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The Influence of Earnings Volatility on The Relationship Between Leverage and Classifications Shifting Earnings Management: An Entrepreneurial View

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ABSTRACT

This study investigates the relationship between leverage and classifications shifting earnings management and how this relationship is influenced by earnings volatility. To achieve the research objective, this study takes the sample of Pakistani non-financial firms listed in Pakistan Stock Exchange for the period of 2004 to 2018. This study discusses the relationship between leverage and classifications shifting earnings management, especially with the interaction of earnings volatility. The study is supported with the Agency Theory and Positive Accounting Theory using the two-step system Generalized Method of Moment (SYS-GMM) dynamic panel estimators. The leverage is measured by using long term debt, short term debt and total debt while earnings volatility captured the measurement of business risk and for the measurement of classifications shifting is used as earnings management. To capture the classifications shifting, McVey model is used that measures the core earnings. Firstly, the study examines the relationship between leverage and classifications shifting earnings management and after that how earnings volatility influences that relationship. The results showed that relationship between classifications shifting and leverage and is positive but when an interaction term is used as earnings volatility it shows negative relationship between classifications shifting and leverage. So, when the firm needs debt in the shape of leverage, it misclassifies the core earnings in the income statement but when there are fluctuations in the earnings like earnings volatility of firm it avoids to use classifications shifting due to professional assessment of the financial institutes and brokers of financial markets. So, in the entrepreneurial firms the managers avoid to use earnings management because these managers keep and show the true financial representations of financial statements.

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INTRODUCTION

Earnings volatility is a crucial factor that influence the relationship among leverage and classifications shifting earnings management specially with the perspective of entrepreneurship. This study aimed to explore the association from the roots and in-depth. The earnings volatility is the fluctuation in the earnings of the firms from period to period. The volatilities are associated with the economic uncertainty, market inefficiency and disturbance in the internal operations of the firm. The higher uncertainty and risk lead to higher volatilities and vice versa.

On the other hand, leverage is the borrowing of the funds to utilize in the operations of the firm and for investment purpose. The leverage is measured by using different ratios like short term, long term and total debt. In the favorable market conditions, the leverage uplift the return on investment while during downturns it could be the reason of losses as well.

The association between leverage and EM has been and extensive and favorite topic in the entrepreneurial finance. The earnings management in the manipulation in the monetary statement to achieve the desired outcomes such as deviating the core expenses in the income statement,

manipulation while recognizing revenues or other aggressive accounting methods. One prominent way to manage earnings used by the entrepreneur through high earnings volatility is classifications shifting earnings management. The classifications shifting is the manipulation of shifting of core expenses or revenues from one sort to another that can change the extent of reported earnings. For instance, to smooth out earnings volatility, a corporation may opt for delaying or accelerate the recognition of certain expenses or revenues.

Earnings management in recent accounting literature has become an important issue and is concerned globally by academic researchers as well as practitioners. It misleads the stakeholders that makes it an imperative issue among practitioners and academicians (Dechow & Skinner, 2000). It is as a result of poor disclosure mechanism in financial reporting and the quality information provided by managers through their reported accounting numbers that led to decline equity markets all over the world in late 2000s (Gaio, 2010). It is intentional manipulation by the managers of external financial reporting practice with the aim to have some personal benefits (Schipper, 1989). The discretion in financial reporting is aimed at changing earnings with a target of predetermined targets and objectives by the forecast of financial analysts or management, resulting to more stable amount from the reports.

The earnings management technique is called switching-based classification where the core expenses are transferred into special items in the financial statement in term of income statement to enhance EBI. There is therefore an ethical and professional issue arising from using earnings management, since it leads to increased uncertainty in the validity of accuracy or reliability financial statements filed by companies on stock exchange. They rise in using the classification switching strategies to falsely lower firms' taxable income. This decrease raises the volume of pressure towards Government (especially in developing countries) with regard to low amount of tax and subsidies provided by firms for their stability.

