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Loyalty shares in Italy: empirical evidence of the influence of board characteristics on short-termism reduction

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Introduction

Loyalty shares are a control-enhancing mechanism granting rewards such as extra dividends or voting rights to shareholders who hold them for a specified period of time ("loyalty period"), the effects of the issuance of such instruments have still not been widely analyzed by scholars even though it is likely that tenured voting will be at the heart of the discussion on voting rights for a long time.

The specific focus of this thesis is on the Italian context as Italy represents one of the countries with a specific legislation concerning loyalty shares since 2014, therefore, a precise moment in time is clearly identified in order to perform analyses before and after the issuance of loyalty shares.

Italian companies with listed shares may introduce increased voting rights of up to two votes for each ordinary share held by the same shareholder for an uninterrupted period of 2 years starting from the date of registration made in a special list maintained by the company. Introducing loyalty shares requires an amendment of the company's bylaws, which has to be approved by the extraordinary general meeting with a two-thirds majority vote.

In particular, this thesis is based on the findings consistent with an "antidote view" of loyalty shares presented in the study of Mio et al. (2020).

Antidote view supports the fact that loyalty shares have the potential to reduce earnings management representing the proxy for managerial short-termism, this assumes that a possible driver of short-termism (as measured by earnings management) is shareholder preference.

Short-termism is usually perceived as a threat for the overall health of the economy as it can lead to foregoing important long-term strategies and preferring short-term earnings. Consistently with previous studies, earnings management was used as a proxy for short-termism as the time horizon of corporate disclosure is symptomatic of short-termism since it may be employed to meet short-term market related goals (Brochet et al., 2015).

The main contribution of this thesis is to test the influence of some selected board characteristics (independence, gender diversity, tenure and CEO narcissism) as moderating variables on the relation between loyalty shares and short termism.

Thus, wondering whether short termism is influenced by boards (or by shareholder preferences through boards).

The sample and methodology follow the empirical approach used by Mio et al. (2020) and include the employment of statistical techniques such as difference-in-differences methodology and regressions.

Further insights into the functioning of loyalty shares as a short termism antidote could be provided by understanding whether the board of directors plays a key role or the most influent driver of long-termism are the shareholders.

In the first chapter it is introduced an overview of various aspects of corporate governance connected to loyalty shares such as short-termism, investor activism, managerial opportunism and corporate sustainability as well as a focus on loyalty shares in the Italian context.

In the second chapter the literature is reviewed both updating the literature being published after the article of Mio et al. (2020) and analyzing the whole loyalty shares literature available considering the different lines of research by countries and the chosen methodologies.

In the third chapter the four hypotheses on the chosen variables and their interaction with the short-termism reduction effect of loyalty shares are developed by relying also on the related literature.

In the fourth chapter it is detailed information about the sample and methodology employed for the analysis including the statistical techniques which were employed such as difference-in-differences methodology and robustness tests, in addition to a focus on the measures of earnings management and the additional moderating variables introduced in the analysis.

The results are presented and discussed in the fifth and final chapter, all the statistical analyses and regressions performed are displayed and conclusions are drawn by relying on this empirical evidence.

1. Corporate governance and loyalty shares

1.1. Corporate governance definitions

The introduction of loyalty shares as it is considered a corporate governance mechanism can of course have an impact on many aspects of corporate governance.

In the literature there is not a unique definition of corporate governance.
Davis (2005) states that corporate governance represents structures, processes and institutions within and around organizations allocating power and resource control among participants.
Di Tommaso and Gulinelli (2019) argue that existing definitions fall into a spectrum of “narrow” and “wider” points of view, the former is limited to the relationship between a company and its shareholders expressed in the "agency theory"; the latter includes a network of relationships between the company and other parties such as employees, customers, suppliers and bondholders. The authors suggest that corporate governance is a system of checks and balances which guarantees that the company fulfills its responsibility towards stakeholders and acts in a socially responsible manner in all areas of activity.
Narrow definitions are focused on corporate responsibility towards shareholders, the wider definition including corporate responsibility towards a larger group was supported by institutional investors thus demonstrating an interest for a broader integrated approach to corporate governance considering that companies are responsible to society, future generations and the environment, therefore based on the perception that companies can maximize long-term value by being responsible to all their stakeholders and optimizing their governance system (Di Tommaso and Gulinelli, 2019).

Corporate governance is a key element in improving economic efficiency and growth and enhancing investor confidence. It involves a set of relationships between management, board, shareholders and other stakeholders by providing the structure through which the objectives, the means of attaining those objectives and monitoring performance are determined. An effective corporate governance system should provide proper incentives to pursue objectives in the interests of the company and its

shareholders. Good corporate governance helps to improve the levels of confidence necessary for the proper functioning of a market economy, lowering the cost of capital and encouraging firms to use resources more efficiently therefore supporting growth (OECD, 2004).

A fundamental concern of corporate governance seems to be the way to regulate large or active shareholders to obtain the right balance between managerial discretion and small shareholder protection (Becht et al., 2003).

Di Tommaso and Gulinelli (2019) view the future corporate governance focused on ensuring business sustainability in the medium to long term and the stability of profits instead of high profits in the short term.

1.2. Corporate short-termism

As highlighted by Mio et al. (2020), loyalty shares are considered a corporate governance mechanism recently adopted by regulators with the aim to reduce corporate short-termism.

Conversely even though short-termism is mostly considered a threat, Roe (2013) states that system-wide short-termism in public firms is something to watch for carefully, but not something that today should affect corporate lawmaking. The author is convinced that the evidence that the stock market is short-termist is inconclusive, with evidence that stock market sectors often overvalue the long-term.

Jackson and Petraki (2011) define short-termism as a situation where corporate stakeholders such as investors, managers, board members, auditors and employees show a preference for strategies adding less value but with an earlier payoff in contrast to strategies that would add more value but have a later payoff. The authors state that short-termism is caused by a self-reinforcing shortening of time horizons produced through the interactions between shareholders and managers.

According to Dallas (2012), current short-term shareholders value managers who engage in earnings management as this provides positive signals to the market thus increasing the likelihood of short-term shareholders selling their shares to more optimistic investors. Thus, in this manner short-term traders have an adverse effect on

decision making by encouraging managers of such firms to engage in earnings management.
Short-term corporate governance can lead to foregoing important long-term strategies such as choosing to generate short-term earnings at the expense of making crucial and necessary capital investments or may push managers to terminate workers if it results in an increase in short-term earnings (Quimby, 2013).
Short-term pressure on managers to hit profit targets may distort R&D investment which may reduce current profits, such short-termist behavior causes a large drag on long-term growth (Terry, 2017).

As reported by Mizik (2010) short-termism can also be defined as underinvestment in intangible assets, such as information technology, relationships with customers, capabilities to innovate, quality processes and personnel capabilities. Moreover, the author states that myopic management can manifest in many forms, it can be undertaken through manipulation of real activities such as cutting discretionary spending, selling off non-essential assets, over-investing into assets that generate immediate payback at the expense of long-term assets with superior future profits, overproducing, discounting, and overselling to distributors.

In practice, manipulation of performance can be undertaken also through accounting-based earnings management given that managers can use judgment in financial reporting (e.g., accelerating recognition of revenues, capitalizing costs, delaying write-offs, understating bad debt), they can manipulate discretionary accruals, the components of earnings subject to accounting discretion, in order to alter earnings numbers in financial reports (Mizik, 2010).
Earnings management in the form of discretionary accruals is the proxy for corporate short-termism chosen by Mio et al. (2020) and employed also in this thesis.

1.2.1. EU approach to short-termism

Directive 2017/828 of the European Parliament and of the Council of 17 May 2017 amends Directive 2007/36/EC on the exercise of rights of shareholders in listed companies. The 2017 revision aims to encourage long-term shareholder engagement to

ensure that decisions are made for the long-term stability of a company and take into account environmental and social issues (EUR-Lex).

The revision of the so-called Shareholder Rights Directive entered into force in 2017 and represents the landing point of a process started in 2012 with the “Action Plan: European company law and corporate governance” by the EU Commission[1] (Martino and Pacces, 2020).

After the 2008 financial crisis there has been a growing concern over potential imbalances caused by short-termism, the EU has focused on promoting corporate sustainability by, among other means, exploring the implementation of control enhancing mechanisms (CEMs) within member states’ legislation breaking the one share, one vote axiom of corporate governance and favoring longer-term investors. Loyalty shares are gaining momentum in EU corporate law systems even though they were present in the draft version of the Directive but ultimately excluded from the final version (Pérez-Schafer and Rios, 2021).

The European Securities and Markets Authority (ESMA) has taken a cautious view on loyalty shares, ESMA prefers to assess the impact of such regulatory novelties before issuing a general recommendation at the EU level (ESMA, 2019).

Johnston and Morrow (2015) report that the long-term shareholding provision would have required Member States to choose between additional voting rights, tax incentives, loyalty dividends or loyalty shares, however the proposal did not pass the plenary vote in Parliament of July 2015.

The introduction of differential ownership rights as part of the revised European Shareholder Rights Directive was proposed by member of EU parliament Sergio Cofferati, in the Cofferati report to the European Parliament. Even if this proposal was rejected, this does not prevent individual countries from introducing loyalty shares (Hodgson, 2016).

[1] This Action Plan outlines initiatives that the Commission intends to take to modernize the company law and corporate governance framework. It identifies three main lines of action: enhancing transparency, engaging shareholders and supporting companies’ growth and competitiveness.

In Italy Legislative Decree 10 May 2019, n. 49, implemented EU Directive 2017/828 on the encouragement of long-term shareholder engagement (Di Tommaso and Gulinelli, 2019).

1.2.2. Short-termism and loyalty shares in the US

According to Porter (1992) USA managers are myopically short-termist and are too focused on potential takeover threats. The author contrasts USA corporate governance with the governance in German and Japanese corporations, where long-term investors allowed managers to invest for the long run while monitoring their performance.

An aspect of Japanese corporate governance praised in the 1980s was the long-run nature of relationships between the constituencies in a company, whereas a criticism of the Anglo-American market-based corporate governance is the excessively short-termist perspective and quarterly performance (Becht et al., 2003).

Loyalty shares with "tenure voting" or "time-phased voting" are also present in the United States, they have gained prominence through the proposal to create the Long-Term Stock Exchange (LTSE) (European Corporate Governance Institute).

In May 2019, the Securities Exchange Commission approved the LTSE, a new stock exchange to list shares outside of the traditional stock exchange promoting a unique approach to governance and voting rights, reducing short-term pressures on public companies (Reuters).

The attention of investors was focused on loyalty shares, one of the core elements of LTSE (Mio et al., 2020).

Greene and Bashaw (2020) state that the LTSE has a set of differentiated listing standards designed to align long-term investors and companies in order to create lasting value for public companies and their like-minded investors, as when companies have a strong long-term investor base believing in their mission and strategy, they are better positioned to have ongoing support.

1.3. Loyalty shares

Loyalty shares are an instrument granting increased voting rights or dividends to long-term investors, these instruments have been promoted to address concerns about short-termism in financial markets and the impact of short-termism on the ability of a company to create long-term shareholder value (Delvoie and Clottens, 2015).

This control-enhancing instrument is becoming increasingly important in the public debate as they have been implemented both in Europe and in the United States.
In Europe they are present in France, Italy, the Netherlands and Belgium.
France is the front runner as loyalty voting rights were already present and since 2014, they have become the default option in listed companies, the company must opt out in its articles of association, which requires a two-thirds majority. In the Netherlands no specific legal basis is present for loyalty shares neither is there a specific prohibition (Delvoie and Clottens, 2015).
Belgium approved a company law reform in 2019 allowing their introduction on a voluntary basis in 2020 (Bajo et al., 2020).
On 24 March 2021, the Spanish Parliament introduces loyalty shares and transposes EU Directive 2017/828 with the aim to incentivize long-term shareholder engagement (Pérez-Schafer and Rios, 2021).

Given that this thesis is focused on the Italian context, a more detailed background to the introduction of loyalty shares in Italy is provided.
The provision on double voting rights to ordinary shares of Italian listed companies was introduced in 2014 along with a series of measures aimed at fostering the development of Italian enterprises and promoting listings and long-term investments on Italian capital markets (Surace, 2020).
The Law Decree No. 91 dated 24 June 2014 known also as "competitiveness decree" (Decreto competitività) introduced measures to support business development in Italy, it was converted with modifications into Law No. 116 dated 11 August 2014 and introduced article 127-quinquies of the Consolidated Finance Act (TUF).
Italian companies with listed shares may introduce in their bylaws increased voting rights of up to two votes for each ordinary share held by the same shareholder for an

uninterrupted period of no less than 24 months starting from the date of registration made in a special list maintained by the company.
Loyalty shares do not constitute a special class of shares, different from the ordinary shares and this potential availability of the loyalty reward to all shareholders should prevent any violation of the principle of equal treatment, therefore loyalty shares are seen as are more equitable than other CEMS. (Surace, 2020).
The granting of enhanced voting rights does not create a new special category of shares as every share meeting the requirements can have its votes increased up to two votes, applicable only to shares continuously held by the same shareholder for at least two consecutive years, the transfer automatically terminates the enhanced voting rights unless they are inherited. To introduce loyalty shares company’s bylaws have to be amended and approved by the extraordinary general meeting with a two-thirds majority (Bajo et al., 2020).

A fact that is believed to have triggered the introduction of loyalty shares in Italy was when Fiat became a Dutch company, in 2014, following its merger with Chrysler and explicitly citing the availability of loyalty voting shares in the Netherlands as a key factor behind this decision. The Italian Parliament responded by voting loyalty shares into law, the same matter was being discussed at the European Parliament in Brussels at the time with the proposed introduction of loyalty shares into the Shareholders’ Rights Directive (Delvoie and Clottens, 2015).

In 2020, Consob reported that the number of Italian listed companies adopting loyalty shares was 53 and consisted mainly of small firms in the industrial sector, in 35 companies loyalty shares vested their increased voting power (active loyalty shares) where the wedge, defined as the difference between the units of capital controlled (on the basis of voting rights in ordinary shareholders’ meetings) and the units of capital owned (on the basis of cash flow rights pertaining to the controlling shareholder) is equal to 12.1% (Linciano et al., 2020).

To date, 68 companies listed on the Italian Stock Exchange Borsa Italiana, have adopted loyalty shares[2].

1.3.1. Deviation from the "one share, one vote" principle

Loyalty shares cause a deviation from the standard one share, one vote principle.
The use of dual-class shares[3] or other CEMs cause deviations from the one share–one vote principle, allocating more voting than cash flow rights to some shares and providing the owners of these shares with more influence than what would be granted by their investment (Eklund and Poulsen, 2014).

Hayden and Bodie (2008) state that corporate law generally accepts the "one share, one vote" standard as a basis for efficient distribution of a company's voting rights, as each shareholder has one vote for each share, so all shareholders have voting power equivalent to their interest in the residual, thus providing the proper incentives to oversee management and maximize wealth, critical to this theory is the notion that all shareholders have the same interest of maximizing the residual value of the corporation. Even if shareholder primacy theory maintains that all shareholders have homogeneity of interest., the authors are convinced that shareholders are not the homogenous share-value maximizers envisioned by the "one share, one vote" theory as they are likely to have interests potentially competing with their interests as shareholders.
Wong (2013) states that rising levels of short-termism among investors should prompt a reconsideration of the principle that all shareholders should have equal say (one share-one vote). The author is convinced that for fairness reasons and in order to avoid entrenching control, all investors should be eligible to receive enhanced voting rights

[2] Data currently available at https://www.consob.it/web/area-pubblica/quotate/main/emittenti/societa_quotate/voto_maggiorato_plurimo_lnk.htm?nav=true .

[3] The stock is split into different categories, known as dual-class shares, to give owners of one class greater voting rights than owners of the other. That allows minority shareholders, typically a company's founders or leaders, to retain control of a business (Bloomberg).

when meeting certain conditions such as holding period like it happens for loyalty shares and should not be distributed only to founders or other insiders such as dual-class shares. Departing from one-share, one-vote with the view to encouraging long-term ownership should be done taking into account these aspects.

Grossman (1988) show that deviations from one share-one vote can be a characteristic of a corporate charter that is in security holders' best interest, therefore the author see no reason to interfere with the ability of a company to choose to deviate from one share-one vote.

Eklund and Poulsen (2014) argue that that it is a fallacy to equate disproportionality with CEMs. Considering just the simple difference leads to an overestimation of the negative relation between firm value and the use of dual-class shares or other CEMs, however, disproportionate influence may also arise without such mechanisms. CEMs may bear potential benefits, particularly in countries with good investor protection by helping to balance power between shareholders and managers.

1.4. Investor activism

The presence of loyalty shares may also impact costs and benefits of activism for "loyal" long-term shareholders, in fact the cost of activism may be lower given that loyal shareholders increase their voting rights and influence on managers after loyalty shares adoption and benefits may be higher given the increase in dividends paid which may be granted by loyalty shares (Mio et al., 2020).

Shareholder activism has been a feature of corporate governance for more than one hundred years especially in the US context (Rose and Sharfman, 2014).

Rose and Sharfman (2014) define shareholder activism as any action of any shareholder or shareholder group which aims to bring change within a public company without trying to gain control. The authors state that shareholder activism is coming in two main forms: performance-driven and corporate governance activism. Performance-driven activism is usually instigated by hedge funds[4] and it focuses on advocating changes in corporate

[4] Hedge funds pool money from investors and invest in securities or other types of investments with the goal of getting positive returns. Hedge funds are limited to wealthier investors who can

strategy, whereas corporate governance activism focuses on changes in governance arrangements even if in some cases the latter is used as a vehicle to achieve the former.

Gillan and Starks (1998) highlight that shareholder activism that has often focused on corporate governance issues arises from the need to solve agency conflicts between shareholders, board and corporate management that are inherent in a company, the basis for this conflict is provided by the separation of ownership and control. All shareholders are benefiting from the actions of monitoring shareholders without incurring the costs, in particular large institutional investors learn management's private information and convey it to other shareholders but for such monitoring to be credible the investment should be maintained for a longer period of time. This last aspect is inherently connected to loyalty shares.

