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RESEARCH ARTICLE

The effect of internal control and corporate social responsibility on conditional accounting conservatism: Evidence from France

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Abstract

This study examines the impact of internal control (IC) and corporate social responsibility (CSR) on conditional accounting conservatism (CAC). We employ legitimacy theory to understand whether managers adopt CSR reports and IC systems to seek legitimacy through symbolic actions or whether they do so to provide substantive actions to their stakeholders.

We adopt a multivariate analysis for a sample of 98 French companies belonging to the SBF 120 index during the period between 2012 and 2021. All accounting and stock market information is extracted from the Thomson Reuter database (Datastream) and the Thomson Reuters ASSET4 ESG database. We found that both IC and CSR have a negative and significant impact on CAC; hence, managers may use CAC levels as a legitimizing tool for corporate activities. French companies are generally characterized by strong IC systems, suggesting a low demand for conditional conservatism. Socially responsible companies may have fewer agency issues and therefore will not practice accounting conservatism (AC) in a pronounced way. Distinct from the previous literature, our study examines the impact of IC as well as CSR on CAC, which provides useful insights regarding how stakeholder pressure, in terms of reporting on social responsibility and maintaining effective control systems, interacts with and impacts upon managers' decisions to adopt CAC in the French context. Given the position of France after Brexit and the new laws adopted regarding an emphasis on the social dimension in corporate reporting, protecting stakeholders' interests, and adopting conservatism, it is worth using such a context to gain a better understanding of AC, as this will enrich the literature.

KEYWORDS

conditional conservatism, corporate social responsibility (CSR), generalized method of moments (GMM), legitimacy theory, internal control

1 | INTRODUCTION

Accounting conservatism (AC) stems from the implementation of accounting methods that result in an undervaluation of the book value and is defined as "asymmetric audit requirements for gains and losses" (Watts, 2003, p. 208). Since listed firms are more likely to announce positive rather than negative events, and investors are generally more sensitive to losses than to profits, AC helps investors to understand the negative functional developments of listed companies. Thus, AC plays a crucial role in enhancing the quality of information disclosure and investor protection by reducing agency problems (Shen et al., 2020).

AC has been examined in accounting literature. For instance, the relationship between AC and auditor tenure (Rickett et al., 2016); value relevance of earnings (Mostafa, 2017); female representation on the board of directors (Yousuf & Aldamen, 2021). AC is manifested in two general but distinct treatments. First, conservatism can be unconditional (ex ante or news independent), meaning that aspects of the accounting procedure determined at the start of assets and liabilities useful lives produce expected unrecorded goodwill (Beaver & Ryan, 2005). Second, conservatism can be conditional (ex post or news dependent), meaning the book value is written down under adverse circumstances but not written up under favorable circumstances (Beaver & Ryan, 2005). Conditional accounting conservatism (CAC) depends on both bad or good business news and reflects the speed at which bad news is integrated into accounting results as opposed to good news (Basu, 1997).We examine the effect of corporate social responsibility (CSR) and the internal control (IC) system on the level of AC. While both types of AC serve the same purposes, we use CAC; we argue that CAC best fits the study's objective. In particular, we investigate how business news is reflected in AC (Ball & Shivakumar, 2005); thus, the study examines the ex-post effect on AC, which depends on the adoption of CSR and IC.

Previous research suggests that the choice of AC level is shaped by corporate governance and, in particular, the IC system (Nikolaev, 2010). An effective IC system fosters a good culture of control that monitors management behavior and minimizes agency costs (Fama & Jensen, 1983; Jensen, 1993). Companies with a good IC system are more likely to perform prudent financial reporting (Goh & Li, 2011). In contrast, a weak IC system generates erroneous financial information and therefore cannot recognize the losses, which leads to less accounting prudence (Yin et al., 2020). Accounting literature has examined the relationship between IC and various themes, for instance, investors' reactions (Ittonen, 2010); operational efficiency (Shin & Park, 2020); firm effectiveness (Länsiluoto et al., 2016).Using a sample of companies that disclose material weaknesses in IC under SOX, Goh and Li (2011) examine the association between IC and conditional conservatism and find a positive relationship between IC quality and conservatism. Companies with material weaknesses exhibit lower conservatism than companies without such weaknesses. Companies that disclose material weaknesses and subsequently remediate these weaknesses exhibit greater conservatism than companies that continue to have material weaknesses. These results support that strong IC acts as a mechanism that facilitates conservatism. Yin et al. (2020) explore the relationship between CEO-board social ties and AC and find a negative relationship between CEO-board social ties and AC. This implies that more CEO-board social ties reduce the board's monitoring function and encourage the CEO's tendency to implement less conservative principles for their gains. A mediating impact of IC quality between CEO-board ties and AC was also found, implying that the IC system decided by the board could be the means via which CEOs implement less conservative principles.

In addition, there is a line of research that investigates the relationship between AC and CSR. Among the Fortune Global 250, the proportion of companies that issue CSR reports increased from 45% in 2002 to 92% in 2015; today, CSR reporting is a prominent business practice worldwide (KPMG, 2020).The literature suggests that managerial decisions, such as deciding the level of AC, are frequently affected by the adoption of CSR reports (Bae et al., 2011; Banerjee et al., 2008; Guo et al., 2020). The current empirical evidence regarding the impact of CSR on AC is mixed. While Cheng and Kung (2016) indicate that government-mandated CSR policy may be sufficient to promote conservative financial reporting, Cho et al. (2020) find that companies engaged in conservative financial reporting are less likely to reveal CSR information. Moreover, Burke et al. (2020) show a negative relationship between CSR performance and CAC. AC can facilitate social contracts in a world where corporate boundaries include implicit and explicit contracts with stakeholders. However, little research has examined whether companies who engage in CSR, to satisfy the wider groups of different stakeholders, use AC as a surety mechanism to mitigate the risk faced by stakeholders.