On the other side, earnings management is widely used by most of the firms as a tool to minimize the volatility in earnings for the attractions of investors especially for debt providers. This artificial increase in financial statements of firms captures the investor's trust about the firms. However, the firm undergoes the revaluation after sometimes that reset the financial statements. Consequently, investors have to face the loss. This possible situation occurs when there are variations in leverage and firms are trying to make financial decisions. Moreover, the leverage utilizations put the firms to undergo the earnings management techniques for avoiding the financial difficulties (Asim & Ismail, 2019).

Accounting earnings management is based on accruals and is used to influence results through accounting decisions. The accruals-based earnings management has become incapable to explain some phenomenon. Now the trends have been shifted to real base and classification shifting earnings management through a vision to manipulate the earnings at operating level. These earnings management techniques help the managers to shape and map the financial statement of firm for their personal benefits.

The debt market in Pakistan is inactive, immature and it does not trust on non-financial firms. The reason for this mistrust is that most of the market capitalization is under the non-financial firms and their extensive usage of earnings management. Moreover, due to continuous mistrust, the rules and regulations for non-financial firms to get debt financing are tightening with the passage of time. (Arif,

2007) studied on expansion of bond market and show that bond market in Pakistan is to be built from scratch and then constructed the rules and regulations for market conduct.

The complexities like political and economic imbalance affect the basic phenomenon that also affects the market instability. The market instability is the reason for business risk like earnings, cash flow and stock market return volatility. The combination of these volatilities affects the financing decisions (Market leverage and Book leverage) which lead to earnings volatility. The financing choices and decisions are very important for firm's success and earnings point of view (Bancel & Mittoo, 2004). This volatility in earnings motivates the firms to use techniques of earnings management. It is a challenging situation for investors who face problems in terms of firm revaluation that impacts the performance of financial market.

In extension, business risk is the standard deviation of cash flows, market returns, stock returns and earnings. With the high level of business risk, the cost of retrieving the leverage is high for the firms. The volatility declines the future earnings of firm and also decreases its ability to fulfil financial obligations. This situation increases the bankruptcy and financial distress cost, leading the firms to default. Financial distress cost of firms' trade-off with tax benefits and choose low optimal debt ratios. A volatile state of financial markets has disproportionately a negative effect on corporate financing and the financial service.

LITERATURE REVIEW

Earnings Management and Leverage

Conspicuously, there are several arguments for positive linkage between leverage and earnings management as well as on the negative association among leveraging and EM. The measurement of leverage is based on liabilities-to total assets ratio (Abdul Rahman & Haneem Mohamed Ali, 2006; Dechow & Dichev, 2002; Haw, Ho, & Li, 2011; Sweeney, 1994), they also indicated that the annual monitoring of externals ("investors") and internals ("corporate governance") roles reduce the occurrence of classification shifting. The firm opportunistically reclassified core expenses to special items. (Pratiwi, Suprasto, Sari, & Ariyanto, 2022), indicated that financial distress is also the source of classifications shifting earnings management.

The classification shifting earnings management is being performed by (McVay, 2006). Classification shifting is the deliberate movement of core costs into the special items' income statement. This practice arises when core earnings are changed, but no net income manipulation has been made (McVay, 2006). Following the same notion (Bansal & Bashir, 2023) found that the firms among higher debt or their intension to used debt are more motivated to employ in expenses misclassification. In addition, (Bansal & Bashir, 2023) revealed that leveraged firm are more pronounced to misclassify the core expenses to avoid from debt contracts. The managers are more conscious at the time of debt contracts and at the time for the extension of debt contract because the professional bodies look at the positions of financial statements. similarly, (Pratiwi et al., 2022) found that financial distress firms effect the practices of earnings management by using misclassifications of core expenses. Once the managers are satisfied with the desire results, they reshape the financial statements in their original form after using different types of earnings management techniques.

