0.244	0.203	0.197	1	
COYLEV	- 0.283	0.075	0.312	- 0.061	0.360	- 0.139	- 0.364	0.334	0.345	0.0853	1

Table 4: Multicollinearity Test

Variables	VIF
BSIZE	7.71
BMEET	5.74
ACEXIST	4.37
ACKNW	2.80
MGROWN	2.55
BLOCK	2.17
FOREGIN	1.74
AQ	1.53
COYSIZE	1.35
COYLEV	1,34

Mean VIF3.13

7. Regression analysis

The table (5) below shows the summary of the regression techniques for model 1 (the relationship between corporate governance and earnings management) that it used in this study.The panel data estimation technique was used to estimate the earnings management model. The $R^2$for the model 1 is 55 % which suggest that the independent variables explain the variation in the earnings management. Based on the regression result in Table (5), the coefficient on (board size, board meeting, audit committee existence, audit committee knowledge, managerial ownership, block share ownership, and foreign ownership) revealed a insignificant relationship with earnings management with coefficient of (0.15 and t-value of 0.884, - 0.084 and t-value of - 0.70, 1.145 and t-value of 0.80, - 0.303 and t-value of - 0.43, -0.027 and t-value of - 1.08, - 1.569 and t-value of - 0.66, 0.099 and t-value of 0.04) .

Table 5: Regression result: Earnings management model 1

EM	Coef.	T	P>t
BSIZE	.051	0.15	0.884
BMEET	-.084	- 0.70	0.484
ACEXIST	1.145	0.80	0.422
ACKNW	-.303	-0.43	0.667

MGROWN	-.027	-1.08	0.279
BLOCK	-1.569	-0.66	0.506
FOREGIN	.099	0.04	0.972
COYSIZE	2.010	3.79	0.000***
COYLEV	-.903	-2.29	0.022***
_CONS	-22.893	-3.36	0.01***
R^2		0.55	
F-value		0.00	
N		21	

Note: **, *** indicates significance levels at 5%, and 1% respectively.

The table (6)below shows the summary of the regression techniques results for model 2 used in this study. The $R^2$for the model is 87 % which suggest that the moderate variable explain the variation in the relationship between corporate governance and earnings management. Based on the regression result in Table (), the coefficient on board meeting, audit committee knowledge, and managerial ownership revealed a significant negative sign with coefficient of - 11.845 and z-value of - 5.87, - 16.814 and z-value of - 3.95, and - 1.267 and z-value of - 5.24 respectively. This result suggests that the moderating effect for external audit with the board meeting, audit committee knowledge, and managerial ownership reduced the value of earnings management. Hence, board meeting, audit committee knowledge, and managerial ownership improves the quality of financial report.

Interestingly, the coefficient of external audit with audit committee existence and foreign ownership revealed a positive and significant sign at the level of 1%. This implies that the external audit with presence audit committee existence and foreign ownership has a significant effect on earnings management practice of listed companies in Iraq.

The coefficient of external audit with board size and block shareholder is positively insignificant. In the case of board size, the coefficient is positively insignificant 0.941. With respect to block shareholder 0.739.

Table 6: Regression result: Earnings management model 2

EM	Coef.	T	P>t
BSIZE * AQ	.941	0.47	0.636
BMEET* AQ	-11.845	- 5.87	0.000***
ACEXIST* AQ	69.580	5.03	0.000***
ACKNW* AQ	-16.814	- 3.95	0.000***
MGROWN* AQ	-1.267	- 5.24	0.000***
BLOCK* AQ	.739	0.04	0.968
FOREGIN* AQ	72.388	3.66	0.000***
COYSIZE* AQ	5.338	2.02	0.043**
COYLEV* AQ	4.954	2.01	0.044**
_CONS	-18.225	-3.13	0.002***
R^2		0.87	
F-value		0.00	
N		21	

Note: **, *** indicates significance levels at 5%, and 1% respectively.

8. Contribution of the study

This study happens to be one of the first researches to introduce audit quality to the mechanisms of corporate governance as represented through the board of directors, the audit committee and the concentration of ownership. The following variables are considered: size of the board of directors; number of board meetings; Audit Committee existence; the Audit Committee knowledge; managerial ownership; foreign ownership; and block shareholder, with their impacts on earnings management in the Iraqi environment. To the best knowledge of the researcher, this study is the first to apply integrated measurement method between governance and audit quality and their impact on earnings management in literature reviews of accounting that deals with governance. Talab, Flayyih and Ali published data on measurements of earnings management using Beneish 1999 Model. The impact of corporate governance mechanisms on earnings management was measured to complement this research and then repeatedly measured through the introduction of audit quality to corporate governance mechanism [41].

9. Conclusion

Many scholars have studied the existence of earning management practices in Iraqi stock exchange. Earnings management has captured attention in the domain of accounting literatures and is of tremendous importance to regulators, practitioners and corporate stakeholders. In recent time, corporate governance issues have been brought to the limelight in most developing countries due to high intensity of scandals, institutional failures and financial crises in United States, Europe and East Asia. The integrity of accounting information are compromised by these scandals and led to low confidence among the investors. Therefore, the board size, audit committee, concentration ownership and outside auditing have become recently the factors of importance in corporate governance as they play paramount role in overseeing the financial report quality and acting as deterrents to management fraud and override of controls [48, 49]

Thus, this study examined relationship between corporate governance and earning management in listed banks in Iraqi stock exchange and the result showed not to be significant. Due to many cases of high-profile earning management in the world, the role of audit quality and external audit to ensure the quality of corporate financial reporting has come under considerate assessment. In a nutshell, this study examined the moderating effect of external audit on the relationship between corporate governance and earnings management among banks companies listed in the Iraqi stock exchange. Therefore, a significant relationship is shown for the moderating effect of external audit on the relationship between corporate governance and earnings management in most of the variables.

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