Given the mixed results regarding the effect of the adoption of CSR and IC systems on AC, little research has examined their relationships (Anagnostopoulou et al. 2020; Guo et al., 2020; Shen et al., 2020).We extend the AC literature by examining the effect of adopting both CSR and IC on CAC in the French context. EU reforms have led to major changes, especially in the accounting systems of countries including those of France, which are anchored in the accounting tradition. Previously, these countries favored the use of historical cost, a precept of AC, as a method for valuing assets and liabilities. However, with the emergence of fair value measurement, many criticisms of fair value measurement appeared relating to the increased volatility of fair value accounting measures and their consequences. This has prompted researchers to highlight the importance of conservatism and to explore the factors that influence the level of conservatism to restore this principle in accounting (Moy et al., 2020).

The French context constitutes an interesting field of investigation. France embodies the features of the accounting model of continental Europe, which is characterized by state control, uniformity, conservatism, and risk aversion. This is unlike Anglo-Saxon countries, which are characterized by high levels of professionalism, flexibility, and transparency. In addition, France is a unique context for current studies, as the role of France as a key financial hub in the EU has been magnified after Brexit. Many international companies have moved their headquarters to France and are currently listed on the Euronext Paris stock exchange. This contextual transformation will reveal useful insights regarding how CSR reporting and IC systems are constructed and, accordingly, how this impacts managers' adoption of AC.

Moreover, there is a set of theoretical lenses that have been employed within AC literature. For instance, stakeholder theory suggests that the degree of AC should increase with companies' efforts to improve their CSR and relationships with stakeholders because AC practices provide stakeholders with protection against risk (Titman, 1984). Alternatively, agency theory suggests that leaders engage in CSR to improve their reputation as socially responsible leaders (Bhandari & Javakhadze, 2017; Ferrell et al., 2016; Jensen & Meckling, 1976), implying an inverse relationship between commitment to CSR, stakeholder satisfaction, and AC. Furthermore, in terms of legitimacy theory (LT), AC can be used as a legitimizing tool to meet social contract obligations towards stakeholders by, for instance, minimizing financial risks. LT has been employed as a theoretical perspective in CSR and IC literature. Companies adopt IC systems to gain legitimacy through reporting CSR practices to reduce the legitimacy gap (Biggart, 1991). The main purpose of firms adopting CSR is to legitimize their activities so that their various stakeholders will have more confidence in them as a result of knowing that the CSR activities carried out by the firms are based on good IC practices (Stuebs& Sun, 2015).

Our motivation in conducting this research does not only apply to empirically examining the under-explored relationship between the adoption of CSR and IC systems and CAC; we aim to explore the theoretical foundations underpinning such relationships. We employ LT to understand whether managers adopt CSR reports and IC systems to seek legitimacy through symbolic actions or whether they do so to provide substantive actions to their stakeholders. Symbolic actions give managers the space to create "superficial impressions to project an appearance that the organizations' activities are consistent with social values and expectations" (Soobaroyen & Ntim, 2013, p. 95). However, managers also seek organizational legitimacy by adopting substantive actions that "involve a real, material change in organizational goals, structures, and processes or socially institutionalized practices" (Ashforth & Gibbs, 1990, p. 178). In terms of LT, we position CAC as a legitimizing tool; thus, if the adoption of CSR and IC results in a significant change in CAC, then managers are seeking legitimacy through substantive actions; otherwise, it is a symbolic action.

We argue that the LT lens also fits the French context. We use a sample of 98 French companies during the period between 2012 and 2021. This enables us to examine the level of CAC after Brexit and the introduction of the New Economic Regulations,[1] which put institutional pressure on French companies to release CSR reports and adopt effective IC systems. This enables us to understand whether French companies take action to implement real substantive changes by adopting CSR and IC practices or whether they act symbolically to gain legitimacy by merely following the regulations to meet their stakeholders' expectations without implementing real changes to their organizational structures.

This study's contributions are threefold. First, despite the abundant literature on IC, only a few studies examine the implications of IC for financial reporting. These studies mainly focus on the mediating effect of the quality of the IC system on the relationship between the CEO, the board, and AC (Yin et al., 2020) and the association between IC and conditional conservatism (Goh & Li, 2011; Ji et al., 2016). Distinct from the previous literature, our study examines the impact of IC as well as CSR on CAC, which provides useful insights regarding how stakeholder pressure, in terms of reporting on social responsibility and maintaining effective control systems, interacts with and impacts managers' decisions to adopt CAC. This leads to our second contribution: we explore the theoretical foundation of the relationship between CSR and IC on CAC which is, to our knowledge, not explored in the AC literature. To explore whether managers use CAC as symbolic or substantive action to legitimize stakeholders' pressures. A greater understanding of how managers react to laws and regulations at the country level in determining the level of

[1] The New Economic Regulations (NER) law adopted by the French parliament, which aims to emphasizeconsideration of the "ethical" aspect of financial reporting, also improves management controlling systems to protect the rights of various stakeholders.

CAC is our third contribution. There is a paucity, if not a complete lack, of studies that examine the effect of CSR and IC on CAC in the French context. Given the position of France after Brexit and the new laws adopted regarding an emphasis on the social dimension in corporate reporting, protecting stakeholders' interests, and adopting conservatism, it is worth using such a context to gain a better understanding of AC, as this will enrich the literature.

