

Factors That Influence CEO Narcissism on Financial Statement



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ABSTRACT: This study aims to empirically examine the effect of CEO narcissism on the disclosure of Environment, Social, and Governance (ESG) by companies. CEO narcissism was measured using an unobtrusive indicator and ESG disclosure was measured by an ESG score from the Thomson Reuters database. The test was carried out on 100 samples of non-financial companies in 10 ASEAN companies obtained through purposive sampling technique with the research period 2019-2021. Observation points in this study amounted to 400 years of the company. The results showed that the CEO's narcissism had a positive effect on ESG disclosure.

KEYWORDS: Narcissism, CEO, Financial statement

I. INTRODUCTION

Chief Executive Officers (CEOs) hold top positions in the company's management and are responsible for the operations and performance of the company (Harymawan., et al, 2019). Companies recruit CEOs based on their expertise, experience, and ability to create shareholder value, this is because CEOs play an important role in guiding and directing the success of their companies (Field et al., 2013; Mendez et al., 2013). The benchmark for the company's success can be seen from the company's performance. According to Helfert (1996) company performance is the result of many individual decisions made continuously by management. In the accrual basis process, it allows management behavior to manipulate earnings or earnings management in order to increase or decrease the accrual number in the income statement.

Several studies have shown that CEO narcissism can encourage unethical actions in companies. Craig and Armenic (2011) say that destructive narcissism is recognized as one of the factors that causes a decline in the value of good corporate leadership and the company's code of ethics. Unethical behavior tends to occur when a leader with destructive narcissism holds power in an organization (Godkin and Allcorn, 2011). Furthermore, Chatterjee and Hambrick (2007) say that narcissistic leaders can have a negative effect on organizational health. Narcissistic CEOs tend to make aggressive and risky decisions, and engage in ethically questionable business practices (Armenic and Craig, 2010).

Narcissistic CEOs believe that their abilities will always have a positive impact on the performance of the companies they lead (Ingersol et al., 2017). Companies led by narcissistic CEOs tend to use accounting methods unethically to improve company performance, manipulate taxes, and increase CEO compensation (Armenic and Craig, 2010; Olsen et al., 2013; 2015). Research conducted by Rijsenbilt and Commandeur (2013) proves that narcissism to commit fraud within the company.

Company size is important in the financial reporting process. The size of the company in this study is measured by looking at how much assets are owned by a company. Research conducted by Wright et.al. (2009) found that firm size has a positive effect on performance. The company's performance will be good if the company is able to control the behavior of the company's top executives to protect the interests of company owners (shareholders), one of which is the existence of an audit committee. This is supported by the research of Siallagan and Machfoedz (2006).

Profit is one of the benchmarks used in assessing company performance by users of financial statements. This is in line with Statement of Financial Accounting Concepts (SFAC) No.1 (1987) (Belkoui, 2011) that earnings information material is the main concern for assessing performance or management accountability. Responsibility arises because narcissism can affect cooperation, trust, risk taking, motivation, decision making, and long-term performance (Campbell et al. 2004, Judge et al. 2006). Concurrent research has begun to explore the impact of personality traits such as narcissism on the potential for

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incorrect financial reporting (Hobson and Resutek 2008; Schrand and Zechman 2012) so that based on these results it can be said that the influence of narcissism on CEO decisions, behavior, and motivation can be an important consideration.

Currently, narcissism has been accepted as a personality trait shared by all individuals (Vazire & Funder, 2006). Emmons (1984) states that narcissism is indeed observed in almost all CEOs of large corporations, so that it is in the top half of the graph of the narcissistic tendencies population. This implies that CEOs in large companies are almost all observed to have this narcissism trait. Thus, narcissism has attracted the attention of researchers and the general public, so it is often used as a key characteristic in explaining CEO behavior (Chatterjee & Hambrick, 2007). Thus, this is the background of this study to empirically prove the effect of a CEO's narcissism on the company's ESG disclosures.

II. LITERATURE REVIEW

2.1. CEO Narcissism

Based on the original concept, psychologists generally regard narcissism as a relatively stable personality trait (Campbell et al., 2005) characterized by a sense of personal superiority (Campbell et al., 2004), grandiosity (Morf & Rhodewalt, 2001), dominance and desire for power (Emmons, 1984), as well as the desire to be noticed and affirmed for their superiority (Bogart et al., 2004). This narcissism can be a significant psychological attribute related to CEO decision-making behavior (Kim et al., 2018). The use of CEO narcissism as a formal construct to explain company strategy and performance is based on Upper Echelon Theory. According to Emmons (1984) narcissism can be observed in almost all CEOs in large companies. It has attracted much attention from the public and researchers, and is often used as a key characteristic in explaining behavior of CEOs (Chatterjee & Hambrick, 2007), which this behavior can be a factor influencing decision making in companies (Campbell et al., 2011), which in this case is the company's decision regarding ESG disclosure.