Cornett et al. (2007) report that monitoring by institutional investors can result in managers focusing more on corporate performance and behaving less in an opportunistic and self-serving way.

Berger et al. (2017) state that shareholder activists often argue that they are long-term holders, given that they are holding their shares longer than the median holding period, therefore tenure voting may affect shareholder activism by enhancing long-term value-creating activism.
Pacces (2016) is convinced that regulation should enable companies to choose whether to curb hedge funds activism depending on what is most efficient, the European experience with loyalty shares is enabling such choice. In dispersed ownership structures activist hedge funds do other investors a favor fostering managerial accountability when managers perform poorly; in concentrated ownership structures, they are guarding minority shareholders against expropriation. However, policymakers are skeptical towards hedge funds activism as they are blamed for injecting short-termism in corporate governance and long-term shareholding is thought to be a solution

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afford higher fees and risks of hedge fund investing, and institutional investors, including pension funds (Investor.gov).

to overcome this issue, loyalty shares are part of this group of proposals as they tilt the balance of powers towards more loyal shareholders.

As mentioned by Fried (2015) long-term shareholders may be more interested to reduce managerial agency costs given that they will have a longer holding period and they may also have a better knowledge of managerial performance as they have more familiarity with it.

Loyalty shares should incentivize managers to favor long-term corporate and match the horizons of long-term shareholders given that they have more votes and will remain for a longer time (Roe and Cenzi Venezze, 2021).

Duruigbo (2012) highlights that a loyalty dividend, apart from serving to incentivize shareholders to keep their shares for a longer term, may also improve investor relations by creating an opportunity for more direct communication between shareholders and management creating an incentive for the engagement of long-term shareholders to boost long-term shareholder activism.

Time horizons of shareholders have an influence on managers decisions, if long-term shareholders have more power than short-term shareholders then managers can be expected to focus more on long-term shareholder value (Fried, 2015).

1.5. Managerial opportunism and takeover

As previously said, the powers of long-term investors are enhanced through loyalty shares and this may have an impact on how actively they engage with management to limit their opportunism and short-termism, as the introduction of loyalty shares can impact how managers view the interests of different shareholders and the fact that long-term shareholders have higher voting rights this could nudge managers (Mio et al., 2020).

If more shareholders with more votes hold for the longer-term then executives' time horizons are expected to adapt and focus more on long-term value (Fried, 2015; Roe and Cenzi Venezze, 2021).

By empowering long-term investors loyalty shares should encourage them to monitor managers, and at the same time protecting managers from financial market short-term pressures, benefiting all shareholders (Belot et al., 2019).
Shareholders as owners of the company have the right to influence the management of the company through the exercise of their voting rights as well as shareholder activism, issues on which shareholders can vote by expressing greater participation (Di Tommaso and Gulinelli, 2019).
Managers have the duty to act in the best interest of shareholders and the corporate governance system is ultimately aimed concerned with the resolution of collective action problems and at reaching a convergence of interests by reconciling conflicts of interest between various corporate claimholders (Becht et al., 2003; Mio et al., 2020).
The "divorce" between ownership and control that leads to the notorious "Agency Problem" is due to the market system organized in such a way that the owners, mainly the shareholders of listed companies, delegate the management of the company (Di Tommaso and Gulinelli, 2019).
Becht et al. (2003) state corporate governance problems can arise when an outside investor wants to exercise control in a different way than the management who is in charge, dispersed ownership may worsen this problem and give rise to conflicts of interest and create a collective agency problem among investors.

Mosca (2019) highlights that a tangible reason shareholders would accrue the increased voting rights lies in their actual interest in attending the general meeting of shareholders. The author also remarks that in the last decade European countries are doing their utmost to revitalize shareholders’ general meeting as a constructive discussion forum and in this regard tenure voting may also ease communication with shareholders, given that the registration process is a necessary condition to accrue tenured voting therefore directors may more easily communicate with shareholders, knowing their identity and send them relevant company information to actively participate during attendance to the shareholders’ general meeting.

On the other hand, managerial entrenchment is an argument of what Mio et al. (2020) classify as the “poison view” of loyalty shares suggesting that loyalty shares are ineffective in decreasing short termism.

CEMs are sometimes viewed as managerial entrenchment mechanisms since they may prevent takeovers that are opposed by management (Moschetto and Teulon, 2015).

According to corporate governance literature opportunistic behavior by managers, which is connected to earnings management and therefore short-termism (Chandra and Wimelda, 2018), will decrease market value of companies (Mio et al., 2020).

As stated by Mio et al. (2020) the alignment of power of the market for corporate control is decreased and this may favor managerial entrenchment, because of the decreased ability of bidding shareholders to takeover the company when an opportunistic management is present, since bidding shareholders should acquire a control bloc and wait for the stock to mature, therefore managers may be less exposed to takeover as external corporate governance mechanism and become short-term oriented.
Pacces (2016) states that loyalty shares may entrench control as in the event of a takeover shareholders loyal to management would retain the extra voting rights and be able to resist a hostile bid. According to the author there would be ways to get around this potential problem for example through capping of the extra voting rights to prevent dominant shareholders from using loyalty shares as a CEM and making the benefits of loyalty shares expire in the event of a takeover bid; however they all would make loyalty shares less attractive.

However, the reduction in earnings management is excluding the hypothesis of managerial entrenchment since hostile takeovers are made more difficult by loyalty shares (Mio et al., 2020).

Still, tenured voting rights is considered as preferable to dual-class shares since they lead to a weaker form of corporate control and a lower degree of immunity to hostile takeovers. In addition, shareholders are treated equally since they are all granted the same option to mature additional voting rights (Mosca, 2019).
The wedge created between insider ownership and control is a smaller wedge than that faced by dual-class companies (Berger et al., 2017).

Another aspect concerning takeovers which is analyzed by Mosca (2019) is the mandatory offer provision, a compulsory rule within the framework of the Takeover Directive (Directive 2004/25/EC) namely, the obligation to announce a public offer in

the case of controlling acquisitions. The author reports that the entry into force of loyalty shares in Italian corporate law was followed by a revision of the system of thresholds of the rules on mandatory offers, the choice, made by the Italian legislator imposes the obligation to launch a bid when the 30 percent threshold is exceeded as a result of increased voting rights.

Tenured voting is going to be at the heart of the discussion on voting rights for a long time, especially in the European Union context where the increase in voting rights may lead to the mandatory offer obligation (Mosca, 2019).

1.6. Corporate sustainability

Loyalty shares can also be viewed as a corporate governance feature fostering corporate sustainability (Mio et al., 2020).

Zumente and Bistrova (2021) highlight that initially shareholder value was mainly described by a short-term profit orientation but nowadays the concept increasingly leans towards the need to act responsibly and sustainably for the organization to ensure its place in the economy in the long-term. The authors explore Environmental, Social and Governance (ESG) as the variable measuring sustainability performance and suggest that the choice between short-term returns and long-term value must not be made, as more sustainable companies perform better with regard to environment and society as well as achieve long-term shareholder value.

World Commission on Environment and Development (1987) published a report entitled “Our common future” which came to be known as the Brundtland Report and defined sustainable development as a development that enables the satisfaction of current needs of societies without compromising this possibility for future generations.

Based on this logic, Bansal and DesJardine (2014) define business sustainability as the ability of firms to respond to short-term financial needs without compromising their (or others’) ability to meet future needs, thus, time is central to the notion of sustainability. Over the years, the concept of sustainable development has evolved by extending to the ESG factors and being recognized as a process that covers more than just strictly environmental factors (Janicka et al., 2020).

In September 2015, the “2030 Agenda for Sustainable Development” is laid down by the United Nations and 17 Sustainable Development Goals (SDGs) are established to guide international action on reaching economic, social and environmental targets (United Nations).

Therefore, sustainability requires the consideration of time as it requires firms to make intertemporal trade-off sis also the ability of a firm to balance the short and long-term therefore temporal imbalances are among sustainability’s greatest threats. (Bansal and DesJardine, 2014).

Janicka et al. (2020) argue that in a broad sense, the concept of “sustainable finance” is mainly related to strengthening financial stability in the economy by considering ESG factors and preferring long-term investments, opposed to the short-term nature of contemporary financial markets, which is inconsistent with the direction of changes towards sustainable and inclusive solutions. Short-termism is defined as a suboptimal state preventing companies from using their potential in the long term or achieving sustainable development goals.
Greenfield (2011) states that the more difficult kind of externality to address when focusing on the sustainability of a company is the future externality intended as the kind of cost that a corporation’s management can externalize to the future since from the perspective of management the future is a more attractive time to push off costs, since stakeholders will be less aware of those costs than current costs.
In a company with a management team oriented toward the long-term, it should be observed a greater dedication to sustain the company as a going concern over time and a larger commitment to maintaining the loyalty of investors whether by way of capital, infrastructure or work (Greenfield, 2011).

2. Literature review

2.1. Updated literature review (with respect to Mio et al., 2020)

In recent years, the introduction of loyalty shares in various legislations has led scholars to analyze and question the validity and the consequences of such instruments.
Starting from a literature update review of the most recent articles and papers since 2018 might prove useful to have a clearer picture of the current framework.

Croci (2018) analyzed the introduction and control enhancing effects of loyalty shares and multiple voting shares in Italy focusing on the likelihood to adopt loyalty and multiple voting shares, as well as on the determinants of the adoption of loyalty shares, stock price reactions and post introduction events such as seasoned-equity offerings (SEOs), acquisitions, delistings and takeovers. In particular by focusing on SEOs and acquisitions, no evidence analyzed by the author supports the fact that loyalty shares are introduced to preserve family control during those ownership-diluting events, as for takeovers and delistings the presence of loyalty shares is negatively associated to such events. The conclusions highlighted by the author were that the presence of institutional investor ownership did not negatively affect the adoption of loyalty shares, however directors that were appointed by minority shareholders did decrease the probability of adoption, suggesting that defensive instruments against the new control-enhancing mechanism (CEM) are present in the Italian system.
Moreover, after the introduction of the law allowing loyalty shares in 2014 a negative reaction was noticed consistently with the increased strength in the controlling shareholders' position, on the contrary at firm level a positive average stock price reaction was observed at the announcement of loyalty shares (Croci, 2018).

As for the French context where loyalty shares have been allowed by the law since 1966 and have been adopted by two-thirds of French listed firms, Belot et al. (2019) analyzed the 2014 passage of the Florange Act from an opt-in to an opt-out provision with shareholder approval, in order to understand how investors judge loyalty shares by considering this change in the law as an exogenous shock for the value of firms. The authors considered a sample of publicly traded French firms and found that after the

Act, firms that decided to opt out experienced a negative reaction from the market, suggesting that shareholders consider loyalty shares positively.
The Florange law appears to primarily benefit blockholders and as the authors state empirical evidence suggests that blockholders benefit the firm (Belot et al., 2019).

The consequences of the introduction of the Florange Act are also analyzed by Bourveau et al. (2019) from an ownership structure and capital market perspective. The authors performed tests on a sample of French firms and found that adopters of Differential Voting Rights (DVR) by default, in particular companies with a large blockholder showed a decrease in foreign institutional ownership and an increase in cost of equity capital. On the other hand, the authors found a positive market reaction to opt-out votes.
Therefore, doubts on regulation-induced tenure voting are highlighted as according to the authors double voting rights reinforce insiders' entrenchment and empower French government on companies where it owns minority stakes. The authors do not exclude different outcomes outside of the French market, depending on capital market institutions, ownership diffusion, and political influence (Bourveau et al., 2019).

Mosca (2019) focuses on the interaction of tenured voting rights with the core principles of the EU financial market law system by using empirical evidence from Italy and France. According to the author, in Continental Europe the importance of tenured voting as an instrument to enhance shareholders' long-term position should not be overestimated in particular when companies have had long-term controlling shareholders. Another additional aspect that the author considers is the integrity of the European market that could be affected by single Member States tailored adoption of tenure voting and lead to an excessive fragmentation. In particular, the author focuses on the interference between loyalty shares and takeover law and mainly on the mandatory offer[5], a special feature of European law. Italian legislators decided to extend the mandatory offer rule

[5] In the event that a person, as a result of his own acquisition or the acquisition by persons acting in concert with him, reaches a certain percentage of voting rights in a company which gives him control of that company, EU member states must ensure that such a person is required to make a mandatory takeover offer in order to protect the minority shareholders of that company. The percentage of voting rights and its calculation are left to be determined by the rules of the EU member state in which the company has its registered office.

to tenured voting, inconsistently with the main purpose of loyalty shares to increase shareholders' participation.
The author is convinced that tenured voting is going to be at the heart of the discussion on voting rights for a long time, especially in the European Union context on specific rules applicable within the framework of the Takeover Directive[6] when the increase in voting rights may lead to the mandatory offer obligation (Mosca, 2019).

Becht et al. (2020) deal with the Florange Act as well and consider this exogenous switch of the default rule from one share-one vote to tenure voting to test the contractual theory of the firm predicting that companies adopt charters maximizing firm value, regardless of the default rule. The Loi Florange established tenure voting as default rule in initial public offerings (IPOs), and one-share-one-vote companies had to act in order to preserve the status previous to the reform. The authors find no significant impact on IPOs' charter choice, but the use of tenure voting increased slightly after the reform, particularly among family firms. The choice by families appears voluntary and is mostly unaffected by the default rule, in accordance with the contractarian theory and with the idea that statutes were allocated efficiently before the reform.
Despite the fact that a supermajority was required to revert to a one-share-one-vote system, the majority of companies reverted. According to the authors the reform allowed the French state to enhance its influence over listed companies it considers strategic (Becht et al., 2020).

Previous literature has mainly focused on the French context, where the Florange Act made loyalty shares mandatory for all listed companies unless they opt out. A specific focus on the Italian context is provided by Bajo et al. (2020) that examine the introduction of loyalty shares in Italy in 2014, allowing double voting rights if shares are held for a continuous period of at least two years.
Italy is a country characterized by family-controlled firms but with an increasing presence of institutional investors. The authors state that the most likely adopters are represented by family-controlled firms and that even though institutional investors voted against the adoption of loyalty shares, they do not reduce and even increase their

[6] Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on takeover bids.

holdings as improved performance of adopting firms compensates for incremental governance costs. The authors conclude that the main effect of the introduction of loyalty shares in Italy is the bolstering of family control (Bajo et al., 2020).

A very recent contribution on whether loyalty shares target corporate short-termism is given by Roe and Cenzi Venezze (2021). The authors review the effects of loyalty shares in countries where they have been implemented, mainly France and Italy, in order to understand how this type of control-enhancing mechanism could be implemented and how it would act to address short-termism in the US context. The view proposed by this article is skeptical on the efficacy of loyalty shares in promoting long-termism, as according to the authors even in Europe control motivations are the dominant drivers favoring insider-controllers.
However, other unexplored reasons could justify the implementation of loyalty shares, such as the value of entrepreneur retaining control which may potentially foster start-ups and original entrepreneurial activity (Roe and Cenzi Venezze, 2021).

2.2. Research questions in previous literature on loyalty shares

By broadening the focus to include a more complete framework of the available literature on loyalty shares it could be of interest to detail the lines of research by country, the research questions on loyalty shares and the chosen methodologies.

2.2.1. Lines of research by country

As for France the common line of research, it is represented by the consequences of the Loi Florange in 2014, scholars studied this reform to draw conclusions on various aspects connected to loyalty shares (Becht et al., 2020; Belot et al., 2019; Bourveau et al., 2019; Delvoie and Clottens, 2015; Ecchia and Visconti, 2016).
Regarding Italy the main aspects that were tackled are mainly short-termism reduction, consequences and determinants of adoption with a focus on family-controlled companies (Bajo et al., 2020; Croci, 2018; Mio et al., 2020; Mosca, 2019).

In the USA authors studied how the diffusion of loyalty shares would impact US public companies and short-termism in financial markets (Berger et al., 2017; Bolton and Samama, 2013; Dallas and Barry, 2016; Edelaman et al., 2019; Quimby, 2013; Roe and Cenzi Venezze, 2021).

These aspects are summarized in Table 2.1.

Table 2.1: Research questions on loyalty shares

Country	Authors	Lines of research
France	Becht et al. (2020); Belot et al. (2019); Bourveau et al. (2019); Delvoie and Clottens (2015); Ecchia and Visconti (2016)	Consequences of the Loi Florange, 2014.
Italy	Bajo et al. (2020); Croci (2018); Mio et al. (2020); Mosca (2019)	Short-termism reduction, consequences and determinants of adoption, focus on family-controlled companies
USA	Berger et al. (2017); Bolton and Samama (2013); Dallas and Barry (2016); Edelaman et al. (2019); Quimby (2013); Roe and Cenzi Venezze (2021)	Possible impact of the diffusion of loyalty shares on US public companies.

Source: Personal elaboration

Concerning the regulatory intervention aimed at generalizing tenure voting in French public companies (Florange Act, 2014) the following authors examine the consequences of this exogenous switch of the default rule from an opt-in to an opt-out provision with shareholder approval.

Delvoie and Clottens (2015) discuss the rewards granted by loyalty shares (i.e., extra dividends or voting rights) to shareholders holding shares for a certain period of time and their effects on addressing short-termism in financial markets.

Ecchia and Visconti (2016) investigate whether this law reform is a real award for loyal shareholders and it incentivizes to shift to long-termism in the holding period by

indirectly supporting business long-termism or whether it is a CEM favoring majority shareholders, the authors also reason on the extension of the French model of loyalty shares to Italy and other countries.
This change in the law is considered as an exogenous shock for the value of firms by Belot et al. (2019) in order to understand how investors judge loyalty shares.
The capital market consequences in particular, foreign institutional ownership and cost of capital are analyzed by Bourveau et al. (2019).
Becht et al. (2020) are testing whether the contractual theory of the firm holds, predicting that companies adopt charters maximizing firm value, regardless of the default rule.

The Italian context has been recently analyzed by various scholars.
Croci (2018) provides many empirical figures following the introduction of loyalty shares and multiple voting shares in Italy and their control-enhancing effects.
The interaction of tenured voting rights with the core principles of the EU financial market law system and how they could coexist are evaluated by Mosca (2019) with a particular focus on Italy.
Bajo et al. (2020) are mainly considering the particular nature of the Italian context characterized by an extensive presence of family-controlled firms and how the introduction of loyalty shares in Italy is impacting such firms.
Mio et al. (2020) are focusing on the effectiveness of loyalty shares as an antidote against short-termism.