The findings of this research will arouse the interest of regulatory bodies and standard setters by providing them with information regarding the level of conservatism practiced by French companies after the introduction of international standards. In addition, this study will be useful to managers, as it provides information regarding the factors on which they can act to achieve the desired level of conservatism. We find that IC and CSR have a negative and significant impact on conditional conservatism. Our study provides investors with a basis for identifying the qualitative characteristics of companies' accounting and financial information. It offers a new way to assess the level of investor protection. CSR information is one of the types of non-financial information that complements the shortcomings of financial disclosure. Moreover, it reduces the asymmetry of information, and its quality can reflect the quality of financial information, which facilitates the assessment of users of accounting information and increases their ability to achieve financial accuracy to make optimal decisions. Both academic debates and corporate practices should take a more proactive rather than a defensive or reactive stance toward CSR. Indeed, corporate responsibility does not only consist of avoiding immoral practices (such as corruption, the falsification of balance sheets, etc.) but also of asking more specifically what contribution companies can make to society through good business practices.

The remaining part of this paper is structured as follows. Section 2 explains the study's theoretical perspective and presents a review of the literature, which discusses the main factors influencing the level of AC and details how the hypotheses are formulated. The third section explains the methodology adopted. The Section 4 discusses the results of the regression model related to the determinants of conditional conservatism. Finally, a conclusion is presented, and future avenues of research are suggested.

2 | THEORETICAL PERSPECTIVE AND HYPOTHESIS FORMULATION

2.1 | Theoretical perspective

LT is derived from the notion that there is a "social contract" between a company and the society in which it operates (Dowling & Pfeffer, 1975). Based on the social contract obligation, organizations try to avoid the "legitimacy gap," which might rise if the organizational practices do not meet the expectations of various stakeholders. Legitimacy is a "generalized perception or assumption that the actions of an entity are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs, and definitions" (Suchman, 1995, p.574). Thus, organizations provide explanations for their existence by enhancing their legitimacy (DiMaggio & Powell, 1983; Dowling & Pfeffer, 1975).

Suchman (1995) classifies legitimacy into two approaches: strategic legitimacy and institutional legitimacy. The strategic legitimacy approach presents legitimacy as an operational resource that managers extract from their cultural environments and use to support their goals (Ashforth & Gibbs, 1990). In that sense, managers seek legitimacy through *symbolic* actions (Soobaroyen & Ntim, 2013). Managers prefer the "flexibility and economy of symbolism" (Suchman, 1995, p. 579) over providing substantive actions to their audiences. Such symbolic actions create a space for managers in which they use "superficial impressions to project an appearance that the organization's activities are consistent with social values and expectations" (Soobaroyen & Ntim, 2013, p. 95).

However, the institutional legitimacy approach "downplay[s] both managerial agency and manager-stakeholder conflict" resulting from the fact that managers' strategies and actions should reflect the same values and expectations as those of the stakeholders (Suchman, 1995, p. 576). Thus, managers seek organizational legitimacy through adopting *substantive* actions "involv[ing] real, material change in organizational goals, structures, and processes or socially institutionalized practices" (Ashforth & Gibbs, 1990, p. 178). Organizations might change their goals and structures to meet the performance expectations of a set of stakeholders upon which they depend for critical resources (Ashforth & Gibbs, 1990). Suchman (1995) argues that if managers consider their audiences' interests as "products," they will feel that there is no need for real organizational change; thus, in such cases, management can act symbolically. However, if managers consider their audiences' interests as "producers" of the larger institutionalized cultural environment, then managers should adopt substantive outcomes.

We investigate whether managers adopt CSR and IC as symbolic actions without implementing significant corporate structural changes or whether managers believe that their adoption reflects the needs and expectations of stakeholders, thus driving managers to adopt real substantive changes. This can be achieved by assessing the impact of the adoption of CSR and IC practices on CAC. Do French companies seek legitimacy by applying rules, or do they believe in the embedded values and principles underlying these rules?

2.2 | The effect of IC on AC

To restore investors' confidence in financial reports, the Sarbanes-Oxley Act 2002 (SOX) requires companies to assess and report on their IC and auditors to certify the effectiveness of IC systems. Regulators set these requirements to improve the quality of IC systems and enhance the reliability of financial reports (Schantl & Wagenhofer, 2020). An effective IC system can improve the quality of financial reports (Ashbaugh-Skaife et al. 2008; Doyle et al., 2007). Confirming that a weak system of IC leads to errors in financial reporting, Feng et al. (2009) find a positive relationship between the quality of IC and the accuracy of management guidance. The other principle that enhances financial reporting quality and helps mitigate agency conflicts is AC (Ball & Shivakumar, 2005; Watts, 2003). The reasoning is that conservatism reduces managers' incentives to overstate profits and assets by reducing their ability to withhold information about losses. Therefore, prior studies suggest that the incentives for prudent information are shaped by the governance of a company (Ball & Shivakumar, 2005; Ball et al., 2000; LaFond & Roychowdhury, 2008; Nikolaev, 2010). Since the IC system is an important governance mechanism within a company, it could monitor the behavior of managers and minimize agency costs (Fama & Jensen, 1983; Jensen, 1993). Moreover, Ewert and Wagenhofer (2020) support the other direction of the relationship; namely, that a prudent accounting system increases the investment of managers in IC to improve accounting quality. Adding to the complexity of the debate, regulators and standard-setters do not necessarily view AC as a desirable attribute of financial reports. According to the International Accounting Standards Board's (IASB) conceptual framework, conservatism is not a qualitative feature of accounting information. This framework specifies that accounting information must be impartial; the absence of bias is an essential characteristic of neutrality and reliability. However, AC allows for the deliberate underestimation of income or assets and/or the deliberate overestimation of charges or liabilities, making financial statements non-neutral and, therefore, compromising the qualities of impartiality and reliability. Consistent with this perspective, the Financial Accounting Standards Board (FASB) states that users' interests are best served by neutral reports accompanied by the convenient disclosure to shareholders of the extentof uncertainty about transactions referred to the shareholders. The FASB focuses on fair value accounting as a means of reducing the asymmetric treatment of good and bad news.