2.2. Environmental, Social, and Governance (ESG) Disclosures

ESG disclosure is measured using three disclosure indicators, namely, environmental disclosure, social disclosure, and corporate governance disclosure (de Villiers et al., 2017). The measurement for the three ESG disclosure indicators can be seen through the ESG Score provided by Thomson Reuters. The ESG Score can be used to measure ESG disclosure because the score is obtained based on data disclosed by the company in a transparent and objective manner. This indicates that the ESG Score of each company's profit is based on the disclosures made by the company regarding its social, environmental, and corporate governance responsibilities, be it through annual reports, each company's website, non-profit organization (NGO) websites, Stock Exchange Filing, CSR reports, and mass media. This indicates that measuring the company's ESG disclosure using the ESG score on Thomson Reuters is the right decision because the disclosures seen are not only limited to annual reports or sustainability reports. In addition, Thomson Reuters uses more than 400 enterprise-level ESG measurements. Then selected subgroups of 178 fields that are most comparable and relevant to strengthen the assessment and scoring process for each company as a whole. This process is based on considerations of comparability, data availability and industry relevance. In addition to the ESG score, Thomson Reuters also presents ESG Controversy Score data calculated based on 23 ESG controversy topics. Throughout the year, if a scandal occurs, the company involved in the scandal will be subject to legal sanctions. This causes an adjustment between the ESG score and the ESG Controversies Score, resulting in what is called the ESG Combined Score.

III. RESEARCH METHOD

Dependent Variable

ESG disclosure as Dependent variable was measured by ESG score from Thomson Reuters database. Galbreath (2013), Thomson Reuters provide credible and objective ESG datasets evaluated by experts. Using the ESG score as a proxy to measure the company's ESG disclosure is the right choice to do in this study because the ESG score for each company is based on disclosures not only from the annual report or CSR report, but also involves other media such as each company's website, website non-profit organizations (NGOs), Stock Exchange Filing, and mass media (Thomson Reuters, 2018).

Independent Variable

CEO narcissism is measured using indicator, which are referred to as unobtrusive indicators adopted from Chatterjee & Hambrick (2007). Unobtrusive indicator is used because usually the top management of the company is very reluctant to participate in survey research. In addition, questions about sensitive traits such as narcissism will result in a low response rate (Cycyota & Harrison, 2006) and allow answers to be influenced by social desirability bias (Kim et al., 2018). Thus, the unobtrusive indicator is the most suitable measure and is in accordance with the Upper Echelon Theory (Chatterjee & Hambrick, 2007).

IV. FINDING AND DISCUSSIONS

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Table 1

Variabel	Prediksi	Koefisien	t-stat	P-value	Sig
NAR	+	1.1107890	1.34	0.090	*
PROFIT	+	-0.0021773	-0.02	0.493	
LEV	+	-0.4055606	-0.95	0.172	
SIZE	+	3.2046960	2.83	0.003	***
FAGE	+	0.0545082	1.36	0.088	*
GDP	+/-	-0.2340167	-0.39	0.698	
AGE	+/-	-0.0087024	-0.07	0.947	
TENURE	-	0.0540879	0.40	0.345	
Cons		-26.25939	-1.05	0.295	
Number of Observation	308				
<i>Adjusted R-Squared</i>	0.1008				
<i>F-stat</i>	24.81				
<i>Prob (F-Statistic)</i>	0.0097***				

*, ** dan *** indication of significant 10%, 5% dan 1%.

Table 1 shows the results of hypothesis testing regarding the effect of CEO narcissism on the company's ESG disclosure. The results prove that CEO narcissism as measured by the unobtrusive indicator has a significant positive effect on the company's ESG disclosure, with a significance of 10%. This indicates that CEO narcissism can be one of the psychological attributes related to CEO characteristics that significantly influence company decisions (Kim et al., 2018). Based on the Upper Echelons Theory, narcissism can be a factor that affects CEO involvement in corporate decision making. This statement is supported by Campbell et al. (2011) which states that the CEO's narcissism has significant implications for his assessment and decision making. The decision is based on how the CEO understands, analyzes, and digests a problem which depends on the characteristics of the CEO himself.

The results of this study are in accordance with the Upper Echelon Theory (Ingersol et al, 2017) which suggests that the organization is a reflection of the values held by its leaders (Hambrick and Mason, 1984). The personality of the company leader will determine the various strategies, policies and practices that run in the company. State-owned companies are always under government supervision so that the allegations of earnings management practices or the desire to make or manipulate profits are very small. The results of this study support this statement.

Large state-owned companies such as TLKM, BBNI, JSMR, and WIKA which have scores of 2 and 3 for their CEO narcissism throughout the year of observation have proven to have the largest profits based on CNBN Indonesia's research for the first semester of 2019. For example, based on the 2017 annual report which has been audited, Waskita Karya was able to record a profit of Rp. 4.20 trillion in 2017. This figure jumped by 132.04% compared to the profit achieved in the previous year of Rp. 1.81 trillion. Operating revenues almost doubled compared to 2016, to Rp45.21 trillion. WIKA has an average CEO Narcissism score of 5 during the year of observation. This further shows that even though the CEO's level of narcissism is high, it even shows that the profit performance they present and their confidence in good performance is very high, so they do not need deviant practices to beautify the profits they generate.

V.CONCLUSIONS

This study also has several research limitations, including the number of samples that tend to be small due to the limited number of companies that have ESG scores and consistently issue press releases during the study period. Future research can expand data sources for ceo narcissism, such as using popular and valid news sites. The next limitation of research is the proxy for CEO narcissism using the unobtrusive indicator by Chatterjee & Hambrick (2007) which has been widely used by several literatures researching the topic of CEO narcissism. Chatterjee & Hambrick (2007) through the upper echelons theory have proven this proxy as a valid proxy because it has been initiated by survey methods and interviews with several company executives. However, for ASEAN countries, there is no research that proves this indicator as a reliable proxy for measuring narcissism. Further research can ensure the reliability of ceo narcissism proxies in ASEAN by conducting surveys and interviews, so that more detailed and accurate information can be obtained in measuring the spectrum of narcissism.

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