Most of the time managers apply the accruals and real earnings management approach instead of classification shifting earnings management during which they use their own, personal knowledge. However, the accounting regulations and standards affect scope of classification changes. After 2001/02 reform, the shifting of classification for abnormal products decreased to a significant extent (Seve & Wilson, 2019). Managers are less inclined to be involved in classification shifting behavior since the implementation of ASSB 101. In addition, there is no substitution impact that affects accruals-based earnings management.

Moreover, through actual and accruals earnings management, the topic of classification shifting in relation to leverage is also important subject in current as well previous part literature. Classification shifting earnings management is the process by which managers misclassify core expenses as exceptional things such as EBIT. Based on these arguments, (Fan, Thomas, & Yu, 2019) used panel regression analysis and assessed the association between debt covenants and classification shifting earnings management and discovered that with an uptick in financial distress classifications shifting also rises.

Moreover, other relevant studies that examine diverse factors influencing the level of core earnings and core expenses misclassifications. For example, the use of proxy market to book values of an equity using a proxy investors growth expectation (McVay, 2006) observed that classification shifting is enhanced in high-growth firms so as to meet those by analysts. Furthermore, (Abernathy, Beyer, & Rapley, 2014; Fan, Barua, Cready, & Thomas, 2010) Classification shifting earnings management may be used as a substitute when other options for earnings management, such as actual and accruals earnings management, are inadequate.

In addition to that, Previous study shows that managers misclassify core expenses as income-reducing special items in order to increase reported core earnings. Studies found that manager use classifications shifting in order to meet or increase analysis and mapping the financial statements (Fan et al., 2010; Fan & Liu, 2017; Haw et al., 2011; McVay, 2006). Additionally, shifting the core item for income increasing with special items, manager is more likely to use core earnings that are more in line with the forecasted analysis (Bradshaw & Sloan, 2002; Gu & Chen, 2004). The managers are motivated and likely to use earnings management in this behavior because meeting or increasing analysts forecast is favorable for the valuation of equity (Bartov, Givoly, & Hayn, 2002; Kasznik & McNichols, 2002). The general perception of core earnings is that core earnings are more persistent that non-core earnings so have multiple higher valuation (Fairfield, Sweeney, & Yohn, 1996; Lipe, 1986). The manager increases the value of equity of their firm by inflating core performance by core earnings to get the confidence of investors are financial institutes.

In contrast, (Fan et al., 2010) describes that manager also inclined toward using core expenses decreasing income tactics in order to avoid from potential losses and decreasing operating income. Moreover, (Fan et al., 2010) reveals two dimensions of core expenses such as selling, general and administrative expenses together with cost of goods sold. The manager utilizes misclassification of core expenses as COGS to generate a slight gross margin increase in the fourth quarter for investment incentive. When core earnings are close to zero or a small change from the previous quarter's core earnings, managers become more motivated and tend to use COGS and SGA in most items.

Furthermore, prior researches analyzing various components influencing the degree of core earnings and expenses misclassification. For instance, the use of proxy for market to book values of an equity based on growth expectations of investors, (McVay, 2006) reveals that classification shifting increases to meet the expectations of analysts in firms having high growth. (Fan et al., 2010) and (Abernathy et al., 2014) conclude that classification shifting is more likely used by managers as a trade-off when other opportunities of earnings management like real and accruals are not possible to use.

In addition to the relationship of financial leverage with classification earnings management, a large number of studies have been shown that manager's motivation for classification shifting i.e. increasing the market pricing (Kasznik & McNichols, 2002; Lipe, 1986); meeting the expectations of investors and analysts (Fan et al., 2010; McVay, 2006); achieving the initial public offerings and seasoned equity offerings requirements (Li, Liu, & Wang, 2015; Lu, Zhang, & Yu, 2019); meeting or exceeding the threshold for executive compensation and performance-based equity incentives (Wang, Wang, Liu, & Li, 2022; Xie, Zhang, & Cui, 2019). While all of the aforementioned research largely focuses on the classification shifting incentives provided by the equity market and compensation contracts and due to the importance of debt financing as source of external financing for business, the debt providers also pay attentions towards the core earnings of the company (Fan et al., 2019). So, the company misclassify the core expenses as special item when EBIT related debt covenant is close to being violated. Moreover, in case of private loan contract, the debt holders also effect classifications shifting.