Even though researchers have studied the relationship between IC and AC, conflicting results have been reported. While Ji et al. (2016) show that the existence of IC weaknesses has a negative effect on AC in Chinese-listed companies, Mitra et al. (2013) show that companies that disclose IC weaknesses exhibit greater AC in the post-SOX period compared to firms with a good IC system and that companies with IC weaknesses have changed their practice of engaging in prudent reporting during the pre- to post-SOX period.

Conservative accounting limits the control rights of managers. For example, in the context of a loan contract, conservatism reduces the ability of managers to avoid restrictions on dividends and transfer wealth from holders to shareholders, thereby mitigating losses and increasing company value (Ahmed et al., 2002; Zhang, 2008).Ahmed et al. (2002) argue that conservatism is evolving as an effective mechanism to mitigate dividend policy and find that the more serious these conflicts, the more accounting choices are conservative. Additionally, Ball and Shivakumar (2005) document that private companies are less conservative than public companies, attributing this result in part to the differences in control and governance mechanisms between these two types of companies. This is in line with LaFond and Roychowdhury (2008), who find that when managerial ownership is low, the severity of the agency problem increases, leading to a demand for more AC.

Arguably, a good system of IC could create an incentive to produce conservative financial reports. Therefore, companies with an effective board of directors that promotes a good culture of IC can encourage the production of conservative financial reporting to provide relevant and reliable accounting information (Goh & Li, 2011). Thus, we can argue that a good system of IC can encourage companies to use conservatism as an effective governance mechanism. Weaknesses in IC could prevent the timely recognition of losses, thus leading to a decrease in AC. For example, the lack of proper procedures and policies for valuing fixed assets or inventories prevents early detection of the impairment of assets and therefore delays the recognition of losses. Unqualified personnel lack the experience to identify any reduction in cash flow, which will lead to early recognition of losses. Similarly, in monitoring investment decisions, the existence of IC weaknesses may encourage managers to avoid the timely recognition of losses (Goh & Li, 2011). In addition, weaknesses in the control of the present value of benefits calculations may ensure that loss-making projects are not discovered and terminated quickly (Goh & Li, 2011). Thus, a good IC system will promote AC. Therefore, IC weakness can influence the level of AC. Based on what has been put forward in existing studies, we propose to test the following hypothesis:

Hypothesis 1: IC has a negative impact on AC.

2.3 | The effect of CSR on AC

A prudent financial report is consistent with promoting stakeholder interests, as this position reduces information asymmetry, helps align management's interests with stakeholders, and alleviates agency issues. Previous research suggests that CSR management is committed to increasing accountability and transparency for stakeholders while the company is engaged in its institutional role of creating value for shareholders (Bozzolan et al., 2015), which accounting conservative promotes. Conflicts of interest between the company and stakeholders are linked to a misleading picture of the financial situation. For example, WorldCom overestimated its profits by incorrectly classifying expenses as investments, against conservatism, thereby causing serious CSR harm not only to WorldCom stakeholders. Likewise, Enron used its entities to present an upward-biased assessment of its financial position by removing debt from its balance sheet, resulting in collapse and bankruptcy. Therefore, stakeholder theory, among ethical and instrumental theories of CSR, suggests that managers are encouraged to be ethical, honest, and trustworthy, and to adhere to high CSR standards in their business processes (Kim et al., 2012) and predicts that managers are incentivized to be conservative (Carroll, 1979; Jones, 1995), since maintaining a good relationship with stakeholders is essential for a company's success (Caplan et al., 2013; Titman, 1984).

Previous research suggests that AC, which encourages prudence in the recognition of assets and income, may benefit stakeholders and reduce the risks they face.AC constrains opportunistic management behavior and improves the efficiency of contracts (Watts, 2003; Watts & Zimmerman, 1986).Since stakeholders bear a substantial risk due to excessive information about accounting, conservatism protects against risk by declaring a verifiable lower bound on the company's results and assets. Conservatism allows the company to underestimate book value over market value, thus creating lower book-to-market ratios (Beaver & Ryan, 2000). Prudent financial reporting mitigates the risk of firm performance accounting measures significantly exceeding the company's cash flow from operations (Givoly & Hayn, 2000). In addition, conservatism helps to inform pressure profits through the choice of accounting methods and inventory estimates, advertising spending, and R&D investments that result in a relatively lower book value of pure assets and higher costs (Penman & Zhang, 2002). AC benefits lenders by underestimating assets and provides signals of standard risk (Zhang, 2008). In addition, AC can benefit stakeholders by reducing the risk of bankruptcy through mitigating earnings management (Biddle et al., 2022).

Previous studies have investigated the relationship between CSR and AC and reported contradictory results. For example, Guo et al. (2020) find a significant and positive relationship between CSR and AC, suggesting that socially responsible companies exhibit more AC compared to non-CSR companies, inconsistence with the stakeholder theory. Using a sample of Chinese companies, Shen et al. (2020) find a positive relationship between CSR and AC. In contrast, Anagnostopoulou et al. (2020) suggest that higher conservatism levels are negatively related to CSR. Similarly, using a sample of Korean companies, Hong (2020) shows that a higher ESG rating reduces AC.