In the United States many authors are highlighting the pros and cons of introducing tenure voting.
Bolton and Samama (2013) state that loyalty shares are a simple contractual innovation that could be useful in restoring the balance between long-term investors and short-term speculators. The approach proposed by the authors is that companies should decide whether they want to experiment with loyalty rewards and tailor them to their individual situation. The authors also draw attention to the few companies that have experimented with loyalty dividends and they are argue that with some modifications loyalty shares could play a key role in contrasting short-termism of US financial markets.

According to Quimby (2013), making a loyalty shares provision available to public corporations would provide a model that helps promote long-term investment and corporate governance but that would not negatively affect the benefits of short-term trading through the use of the tax code to encourage shareholders to invest long-term.
Dallas and Barry (2016) state that in recent years Time-Phased Voting (TPV) has gained attention as a remedy for corporate myopia as by decreasing the influence of short-term shareholders managers may be encouraged to act in the long-term interests of their companies. In fact, controlling shareholders who are generally long-term shareholders are enabled to maintain their control with lower levels of ownership thus resembling a milder form of dual-class stock but more targeted toward myopic behavior. According to the authors TPV empowers long-term shareholders, but does not do much to encourage long-term shareholding maybe because of lack of investor awareness given that few companies have adopted TPV in the United States
Berger et al. (2017) are convinced that a tenure voting model might impact short-termism and compare this model to other "one share, one vote" alternatives, such as dual-class stock. The authors affirm that they are providing an initial roadmap of legal and practical considerations for companies who are interested in this innovative capital structure.
Edelaman et al. (2019) are wondering whether tenure voting is a better alternative with respect to dual-class stock for corporate management and shareholders by reviewing the arguments for and against tenure voting made in the literature.
Roe and Cenzi Venezze (2021) are not convinced that the true value of loyalty shares resides in their effectiveness in reducing short-termism as insiders and management would use such instruments to capture extra voting powers to target their goals which may not necessarily be long-term oriented. Nevertheless, the authors are convinced that founders may be motivated by loyalty shares as they would be able to maintain control even after the business goes public.

2.2.2. Methodologies

The methodologies that are utilized by scholars are mainly empirical.

Ecchia and Visconti (2016) carry out empirical analyses of loyalty share performances in the French context under different aspects, in particular the spread of this voting system, the effects on share liquidity and company's market value, the length of the required loyalty period, the influence on the actual growth of the power of majority shareholders and the anti-takeover role.
By focusing on all firms classified as French and publicly traded, Belot et al. (2019) perform univariate analyses of differences in characteristics for firms granting double voting rights and differences in firm characteristics using double voting rights before the Florange Act.
On a sample of 257 French firms headquartered and listed in France, Bourveau et al. (2019) test the effect of regulatory-induced changes in voting rights on firms' ownership structures by employing hand-collected data on firms' adoption or rejection of double voting rights through online searches and multivariate tests in order to compare the change in ownership structure across default adopters relative to a pooled group of voluntary adopters and rejecters in the period.
Becht et al. (2020) perform an empirical test for two groups, the population of IPO firms and a sample of midstream firms, including all the IPOs by firms incorporated in France four years prior to the reform and four years after the reform to check if the company had opted-out of one share-one vote rule.
A more discursive approach is adopted by Delvoie and Clottens (2015) who review the experience with loyalty shares in EU Member States and discuss the developments at the EU level by suggesting to let companies and Member States experiment with loyalty shares in order to put them to the market test.

Croci (2018) implements empirical analyses and regressions on a sample of firms that adopted loyalty shares and multiple voting shares and firms that have not adopted them to understand the determinants of the adoption of loyalty shares, as well as stock price reactions, post introduction events and the use of loyalty shares as takeover defense.
Empirical evidence from the Italian and French context is gathered by Mosca (2019) to highlight the interactions between tenured voting and European takeover law using a sample of companies.

Bajo et al. (2020) contrast the sample of Italian listed firms adopting loyalty shares between 2015 and 2019 to the total of Italian listed firms, divided into newly listed companies (IPOs) and already listed firms together with total number of listed firms and the time distribution of other CEMs by year.
Earnings management is used as a proxy for corporate short-termism by Mio et al. (2020) and econometrics main tests and robustness tests are carried out, on a hand-collected database of Italian firms, to test the hypothesis that loyalty shares reduce short-termism.

Bolton and Samama (2013) develop various proposals on how loyalty shares would work and would be implemented, their benefits and uses and how they would reward long-term monitoring by large shareholders such as blockholders and activist shareholders[7] and the possible effects on the market.
By focusing on reviewing the experiences of European and Canadian companies using CEMs, Quimby (2013) includes suggestions on features and procedural safeguards as default rules to avoid the potential drawbacks of uncapped systems of enhanced voting rights.
Berger et al. (2017) describe tenure voting under current market conditions and regulations by discussing historical use, potential benefits, effects on shareholder short-termism, practical considerations for the adoption of tenure-voting, such as the legal framework under state law and exchange listing rules by identifying possible features that could be introduced in tenure-voting plans.
Edelaman et al. (2019) generate a database documenting institutional investor portfolio turnover rates for stocks and use this data to test how the adoption of tenure voting would affect control rights through a mathematical voting model of tenure voting. The authors show that tenure voting represents an intermediate form of manager's voting control, as it does not ensure management control like dual-class shares but it gives control only if managers continue to hold a significant block of shares over time.

[7] An activist shareholder attempts to use his or her equity stake in a company to achieve certain goals and bring change, through the exercise of voting power or influence of other shareholders. The most common forms of shareholder activism include shareholder resolutions, proxy fights, publicity campaigns, negotiations with management and litigation (Corporate Finance Institute).

Moreover, a better balancing of managerial and shareholder control is achieved through tenure voting as it potentially gives all investors equal access to superior voting power if they are willing to hold the shares for the long-term (Edelaman et al., 2019).
Dallas and Barry (2016) include both a theoretical and a practical analysis comparing TPV to other corporate voting structures such as one-share-one-vote and dual-class stock and TPV occupies a position between these voting structures. The practical experience of US companies with TPV is then investigated, even though the sample size is limited given the limited experience in the US with TPV, the authors are convinced that shareholders and corporations should be free to experiment with reasonable TPV plans.
Roe and Cenzi Venezze (2021) review the main aspects concerning loyalty shares as an instrument promoting long-termism, namely winners and losers from loyalty shares which the authors identify respectively in controlling shareholders and index funds[8] and in outside blockholders and shareholder activists. Moreover, the French and the Italian experiences with loyalty shares are analyzed and finally the existing rules and the reforms proposed in the United States emphasizing the American corporate lawmaking approach to allow companies to adopt "tailor-made" structures and the potential impact that this approach would have on the implementation of loyalty shares.

[8] An index mutual fund or ETF (exchange-traded fund) tracks the performance of a market benchmark, such as the S&P 500 Index. Therefore, instead of selecting which stocks or bonds the fund will hold, the fund's manager buys all of the stocks or bonds in the tracked index (Vanguard).

3. Hypothesis development

3.1. Board independence

Hypothesis 1: board independence strengthens the effectiveness of loyalty shares in reducing earnings management and short-termism

As proven by Mio et al. (2020), the implementation of loyalty shares leads to a reduction in corporate short-termism proxied by a reduction in earnings management.
This relation assumes that one of the possible drivers of short-termism as measured by earnings management is shareholder preference.
In particular, a shareholder constituency that is generally believed to have such short-term biases is the institutional investor community (Bolton and Samama, 2013).
Even if evidence of institutional investors enhancing corporate monitoring exists (Cornett et al., 2007).
Therefore, it could be interesting to include board independence as a moderating variable in the relationship between loyalty shares and short-termism in order to speculate about whether short-termism is influenced by boards or by shareholder preferences through the activity of boards.
As a matter of fact, various scholars find that more independent boards reduce earnings management and are more prone to be long-term oriented. In addition, being independent means also to be less connected to shareholders and therefore less influenced by shareholder preferences.
Further insights into the functioning of loyalty shares as a short-termism antidote could be provided by understanding whether board independence plays a key role or whether the most influent driver remain the shareholders.

A strong part is played by a firm’s internal corporate governance structure and mechanisms in constraining the practice of earnings management especially by the presence of independent non-executive directors on the board (Davidson et al., 2005).

Several studies have focused on the relationship between board independence and earnings management which is related to short-termism, defined by Dallas (2012) as

managerial myopia with an excessive focus on short-term results, in particular quarterly earnings and short-term portfolio returns, encouraging the use of earnings management to the detriment of long-term value creation.

Klein (2002) finds a negative correlation between board independence from management and earnings manipulation in the form of abnormal accruals. The author tests how changes in board independence affect abnormal adjusted accruals (AAACs) and finds that firms reducing the percentage of outsiders on the board experience an increase in AAACs compared to the other firms experiencing a decrease. Moreover, firms that shifted from a majority to a minority of outside directors had large increases in AAACs with respect to their counterparts.

Kao and Chen (2004) agree with this view and state that outside directors are more efficient at monitoring management and therefore a lower presence of earnings management is observed. The authors add also that information disclosed in financial statements should be more reliable when outside directors are present in the board.

The negative relation between earnings management and board independence is confirmed by Ebrahim (2007) who finds that the absolute value of discretionary accruals has a negative and significant correlation coefficient with the per cent of independent directors on the board, as independent boards will be monitoring more effectively the financial reporting process of the firm.

Epps and Ismail (2009) observe a reduction in discretionary accruals when boards are composed mainly of independent outside directors, the authors find that boards controlled by a supermajority of independent outsiders are negatively associated with income-decreasing earnings management.

Gonzalez and André (2014) include board independence as one of the criteria to determine board effectiveness and find that firms with more effective boards are less prone to engage in short-term risky strategies not connected to long-term value, caused by short-termist actions such as earnings management and suboptimal investment choices.

According to Chen et al. (2015) independent directors are more objective monitors given that they are less influenced by managers. The authors directly test the effect of a US regulatory change requiring majority board independence and show that it is associated

to a decline in earnings management by comparing the change in the absolute value of performance-matched discretionary accruals from the per-regulation to the post-regulation period, on average compliant firms experienced a significant reduction in discretionary accruals compared to non-compliant firms. In addition, the authors demonstrate that this effect is strengthened when independent directors have lower information acquisition cost and therefore easier access to information.

Moreover, direct evidence that the effectiveness of these board structure reforms on reduction in earnings management is linked to improvements in future performance are provided (Chen et al., 2015).

Boards contribution towards financial reporting integrity and credibility as predicted by agency theory is analyzed also by Peasnell et al. (2005) that indicate that the possibility of abnormal accruals being large enough to transform a loss into a profit or to prevent profit from declining, in an attempt to delay or minimize negative reporting news is significantly lower for firms with a high proportion of outside board members. On the other hand, no evidence of outside directors influence on constraining income-decreasing abnormal accruals is found.

In fact, boards have more incentives to monitor income-increasing earnings management because of asymmetric loss functions[9] as penalties related to earnings overstatement mainly reputation loss are most likely exceeding costs of understating earnings (Peasnell et al., 2005).

Nevertheless, even though the majority of studies prove in an almost univocal way that board independence is positively correlated to a reduction in earnings management and short-term practices there is also some evidence of the influence of variables which may be able to compromise the positive effect of board independence in reducing earnings management and short-termism and possibly its interaction with loyalty shares implementation.

Bradbury et al. (2006) were not able to observe a significant correlation between board independence and reduced abnormal accruals as a proxy for higher quality financial reporting.

[9] An asymmetric loss function applies a different penalty to the different directions of loss (Towards Data Science).

Park and Shin (2004) find that despite the general belief, the presence of outside directors on their own does not lead to a reduction in discretionary accruals, while directors who are officers of financial intermediaries decrease earnings management in particular abnormal accruals activity, given that with respect to ordinary outside directors they have a higher level of financial experience.

In their study on the impact of board independence on earnings manipulation in Italian family-controlled companies, Prencipe and Bar-Yosef (2011) are estimating board independence by including the proportion of independent directors on the board as a parameter. The authors show that in family-controlled companies, the percentage of independent members on the board of directors, a common proxy for board independence has a weaker effect on earnings management than in a non-family-controlled company given the tendency to have lower board members substantial independence, which in turn reduces the effectiveness of board independence on limiting the extent of earnings management.

A special attention should be paid to the selection of board members to benefit all shareholders a substantial level of board independence should be guaranteed (Prencipe and Bar-Yosef, 2011).

Chtourou et al. (2001) put in evidence the role of ownership stakes held by non-executive directors, as well as experience as board members with the firm and with other firms. In essence, to encourage outside directors to engage in ownership in the firm provides them with an incentive to better monitor management and multiple directorships allows them to improve governance competencies and gain additional knowledge of best practices. However, some doubts about the overall effectiveness of financial motivation used to align the interests of directors with those of shareholders are presented, since the authors find that non-executive directors' ownership stake is negatively associated with negative earnings management whereas it is positively associated with positive earnings management, although the association is not significant. Therefore, these measures may reduce the capability of non-executive directors to oversee the reliability and soundness of financial statements.

Wu et al. (2016) focus on the weakening effect of controlling shareholders' control on the ability of independent directors to inhibit earnings management. According to the authors, this happens because controlling shareholders have a stronger ability and

motivation to expropriate the wealth of minor shareholders and lead to a higher level of engagement in earnings management in order to cover such activities.
Moreover, controlling shareholders may have a tendency to elect external directors who are not really independent to maintain their control. In fact, since controlling shareholders have the majority of voting rights they can prevail in the election of independent directors, therefore the nomination process should be as transparent as possible (Wu et al., 2016).

Another critical aspect highlighted by Wu et al. (2016) is the role of the divergence of cash-flow right and control of controlling shareholders that as stated by the authors leads to a reduction in independent directors' capability of inhibiting earnings management. In fact, a significant positive relationship between this divergence and earnings management is observed, given the fact that the higher this divergence is the more inclined controlling shareholders are to expropriate minor shareholders' equity and increase the likelihood that such appropriations are concealed with earnings management.
In the case of controlling shareholders, this disparity between voting and cash flow rights intensifies earnings manipulation, especially when the level of separation is relatively high (Bozec, 2008).
Haw et al. (2004) argue that to avoid external monitoring, legal costs and reputation losses, these control benefits and non-value maximizing decisions bring a higher tendency to manage reported accounting income through discretionary accruals, likely to be less costly than real operating decisions.
This is confirmed by Grimaldi and Muserra (2017) for the Italian context, controlling shareholders and mangers have incentives to acquire private control benefits and then to manipulate accounting reports in order to conceal their diversion activities. In addition, the authors also confirm that minority investors are vulnerable to expropriation particularly when the controlling shareholder holds control rights in excess of a commensurate capital investment.

This wedge is potentially leading to agency problems and conflicts of interests between minority and majority shareholders (Type II agency conflict).

As stated by Alvaro et al. (2014), the proportionality between cash-flow rights and voting rights is commonly recognized as beneficial as it allows economic interests and voting power to be aligned, driving controlling shareholders to be more likely to pursue value-maximizing strategies. However, there are various control-enhancing mechanisms adopted by various jurisdictions, of which loyalty shares are part, allowing shareholders to increase control without detaining a proportional equity stake and therefore creating the aforementioned wedge.
As confirmed by Becht et al (2020) who found that the divergence of the control rights and cash flow rights in state-controlled firms increased from 0.69 percent before the Loi Florange to 5.7 percent after passage of the act. Therefore, the French government enhanced its control rights through this reform.

As the word independence itself says, the more independent the members of a board are the more likely they will be able to effectively and impartially monitor the use of practices shaped by the focus on short-term results such as the manipulation of earnings.
Therefore, the evidence that board independence is correlated to a lower level of earnings management and thus less short-termism is almost unambiguous even if some authors prove that the influence of other moderating variables appears to weaken this relationship, namely the family-controlled status of a company, independent directors ownership stakes and the presence of controlling shareholders.
Most importantly, according to some authors the presence of a divergence of control and cash flow rights for controlling shareholders which is related to the introduction of control-enhancing mechanisms, such as loyalty shares could potentially impair the ability of independent directors to curb the management of earnings.

3.2. CEO narcissism

Hypothesis 2: the introduction of loyalty shares helps reducing earnings management and short-termism to a higher extent in the presence of a narcissistic CEO

As previously mentioned, one of the possible drivers of short-termism are assumed to be the shareholders that are the subjects directly targeted by loyalty shares, in fact

behind a shareholder willing to hold loyalty shares there is an incentive, provided by rewards, to be more focused on long-term results.

Another possible driver of short-termism in accordance with agency theory are opportunistic managers (Mio et al., 2020).
In fact, scandals such as Enron[10] contributed to the public perception that earnings management is utilized opportunistically by firm managers for their own private benefits (Jiraporn et al. 2008).
Heflin et al. (2002) argue that managers tend to apply accounting methods in order to mitigate contractual restrictions on their behavior and maximize personal welfare, even though agency theory indicates that accounting-based contractual and governance mechanisms such as compensation agreements and dividend payment restrictions are imposed on managers to reduce opportunistic behavior and agency costs.

However, as stated by Mio et al. (2020) assuming that short-termism is determined by shareholders, the acquisition of more voting power by "loyal" shareholders may push management to focus on satisfying them through more long-term oriented decisions. Moreover, if managers are considered the driver of short-termism, loyalty shares give shareholders motivation and authority to engage with managers in order to limit managerial opportunism and short-termism through shareholder activism.
But despite this opportunity provided by loyalty shares to enhance the monitoring role of more long-term oriented shareholders, opportunistic managers may still be able to interfere by engaging in earnings management practices.

Many scholars have focused on the role of management personality regarding decisions to manage earnings.
A personality trait commonly attracting interest in leadership research is narcissism (Capalbo et al., 2018).
In particular, the relationship between CEO narcissism and earnings management as well as criteria to determine the levels of CEO narcissism is widely analyzed.