H1. A firm's financial leverage effect classifications shifting earnings management of Pakistan listed firms.

Earnings Volatility and Classification Shifting Earnings Management:

The business risk can be defined as the volatility. These business risks are the way of allocation of resources to expenditures and from business policies. The volatility is the fluctuations in the particulars of business risk. These business risk particulars are the earnings volatility and cash flows volatility. These volatilities are the possibilities of disturbing earnings of firm in term of volatility. The shareholders want stability in volatilities but the management wants to alter these volatilities for their own and short-term purpose and fluctuate the earnings in financial statement. These fluctuations in financial statements are the reason of the earnings management. The managers use these earnings management to fulfil the requirements of internal stakeholders and financial institutes as well. On the other side if internal scrutiny is strict and financial institutes keep observing professionally then the use of these earnings management can be decreased. So the internal owners and financial institutes who are financing the company are most concerned with the activities of company. The concerned relation between business risk and earnings management is discussed in the extended literature.

Earnings figures are the most prominent figures in accounting information system and most authentic source of accounting system. Information regarding earnings are benchmarked with some specific measures to provide valuable perception of financial issues for economic decision making. On the base of time series data and horizontal analysis, a healthy comparison regarding earnings figures can be conducted to analyze earnings quality by using annual and quarterly earnings data. The volatility of earnings is a key indicator for earnings quality in such analysis. Earnings volatilities are the fluctuation in earnings over the period of time. In the financial market there are two investment behavior i.e. risk taker and risk averse and risk taker and risk averse investor avoids so many fluctuations in earnings.

These stable earnings can be useful to predict future performance of company (Hairston & Brooks, 2019).

In addition to that, (Phua, Lok, Chua, & Lim, 2021) demonstrated there is positive relationship between earnings volatility on derivatives and earnings management. The earnings volatility of firms are the fluctuations in earnings that decrease the confidence of investors and financial institutes. Under the condition of earnings volatility, the manager wants to compensate the volatility of earnings and used earnings management for retaining the confidence of investors and financial institutes. The firms also encouraged to engaged in derivatives in order to diminish the earnings volatility. So, in that case derivatives are the source of reducing the earnings volatility by using earnings management. In addition, the derivatives play its role on the both good or worse side that when firm face high risk the derivative can be a tool to increase earnings volatility and on the other and good side derivative can be use a risk management tool to mitigate the earnings volatility. The derivatives are used as tool of capitalization on discrepancies in the financial market (Phua et al., 2021). These derivatives are the shaping instrument of earnings volatility in the financial statements that effect the investors decisions. In that case, manager use earnings management as an incentive with the purpose of increasing or decreasing the earnings volatility for the better predictions of future earnings of the company. So, earnings volatility is used as a driver to use earnings management. (Phua et al., 2021) used panel regression to depicts the relationship of earnings volatility, derivatives and earnings management in the phase of COVID crisis and found that earnings volatility significantly positive effect earnings management.

H2: Earnings volatility positively effects Classification Shifting earnings management.

Leverage and earnings volatility will increase classifications shifting earnings management, so the manager gets rewarded from its financial statement strategies. On the basis of these financial statements and asymmetries, investors as well as other financial institutes in the financing market have confidence in that particular manager. These financial institutions are the debt providers who monitor activities based on accounts in order to ensure that they pay off interest and principal. The manager will apply positive earnings management so that the financial institutions shall get their interest and principal during high earn in volatility. Only after the financial institutions confirm that they will provide debt or extend the term of this loan, it shall be provided.