Conservatism can be induced by a company's efforts to build relationships with stakeholders, as evidenced by its commitment to CSR. As companies allocate resources for stakeholder management to act in the interests of stakeholders, companies engaged in CSR should be more likely to place a lower limit on profits and net assets via AC compared to their non-socially responsible counterparts. This suggests that CSR-oriented companies use AC as a governance mechanism to improve stakeholder benefits. Therefore, consistent with stakeholder theory, we predict that CSR-oriented companies are more likely to behave cautiously in financial reporting (Guo et al., 2020). Therefore, in our research, we assume that CSR has a negative effect on AC, making the following hypothesis:

Hypothesis 2: CSR has a negative impact on AC.

3 | RESEARCH METHODOLOGY

This section is dedicated to presenting the sample studied, data collection, variable measurements used, and the model specifications.

3.1 | Sample selection

The study is carried out using a sample of French listed companies listed in the SBF 120 index over a period of ten years, from 2012 to 2021. The choice of this index is justified by its representativeness and the broad, faithful, and diversified vision of the market offered by the SBF 120, which allows us to obtain a sufficiently large population to allow for statistical tests to be carried out. The study period begins from the date of the adoption of the

Grenelle II law, which came into force in 2012, to avoid any kind of controversy concerning the level of conservatism after the adoption of the new economic regulations. We remove financial and real estate companies from the initial population because of sector specificities and the accounting regime of credit institutions. Thus, the final sample is made up of 98 companies covering a period of 10 years: a total of 980 observations. All accounting and stock market information is extracted from the Thomson Reuter database (Datastream) and the Thomson Reuters ASSET4 ESG database.

3.2 | Variable measurements

3.2.1 | The dependent variable: AC

A literature review on the measurement of conservatism identifies five main measures (Wang et al., 2008). Stober (1996) introduced the market-to-book (MTB) measure to assess the level of conservatism. Basu (1997) emphasized the asymmetric recognition of gains and losses. Penman and Zhang (2002) looked at the measurement of occult reserves, and Givoly and Hayn (2002) analyzed the measurement of negative accruals. Ball and Shivakumar (2005) propose a measure based on the same fundamental idea as the measure introduced by Basu, that of the asymmetric recognition of losses and gains. In addition, Khan and Watts (2009) estimate the regression of Basu (1997) and consider the coefficient of Basu as a linear function of the characteristics specific to the company; namely, its size, MTB ratio, and debt.

The measure of conservatism proposed by Basu (1997) has formed the basis of various studies that assess the level of conservatism (Anagnostopoulou et al. 2020; Ball et al., 2000; Givoly and Hayn, 2000; Hong, 2020; Mitra et al., 2013; Moy et al., 2020; Shen et al., 2020; Yin et al., 2020). It is considered the most popular measure in the accounting literature (Ryan, 2006; Wang et al., 2008). However, it has always been criticized on the pretext that there are econometric biases (Dietrich et al. 2007; Patatoukas & Thomas, 2011). In addition, the use of stock price variation to determine good and bad news is a limitation of this model (Givoly & Hayn, 2000). This measure, and the criticisms it has attracted, have catalyzed the evolution of research (Ball & Shivakumar, 2005; Khan & Watts, 2009; Penman & Zhang, 2002). However, the models developed are not exempt from weaknesses. Thus, Ryan (2006) questions the usefulness of measuring the accumulation of negative accruals (Givoly & Hayn, 2002) and the MTB ratio (Stober, 1996) to assess conditional conservatism, given that they are used to assess conservatism globally. In addition, although it can be used to measure the degree of conservatism in a company, it requires several items which are generally unavailable. Therefore, due to the unavailability of the stock market returns of all the companies belonging to the SBF 120 index since 2005 and the insignificance of the model of Basu (1997), we base our study on the model by Ball and Shivakumar (2005), which draws heavily on Basu's (1997) model. This measurement is a valid representation of the levels of conditional conservatism in accounting income and is unbiased (Wang et al., 2008). This measure was used by Goh & Li (2011) and Mitra et al. (2013).

The measure developed by Ball and Shivakumar (2005) is based on the same idea as the model of Basu (1997), that of the asymmetric recognition of profits and losses. The main difference is in the measurement of news. Basu's model chooses stock returns as an indicator of news, while Ball and Shivakumar use operating cash flow as a measure of news. As a result, this model is suitable even for unlisted companies, since they do not have information on stock prices and therefore on returns. Ball and Shivakumar (2005) argue that accruals do not only play this role; they are also used to incorporate good and bad news into outcomes on time. In this sense, Ball et al. (2000) argue that accruals recognize bad news and incorporate it into current profits. To estimate the total accruals, we base ourselves on the modified model of Jones (1995) adjusted by a performance indicator; namely, the return on assets (Kothari et al., 2005).This model makes it possible to clarify the two roles associated with accruals: noise attenuation in cash flows and the asymmetric recognition of unrealized gains and losses. The model is formulated as follows:

$$\mathrm{TACC}_{it} = \beta_0 + \beta_1 \mathrm{DCFO}_{it} + \beta_2 \mathrm{CFO}_{it} + \beta_3 \mathrm{CFO}_{it} * \mathrm{DCFO}_{it} + \varepsilon_{it}$$

$\mathrm{TACC}_{i,t}$: the total accruals standardized by the total assets for the year (t–1) estimated from the results management measurement model. $\mathrm{DCFO}_{i,t}$: a binary variable equal to 1 if operating cash flows are negative, and 0 otherwise. The integration of this variable is used to separate the good news from the bad news. $\mathrm{CFO}_{i,t}$: cash flow from operating activities standardized by total assets for the year (t–1). The coefficient β_3 provides information on the level of conservatism. Thus, the higher the coefficient β_3, the higher the degree of AC.