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[10] One of the most notorious accounting scandals of all time. Enron Corporation through deceiving accounting practices was able to distort the performance of the company and trick investors. Agency issues and misalignment of corporate objectives versus management incentives were believed to be a key triggering aspect (Corporate Finance Institute).

Thus, a more complete understanding of the impact of loyalty shares could be given by looking at whether loyalty shares are able to limit the fact that CEOs with a narcissistic personality trait seem to be particularly focused on short-term performance and results. In fact, in order to deliver a successful image of the company they manage, narcissistic CEOs are inevitably prone to a short-termist approach in the management of earnings.

Quarterly and annual releases of accounting information are an opportunity for CEOs to be positively recognized for the performance of their company and narcissistic characteristics could ease high levels of performance but may also lead CEOs to use their influence over financial and accounting figures (Olsen et al., 2014).

Olsen et al. (2014) argue that a significantly positive relationship between CEO narcissism and reported financial performance numbers exists. The authors are using a measure composed of CEO's relative cash pay and non-cash pay to the second-highest paid executive and the size and composition of CEO's picture in the annual report to infer narcissism by examining and rating the prominence of the CEO's photograph. The results obtained by the authors show that narcissistic personality characteristics of top executives are more likely to have an effect on financial performance measures through decisions regarding real and operational activities rather than accrual-based and accounting manipulations.

Lin et. al. (2020) state that CEOs with narcissistic tendencies are more likely to be involved in earnings management in response to the pressure to satisfy earnings thresholds and to compensate for their performance. The authors argue that CEOs are manipulating earnings in order to meet three main earnings thresholds: prior year's reported earnings, zero earnings[11] and analysts' forecasts.

Capalbo et al. (2018) are also highlighting that CEO personality has an important effect on accounting choices, as narcissistic leaders tend to over-identify themselves with the organization they manage. The authors report a positive and statistically significant relation between changes in CEO narcissism score and changes in earnings management.

[11] The zero earnings level is the loss-avoidance benchmark describing the goal that firms would rather have a small profit instead of a small loss (Ronen and Yaari, 2008).

However, organizational identification can help expose the positive side of narcissism, when CEOs strongly identify with their firms, they tend to have alignment between self-enhancing goals and organizational goals and will act in order to benefit the organization in addition to themselves (Reina et al., 2014).

Kontesa et al. (2020) argue that shareholders should be warned by the number of CEO photographs in annual reports, a possible signal of self-centric earnings management.

Narcissistic CEOs are managing corporate earnings to fulfil their ego thereby creating new agency costs[12] for the company and impacting shareholders' wealth (Kontesa et al., 2020).

Buchholz et al. (2020) discuss results supporting evidence of narcissistic CEOs engaging in accrual-based earnings management both income-increasing and income-decreasing. In particular, income-decreasing earnings management is observed at a specific moment, which is the change from a weakly to a highly narcissistic CEO so as to make the predecessor accountable for poor performance or to opportunistically improve personal position before executive compensation negotiations.

Accounting choices by narcissistic CEOs are motivated by self-serving behavior influencing shareholders' perception of current and future earnings performance leading to lower earnings quality (Buchholz et al., 2020).

Therefore, the available literature provides evidence that CEOs identified as narcissistic are linked to the practice of earnings management in order to boost the positive perception of their job in managing the company both accounting and real manipulations. As reported by Olsen et al. (2014) narcissistic CEOs pursue operational strategies by engaging in real activities, such as increases to production and sales to increase accounting performance measures.

By analyzing how loyalty shares interact with the narcissistic personality of a CEO could give a useful insight related to whether the mechanism by which loyalty shares reduce short-termism is negatively influenced by CEO narcissism or whether it is able to reduce earnings management in spite of a narcissistic CEO.

[12] Agency costs are internal costs incurred due to the competing interests of shareholders (principals) and the management team (agents). Expenses that are associated with resolving this disagreement and managing the relationship are referred to as agency costs (Corporate Finance Institute).

As stated by Fried (2015) long-term shareholders may have a greater interest in reducing managerial agency costs than short-term shareholders because they hold their shares for a longer time, they may also find it easier to evaluate managerial performance as they are more familiar with it. Managers may be more willing to satisfy the demands of long-term shareholders than the demands of short-term shareholders, given that the long-term shareholders are there to stay.

CEOs engage in myopic behavior if they enjoy a short-term benefit with little exposure to long-term costs, a critical incentive for executives is represented by stock option vesting periods, given that options can be exercised after they vest. The shortening of vesting periods leads to short-term oriented actions as well as higher short-term reported earnings since equity holdings can be sold before the long-term costs of their decisions take place (Ladika and Sautner, 2020).

The role of stock options is highlighted also by Bolton and Samama (2013), the authors state that CEOs remain concerned about quarterly performance because they know they can be dismissed before their stock options vest if shareholders are not satisfied with their reported quarterly earnings. Consequently, many CEOs boost short-term earnings at the expense of long-run value maximization.

As stated by Patel and Cooper (2014) narcissistic CEOs are sensitive to option-based incentives.

Narcissistic CEOs tend to receive more total direct compensation (salary, bonus, and stock options) and have larger pay gaps between their own higher compensation and the other members of the senior management team compared to CEOs who are less narcissistic (O'Reilly et al., 2014).

And as expressed by Buyl et al. (2019) the specific features of a narcissistic personality, such as focus on personal rewards make narcissistic CEOs more responsive to stock options, also increasing the riskiness of policies.

Wowak and Hambrick (2010) state that high levels of self-confidence meaning the subjective belief in one’s capability to generate outcomes yielding a payoff, a trait characterizing narcissism, make executives more responsive to incentives therefore leading them to engage in actions aimed at boosting firm performance in order to attain rewards.

However, even if CEOs may exhibit a “horizon problem” whereby they are reluctant to make decisions beneficial to the firm in the long term but potentially costly to personal wealth in the short-term, a moderating role is played by strong organizational identification which leads to a lower likelihood to behave opportunistically (Abernethy et al., 2019). And as previously stated, narcissistic CEOs are prone to organizational identification.

In their survey to executives, Graham et al. (2005) report that for the majority of respondents, both CEOs and CFOs, the main reason to reach a certain earnings benchmark is driven by career concerns and that the career concern motivation for managing earnings is gaining attention among scholars.

As it is commonly acknowledged narcissism is peculiar of leaders such as CEOs and traits such as dominance, self-confidence, sense of entitlement and grandiosity often lead narcissists to emerge as leaders (O'Reilly et al., 2014).

Rovelli and Curnis (2020) fill a gap in the literature and analyze the role of a highly narcissistic personality in CEO career development and find that narcissistic CEOs become CEOs sooner, have quicker career development and climb the hierarchical chain faster.

Therefore, it seems evident that much like CEOs in general, narcissistic CEOs exhibit career concerns as well as showing a particular responsiveness to stock options and performance-based incentives. Consistently with their personality traits they are extremely focused on reaching career goals and attaining rewards, both these aspects have an important influence on the practice of earnings management.

Various reasons could increase the tendency of narcissistic CEOs to engage in earnings management but it is still not known if loyalty shares might be able to contain, through the enhanced monitoring of empowered long-term oriented holders of loyalty shares, their propensity to be strongly focused on short-term performance, rewards and career concerns often at the expense of long-term value maximization.

Some scholars find elements which could limit CEO narcissism consequences on the relationship with shareholders and possibly have an impact on the relation with loyalty shares, such as a well-designed compensation plan with publicly available performance measures that could improve the alignment of narcissistic CEOs’ self-perceived interests

with those of the shareholders and a strong and independent board of directors that can closely monitor managers for deceptive and self-interested behavior as well as quickly remove a problematic CEO (Alderman et al., 2020).
Moreover, when CEOs are highly identified with their organizations, narcissistic CEOs may still use the organization and the top management team (TMT) in order to serve their own needs for admiration and applause, however they are less likely to pursue these goals at the cost of the collective good of the organization and they are likely to be perceived as more charismatic due to the content of their charisma which is rooted in the organization's values and its collective identity (Reina et al., 2014).
Loyalty shares should favor a more long-term corporate orientation leading executives' horizons to match shareholders' horizons. If more shareholders, with more votes, hold for the longer-term, then executives' time horizons should adapt (Roe and Cenzi Venezze, 2021).

3.3. Gender

Hypothesis 3: women directors positively interact with loyalty shares to reduce earnings management and short-termism

The role of women on boards is widely analyzed by literature in various aspects, given that historically women have been excluded from participation in corporate boards, scholars investigate the changes brought by the increased presence of women determined also by the introduction of gender quota systems in some countries.

A prevalent aspect considered by scholars is the relation between female directors and earnings management which could be useful to understand how loyalty shares are influenced by women on boards.

In particular, women directors seem to enhance monitoring on managerial opportunism which as previously said could be a potential driver of short-termism.
Zalata et al. (2019) investigate which of the two board of directors' roles, advisory or monitoring is performed more effectively by female directors and has an impact on shareholders, focusing on the effect on managerial opportunism and earnings management. The authors find evidence indicating that female directors who hold

monitoring roles weaken managerial opportunism as measured by discretionary accruals. Therefore, according to the authors this represents an important implication for corporate boards gender diversity and for regulating gender quotas, as in order to increase the level of integrity of financial reporting and investors' confidence it would be more efficient to appoint inside corporate boardrooms female directors into monitoring roles that appear to be more value-adding than advisory ones.

The mere participation of women directors within boardrooms may not necessarily lead to an improvement in the integrity of financial reporting, however the presence of female monitoring directors shows a tendency to exhibit better earnings quality (Zalata et al., 2019).

Gull et al. (2018) reveal a negative association between the presence of women on the board and the magnitude of earnings management, implying that specific characteristics of female directors may improve the effectiveness in monitoring and curbing earnings management, such as women directors' business education and expertise in fact, women directors with a business educational background and financial expertise are more likely to decrease the trend of managers to manipulate earnings. However, the authors also take into consideration other statutory and demographic variables and find a positive relationship between female directors and earnings management after these factors are added. Thus, suggesting that specific attributes of women directors have a higher degree of importance for the monitoring of earnings management than simply the presence or percentage of women on the board. In particular, experience has a positive effect on the magnitude of current discretionary accruals in accordance with the busyness and the contagion effect hypotheses.

As analyzed by Ahn et al. (2010), multiple directorships affect the quality of managerial oversight and shareholder wealth indicating that when directors become too busy the costs offset the benefits, given that it results in weakened managerial oversight and agency conflict. Fich and Shivdasani (2006) state that firms in which the majority of outside directors hold more than three directorships are associated with weaker corporate governance and result in reduced abnormal returns.

Chiu et al. (2013) are testing whether earnings management is spreading between firms via shared directors, in fact a firm has an increased likelihood of managing its earnings when it is sharing a director with a firm engaging in earnings management and a lower

likelihood in case of a common director with a non-manipulator. Earnings management contagion has a stronger effect when the interlocked director holds a leadership role or a position with accounting relevance.
Consequently, the decision to appoint women should not be based on the blind implementation of gender quotas but the priority should be given to specific statutory and demographic attributes (Gull et al., 2018).

However, not only specific statutory and demographic characteristics of women directors play an important role but also the environment both inside and outside the board may constraint or improve the ability of female directors in monitoring opportunistic managers and mitigating earnings management.
According to Kyaw et al. (2015) gender diverse boards are mitigating earnings management in countries where there is a higher level of gender equality, women's right empowerment by the institutional system represents the real supporting factor and not just the proportion of female board members nor the gender regulations. Therefore, benefits can be brought to the company by the presence of female directors if the environment truly empowers women in their workplace.
Kouaib and Almulhim (2019) agree that board gender diversity is negatively associated with accruals-based and real earnings management activities. Increased female representation on corporate boards in Europe mitigates earnings management especially when there is a similar level of empowerment in the workplace with respect to male counterparts. Firms with more gender-diverse boards are monitoring managers more intensely and show increased earnings quality.
Arun et al. (2015) analyze the UK context and find that female and independent female directors adopt reduced earnings management practices. The authors distinguish between complex and simple companies depending on the level of debt, female directors are positively and significantly associated to earnings management in simple companies, as female and independent female directors are more likely to act conservatively in applying financial reporting policies and engage in income-decreasing earnings management. Therefore, indicating that in low-debt firms with more female directors are manipulating earnings downwards more than their counterparts with a low number of females. The authors argue that female directors may reduce the level of

income-increasing earnings management. In high-debt firms no significant association to earnings management is found and given that low-debt firms have smaller boards than high-debt firms, females on boards are more effective at constraining earnings management on smaller than on larger boards, however since female representation in corporate boards is still limited their substantial impact on earnings management may also be limited.

Many authors focus specifically on recent policies implemented by various legislations to increase the presence of women on corporate boards, the evidence provided regarding the effects of such policies is mixed.

The empirical results by Mnif and Cherif (2020) indicate that the participation of female directors in boards is reducing the degree of earnings management, therefore confirming a negative relation between female board directorship and the management of earnings and the same is observed for independent female directors. However, this relation is not holding in the case of family-affiliated female directors in family-owned and –controlled firms as a positive relationship emerges between family-affiliated female directors and earnings management upon the gender quota reform. The authors are focusing on comparing the pre- with the post- mandatory gender quota implementation in France and demonstrate that the reform is mitigating the favorable impact of women directorship on earnings quality. The meeting of thresholds established by gender quota legislation leads to appointment of family-affiliated female directors thus increasing the likelihood of less qualified women directors.

Therefore, the implementation of gender quotas should be aimed at increasing the proportion of independent female directors rather than their family-affiliated counterparts that are more likely to be selected based on their family links instead of merit. Female directors’ attributes such as independence seem to be the real driver for enhancing board proceedings and financial reporting quality rather than the mere participation on the company’s board (Mnif and Cherif, 2020).

Saona et al. (2019) adopt a multi-country approach in investigating the role of gender quotas among European countries, their results confirm that having gender balanced boards is beneficial even in terms of earnings management practices as in countries adopting gender quota systems companies are manipulating earnings less aggressively

with respects to countries not applying quota systems. As women are more concerned about business ethics and risk aversion, board gender diversity is limiting managerial opportunistic behavior and leading to more informative financial statements. The authors consider board gender diversity as an instrument of corporate governance that is reducing earnings management practices in European companies.
Even if Adams and Funk (2012) provide evidence that female directors can be more risk-loving than male counterparts.

The consideration of women equality perception is undoubtedly a fundamental factor that influences the effectiveness women contribute to board decision-making and strategic involvement (Nielsen and Huse, 2010). Measures to promote family conciliation and reduce gender discrimination could foster a more active participation of women in the corporate sector so as to remove the so called "glass ceiling"[13] limiting the advancement of women in senior positions (Saona et al., 2019).
Always focusing on the French context, Triki Damak (2018) conclude that the implementation of gender quotas in France has led to a decreased level of earnings management as women have proven to be more ethically concerned as well as more effective in their monitoring role with respect to male directors. This relation appears more significant in firms with a lower institutional participation.
Lakhal et al. (2015) suggest that the proportion of women on the board is a crucial corporate governance device resulting in more effective monitoring and therefore lower earnings management. The authors find that the presence of at least three women on the board supports this negative relation indicating that by increasing the number of women on boards through legislation French firms are likely to improve the board effectiveness in detecting this practice.
In fact, as stated by Adams and Ferreira (2009) female directors actively participate to board meetings therefore strengthening the supervision of the board, as they have better attendance records than male directors, additionally male directors have less

[13] "Glass ceiling" refers to the idea that there is an invisible barrier that blocks the progression of some groups within an organization, such as women and other minorities (Broughton and Miller, 2009).
This popular notion implies that these disadvantages are stronger at the top of the hierarchy than at lower levels and worsen later in one's career (Cotter et al., 2011).

attendance problems in more gender diverse boards. Female directors appear to have an impact that is comparable to that of independence directors. Despite that, according to the authors there is not enough evidence in support of quota-based policies. Even if a tougher monitoring, higher incentive alignment and higher participation by directors are expected to have positive consequences on corporate performance as boards are essential in mitigating agency problems between managers and shareholders and therefore stronger governance should increase shareholder value.

However, there is also some evidence that over monitoring could potentially decrease shareholder value, Adams and Ferreira (2007) state that greater board interference could affect communication between managers and directors. If increased participation by directors leads to more interference, gender diversity in the boardroom could negatively influence performance (Adams and Ferreira, 2009).

Marchini et al. (2017) are focusing on the Italian context and find a negative but not statistically significant coefficient between the presence of women on the board and earnings management.

Evidence from Italy is also provided by Bianco et al. (2013) showing that in the majority of diverse boards at least one of the female members has a family connection with the controlling shareholder, this situation is more frequent in smaller companies, firms with a concentrated ownership, firms operating into the consumer sector and firms with larger boards. On the contrary, unaffiliated women are common in widely held companies, companies with educated boards, those with more independent directors and those with fewer connected directors. Moreover, the number of board meetings is positively related with women directors.

Theories of gender literature are used by scholars to quote the characteristics that seem to be stronger in women with respect to men and that may have an impact on earnings management.

Gavious et al. (2012) find that firms having a higher female representation in corporate governance show a lower extent of earnings management despite receiving weaker external monitoring suggesting that firm valuations are positively affected. The authors rely on theories in gender literature and the distinctive characteristics of women in decision-making and risk-taking. In fact, a higher level of morality is reported among

women as well as higher levels of anxiety given that women tend to blame themselves for failures whereas men display more self-confidence, furthermore men have higher expectations and they may take more risks in order to realize expectations. Consistently with gender literature, the authors confirm that female directors lead to an improvement in board functioning and efficiency as women are given less space for mistakes than men and in practice means that they are more risk-averse and would prefer to avoid managing earnings.

Carter et al. (2003) suggest that a more diverse board should be a less likely to undermine shareholders' interest as well as being a better monitoring mechanism for managers, primarily because board independence is expected to be enhanced by the presence of diversity of gender or ethnicity or culture. In fact, a more diverse board might be a more activist board due to the presence directors with non-traditional characteristics. Moreover, the authors provide evidence that firms that commit to increasing the number of women on the board also exhibit a higher presence of minorities and vice versa, resulting in a positive relation between firm value and board of directors' diversity.