The level of leverage is calculated by means of the debt; hence, greater the debt leads to higher leverage, it follows that there will be more risk in proportion. Due to the high degree of risk and earnings volatility, managers are forced to manage core expenses. The manager implements classifications shifting earnings management to maintain the faith of investors and financial institutions. Including confidence and desired benefit to investors, financials institutes' actual performance will be reviewed by the manager again based on a market that mistrusts finical which is assured by these financial statements.

It has been revealed from the literature and same context that classifications shifting earnings management is positively influenced by leverage, while it also implies that increases in earnings volatility have a positive influence on classifications shifting earnings management. It also exhibits a considerably positive association between leverage and classifications shifting earnings management when earnings volatility is used as an interaction term. Furthermore, considering the fact that

classifications shifting earnings management can be difficult for auditors to detect, a manager increases this form of earnings management as leverage grows. Earnings volatility refers to the impact of leverage and classifications shifting earnings management which interact with each other. Based on the results, business risk measured as earnings volatility shows a significant negative relationship with classifications shifting earnings management when used to interact leverage.

H3. Business risk is a significantly negatively factor that moderates the relationship between classifications shifting earnings management and leverage.

RESEARCH METHODOLOGY

Classification shifting is employed to measure earnings management. Classification shifting can be described as "deliberate misclassification of items in the income statement" (McVay, 2006) since managers shift items between categories. (McVay, 2006) discusses the third type of earnings management. The net income number will not be affected and there won't be any accruals to reverse in the future. Manager switch the cost of goods to core expenses (COGS and selling & administrative expenses) to special items opportunistically. In general, if there is an increase in leverage or the companies are close to deviating from debt covenants; they manipulate earnings by classifications shifting as they need to motivate with respect of financial statements for leverage increase. Thus, there might be a positive association between classification shifting earnings management and leverage or debt covenants. (Fan et al., 2019) reveal that classification shifting is more significant if the firm approaches a technical violation of at least one covenant with regards to EBITA. The outcomes also indicate that the more financial distress of firm is, the greater extent of classification shifting. So, the equation presents classification shifting of earnings management as dependent variables and leverage as independent variables with risk as moderating variable along with control variables.

$$CSEM_{it} = \beta_1 CSEM_{it-1} + \beta_2 Lev_{it} + \beta_3 risk_{it} + \beta_4 Lev_{it} * risk_{it} + \beta_5 ControlVariables_{it} + \varepsilon_{it} \quad (11)$$

To determine whether firms are undertaking classification shifting, the basic two-stage regression method utilized in (McVay, 2006) research design is used, first core earnings were measured with the (McVay, 2006) model, subtracted from reported core earnings in order to determine unexpected core earnings. In (McVay, 2006) model, total accruals are used to predict core earnings; this variable is replaced by operating accrual to reduce the model bias thus improving the research design's construct validity. In many empirical papers that have a country-specific or global parameters in which classification shifting is investigated and soundly established, this model serves and used as the standard. Consequently, the core earnings estimation and unexpected core earnings are as follow:

$$CE_{i,t} = \beta_0 + \beta_1 CE_{i,t-1} + \beta_2 ATO_{i,t} + \beta_3 Accruals_{i,t-1} + \beta_4 Accruals_{i,t} + \beta_5 \Delta Sales_{i,t} + \beta_6 NEG\Delta Sales_{i,t} + \varepsilon_{i,t} \quad (12)$$

RESULT AND DISCUSSION

Descriptive Statistics:

The following table is showing the results of descriptive statistics that shows the average behavior of variables and distribution of the entire data and no outlier in the data.