3.2.2 | Measurement of independent and control variables

IC is adummy variable coded 1 if the company discloses information on IC weaknesses, and 0 otherwise (Boulhaga et al., 2022; Goh & Li, 2011); data on IC weaknesses were collected manually from financial reports and reference documents published on the French listed companies' websites (Ji et al., 2016). CSRis measured by the ESG score retrieved from Thomson Reuters ASSET4 ESG (Boulhaga et al., 2022; Lahouel et al., 2019; Yang & Baasandorj, 2017).Company size corresponds to the logarithm of total assets (Anagnostopoulou et al. 2020; Goh & Li, 2011; Guo et al., 2020; Mitra et al., 2013). LEV is measured by the ratio of long-term debt deflated by total assets (Hong, 2020; Mitra et al., 2013; Shen et al., 2020). ROA is calculated by the ratio (net income to total assets) (Yin et al., 2020). MTB corresponds to the ratio between the market value and the book value of the shares (Mitra et al., 2013; Shen et al.2020). CFO is the ratio of cash flow from operating activities to total assets (Goh & Li, 2011; Guo et al., 2020; Hong, 2020; Mitra et al., 2013). BIG Fouris a binary variable coded 1 if the company is audited by at least one firm belonging to the BIG Four network (Anagnostopoulou et al. 2020; Chouaibi & Boulhaga, 2020; Guo et al., 2020; Shen et al., 2020).

3.3 | Model specification

In this study of the French context, we are interested in certain organizational factors explaining the inter-company disparities in the level of conservatism. The developed model is as follows:

$$\begin{aligned} \mathrm{CONSERV}_{it} &= \beta_0 + \beta_1 \mathrm{IC}_{it} + \beta_2 \mathrm{FSIZE}_{it} + \beta_3 \mathrm{LEV}_{it} \\ &+ \beta_4 \mathrm{ROA}_{it} + \beta_5 \mathrm{CFO}_{it} + \beta_6 \mathrm{MTB}_{it} + \beta_7 \mathrm{AUDTQ}_{it} \\ &+ \beta_8 \sum \mathrm{Industry}_{it} + \beta_9 \sum \mathrm{YEAR}_{it} + \varepsilon_{it} \end{aligned} \tag{1}$$

$$\begin{aligned} \mathrm{CONSERV}_{it} &= \beta_0 + \beta_1 \mathrm{CSR}_{it} + \beta_2 \mathrm{FSIZE}_{it} + \beta_3 \mathrm{LEV}_{it} \\ &+ \beta_4 \mathrm{ROA}_{it} + \beta_5 \mathrm{CFO}_{it} + \beta_6 \mathrm{MTB}_{it} + \beta_7 \mathrm{AUDTQ}_{it} \\ &+ \beta_8 \sum \mathrm{Industry}_{it} + \beta_9 \sum \mathrm{YEAR}_{it} + \varepsilon_{it} \end{aligned} \tag{2}$$

CONSERV: a measure of CAC (estimated from the model of Ball & Shivakumar, 2005); IC: dummy variable coded 1 if the firm discloses information on IC weaknesses, and 0 otherwise; CSR is measured by ESG score; SIZE corresponds to the logarithm of total assets (TA) for year t; LEV is measured by the long-term debt/total assets ratio; ROA is calculated by the ratio (net income to total assets); CFO is the ratio of cash flow from operating activities to total assets; MTB corresponds to the ratio between the market value and the book value of the shares; BIG4 is a variable which takes the value 1 if the company is audited by at least one firm belonging to the BIG Four network. To capture possible impacts related to the industry and the year, industry and year dummies are incorporated. $\beta\_0 \rightarrow \beta\_9$: parameters to be estimated; ε_{it}: error term.

4 | RESULTS AND INTERPRETATIONS

This part is dedicated to the presentation of the results of statistical processing. First, we focus on the descriptive statistics of the model, then we present the analysis of the correlations between the variables and finish with the results of the regression model.

4.1 | Descriptive statistics

The analysis of the descriptive statistics of our sample (Table 1) reveals the following salient points: the mean value and the standard deviation of the level of CAC are almost equal to the respective values of .095 and .264. The level of conservatism peaks at a value of .993. Regarding the independent variables, the average IC weaknesses of the firms in our sample are about .687. The results also show that, on average, CSR is 56.951.

As for the control variables, companies have an average size of around 15.953 employees. We find that the average debt ratio is 25.96%, which shows that the weight of

TABLE 1 Descriptive statistics

Variables	*N*	Average	Standard deviation	Minimum	Maximum
CONSERV	980	.095	.264	–.252	.993
IC	980	.687	.463	0	1
CSR	980	56.951	27.964	12.77	93.68
FSIZE	980	15.953	1.942	9.964	19.699
LEV	980	.259	.156	.0002	.804
ROA	980	.014	.470	–.221	.702
CFO	980	.084	.126	–.795	2.152
MTB	980	2.435	3.200	–28.61	35.78
AUDTQ	980	.9612	.193	0	1

TABLE 2 Pearson Correlations and VIF Test

	CONSER	IC	CSR	FSIZE	LEV	ROA	CFO	MTB	AUDTQ	VIF
CONSERV	1.000									
L.CONSER	.406***									
IC	−.162***	1.000								1.13
CSR	−.217***	.307***	1.000							1.45
FSIZE	.158***	.128***	.463***	1.000						1.38
LEV	.081**	−.0006	−.095***	.155***	1.000					1.11
ROA	.084***	.147***	.116***	−.026	−.181***	1.000				1.17
CFO	−.102***	.088***	.064**	.043	−.125***	.256***	1.000			1.09
MTB	−.085***	.020	.033	−.123***	−.147***	.235***	.112***	1.000		1.08
AUDTQ	−.007	.081***	.128***	.148***	.017	−.021	.053*	.023	1.000	1.04

*, **, *** significant relationship at the 10%, 5%, and 1% threshold.

long-term financing is quite low for all the companies constituting our sample. The economic profitability is equal, on average, to .014. We also note that the companies have an average MTB ratio of 2.43, while the average (CFO/TA) ratio is 8.42%. Finally, we note that 96.12% of the companies in our sample choose a BIG Four firm to perform the audit mission.