Srinidhi et al. (2011) state that the inclusion of female directors could improve board oversight and independence and thereby earnings quality by reducing the extent of opportunistic earnings management. Gender literature suggests that women might be less tolerant with respect to men towards opportunistic behavior. The board is the body facing higher risk of litigation when lower earnings quality is affecting investors and given that female directors are more averse to litigation and reputation loss they are presumably acting resolutely for the improvement in earnings quality. Female participation is associated with better monitoring and improved earnings quality, a tangible consequence of the higher monitoring level.

Considering that earnings quality is recognized as a fundamental outcome of good governance required by investors, boards could plausibly increase female participation in order to improve board oversight and consequently achieve the objective of better earnings quality (Srinidhi et al., 2011).

Gavious et al, (2012) note also that although male and female directors do not necessarily show different abilities in detecting accounting irregularities as this ability is determined by financial background rather than gender, the response once accounting

manipulations have been detected is different, female directors tend to value more moral considerations and to avoid the potential negative effects resulting from a misrepresentation of earnings. Moreover, women consider works as a source of self-fulfillment whereas men are more focused on advancement and compensation which create incentives for earnings management.
Alternatively, firms employing more women in top management and governance positions are firms with a higher awareness for social, environmental, legal and ethical matters as they care more about their reputation, in such firms the probability that the firm engages in earnings manipulation might be already lower because of higher standards rather than the presence of women in the firm (Gavious et al., 2012).

Therefore, the evidence that women directors are negatively correlated to earnings management is not totally unambiguous as there are factors which according to the results provided by some scholars reverse the relationship. Moreover, doubts on quota systems are also highlighted given that in reaction to the pressure to reach those thresholds family-owned and -controlled companies might appoint family-affiliated women directors instead of engaging in a selection process based on merits.

As mentioned, according to some authors women directors appear to be more effective in monitoring roles, this might have an effect on loyalty shares implementation and more specifically on the enhancement in the monitoring of opportunistic managers. Even if undoubtedly, an important aspect is played by the specific characteristics of a director and not just the gender as well as the level of empowerment provided by the institutional system and by the workplace.
Arguments supported by gender theories show that women exhibit higher concerns about business ethics and risk aversion. Conversely, evidence about women being more risk lovers is also provided.
Moreover, presence of women directors may lead to increased board participation but on the other hand concerns about the effects of board interference are present.
If the positive aspects in support of women being less prone to engage in earnings management and more effective monitors prevail over the criticalities, their presence might indeed strengthen the evidence of loyalty shares reducing short-termism.

3.4. Tenure

Hypothesis 4: board tenure positively interacts with loyalty shares to reduce earnings management and short-termism

In the business world, experience is generally considered as a positive aspect, nonetheless for what corporate directors are concerned, tenure is increasingly viewed with suspicion (Pozen and Hamacher, 2015).

Director tenure is gaining considerable attention among governance experts and market participants and a growing number of countries have introduced rules capping maximum tenure between nine and twelve years in order to be qualified as independent director. While some argue that boards with many long-serving directors become entrenched and indifferent to shareholders preferences and concerns, others are convinced that long-tenured directors are meaningful components of a firm and contribute to long-term value creation for stakeholders in general (Bonini et al.,2017; Huang and Hilary, 2018).

Considering this aspect, even if the evidence available in the literature is contrasting, could give an additional insight on how loyalty shares relate to corporate governance and mainly board of directors' fundamental characteristics.

Many scholars find a negative association with earnings management, which could possibly reinforce the effect produced by the introduction of loyalty shares.
Chtourou et al. (2001) are empirically testing the fact that earnings management has a negative association with average non-executive director's tenure. Thus, supporting the view that experience as board members leads non-executive directors to gain competencies in corporate governance as well as a better understanding of the firm and its executive directors.
Bonini et al. (2017) find that the presence of a director with very long tenure provides a benefit for the company leading to higher information acquisition and disclosure.
Beasley (1996) examines also the likelihood of financial statement fraud associated to outside directors tenure and find a negative association even if longer tenures may lead to entrenchment with top management whereas new directors may be more vigilant.

As argued by Perols and Lougee (2011) there is a relation between earnings management and financial statement fraud, the authors find that fraud firms have an higher likelihood to have managed earnings in previous years and that earnings management in prior years is associated with a higher probability that firms beating analyst forecasts commit fraud.

In support of the fact that longer tenured directors are more effectively monitoring, Dou et al. (2015) argue that efforts to impose term limits may be misguided as they find that firms with a higher proportion of directors with extended tenures have higher CEO turnover-performance sensitivity and lower likelihood of intentionally misreporting earnings, suggesting that experienced directors on the board may alleviate agency problems. Firms with more experienced directors, with a tenure greater than 15 years are less likely to make earnings restatements, therefore providing evidence that such directors provide a balance of power in the boardroom. Excessive monitoring may lead managers to withhold information from the board, however experienced directors may have developed firm-level expertise and therefore do not necessarily have the need to rely on management for insight into firm operations. Thus, showing that the presence of experienced directors improves both strategic advice and monitoring decision-making, making a valuable contribution to corporate governance (Dou et al., 2015).

Pozen and Hamacher (2015) argue that the logic behind board term limits is faulty and represents a threat to performance. In fact, turnover in executive ranks is relatively high and this would inhibit the building of close relationships between board and management. While term limits refresh the board which can be desirable, they lead also to loss in experience and knowledge.

As suggested by Bushee (2018), corporate managers have a tendency to reduce investment in R&D to meet short-term earnings goals.

Kim and Lee (2019) focus on R&D and SG&A expenses as the management team can easily manipulate these items when facing pressure to improve the bottom line. However, the authors find that firms with long-tenured boards have smoother investment patterns human or organizational capital, moreover the conjecture that low return volatility is caused by earnings manipulation is not supported by this analysis.

Livnat et al. (2021) view longer board tenure as an index of a firm’s stability, indicating that shareholders are satisfied with the appointed directors and that the board is

effective at monitoring and advising management. If shareholders are dissatisfied with its functioning, they refresh the board with a more relevant mix of director capital consequently reducing average board tenure.

On the other hand, a positive association with earnings management is highlighted by another stream of literature contrasting with the previously reported ideas. This could suggest that loyalty shares effect on earnings management may be potentially hindered by the presence of long-tenured boards.

The impact of social ties is expected to grow as tenure grows, board members who have served with the same close group for several years are more likely to suffer from "social bias" which could potentially affect independence. Nevertheless, as a board member tenure grows the confidence, networking and knowledge may also increase the level of independence in the context of the board relationship with the CEO. Since, tenure of CEOs is on average shorter than that of a director it can be argued that a tenured director is more independent vis-à-vis the CEO and not vice versa. Moreover, when both managers and directors hold substantial equity interests in the company their interest might be better aligned to maximize firm value, but on the other hand this alignment between the monitor and the management might affect shareholders' interests leading to the risk of earnings management and monitoring failure (Nili, 2016).

Park and Shin (2004) were not able to find evidence that earnings management decreases with average tenure as board members for outside directors. The authors are investigating this variable because of the acquired experience on the company board by directors serving for longer periods. In fact, a more complete understanding on the firm and its people may help directors to be improve their monitoring competencies of earnings management activity.

Xie et al. (2003) show a positive relation between tenure of outside directors and the level of discretionary current accruals as board members with a longer director tenure may be less effective in monitoring as they may have been co-opted by management.

Katz et al. (2016) mention that concerns are raised by some investors about directors' independence defined as the linchpin of good corporate governance and according to those investors director term limits might represent another avenue to address these concerns. In fact, shareholder groups and institutional investors have started to include

director tenure considerations into company evaluations. A source of these pressures may be that recently the average age of directors has risen and mandatory director retirement ages have been increased or eliminated, as public companies wish to retain experienced directors and many are active later in life with respect to previous generations. A long service as an independent director on boards is considered by some as creating a conflict given that extended tenure may lead to a closer relationship with executives.

Nili (2016) states that a related issue stems from the impact of long-tenured directors on the independence of new coming directors and the ability of the boardroom to foster an openness to new ideas because of the level of influence of longer tenured directors, they may intentionally or inadvertently encourage conformity to group thinking. Even if a unified board may be more effective against managerial opportunism, when tenured members become entrenched with management or when the interest of shareholders diverges from the interests of some board members this may pose a threat to objective decision making.

Huang and Hilary (2018) show that board tenure has a quadratic relation with the quality of corporate decisions such as financial reporting quality measured also by abnormal accruals. These results indicate that for short-tenured board the marginal effect of board learning dominates the entrenchment effect, vice versa for long-tenured boards where on-the-job learning is improving the firm's value until it reaches a certain threshold after which entrenchment is dominating.

As found by Vafeas (2003) the presence of directors with twenty or more years of service represents a sign of CEO entrenchment thus suggesting that extreme lengths of board tenure may be detrimental to shareholders interests. Appropriate board tenure appears to be a relevant corporate boards policy issue, given that seasoned board are less likely to effectively monitor managers as directors become less mobile and less employable. The authors show that committees with a senior director participation are inflating CEO salaries thus compromising shareholder interests.

Libit and Freier (2016) present some arguments in favor and against director tenure limits. In particular, the authors state that such policies may strengthen independence given that lengthy tenure may foster deference to management instead of loyalty to the company and the shareholders, as well as encouraging new perspectives and board

diversity. Moreover, such policies would address the so-called “zombie” directors who have served on a board for several years that may lose enthusiasm and simply go through motions. On the other hand, long-serving directors often acquire considerable experience or organizational knowledge which may require several years to be obtained. Such policies may be unnecessary because long-term shareholder value may be more influenced by other factors including corporate management and strategy. Longer-tenured directors may be more likely to challenge and have a better ability to evaluate management compared to newer members. And lastly, the empirical evidence about whether director tenure influences long-term shareholder value is conflicting.

Therefore, board tenure is widely considered by both scholars and investors, however there is no unambiguous evidence on whether long-term director are more effective monitors given their level of knowledge and experience or they become entrenched and socially biased towards management or indifferent to shareholders preferences and less engaged in monitoring.

If the positive effects provided by a higher level of experience and knowledge of the specific business and company overcome the potential entrenchment with management, implementing loyalty shares in firms with long-tenured board may increase their effectiveness, contrarily if entrenchment is indeed stronger the limiting of short-termism brought by loyalty shares may be compromised.

4. Methodology

The empirical analysis performed in this thesis is based on the sample and follows the methodology developed and adopted by Mio et al. (2020). The focus is on Italy, one of the countries that has a specific legislation about loyalty shares since 2014.

4.1. Sample selection

The sample was the same used by Mio et al. (2020), 1,316 firm-year observations of Italian listed firms with a data sampling period from 2008 to 2017, excluding financial companies because of the peculiarity of their accounting practices.
Firms with sufficient data for the estimation of accrual-based earnings management on Refinitiv Eikon database (previously known as Thomson Reuters Eikon) were included.
Data about the issuance of loyalty shares and the date of issuance was hand-collected by the authors in October of 2018 from the investor relations section on the companies' websites.

4.2. Measures of earnings management

Consistently with previous literature Mio et al. (2020) selected as a proxy for short-termism earnings management, using the modified Jones model developed by Dechow et al. (1995).
As investigated by Brochet et al. (2015) the time horizon of corporate disclosure is symptomatic of short-termism, the short-termism proxy has a positive association with accruals and real earnings management in order to meet short-term market related goals.

According to Dechow (1994), discretionary accruals provide managers the opportunity to manipulate earnings due to the flexibility available.
To detect earnings management, Healy (1985) was the first to introduce discretionary accruals (Sun and Rath, 2010).
Given that the manager can choose discretionary accruals from an opportunity set of generally accepted procedures defined by accounting standard-setting bodies, such as

the method of depreciating long-lived assets or the method for allocating fixed overheads (Healy, 1985).
According to Healy (1985), voluntary changes in accounting procedures reflect only discretionary accounting procedure decisions.
Moreover, DeAngelo (1986) considers that the average change in non-discretionary accruals is zero, so that a change in total accruals reflects a change in discretionary accruals.
As stated by Sun and Rath (2010), both Healy (1985) and DeAngelo (1986) neglected the changes in non-discretionary accruals, misclassifying all accruals as the discretionary component and stating that earnings management activities can be captured by total accruals. Therefore, these approaches tend to detect earnings management with error.

To overcome this limitation, Jones (1991) controls for the non-discretionary determinants of accruals (Sun and Rath, 2010).
To relax the assumption that the difference between current- and prior-year accruals is due only to changes in discretionary accruals as non-discretionary accruals are assumed to be constant from period to period, Jones (1991) used changes in revenues to control for non-discretionary accruals of working capital accounts (receivables, inventory and payables) and gross property, plant and equipment to control for the non-discretionary component of depreciation expense. The proxy for earnings management that is discretionary accruals was estimated as residuals from regression of total accruals on non-discretionary determinants of accruals.

However, according to Dechow et al. (1995) the model developed by Jones (1991) is successful at explaining around one quarter of the variation in total accruals. The authors also state that the previously quoted models (DeAngelo, 1986; Healy, 1985; Jones, 1991) have low testing power for earnings management of economically plausible magnitudes such as 1%-5% of total assets.
The Jones model shows a low explanatory power, about 10% of the variation in accruals, one possible interpretation is that managers have a considerable discretion over the accrual process used to disguise fundamental performance (Dechow et al., 2010).

Xie (2001) states that Jones model-estimated abnormal accruals capture managerial discretion with error, although the author develops a sensitivity analysis controlling for major unusual accruals to improve this proxy for managerial discretion.
There are factors systematically contaminating the Jones (1991) model residuals' ability to capture managerial discretion, given that residuals are capturing also unusual nondiscretionary accruals and unintentional misstatements, due to this measurement error it is difficult to determine whether the market overprices the abnormal accruals from earnings management or from unusual business circumstances. It appears that the market overprices abnormal accruals for what one-year ahead earnings are concerned (Xie, 2001).

Misclassification errors can comprise type I errors[14] classifying accruals as abnormal when in truth they are representing fundamental performance and type II errors[15], classifying accruals as normal when they abnormal (Dechow et al., 2010).
All models of discretionary accruals run the risk of misclassifying nondiscretionary accruals as discretionary. Total accruals are strongly correlated (around 80%) with discretionary accrual estimates (Dechow et al., 2003).

As a proxy for corporate short-termism Mio et al. (2020) used earnings management measured by the Modified Jones Model (Dechow et al., 1995), the same model is employed in this thesis.
The model residual of the following regression was followed to isolate the discretionary accruals.

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[14] Type I error, also known as “false positive” is the error of rejecting a null hypothesis when it is actually true, the error of accepting an alternative hypothesis (the real hypothesis of interest) when the results can be attributed to chance. It occurs when a difference is observed when in truth there is no statistically significant difference (University of California, Berkeley).
Type I errors arise when the null hypothesis that earnings are not systematically managed in response to the stimulus identified by the researcher is rejected when the null is true (Dechow et al., 1995).

[15] Type II error, also known as "false negative" is the error of not rejecting a null hypothesis when the alternative hypothesis is the true state of nature. In other words, this is the error of failing to accept an alternative hypothesis. It occurs when a difference is not observed when in truth there is one (University of California, Berkeley).
Type II errors arise when the null hypothesis that earnings are not systematically managed in response to the stimulus identified by the researcher is not rejected when it is false (Dechow et al., 1995).

Modified Jones model (Dechow et al., 1995)

$$Acc_t = \alpha + \beta_1(\Delta Rev_t - \Delta Rec_t) + \beta_2 PPE_t + \varepsilon_t$$

where ACC represents total accruals; ΔRev_t the variation on revenues; ΔRec_t the variation on receivables and PPE_t property plant and equipment.

The Modified Jones Model developed by Dechow et al. (1995) provides powerful tests of earnings management, the adjustment relative to the original Jones Model consists in considering the change in revenues adjusted for the change in receivables in the event period and assumes that all changes in credit sales in the event period are the consequence of earnings management in an attempt to reduce type II errors. On the contrary, the original Jones Model assumes that discretion over revenue is not exercised.

This modified model assumes that all changes in credit sales in the event period result from earnings management, based on the reasoning that managing earnings is easier through the exercise of discretion over the recognition of revenue on credit sales than cash sales, thus avoiding the bias towards zero where earnings management has happened through the management of revenues (Dechow et al., 1995).

However, according to Holthausen (1995), the modified Jones model is biased in favor of rejecting the null hypothesis (Type I error).

Following Kothari et al. (2005), Mio et al. (2020) calculated accrual-based earnings management, through performance-matched discretionary accruals.

Kothari et al. (2005) introduced modifications into the Modified Jones Model (Dechow et al., 1995) in order to control for a firm’s performance, return on assets (ROA) was used as an additional regressor.

Performance matching on ROA controls for the effects of performance on discretionary accruals enhancing the reliability of inferences in hypothesis tests implying earnings management not varying with performance or where control firms are not expected to have managed earnings. For the Jones and Modified Jones models over-rejection of the null hypothesis is apparent in tests of negative discretionary accruals and under-rejection frequently occurs when testing for positive discretionary accruals.

Performance-matched discretionary accrual measures are useful in mitigating type I errors when the variable of interest is correlated with performance (Kothari et al., 2005).

The variable of interest for the empirical analysis is discretionary accruals (DA), Mio et al. (2020) initially calculated total accruals as earnings before extraordinary items and discontinued operations minus operating cash flows reported in the statement of cash flows in year t (Zang, 2012).

Then, in order to isolate the discretionary component, the authors generated the residuals of Equation (1), which is an absolute value:

$$\frac{TA_{it}}{Assets_{it-1}} = \beta_0 + \beta_1 \frac{1}{Assets_{it-1}} + \beta_2 \frac{\Delta Sales - \Delta REC}{Assets_{it-1}} + \beta_3 \frac{PPE}{Assets_{it-1}} + \beta_4 Industry_i + \epsilon_i \quad (1)$$

where TA represents total accruals; $Assets_{it-1}$ the total assets of the previous year; ΔSales the change in sales from year t − 1 to year t; ΔREC the change in net receivables from year t − 1 to year t; PPE gross property, plant, and equipment in year t; and Industry a dummy variable for each industry in the sample.