Table I

Variables	Obs	Mean	Std.Dev	Min	Max
CLS	6825	-.0625	.8628	-3.9884	2.5812
SDT	6825	.3113	.1201	.05	.4444
LTD	6825	.4212	.1210	.2001	.6597
TD	6825	.5196	.0806	.3798	.7081
MKTL	6825	2.1695	1.7607	.5	5.8995
BR1	6825	.5644	.2622	.1001	.9999
STD*BR1	6825	.1754	.1104	.0054	.4421
LTD*BR1	6825	.2376	.1331	.0211	.6593
TD*BR1	6825	.2937	.1466	.0422	.6907
MKT*BR1	6825	1.2114	1.2145	.0533	5.8459
SIZE	6825	9.3285	4.0962	2.5694	21.976
PROF	6825	.3341	.4334	-.4997	1.5055
TANG	6825	.4265	.1059	.3	.7
MBR	6825	1.4841	.7361	.7	2.9995

Correlation Analysis

The correlation analysis indicates the strength and direction of the association between the research variables. This direction might be either positive or negative. The results of correlation analyses are acknowledged and reported for brevity, although they are consistent with the study's objectives.

Table II

Variables	CLS	STD	LTD	TD	MKTL	BR1	STD*BR1	LTD*BR1	TDB*R1	MKT*BR1	SIZE	PROF	TANG	MBR
CLS	1													
SDT	.0001	1												
LTD	.0162	-.0183	1											
TD	.0455	.022	-.0293	1										
MKTL	.0106	.0046	-.0202	.0391	1									
BR1	.0024	-.0087	-.0017	.021	-.0282	1								
STD*BR1	.0013	.461	-.0179	.0253	-.024	.4733	1							
LTD*BR1	.0107	-.0211	.5134	.0039	-.0369	.2822	.3592	1						
TD*BR1	.0147	-.0032	-.0098	.3307	-.0128	.1939	.3691	.2769	1					
MKT*BR1	.0084	-.0083	-.0224	.045	.3797	.4459	.3207	.3515	.4335	1				
SIZE	-.0174	.205	0	-.0714	.0515	.0187	.1365	.0099	-.0056	.0496	1			
PROF	-.1538	.0119	-.0123	-.1289	-.1489	.0002	.0051	-.0089	-.0384	-.1168	-.0119	1		
TANG	.0314	.0296	-.0157	.0232	.0643	.0184	.0332	.0079	.0241	.0485	-.025	.0391	1	
MBR	-.0047	.018	-.0432	.0111	-.1105	.0172	.0157	-.008	.0219	-.085	.0066	.0833	-.0192	1

Classification Shifting earnings management and Leverage. Role of business risk (BR1)

This section shows the role of business risk between classification shifting earnings management and leverage decisions of firms in Pakistan. Here, the business risk is measured as standard deviation of earnings of firms. Leverage is measured through book leverage like short debt, long term debts and total debt ratios while as well as market leverage ratios. All these variables are regressed with classification shifting earnings management. Table shows the results related to the role of business risk in the relationship between classification shifting earnings management and leverage decisions of firms. The lagged dependent variable has been used as an independent variable in order to create a dynamic panel model. The significance of this lagged dependent variable in all columns supports the dynamic panel model, justifying the use of GMM. This shows current level of earnings management is dependent upon prior period's earnings management.

The results indicate that leverage displays a significant positive role towards the classifications shifting based earnings management that specify as leverage of a firm increases the classifications shifting based earnings management. (Dechow & Dichev, 2002) noted that earnings management will most likely be more aggressive prior to equity issuances and when the amount of shifted expenses permits the manager to match the analyst prediction when they would not otherwise. Earnings management studies in many countries by investigating classificatory manipulation in a different setting, namely before seeking external finance. Previous studies showed that external finance provides firms with fruitful motivation for earnings manipulation (Rangan, 1998; Teoh, Welch, & Wong, 1998).