4.2 | Verification of the absence of the multicollinearity problem between the explanatory variables: Correlation matrix and the VIF test

Table 2 presents the correlation matrix between the variables tested in the model. The correlation matrix indicates that most variables are related to each other in a significant way. The SIZE variable, for example, is significantly correlated at the 1% level with all the variables in the model. The CSR variable also shows a significant correlation with all the variables, except with the variablesROA and CFO. However, the intensity of these correlations is not considered excessive since the correlation coefficients do not exceed .8.To further ensure the absence of multicollinearity, we performed a multicollinearity diagnosis via STATA using the Variance Inflation Factor (VIF) (an indicator of the proportion of variance of each independent variable explained by all the other variables). From Table 2, we notice that the VIF does not exceed 10, which leads us to conclude that there are no significant multicollinearity issues.

4.3 | Multivariate analyses

We have established evidence that socially responsible companies are more likely to be conservative in their financial reporting. In this section, we examine the relationship between IC, CSR, and CAC in a multivariate setting. We employ the proxy of CAC from the model of Ball and Shivakumar (2005) in the empirical analysis. Table 3 shows the regression results of the relationship between internal control, CSR, and CAC as the dependent variables.Consistent with Goh and Li (2011), we use the dichotomous variable of internal control weaknesses (ICW). We also use CSR scores from the Thomson Reuters ASSET 4 Database (Lahouel et al., 2019; Yang & Baasandorj, 2017). We control for industry and year-fixed effects in all regression models.

From Table 3 (Model 1), we notice that the calculated F (28.79) is statistically very significant (Sig. = .00 < 5%), which makes it possible to reject the null hypothesis of the absence of the effect of explanatory variables on the endogenous variable. The model is therefore globally significant. In Model 1, we find that the coefficient on ICW is −.057, suggesting that the companies withICWs exhibit lower conservatism. Model 2 relates to CSR and CAC. Consistent with our findings from Model 1, we report that the coefficient on CSR is negatively related to this CAC measure at the 1% level of statistical significance.

4.4 | Additional robustness analysis

To ensure the robustness of our empirical results, we use the GMM method.Traditional methods; for example, OLS and fixed effect, do not allow unbiased estimates of such a model to be obtained.This method provides solutions to the problems of reverse causality, simultaneity bias, and possible omitted variables. In addition, it allowsus to control for specific temporal and individual effects and to reduce endogeneity biases. This is achieved using STATA.

The Sargan test and the Arellano-Bond test (AR2) are the most important criteria for validating our estimates. According to Sargan's test (Table 4, Model 1), the probability is .000—less than 5%—so the null hypothesis of

TABLE 3 Results of OLS regression

	Model 1. Internal control and CAC			Model 2. CSR and CAC		
	Coeff.	t-stat.	Prob.	Coeff.	t-stat.	Prob.
ICW	−.0574	−3.03	.003			
CSR				−.0013	−3.78	.000
FSIZE	.0165	3.46	.001	.0088	1.67	.096
LEV	.0880	1.57	.116	.1177	2.09	.037
ROA	.0047	2.61	.009	.0048	2.69	.007
CFO	−.2308	−3.46	.001	−.2276	−3.43	.001
MTB	−.0052	−1.99	.047	−.0058	−2.22	.027
AUDTQ	−.0390	−.88	.381	−.0406	−.92	.360
Constant	−.1909	−2.32	.021	−.1097	−1.30	.194
Industry	Yes			Yes		
Year	Yes			Yes		
F statistic	28.79			29.59		
Prob (F)	.0000			.0000		
R^2	.2093			.2139		
R^2 adjusted	.2021			.2066		
Durbin- watson stat	1.5378			1.5397		
Observations	980			980		

TABLE 4 System GMM regression of the effect of IC and CSR on CAC

	Model 1. IC and CAC			Model 2. CSR and CAC		
	Coeff.	t-stat	Sig	Coeff.	t-stat	Sig
L. CONSERV	.4238	79.96	.000	.4148	32.72	.000
ICW	−.0518	−38.18	.000			
CSR				−.0012	−36.60	.000
FSIZE	.0256	56.25	.000	.0118	16.57	.000
LEV	−.0142	−2.15	.034	.0719	5.09	.000
ROA	.0044	17.12	.000	.0047	17.46	.000
CFO	−.2454	−45.66	.000	−.2269	−17.00	.000
MTB	−.0045	−31.40	.000	−.0063	−23.24	.000
AUDTQ	−.0055	−.34	.732	−.0272	−2.02	.046
Constant	−.3398	−18.80	.000	−.1558	−7.58	.000
Industry	Yes			Yes		
Year	Yes			Yes		
Arellano-Bond test AR(1) (z, *p*-value)		−5.08	.000		−5.08	.000
Arellano-Bond test AR(2) (z, *p*-value)		1.19	.234		1.50	.135
Sargan test (Chi-square, *p*-value)		712.70	.000		713.53	.000

uncorrelation is rejected. Moreover, according to Table 4, we note that there is no second-order autocorrelation.The probability of the Arellano and Bond test (AR2) is equal to .234, whichdoes not allow us to reject the null hypothesis. Table 4 shows the results of the system GMM regression.