Thus, the difference of cash and profit not described by assets, by the change in cash generated by the activity and the investment in property, plant and equipment is considered to be the DA, calculated as the absolute value of the residuals estimated from Equation (1) (Mio et al., 2020).

4.3. Difference-in-differences methodology

The difference-in-difference methodology was employed in the analyses for this thesis following the approach chosen by Mio et al. (2020).

The difference-in-difference methodology is applied in situations where certain groups are exposed to a given event and others are not. The logic of this methodology is best explained where there are two groups and two periods, in the first period none of the groups is exposed to the event, whereas in the second period one of the groups is exposed and the other is not (Schwerdt and Woessmann, 2020).

Therefore, given that loyalty shares have been legally allowed in Italy since 2014, a clear point in time is identified to test the periods before and after the issuance of loyalty shares with the aim to isolate the effects of such instruments. Moreover, loyalty shares are not compulsory and so it is also possible to identify the two groups of companies, the ones issuing loyalty shares and the ones not issuing them.

This method was chosen by Mio et al. (2020) given that it has been extensively employed even in accounting research with the objective of examining the effect of an event under two dimensions; "state" discriminating individuals being subject to treatment or not and "time" discriminating the period before and after treatment. The authors employed the difference-in-differences research design with the purpose of analyzing the effect of the implementation of loyalty shares under two dimensions "state" and "time". The "state" dimension compares the Italian listed companies issuing loyalty shares (LS = 1), representing the treated group with a benchmark group of Italian listed companies not issuing loyalty shares (LS = 0), the control group. The control group has the function of controlling for changes in the economic environment affecting earnings management but not related to issuing loyalty shares.
The other dimension, "time" is analyzing the period pre loyalty shares issuance (POST = 0) and post-issuance (POST = 1). For companies issuing loyalty shares the year of issuance was considered; whereas for non-issuers, POST that has a value of 1 corresponds to the period following 2014, after which companies in Italy were allowed to issue loyalty shares.

The variable of interest always relying on Mio et al. (2020) is the interaction term LS * POST between LS and POST, taking the value of one for issuers of loyalty shares in the post-issuance period.
This coefficient of the interaction variable defined "diff-in-diff estimate" is capturing the incremental variation in earnings management for loyalty shares issuers compared with loyalty shares non-issuers. Thus, the difference-in-difference methodology allows this coefficient to reflect only changes due to the implementation of loyalty shares and excludes other events that may have an impact on companies both in the treatment and control group during the sample period.

Mio et al. (2020) relied on a multivariate model introduced in Equation (2).

$$DA = \beta_0 + \beta_1 LS_{ij} + \beta_2 post_{ij} + \beta_3 \, LS * POST_{ij} + \beta_4 lsize_{ij} + \beta_5 leverage_{ij} + \beta_6 ROA_{ij} + \beta_7 LOSS_{ij} + \beta_8 industry_i + \beta_9 year_j + \varepsilon_i \quad (2)$$

where LS is the indicator variable that for loyalty share issuers is equal to 1 and for non-issuers it is equal to 0; POST is the indicator variable assuming the value of 1 for the years following the issuance of loyalty shares; LSize represents the natural logarithm of total assets; Leverage is the ratio between liabilities and total assets; ROA is the ratio between net income and total assets; LOSS is a dummy variable denoting loss years.
The expectation for the coefficient of this interaction term of loyalty shares and POST (LS * POST) is to be negative and significant.

4.4. Robustness test

Mio et al. (2020) also included a robustness test performed in order to alleviate issues such as endogeneity[16] and omitted variables bias by conducting placebo tests in the treated group.
The same approach is followed in this thesis through simulation of earlier loyalty shares issuance (one year), therefore the regressions are run lagging the variable of loyalty shares adoption 1 year, indicating that the company issued loyalty shares a year before than the company actually issued them.
The aim of these tests is to examine the impact of the placebo variable that identifies earlier loyalty shares issuance, a significant impact of this variable would indicate that there is some impact on earnings management and that what it is driving this result is an omitted unobservable variable.
The expectation is that there should be an insignificant impact of the placebo variable identifying the earlier loyalty shares issuance on earnings management so as to confirm that the effect on earnings management is solely due to loyalty shares issuance that should influence earnings management only after the company issued them.

[16] Endogeneity occurs when a variable, observed or unobserved, that is not included in the models, is related to a variable incorporated in the model (Stata).

4.5. Introduction of additional moderating variables

The main contribution of this thesis is to enrich the results already provided by Mio et al. (2020), introducing data about some moderating variables related to corporate governance, namely some characteristics of the board and using the same models employed by the authors conducting the regressions and econometrics tests performed with the inclusion of these additional variables.

Given that loyalty shares have been recently introduced in the Italian legislation and worldwide they are still considered a relatively unexplored control-enhancing mechanism, its effects have not been widely studied by scholars. In order to gain further insights into how loyalty shares interact with board characteristics, data about moderating variables associated to the companies already present is incorporated in the sample.

Four moderating variables are chosen with a view to understand how they interact with the earnings management reduction effect of loyalty shares detected by Mio et al. (2020).

In particular, data about independence, gender and tenure was collected from Refinitiv Eikon database whereas data about the CEO narcissism proxy was hand-collected.

Namely, Board Independence is represented as the percentage of independent non-executive[17] directors on the board.

This variable is of particular interest as various scholars bring evidence that more independent boards tend to reduce earnings management and are more prone to a long-term orientation, in addition, more independence implies less influence by shareholder preferences. On the other hand, some authors report that divergence of control and cash flow rights for controlling shareholders related to control-enhancing mechanisms, such as loyalty shares could potentially reduce the potential of independent directors to limit earnings management and short-termism.

[17] Not being involved in the management of the company defines the director as non-executive. The non-executive director plays an important role in providing objective judgement independent of management on issues facing the company (Deloitte).

The Italian *Corporate Governance Code*[18] by Comitato per la Corporate Governance (2018) states that independent non-executive directors do not hold or have recently held, directly or indirectly or on behalf of third parties commercial, financial or professional relationships with the issuer or subjects linked to the issuer, with a significance that may be able to condition their autonomous and unbiased ability of judgement of the management activity. Moreover, he/she should not be able to exercise a dominant influence over the issuer, be a close relative, have been holding the position of director of the issuer for more than nine years in the last twelve years; in addition, he/she should not receive a significant additional remuneration also in the form of incentive plans linked to the company's performance, such as stock option plans (Comitato per la Corporate Governance, 2018).

The variable gender indicates the percentage of women directors on the board. The inclusion of this variable is of interest because many scholars are reporting that women directors may lead to enhanced monitoring on managerial opportunism and reduced earnings management, this is supported also by theories of gender literature.
However, some authors are skeptical about blind implementation of gender quotas, stating that the specific statutory and demographic attributes of women directors play a more important role than simply the percentage of women on the board, as well as the level of real empowerment of both the inside and outside board.
As stated by Linciano et al. (2018) in the *Report on corporate governance of Italian listed companies* by Consob (Italy's supervisory authority for the Italian financial markets), like it happened in other European countries, representation of women on boards in Italy has been mostly driven by Law 120/2011 (Legge Golfo-Mosca) mandating gender quotas after 2012, the majority of listed companies have already reached the one-third quota. Since 2015, women have been present in nearly all corporate boards of Italian listed companies leading also to a slight decrease in the average age of directors given that newly appointed women tend to be younger with respect to men (Consob).

[18] The Corporate Governance Code is a voluntary code developed by the Corporate Governance Committee aimed at all companies with shares listed on the Mercato Telematico Azionario ("MTA"), the leading Italian Equity Market managed by Borsa Italiana.

Moreover, as reported by Solimene et al. (2017) the characteristics of women on Italy's corporate boards are generally Italian ethnic origin, high levels of education (master's and post-master's degree) and experience as professional figures.

The variable average tenure indicates how many years on average directors have served on the board. Some scholars find a negative association between tenure and earnings management whereas another stream of literature highlights a positive association. The two main arguments which are counterposed are experience and entrenchment with management.
An extended debate concerning board tenure and refreshment is occurring among both practitioners and academics, given that long-tenured directors tend to be associated with alignment with management whereas a shortening of directors' tenure may lead to insufficient experience in understanding the company and thus possible failures in their advisory and monitoring roles (Ji et al., 2021).
In fact, governance practitioners and investors have paid significant attention to the issue of board refreshment, as a stale board may become complacent, lacking of independence, new perspectives and diversity thus posing risks in relation to long-term performance and oversight of management. Therefore, companies may gain benefits by maintaining a balance of experience and new capacity on the board (Institutional Shareholder Services).

Another very widespread topic studied by scholars is CEO narcissism representing an important area of research due to the strategic implications of how this personality trait affects the behavior of CEOs (Cragun et al., 2020).
According to the literature CEOs with a narcissistic personality trait seem to be particularly focused on short-term results and career goals associated to increased earnings management.
On the other hand, as stated by Reina et al. (2014) narcissism is also associated to organizational identification that may potentially limit opportunistic behavior, which is connected to earnings management and therefore short-termism (Chandra and Wimelda, 2018).
Other factors which may potentially have an impact on the relation with loyalty shares, such as a well-designed compensation plan to improve the alignment of narcissistic

CEOs' interests with those of the shareholders as well as an independent board (Alderman et al., 2020).

Given that loyalty shares should favor a long-term orientation they should lead executives to match shareholders' horizons. If more shareholders with more votes hold shares in the long-term, then executives' time horizons should adapt (Roe and Cenzi Venezze, 2021).

The proxy that was used in order to infer data about CEO narcissism is one of the parameters chosen by Olsen et al. (2014) namely the presence and dimension of the CEO photograph on the company's annual reports as well as the presence of other executives in the photo. Various authors adopted this approach in their studies such as the previously cited Kontesa et al. (2020) and Lin et al. (2020).

This data was hand-collected from the annual reports on the website of each company included in the database specifically for the purpose of this thesis. A score from 1 to 5 following Olsen et al. (2014) was assigned, 1 indicating that there is no presence of CEO photograph on the annual report; 2 that the CEO was photographed with other executives; 3 that the CEO was photographed alone but the picture occupies less than half a page; 4 that the CEO was photographed alone and the picture occupies more than half a page with text taking up some space; 5 that the CEO was photographed on its own and the picture occupies the entire page.

All of these variables are interacted both with LS and with the term LS * POST in order to infer how they influence loyalty shares reducing earnings management and short-termism.

Further insights into the functioning of loyalty shares as a short-termism antidote could be provided by understanding whether the board of directors and its characteristics play a key role or the most influent driver of long termism is represented by the shareholders.

5. Results and discussion

5.1. Results

This part is summarizing the main results obtained through the employment of statistical techniques such as difference-in-differences methodology and regressions on the selected sample of Italian listed companies.

5.1.1. Descriptive statistics

The following data is the same reported in the study of Mio et al. (2020) and it is included for the sake of completeness given that the same sample was used to perform the statistical analyses for this thesis.

Table 5.1: Frequencies of the sample by year

	(1)	(2)	(3)	(4)
LS	No	No	Yes	Yes
POST	No	Yes	No	Yes
YEAR	Freq	Freq	Freq	Freq
2008	109		25	
2009	109		24	
2010	108		24	
2011	109		24	
2012	101		21	
2013	104		20	
2014		113	24	2
2015		109	12	15
2016		102	10	18
2017		106	3	24
Total	640	430	187	59

In Table 5.1 it is reported the frequency of the companies in the sample issuing loyalty shares by year and it can be seen 2015 was the year with the largest increase in the number of issuers.

As previously said LS is the dummy which indicates whether a company is issuing loyalty shares; POST is the dummy indicating the period after the issuance of loyalty shares, after 2014 that is the year in which Italian legislation allowed companies to issue this type of shares.

Another interesting aspect highlighted in the descriptive statistics by Mio et al. (2020) is the frequencies by industry, in Table 5.2, which reports the frequencies divided by industry, the top three industries for the number of loyalty shares issuers are

Table 5.2: Frequencies of the sample by industry

	(1)	(2)	(3)	(4)
LS	No	No	Yes	Yes
POST	No	Yes	No	Yes
SECTOR	Freq	Freq	Freq	Freq
Consumer discretionary	208	143	42	12
Consumer Staples	31	24	8	3
Energy	26	19		
Health Care	39	21	15	5
Industrials	140	103	64	19
Information technology	62	38	46	14
Materials	47	30	7	3
Real Estate	30	15		
Telecommunication services	18	11		
Utilities	39	26	5	3
Total	640	430	187	59

industrials, information technology and consumer discretionary[19]. In the following industries no companies have issued any loyalty share: energy, real estate and telecommunication services.

Finally, Table 5.3 reports the mean, standard deviation, minimum and maximum value of the main variables used for the estimations of Equation (2) as well as for the additional

[19] Companies that manufacture products and provide services purchased on a discretionary basis by consumers such as textiles, apparel and luxury goods, household durables and auto components.

moderating variables interacted with Equation (2). CEO duality (when the CEO is also the chairman of the board) and average age are also included as control variables.

Table 5.3: Descriptive statistics

	(1)	(2)	(3)	(4)	(5)
VARIABLES	N	mean	sd	min	max
LS	1,316	0.187	0.390	0	1
POST	1,316	0.372	0.483	0	1
LS * POST	1,316	0.0448	0.207	0	1
Ind %	1,159	0.415	0.175	0	0.867
Gender %	1,145	0.364	0.0594	0.140	0.570
CEO/Chair	1,159	0.319	0.466	0	1
Average Tenure	1,152	7.627	3.862	0.825	21.51
Average Age	1,159	56.36	4.400	40	71
CEO photo size	1,159	1.271	0.732	1	5
ROA	1,316	0.0237	0.119	-1.106	0.562
LSize	1,316	20.10	1.795	15.44	25.69
Leverage	1,316	0.835	0.294	0.169	1.833
LOSS	1,316	0.289	0.453	0	1
Da	1,316	-3.443	1.249	-7.250	-0.991

5.1.2. Univariate analysis

Always following Mio et al. (2020), an initial analysis of the association of variables is performed, namely a correlation test between the main variables involved in this thesis. The results can be seen in Table 5.4, as expected by the authors and confirmed in this study the relation between discretionary accruals (DA) and the interaction variable (LS * POST) is negative and significant.

Almost all variables are significantly correlated with DA, thus indicating that these variables are adequate controls for the regression. Relatively few correlations between the other variables in the models and the relatively low correlation coefficients suggest that there are no multicollinearity[20] issues.

[20] Multicollinearity occurs when an independent variable is highly correlated with one or more of the other independent variables in a multiple regression equation. An independent variable can be linearly predicted from one or multiple other independent variables with a substantial degree of certainty (Towards Data Science).

Table 5.4: Correlation matrix–Pearson

	1	2	3	4	5	6	7	8	9	10	11	12	13	14
1. Da	1													
2. ls	-0.0265	1												
3. post	-0.107***	-0.151***	1											
4. ls_post	-0.0923**	0.437***	0.287***	1										
5. ceo photo size	-0.0720*	-0.00103	0.00928	-0.0446	1									
6. ind	-0.105***	-0.0424	0.0434	0.0159	0.111***	1								
7. gender	0.00481	-0.0371	-0.0508	-0.0825**	0.158***	0.234***	1							
8. ceo chair	0.0428	0.0502	-0.0252	0.0340	-0.168***	-0.178***	0.0237	1						
9. average tenure	0.0748*	0.0707*	-0.0562	-0.00557	-0.0859**	-0.493***	-0.153***	0.268***	1					
10. average age	-0.000133	0.153***	-0.00179	0.0303	-0.0520	-0.0548	-0.0856**	-0.116***	0.319***	1				
11. lsize	-0.234***	-0.0182	0.0729*	0.0282	0.190***	0.284***	-0.120***	-0.336***	-0.181***	0.112***	1			
12. leverage	-0.0168	0.109***	-0.308***	-0.0323	-0.0197	0.192***	0.0923**	-0.00264	-0.0160	-0.109***	0.137***	1		
13. roa	-0.0576	0.159***	0.00639	0.0415	0.0890**	-0.0126	-0.0762*	0.0204	0.0766**	-0.0455	0.0961**	-0.0253	1	
14. loss	0.176***	-0.105***	-0.0867**	-0.0546	-0.0571	-0.0618*	0.0149	-0.0157	-0.0578	-0.0274	-0.194***	0.00258	-0.629***	1

* $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Given that the controls have not yet been inserted it is still a preliminary evidence, in order to complement and add relevance to the analysis additional variables and interactions will be included in the multivariate analysis.

5.1.3. Multivariate analysis

The results displayed in the following tables are based on the estimation of Equation (2) employing the difference-in-differences model of the effect of issuance of loyalty share on discretionary accruals including various controls and interactions with additional variables.

Year and Industry fixed effects[21] were controlled for in every regression, these effects were controlled in order to consider the differences in the tendency to manage earnings in the various industries as well as control time to take into account specific events which may have happened in a specific year.

In Table 5.5 it can be seen that the coefficient of the interaction variable (LS * POST) capturing the incremental change in discretionary accruals for companies issuing loyalty shares compared to non-issuers it is negative and significant at the 10% level. This result is in line with the results already provided by Mio et al. (2020) confirming that loyalty shares issuers show a decrease in earnings management after issuance, consistently with the difference-in-differences methodology that was employed this decrease is due to loyalty shares being issued.

In model 2, gender and average tenure are dropped since they exhibit correlations respectively with independence and average age, still the correlation between DA and the interaction variable LS * POST is not impacted.

In addition, board characteristics variables are included in this regression, the two significant ones are CEO photo size that is the proxy for CEO narcissism and independence of directors both showing a negative correlation with discretionary accruals at a 5% level for independence and at a 10% for CEO photo size. However, in

[21] In a fixed-effect statistical model the values of independent variables are assumed to be constant and only the dependent variables are changing in response to the level of independent variables (Salkind, 2010).

order to gain further insight, it is necessary to analyze the interactions with the selected board characteristics.