Earnings manipulation is more pronounced when it allows management to affect the perceptions of finance providers (either investors or debtors), the present study as well will extend UK and USA studies by investigating classification in external finance setting. This chosen because some recent studies showed that the positive relationship between bottom line earnings and stock prices lead some firms to manipulate their earnings before issuing new equity. However, since investors now pay more attention to core earnings, and consider it to be more value relevant than GAAP earnings (Bhattacharya, Black, Christensen, & Larson, 2003; Bradshaw & Sloan, 2002; Collins, Maydew, & Weiss, 1997; Francis & Schipper, 1999), firms might manipulate their core earnings through the misclassification of some recurring items. Furthermore, (Francis & Schipper, 1999) pointed out that earnings management is more likely to occur when managers have a direct stake in reported earnings and believe that users are unable to undo its effects. Given the close relationship between stock prices and reported core earnings which thereby affects managers' wealth coupled with the difficulty in detecting classification shifting, external finance offering is more likely to be ripe area for classification shifting.

The results also show that there is also a significant positive and negative relationship between earnings volatility and classifications shifting based earnings management that shows high earnings volatility firms tend to use classifications shifting based earnings management. (Ha, 2021) founds the results that are consistent with our study results that the propensity of firm to engage in classifications earnings management is negatively correlated with earnings volatility.

The results also indicate that when earnings volatility is used as an interaction term with leverage it shows significant negative relationship with classifications shifting based earnings management.

Table III

Variables	Panel A	Panel B	Panel C	Panel D
CLS $_{t-1}$	-.1995***	-.3055***	-.4039***	-.3764***
	(.0612)	(.0914)	(.1822)	(.0400)
Lev	-2.1565***	1.1079**	1.7465***	.1844***
	(.8940)	(.5733)	(.4578)	(.0544)
BR1	1.2825***	1.6647***	2.5757***	.5643**
	(.4182)	(.3861)	(1.1496)	(.2731)
Lev*BR1	4.0106***	-2.9513***	-5.0012***	-.2800***
	(1.3550)	(.8734)	(2.1948)	(.0853)
Size	-.0109	-.0095	-.0182	.0013
	(.0105)	(.0062)	(.0136)	(.0107)
Prof	-.5983***	-.4462***	-.3612***	-.4176***
	(.1083)	(.0234)	(.1270)	(.1159)
Tang	.2920	-.9752***	.6482	.2009
	(.3466)	(.2297)	(.4599)	(.4245)
MBR	-.1673***	-.0072	.1204**	-.0417
	(.0481)	(.0109)	(.0625)	(.0484)
Cons	1.0412***	-.1337	-1.1162	-.3613
	(.3444)	(.2745)	(.8106)	(.2704)
AR (1)	.000	.000	.000	.000
AR (2)	.413	.605	.208	.749
Sargan/Hansen	.670	.289	.707	.206
Instruments	203	193	177	193
No of groups	455	455	455	455

CONCLUSION AND IMPLEMENTATION

The study findings demonstrate that the earnings volatility moderates the relationship between leverage and classifications shifting earnings management. Specifically, high earnings volatility discourages the managers from engaging in classification shifting techniques to manipulate the earnings. This suggests the firms with substantial uncertainty in profits are less inclined to smooth or obscure the actual financial performance.

Several implications stem from these many results. Entrepreneurs operating high-growth ventures should be very cognizant that volatility in earnings, particularly when combined with high leverage, places a greater pressure on profit management activities. Maintaining realistic expectations around the volatile earnings is prudent. Additionally, establishing a strong governance and internal controls can help to deter aggressive earnings management and also preserve the credibility. Moreover, the skilled base entrepreneurship contributes towards the economic growth of the country (Kumar & Alwi, 2023).

Regulators may consider targeting the oversight efforts on firms exhibiting both earnings variability and high debt levels. Warning signs of classification shifting to meet the earnings targets should warrant scrutiny. Strict reporting requirements and penalties for any non- compliance can also be the solution to the discourage this behavior. However, room for judgment in the classifying expenses still exists, making detections very difficult.

Overall, these findings reinforce the need for diligence on the part of the managers, investors and the regulators when assessing the quality of the reported earnings. Transparency around the source of the profits, and discipline in the financial reporting, is vital. Continued research on the drivers and methods of earnings management will support the stakeholders in making informed assessments of the corporate financial health.

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