We find that the coefficient of the IC variable is negative ($\beta_1 = -.051$) and significant ($p = .00 < 5\%$), which means that IC has a negative and significant impact on CAC. This could be interpreted as evidence of the fact that the French companies are more mature and have rich information and are therefore characterized by lower information asymmetry, suggesting a decrease in the demand for conditional conservatism. This result confirms the results found in the research work of Ji et al. (2016), who found that IC has a negative impact on AC. Goh and Li (2011) indicate that companies with material IC deficiencies exhibit lower AC compared with companies with no such deficiencies and that the subsequent remediation of IC weaknesses leads to greater conservatism. Their results demonstrate that effective IC leads to the adoption of a reporting strategy that is based on more conservatism andthat IC quality facilitates AC. Furthermore, Mitra et al. (2013) show that higher post-SOX regulatory scrutiny and increased firm oversight collectively affect companies' IC weaknesses and their inclination to adopt a more conservative financial reporting strategy. The use of more conservatism could be a part of their total effort to reduce the risk of inaccurate reports, improve the reliability of financial reporting, and promote contracting efficiency.

Regarding CSR, the coefficient is negative (–.001) and significant ($p = .000$), which means that socially responsible companies do not practice AC in a pronounced way.CSR engagement helps improve companies' information environment and reduce information asymmetry between the company and investors (Cho et al., 2013; Cui et al. 2018). Since information asymmetry also generates demand for conditional AC (LaFond & Watts, 2008), a company with stronger CSR performance will likely face lower demand for CAC as well. This result is consistent with that of the study by Anagnostopoulou et al. (2020), which found a negative relationship between conditional conservatism and CSR. Conversely, our results contradict the results found in the research work of Guo et al. (2020), who state that socially responsible companies exhibit more AC than their non-CSR companies, which is consistent with stakeholder theory. Likewise, Shen et al. (2020) find a positive association between CSR and AC. The mixed empirical results can be explained by the failure to consider the endogeneity problem (Lahouel et al., 2019). It is for this reason that the GMM method is necessary to remedy the endogeneity biases of the variables. If companies engage in stakeholder relationships in anattempt to cover up their selfish policies, CSR companies are less likely to disclose conservative accounting information, thereby gaining an informational advantage over their stakeholders. Previous research (Francis et al., 2013; Ramalingegowda & Yu, 2012) suggests that conservatism could be seen as a governance mechanism that alleviates agency problems and information risk. If CSR takes stakeholder orientation into account, a stakeholder-oriented business may have fewer agency issues and, as a result, shareholders may require less record keeping. This perspective suggests that social responsibility is negatively associated with AC.

These results suggest that strengthening corporate oversight and control has prompted companies with weaknesses in IC to use more ACto reduce uncertainty in financial reporting, improve the reliability of the information, and improve the efficiency of contracts.Integrating CSR into control processes and decision-making can improve the competitiveness of the firm, protect itsbrand image, and help it achieve continued profitability, thus ensuring the sustainability of the firm. The establishment of an IC system makes it possible to improve the efficiency of financial decision-making and avoid risks. Thus, companies facing higher market risk can provide more conditional conservatism to mitigate that risk.

5 | CONCLUSION

After years of applying international standards, the issue of prudence has become relevant, as the producers of financial statements regularly complain about the backlash associated with fair value measurement. Therefore, some researchers have focused on studying the determinants of conservatism to take action on it; they have shown that there are four main factors triggering conservatism; namely, contracts, the likelihood of litigation, the tax system, and regulation (Ball & Shivakumar, 2005; Watts, 2003). The objective of this paper is to broaden these studies and identify the factors that influence the level of CAC in the French context. The objective is to study the impact of IC, as well as the social responsibility of companies, on the level of conditional conservatism. Using a sample made up of 98 French firms belonging to the SBF 120 index, we have identified the factors responsible for the decrease in the level of conditional conservatism. The robustness of the results is checked through GMM regression.

Our results show that increased attention from analysts and investors on companies offering high-quality CSR information is the main factor driving companies to choose prudent accounting methods. Also, our results provide a possible direction for further research. Our results have important implications for corporate governance. We have found that IC and CSR can significantly reduce CAC. Therefore, to encourage AC, companies need to improve the quality of their IC. One way to improve the quality of IC, as our findings suggest, is to integrate CSR into the control process. In terms of LT, CSR, and the IC structure are consideredsubstantive actions that result in a significant changeconcerning the adoption ofCAC. We argue that French companies gain legitimacy bydisclosing informative corporate social reports and implementing effective IC structures; as a result, such companies tend to be less likely to adopt CAC. In the French context, companies do not consider adopting CSR and IC as a symbolic practice; rather, doing so is a substantivepractice that has real accounting and reporting implications, such as reducing the adoption of CAC.

The results of this research have some practical implications that could guide policymakers, managers, and stakeholders concerning CSR disclosure and IC. Policymakers should devise a measurement of CSR disclosure that can be used to control and regulate it, as this will enhance the association between market equity and accounting information. The building of CSR is crucial to the success of future reforms to improve investor protection, market efficiency, and social activities. Managers should maintain and develop high-quality CSR that provides a general framework for integrating CSR activities and initiatives into financial reports. Stakeholders are interested in the more reliable and relevant information. Therefore, regulators should use CSR practices as guidelines to improve the quality of financial reporting to enhance the allocation of resources in markets.

While our results contribute to the literature on the determinants of AC in the French context, our study has certain limitations. Although the sample is relatively large, it does not cover the entire French market, as it does not include financial firms and companies with missing data. Also, the application of the model of Ball and Shivakumar (2005) to measure AC is in itself a limitation; it is advisable to use several measures of AC. Moreover, this paperis not an exhaustive analysis of the various determinants of conditional conservatism. We propose that others should study the impact of certain organizational characteristics such as the sector of activity, the ownership structure, and the impact of certain governance mechanisms on conditional conservatism.

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