Table 5.5: Analysis of loyalty shares issuance on DAs

	(1)	(2)
VARIABLES	DA 1	DA 2
LS	-0.00199 (0.113)	-0.00690 (0.113)
POST	0.0274 (0.202)	0.00778 (0.202)
LS * POST	-0.411* (0.232)	-0.424* (0.232)
CEO photo size	-0.101* (0.0555)	-0.0966* (0.0538)
Ind %	-0.413 (0.261)	-0.464** (0.223)
Gender %	0.551 (0.698)	
CEO/Chair	-0.100 (0.0804)	-0.0869 (0.0781)
Average Tenure	0.00943 (0.0116)	
Average Age	0.0102 (0.0107)	0.0109 (0.00916)
LSize	-0.126*** (0.0289)	-0.130*** (0.0267)
Leverage	0.0183 (0.142)	0.0102 (0.136)
ROA	1.037** (0.511)	0.864* (0.458)
LOSS	0.504*** (0.115)	0.483*** (0.111)
Constant	-1.155 (0.814)	-0.834 (0.697)
Observations	1,138	1,159
R-squared	0.134	0.135
Industry FE	YES	YES
Year FE	YES	YES

Robust standard errors in parentheses
Abbreviation: FE, Fixed-Effects
*** $p<0.01$, ** $p<0.05$, * $p<0.1$

Moreover, the two main variables connected with loyalty shares (LS and POST) are insignificant as it was already observed by Mio et al. (2020).

This result is indicating the similarity in the level of earnings management for companies in the control and treatment group in the overall sample period from 2008 to 2017. The insignificance of the variable POST indicates that there has not been a significant change in earnings management after 2014 for Italian companies this is reasonable given that Italy did not pass a compulsory legislation for listed companies expecting to reduce earnings management (Mio et. al., 2020).

Table 5.6 is reporting the interaction between the variables regarding board characteristics and the indicator variable LS that for loyalty share issuers is equal to 1 and for non-issuers it is equal to 0. Given that a difference-in-differences methodology is employed, this can be identified as the "state" dimension that compares the companies issuing loyalty shares (treated group) with a benchmark group not issuing loyalty shares (control group).

Table 5.6: Interaction between board characteristics and LS

	(1)	(2)	(3)
VARIABLES	DA	DA	DA
LS	0.572** (0.273)	-1.039 (0.692)	-0.340 (0.288)
Ind %	-0.180 (0.270)	-0.422 (0.260)	-0.410 (0.263)
LS * IND	-1.654** (0.649)		
Gender %	0.195 (0.690)	-0.0506 (0.738)	0.279 (0.689)
CEO/Chair	-0.124 (0.0808)	-0.0804 (0.0810)	-0.0963 (0.0814)
Average Tenure	0.00978 (0.0115)	0.00712 (0.0116)	0.00551 (0.0118)
Average Age	0.0130 (0.0106)	0.0128 (0.0106)	0.0133 (0.0106)
LS * GENDER		2.587 (1.908)	
LS * TENURE			0.0289 (0.0315)
LSize	-0.145*** (0.0286)	-0.137*** (0.0284)	-0.143*** (0.0286)
Leverage	0.0303 (0.141)	0.0398 (0.141)	0.0491 (0.141)
ROA	1.003** (0.495)	0.963* (0.508)	1.032** (0.505)
LOSS	0.491*** (0.114)	0.481***(0.116)	0.492*** (0.114)
Constant	-1.003 (0.818)	-0.965 (0.817)	-0.989 (0.816)
Observations	1,138	1,138	1,138
R-squared	0.134	0.130	0.129
Industry FE	YES	YES	YES
Year FE	YES	YES	YES

Robust standard errors in parentheses
Abbreviation: FE, Fixed-Effects
*** p<0.01, ** p<0.05, * p<0.1

From this table it can be observed that, consistently with hypothesis 1, board independence has indeed an effect on discretionary accruals, as the results indicate that between the companies that issue loyalty shares the higher the independence of the board the higher the reduction of earnings management. The results are significant at a

5% level. Therefore, it seems to be confirmed that independence strengthens the effectiveness of loyalty shares in reducing earnings management and short-termism.
As for hypothesis 3, it is not confirmed by the results in Table 5.6, in fact the interaction between loyalty shares and % of women on the board of directors is positive and not significant therefore not indicating that women directors may improve the effect of loyalty shares in reducing earnings management.
The same applies to hypothesis 4, board tenure does not appear to have a role in reducing short-termism, as LS * Tenure is positive and non-significant.

The other dimension is displayed in Table 5.7, "time" analyzing the period pre-issuance (POST = 0) and post-issuance (POST = 1) that for companies issuing loyalty shares considers the year of issuance and for non-issuers the period from 2014, after which Italian legislation allowed loyalty shares.
In particular, the main coefficient of interest (LS * POST) that captures the incremental change in earnings management for loyalty shares issuers compared with loyalty shares non-issuers interacted with independence is negative and significant at the 10% level meaning that companies that issue loyalty shares and have independent board are more likely to reduce short-termism. This indicates that post issuance matters and therefore the act of issuing loyalty shares has an effect in the post issuance period.
As for gender and tenure interacted with LS * POST, they respectively exhibit a negative and positive correlation with DAs, however these correlations are insignificant, therefore these variables do not seem to contribute to short-termism reduction connected to loyalty shares.
For the board characteristics variables whose interaction with LS and LS * POST is non-significant (gender and tenure) the variation in the level of discretionary accruals is explained by the control variables size, return on assets (ROA) and loss, all significant whereas leverage, ceo/chair and average age do not seem to have a role.
As confirmed by the literature when a loss is reported or the ROA is higher, a company is more likely to manage earnings whereas larger companies are less likely to manage earnings.

Table 5.7: The effect of loyalty shares issuance on DAs: interaction with board characteristics

	(1)	(2)	(3)
VARIABLES	DA	DA	DA
LS	0.450 (0.294)	-0.889 (0.784)	-0.0438 (0.304)
POST	0.198 (0.267)	-0.230 (0.542)	0.0608 (0.250)
LS * POST	0.611 (0.585)	-0.0976 (1.706)	-0.957 (0.693)
Ind %	-0.00161 (0.325)	-0.410 (0.259)	-0.402 (0.262)
LS * IND	-1.118 (0.681)		
ind_post	-0.418 (0.444)		
LS * IND * POST	-2.268* (1.287)		
LS * GENDER		2.416 (2.181)	
gender_post		0.743 (1.379)	
LS * GENDER * POST		-0.702 (4.800)	
LS * TENURE			0.00458 (0.0329)
averagetenure_post			-0.00438 (0.0185)
LS * TENURE * POST			0.0754 (0.0769)
Gender %	0.171 (0.695)	-0.405 (1.014)	0.211 (0.693)
CEO/Chair	-0.119 (0.0811)	-0.0791 (0.0810)	-0.0919 (0.0817)
Average Tenure	0.0106 (0.0115)	0.00711 (0.0116)	0.00805 (0.0144)
Average Age	0.0115 (0.0106)	0.0119 (0.0106)	0.0119 (0.0107)
LSize	-0.143*** (0.0285)	-0.138*** (0.0285)	-0.142*** (0.0286)
Leverage	0.0311 (0.141)	0.0430 (0.141)	0.0451 (0.140)
ROA	1.003** (0.504)	0.935* (0.509)	0.980* (0.511)
LOSS	0.498*** (0.114)	0.483*** (0.116)	0.490*** (0.115)
Constant	-1.055 (0.818)	-0.796 (0.887)	-0.950 (0.821)
Observations	1,138	1,138	1,138
R-squared	0.140	0.132	0.132
Industry FE	YES	YES	YES
Year FE	YES	YES	YES

Robust standard errors in parentheses
Abbreviation: FE, Fixed-Effects
*** p<0.01, ** p<0.05, * p<0.1

An additional variable is considered in Table 5.8 that displays data about CEO narcissism interacted both with LS and with the term LS * POST to infer how it may influence loyalty shares reducing earnings management and short-termism.

The results seem counterintuitive at first, in fact preliminarily in Table 5.5 CEO photo size is negatively correlated with DAs, this may be due to the phenomenon of

organizational identification which is frequent for narcissistic CEOs and it is linked to a lower likelihood to behave opportunistically (Abernethy et al., 2019; Capalbo et al., 2018; Reina et al., 2014).

Table 5.8: The effect of loyalty shares issuance on DAs: interaction with CEO narcissism

	(1)	(2)	(3)	(4)
VARIABLES	DA	DA	DA	DA
LS	0.0220 (0.173)	0.0159 (0.172)	0.0404 (0.177)	0.0832 (0.183)
CEO photo size	-0.0677 (0.0644)	-0.0614 (0.0644)	-0.0602 (0.0677)	-0.0925 (0.0904)
LS * NAR	-0.0805 (0.118)	-0.0827 (0.117)	-0.112 (0.119)	-0.0785 (0.132)
POST				-0.0894 (0.248)
POST * NAR				0.0685 (0.118)
LS * POST * NAR				-0.321* (0.171)
Ind %		-0.446** (0.221)	-0.429 (0.261)	-0.394 (0.261)
Gender %			0.695 (0.697)	0.566 (0.700)
CEO/Chair			-0.112 (0.0807)	-0.110 (0.0809)
Average Tenure			0.0107 (0.0116)	0.0111 (0.0117)
Average Age			0.0114 (0.0107)	0.0103 (0.0107)
LSize	-0.127*** (0.0250)	-0.120*** (0.0249)	-0.132*** (0.0292)	-0.131*** (0.0293)
Leverage	-0.0621 (0.133)	-0.0284 (0.135)	0.0149 (0.142)	0.0179 (0.142)
ROA	0.851* (0.450)	0.802* (0.456)	1.046** (0.505)	0.997** (0.504)
LOSS	0.493*** (0.110)	0.480*** (0.111)	0.505*** (0.114)	0.501*** (0.115)
Constant	-0.436 (0.503)	-0.426 (0.502)	-1.188 (0.815)	-1.099 (0.819)
Observations	1,159	1,159	1,138	1,138
R-squared	0.127	0.130	0.132	0.135
Industry FE	YES	YES	YES	YES
Year FE	YES	YES	YES	YES

Robust standard errors in parentheses
Abbreviation: FE, Fixed-Effects
*** p<0.01, ** p<0.05, * p<0.1

Conversely, in Table 5.8 the relationship between CEO narcissism and discretionary accruals cannot be seen when the interaction with LS is included as LS * NAR is insignificant, this may indicate the presence of real earnings management which according to Olsen et al. (2014) is preferred by narcissistic CEOs. Furthermore, loyalty shares seem to help reducing earnings management to a higher extent when the CEO is narcissist as the significance appears again when the interaction with the control of time

POST is added, thus suggesting that the act of issuing loyalty shares matters, as after issuance the effect of loyalty shares on earnings management reduction can be seen, organizational identification is another factor that may help explain these results.

All models display a R-squared[22] ranging from 13% to 14%.

5.1.4. Robustness test

To further validate the results a robustness placebo test is conducted. An early loyalty shares issuance (1 year) by treated firms is simulated like Mio et. al (2020) have done in their study. The results provided in tables 5.5, 5.7 and 5.8 will prove to be robust if the interaction variables in the placebo are not significant. On the other hand, significant results would indicate that the interaction variables are influenced by other effects different than the ones resulting from the interaction between loyalty shares issuance and board characteristics, therefore suggesting that unobserved variables are affecting the results which would be biased by endogeneity.

Table 5.9, 5.10 and 5.11 are displaying the results of these placebo tests applied to the regressions in Tables 5.5, 5.7 and 5.8.

The regressions are run lagging the variable of loyalty shares adoption 1 year, indicating that the company issued loyalty share a year before it actually issued them. As expected, there is no effect on earnings management in this setting, thus corroborating the evidence that the reduction in earnings management is related to the issuance of loyalty shares and their interaction with board characteristics.

The results in Table 5.9 indicate that the interaction between LS and POST (placebo) is insignificant, therefore as expected the association between loyalty shares and earnings management is not significant in this placebo test. This evidence confirms the confidence about the fact that loyalty shares caused earnings management to decrease.

[22] R-squared or coefficient of determination is a statistical measure in a regression model that determines the proportion of variance in the dependent variable that can be explained by the independent variable. It shows how well the data fit the regression model, namely the goodness of fit (Corporate Finance Institute).

Table 5.9: Robustness placebo test simulating an early LS issuance by the treated group in 1 year

	(1)	(2)
VARIABLES	DA	DA
LS	0.00166 (0.119)	0.000146 (0.119)
POST	0.209 (0.230)	0.199 (0.230)
LS * POST	-0.203 (0.200)	-0.217 (0.200)
CEO photo size	-0.0973* (0.0553)	-0.0912* (0.0536)
Ind %	-0.438* (0.262)	-0.481** (0.223)
Gender %	0.628 (0.696)	
CEO/Chair	-0.104 (0.0805)	-0.0911 (0.0782)
Average Tenure	0.00924 (0.0116)	
Average Age	0.0112 (0.0107)	0.0117 (0.00917)
LSize	-0.127*** (0.0289)	-0.131*** (0.0266)
Leverage	0.0179 (0.142)	0.0103 (0.136)
ROA	1.073** (0.512)	0.895* (0.457)
LOSS	0.502*** (0.115)	0.481*** (0.111)
Constant	-1.214 (0.816)	-0.848 (0.699)
Observations	1,138	1,159
R-squared	0.132	0.133
Industry FE	YES	YES
Year FE	YES	YES

Robust standard errors in parentheses
Abbreviation: FE, Fixed-Effects
*** $p<0.01$, ** $p<0.05$, * $p<0.1$

As it is shown in Table 5.10 and 5.11 the interaction terms with the board characteristics variables in particular independence and CEO narcissism, which were the only two factors that appeared significant in earnings management reduction, are insignificant in this placebo setting. Thus, corroborating the evidence that the issuance of loyalty shares is indeed the triggering factor that matters in leading to a reduction in earnings management.

Table 5.10: Robustness placebo test simulating an early LS issuance by the treated group in 1 year interacted with board characteristics

	(1)	(2)	(3)	(4)
VARIABLES	DA	DA	DA	DA
LS	0.434 (0.318)	-1.225 (0.843)	0.0531 (0.141)	-0.0473 (0.331)
POST	0.325 (0.287)	-0.370 (0.568)	0.332 (0.238)	0.271 (0.274)
LS * POST	0.677 (0.522)	0.283 (1.434)	-0.357 (0.254)	-0.669 (0.600)
Ind %	-0.0730 (0.344)	-0.440* (0.261)	-0.425 (0.263)	-0.423 (0.263)
LS * IND	-1.067 (0.736)			
ind_post	-0.223 (0.434)			
LS * IND * POST	-1.958 (1.192)			
gender_post		1.663 (1.403)		
LS * GENDER		3.331 (2.297)		
LS * GENDER * POST		-1.118 (3.981)		
averagetenure_post				-0.00666 (0.0182)
LS * TENURE				0.00528 (0.0352)
LS * TENURE * POST				0.0647 (0.0657)
Gender %	0.236 (0.692)	-0.964 (1.115)	0.369 (0.689)	0.290 (0.689)
CEO/Chair	-0.127 (0.0810)	-0.0846 (0.0812)	0.0747 (0.118)	-0.0977 (0.0816)
Average Tenure	0.0104 (0.0115)	0.00643 (0.0116)	0.00867 (0.0115)	0.00902 (0.0147)
Average Age	0.0128 (0.0106)	0.0129 (0.0107)	0.0130 (0.0106)	0.0128 (0.0107)
LSize	-0.145*** (0.0286)	-0.140*** (0.0285)	-0.138*** (0.0283)	-0.142*** (0.0287)
Leverage	0.0315 (0.141)	0.0387 (0.141)	0.0393 (0.141)	0.0459 (0.140)
ROA	1.046** (0.505)	0.991*(0.512)	0.991** (0.504)	1.034** (0.512)
LOSS	0.493*** (0.114)	0.483*** (0.117)	0.497*** (0.114)	0.491*** (0.115)
Constant	-1.077 (0.825)	-0.586 (0.913)	-1.181 (0.818)	-1.011 (0.822)
Observations	1,138	1,138	1,138	1,138
R-squared	0.137	0.132	0.133	0.131
Industry FE	YES	YES	YES	YES
Year FE	YES	YES	YES	YES

Robust standard errors in parentheses.
Abbreviation: FE, Fixed-Effects.
***p<0.01, ** p<0.05, * p<0.1

Table 5.11: Robustness placebo test simulating an early LS issuance by the treated group in 1 year interacted with CEO narcissism

	(1)	(2)	(3)	(4)
VARIABLES	DA	DA	DA	DA
LS	0.0220 (0.173)	0.0159 (0.172)	0.0404 (0.177)	0.0479 (0.189)
CEO photo size	-0.0677 (0.0644)	-0.0614 (0.0644)	-0.0602 (0.0677)	-0.138 (0.0996)
ls_nar	-0.0805 (0.118)	-0.0827 (0.117)	-0.112 (0.119)	-0.0321 (0.135)
POST				0.0216 (0.264)
post_nar				0.135 (0.118)
ls_post_nar				-0.180 (0.148)
Ind %		-0.446** (0.221)	-0.429 (0.261)	-0.424 (0.262)
Gender %			0.695 (0.697)	0.632 (0.700)
CEO/Chair			-0.112 (0.0807)	-0.115 (0.0812)
Average Tenure			0.0107 (0.0116)	0.0109 (0.0117)
Average Age			0.0114 (0.0107)	0.0109 (0.0107)
LSize	-0.127*** (0.0250)	-0.120*** (0.0249)	-0.132*** (0.0292)	-0.131*** (0.0293)
Leverage	-0.0621 (0.133)	-0.0284 (0.135)	0.0149 (0.142)	0.0213 (0.142)
ROA	0.851* (0.450)	0.802* (0.456)	1.046** (0.505)	1.024** (0.506)
LOSS	0.493*** (0.110)	0.480*** (0.111)	0.505*** (0.114)	0.498*** (0.115)
Constant	-0.436 (0.503)	-0.426 (0.502)	-1.188 (0.815)	-1.088 (0.823)
Observations	1,159	1,159	1,138	1,138
R-squared	0.127	0.130	0.132	0.134
Industry FE	YES	YES	YES	YES
Year FE	YES	YES	YES	YES

Robust standard errors in parentheses
Abbreviation: FE, Fixed-Effects.
*** p<0.01, ** p<0.05, * p<0.1

5.2. Discussion

The aim of this thesis is to empirically test whether board characteristics have an influence on the effect of loyalty shares on corporate short-termism reduction effects which were demonstrated by the study of Mio et al. (2020).

Loyalty shares as a means of addressing short-termism in financial markets have been hotly debated in international policy circles recently and several countries have already allowed companies to issue loyalty shares such as Italy, France and the Netherlands (Delvoie and Clottens, 2015). Belgium approved a company law reform in 2019 allowing

their introduction on a voluntary basis in 2020 (Bajo et al., 2020). In 2021, Spain has introduced loyalty shares as well (Pérez-Schafer and Rios, 2021).
And in the United States they have gained prominence through the creation of the Long-Term Stock Exchange (European Corporate Governance Institute).

It is commonly believed that shareholders who own shares for a considerable period of time would take an "ownership approach" to their interest in the corporation, instead of trying to make the best of their temporary stay, without regard to what happens when they leave (Duruigbo, 2012).
Corporate short-termism is a prominent topic in the current debate both for scholars and for the general public, Mio et al. (2020) gave a significant contribution to this debate by providing an empirical investigation on loyalty shares as a corporate governance mechanism reducing short-termism.
Literature defines short-termism as the behavior showing preference for actions in the near term that have detrimental consequences for the long term (Marginson and McAulay, 2008).
The costs of short-termism are borne both by long-term and future shareholders who purchase shares in the short-term (Fried, 2015).

Despite the implications of this topic appear relevant, few empirical evidence is provided by scholars about loyalty shares as short-termism reducing corporate governance mechanism. Evidence supporting both antidote (Belot et al., 2019; Berger et al., 2017; Edelman et al., 2018; Mio et al., 2020; Quimby, 2013) and poison view (Bourveau et al., 2019; Mosca, 2019; Roe and Cenzi Venezze, 2021) of loyalty shares are present in the literature.

The methodology that was employed (diff-in-diff) allowed to test the impact of loyalty shares issuance on treated companies while other variables have also been considered that could have possibly impacted both control and treated companies.
The main dependent variable that is employed is earnings management which consistently with previous literature has been identified as a proxy for short-termism (Brochet et al., 2015).
All the analyses are run on a sample of Italian listed companies excluding financial companies since Italy has been allowing loyalty shares from 2014.

Some preliminary evidence is provided in the correlation test between the main variables involved, in the correlation matrix (Table 5.4) the relation between DA and LS * POST already appears negative and significant.

In the multivariate analysis, additional variables and interactions are included, the interaction variable between LS and POST is confirmed to be negative and significant even when the control variables are added in the regression and directors' independence and CEO narcissism are already negatively and significantly correlated with DAs (Table 5.5). The negative correlation between DAs and board independence was expected as it is confirmed by the evidence present in the literature, whereas the one with CEO narcissism was surprising but there may be some factors explaining this result that still it is statistically weaker than the result regarding board independence.

In accordance with Mio et al. (2020), the result that treated companies experienced a decrease in earnings management after they started issuing loyalty shares is confirmed. The impact of loyalty shares goes beyond other possible effects that may have influenced earnings management of the companies in the sample during the analyzed period.

The fact that LS and POST are not significant implies respectively that treated and control companies have a similar level of earnings management when not partitioning before and after adoption; and that the level of DAs is not changing before and after 2014 or the year of issuance, this is reasonable given that this change in legislation was not compulsory and expected to have an effect on earnings management (Mio et al., 2020).

The strongest evidence that it is provided in accordance with literature and consistently with hypothesis 1 (board independence strengthens the effectiveness of loyalty shares in reducing earnings management and short-termism), it is concerning board independence (Tables 5.6 and 5.7).

In fact, considering a diff-in-diff model the interaction of loyalty shares and post issuance with board independence is negative and significant thus meaning that a reduction in earnings management is observed for companies that issued loyalty shares in the period after the issuance of this type of shares, also that the independence of the board is a significant factor to reduce earnings management as well. Therefore, between the

companies that issue loyalty shares the higher the independence of the board the higher the reduction of earnings management.

Since board independence is a widely treated topic in corporate governance, especially in relation to earnings management reduction (Chen et al., 2015; Ebrahim, 2007; Gonzalez and André, 2014; Kao and Chen, 2004; Klein, 2002), it seemed even more relevant to insert this variable in order to understand how it would interact with loyalty shares to reduce short-termism. Therefore, the role of board independence seems to be confirmed together with the fact that independent directors are more likely to effectively monitor and curb the use of practices focused on short-term performance such as earnings management.

This result seems quite powerful given that it holds and it is constant even changing and adding several controls in all the various regressions.

The other significant result is related to another widely discussed topic in corporate governance, CEO narcissism and in particular how CEO narcissism influences the effect of loyalty shares issuance on earnings management (hypothesis 2: the introduction of loyalty shares helps reducing earnings management and short-termism to a higher extent in the presence of a narcissistic CEO).

Despite various scholars report evidence that CEO narcissism is connected to increased earnings management, in Table 5.5 the proxy for CEO narcissism shows a negative and significant correlation with DAs.

This result may be associated to organizational identification, as previously stated, and some aspects that may improve the alignment of narcissistic CEOs' self-perceived interests with those of shareholders, such as a compensation plan with publicly available performance measures and an independent board of directors closely monitoring managers for self-interested behavior (Alderman et al., 2020).

An important factor connected to CEO narcissism is organizational identification that occurs when a person's identity is tied closely to the organization of which he or she is part, such individuals generally show greater organizational commitment, work more cooperatively, exhibit higher work effort and are less likely to quit (Fuller et al., 2018).

This goal congruence creates a desire for narcissistic CEOs to promote effective TMT processes because doing so is in the organization's best interest as it is analogous to self-protection and self-enhancement (Reina et al., 2014).

The interaction terms in Table 5.8 at first seemed counterintuitive, as LS * NAR is insignificant therefore suggesting that narcissism may not have an impact on earnings management, in the literature narcissistic CEOs because of their personality are generally associated with higher earnings management, however, there is also evidence reported by Olsen et al. (2014) that narcissistic CEOs are more likely to pursue operational strategies through real activities such as increases to production and sales to boost reported earnings bringing recognition to the CEO rather than employing discretionary accruals.

Always in Table 5.8 the interaction term LS * POST* NAR is added suggesting that loyalty shares help reducing earnings management to a higher extent when the CEO is a narcissist, which may be connected to the previously cited factors that expose the positive side of narcissism. In fact, even in the presence of potential "horizon problems" when CEOs are reluctant to make beneficial decisions for the long-term but costly to short-term personal wealth, a mitigating role is played by strong organizational identification (Abernethy et al., 2019). Possibly this result in the context of this analysis may be suggesting that shareholders are the main driver of short-termism.

Thus, CEO horizon problems for narcissistic CEOS can be moderated by organizational identification, compensation plans and an independent board leading to a lower likelihood to behave opportunistically.

In addition, loyalty shares should push managers to favor long-term corporate orientation to satisfy long-term shareholders and to match their horizons given that they hold more votes and will remain for more time (Fried, 2015; Roe and Cenzi Venezze, 2021).

Assuming that short-termism is determined by shareholders, the acquisition of more voting power by "loyal" shareholders may push management to focus on satisfying them through more long-term oriented decisions. Whereas, if managers are assumed to be the driver of short-termism, loyalty shares give shareholders authority to limit managerial opportunism and short-termism through shareholder activism (Mio et al., 2020).

Therefore, hypothesis 2 is confirmed.

Finally, hypotheses 3 (women directors positively interact with loyalty shares to reduce earnings management and short-termism) and 4 (board tenure positively interacts with loyalty shares to reduce earnings management and short-termism) are not confirmed given the insignificance in all models (Tables 5.6 and 5.7), neither gender nor tenure seem to have an impact on short-termism reduction.
Experience and knowledge of the business associated to higher tenure and aspects in support of women being less prone to earnings management and more effective monitors identified in the literature are not supporting the effectiveness of loyalty shares in this analysis.

For gender and tenure whose interactions with LS and LS * POST are not significant the variation in DAs is explained by the control variables size, ROA and loss. As confirmed by the literature loss, a higher ROA and small size are factors that may increase the likelihood to manage earnings.

As stated by Kim et al. (2003) the larger the size of a firm the less the practice of earnings management may be feasible for several reasons. Firstly, a more sophisticated internal control system and more competent internal auditors of largest companies compared to smallest companies contributing to an improved reliability of financial information publicly disclosed. Secondly, larger firms are usually audited by auditors from the big five[23] accounting firms that could help preventing earnings misrepresentation. Thirdly, large firms tend to consider the reputation cost that may stem from the engagement in earnings management given their better appreciation of market environment and better control over operations and prevent them from manipulating earnings.
Therefore, large-sized firms usually have established credibility in business community and social responsibility as well as better ability to generate reliable and timely information hence the cost of earnings management will be higher than for small-sized firms, moreover they are followed by more financial analysts (Kim et al., 2003).

[23] The big five were Ernst & Young, Deloitte & Touche, Arthur Andersen, KPMG and Price Waterhouse Coopers, before the insolvency of Arthur Andersen stemming from their involvement in the 2001 Enron Scandal leading to the current big four.

Bradbury et al. (2006) report that a prior year loss is positively related to income increasing accruals and negatively to income decreasing accruals.
Dechow et al. (2003) find that small loss firms appear to be managing earnings leading to think that loss avoidance is one of the primary motivations for accrual management in small profit firms.
Burgstahler and Dichev (1997) provide evidence that earnings decreases and losses are frequently managed away by firms to avoid reporting losses, the authors find that 30% to 44% of firms with slightly negative pre-managed earnings exercise discretion to report positive earnings.
Habib and Hansen (2008) focus on earnings management around earnings benchmarks including the earnings level benchmark (loss avoidance), this benchmark describes managers who wish to avoid reporting losses and focuses on firms around the zero-earnings level given that generally firms' management has capital market and compensation incentives to meet earnings benchmarks.

Lee et al. (2006) provide evidence of a positive relationship between discretionary accruals estimated from the Jones model and firms' performance, given the positive and significant correlation between earnings management and ROA. The authors state that firms with higher performance over-report earnings by a larger amount because price responsiveness (sensitivity of price response to reported earnings) increases with earnings performance since the market rationally expects this and the price responsiveness increases with reported earnings, inducing managers with higher economic earnings to overstate earnings by a larger amount.

The insignificant results in the final robustness tests simulating a one year earlier issuance (Tables 5.8 ,5.9, 5.10 and 5.11) are further validating the results provided in this thesis.

What emerges from this thesis is that the independence of directors and CEO narcissism seem to play a significant role in the interaction with loyalty shares reducing earnings management. In order to broaden the empirical evidence concerning loyalty shares such variables are included in this analysis given the crucial role that the bord of directors and the CEO play in a company.

Thus, this empirical evidence is supporting the “antidote” view of loyalty shares and as stated by Mio et al. (2020) there are two potential mechanisms that may play a role, namely an increased activism of long-term-oriented shareholders if short-termism is assumed to be driven by opportunistic managers; or a higher relevance of “loyal” shareholders assuming that shareholders' preferences are driving the orientation of companies.
Dallas and Barry (2016) state that the main reason for US companies adopting Time-Phased Voting (TPV)[24] was to increase the influence of long-term investors to insulate managers from short-term market pressures and foster a corporate culture[25] focused on long-term performance.

The decrease in earnings management is also excluding the hypothesis of managerial entrenchment since hostile takeovers are made more difficult by loyalty shares (Mio et al., 2020).
Control-Enhancing Mechanisms (CEMs) are viewed as managerial entrenchment mechanisms since they can prevent takeovers that are opposed by management (Moschetto and Teulon, 2015).
As reported by Mio et al. (2020) the alignment of power of the market for corporate control is decreased and this may favor managerial entrenchment, because of the decreased ability of bidding shareholders to takeover the company when an inefficient or opportunistic management is present. This is due to the fact that bidding shareholders to take over the board should acquire a control bloc and wait for the stock to mature, therefore managers are less exposed to takeover as external corporate governance mechanism and may become short-term oriented.

Another argument of the “poison view” of loyalty shares reported by Mio et al. (2020) is that past holding periods may not guarantee for monitoring efforts and future ownership (Delvoie and Clottens, 2015; Quimby, 2013). However, Quimby (2013) argues

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[24] Loyalty shares.

[25] A system of shared values that define what is considered important and norms that define appropriate attitudes guiding members’ behaviors. “Strong culture” is referring to norms widely shared across the organization (O'Reilly and Chatman, 1996).

that an ex-post view of the duration of ownership may be an adequate proxy for the duration of future ownership.

As mentioned by Fried (2015) long-term shareholders may be more interested to reduce managerial agency costs[26] than short-term shareholders given that they will hold their shares for a longer time, they may also more easily evaluate managerial performance as they are more familiar with it.

Time horizons of shareholders have an influence on managers decisions, if long-term shareholders have more power than short-term shareholders then managers can be expected to focus less on the short-term stock price and more on long-term shareholder value (Fried, 2015).

As stated by Mio et al. (2020) even though there are countries who already decided to allow loyalty shares others are considering the potential problems that may arise after their implementation and issuance.

Adding empirical evidence regarding loyalty shares including in the analysis critical variables such as board characteristics may contribute to better understand the effects of such instruments, given how this would impact the value creation process of many companies.

[26] When managers who directly control the firm pursue their own interests rather than those of shareholders (Fried, 2015).

Conclusions

This analysis confirms that loyalty shares decrease earnings management and short-termism and in addition that board independence and CEO's personality play a key role in the functioning of loyalty shares as a short-termism antidote.

Many efforts have been made by policymakers with the aim to target and reduce the tendency to short-termism, of which the practice of earnings management is part, whose detrimental effects are almost universally recognized by academics.

As analyzed in the first chapter the orientation of the European Union is clearly towards long-termism and favoring shareholder engagement to encourage companies to promote long-term stability and consider socio-environmental issues with the so-called Shareholder Rights Directive that entered into force in 2017 and was the final point of a process started by the Commission in 2012 that intends to modernize company law and corporate governance framework.

Even though loyalty shares are not explicitly included in the final draft of the directive they are still an instrument that is generally adopted with the purpose of reducing corporate short-termism and although ESMA has preferred to take a cautious view before issuing a general recommendation at the EU level this does not prevent individual member States from introducing loyalty shares.

Given that loyalty shares are considered a corporate governance mechanism many aspects in the sphere of corporate governance would be impacted. As highlighted in chapter 1, these aspects may range from managerial opportunism which is connected to earnings management and therefore short-termism to investor activism following the empowerment of "loyal" shareholders and corporate sustainability that is a broad concept limited not only to the environmental area but includes also to the balance between short and long-term perspectives.

Loyalty shares are gaining momentum not only in the EU but also in the United States with the recent institution of the Long-term stock exchange promoting an approach to governance and voting rights focused on reducing short-term pressures on public companies and involving the use of loyalty shares.

Even though the literature is not very vast this instrument is gaining attention also among scholars that are increasingly considering it in their studies. As analyzed in chapter 2 the three main lines of research by country are Italy and France where the consequences and determinants of the 2014 legislation respectively introducing and modifying loyalty shares adoption are analyzed; and the USA where authors are wondering which effects widespread loyalty shares adoption would have in the US context.

As detailed in the third chapter the moderating variables chosen for this thesis broadening the analysis of Mio et al. (2020) are aspects concerning characteristics of directors and CEOs.

Board independence is of particular interest as many scholars bring evidence that more independent directors tend to reduce earnings management and are more prone to be long-term orientated, conversely, some authors report that divergence of control and cash flow rights for controlling shareholders related to control-enhancing mechanisms, such as loyalty shares could potentially reduce the ability of independent directors to limit earnings management and short-termism.

Gender is of interest as many scholars are reporting that women directors may lead to enhanced monitoring on managerial opportunism and reduced earnings management, in accordance also with theories of gender literature. However, skepticism about blind implementation of gender quotas is also present, with authors stating that specific attributes of women directors are more important than simply the percentage of women on the board, as well as the level of empowerment both inside and outside the board.

As for average tenure, some scholars find a negative association between tenure and earnings management whereas others highlight a positive association. The two main arguments which are counterposed are experience and entrenchment with management.

A widespread topic studied by scholars is CEO narcissism, many scholars argue that CEOs with a narcissistic personality usually tend to be focused on short-term results and career goals associated to increased earnings management. Conversely, there is also evidence that CEO narcissism is associated to organizational identification that may limit opportunistic behavior and therefore earnings management and short-termism.

As it emerged from the fourth and fifth chapter, the methodology was empirical and it involved the employment of difference-in-differences methodology and regressions.

In the multivariate analysis, the negative and significant correlation between the issuance of loyalty shares and discretionary accruals is confirmed. The interaction of loyalty shares and post issuance with board independence is negative and significant meaning that a reduction in earnings management is observed for companies that issued loyalty shares in the period after issuance and independence is a significant factor to reduce earnings management. Similarly, the negative and significant correlation of the interaction term with DAs for CEO narcissism is suggesting that loyalty shares help reducing earnings management to a higher extent when the CEO is a narcissist.

The negative correlation between DAs and board independence was expected as it is mostly confirmed by the evidence in the literature, whereas the one with CEO narcissism was surprising, this result may be associated to organizational identification which may help expose the positive side of narcissism.

Conversely, neither gender nor tenure seem to have an impact on short-termism reduction given the insignificance of the correlations of these variables with reduction in DA in all models of this analysis.

Moreover, the insignificant results in the final robustness tests simulating a one year earlier issuance are further validating the results.

As stated by Mio et al. (2020) even though there are countries who already decided to allow loyalty shares such as Italy, France, the Netherlands, Belgium and Spain, others are considering the problems that may arise after their implementation and issuance.

Many are the questions and analyses that still need to be investigated and tackled regarding the implementation of loyalty shares given that it is a hotly debated topic and it is likely to remain in the public debate for the years to come considering the importance that short-termism is playing in the decisions of policymakers. Adding empirical evidence regarding loyalty shares including in the analysis critical variables such as board characteristics may contribute to better understand the effects of such instruments, given that these decisions would impact the value creation process of many companies, an increasing stream of empirical results are needed as a guidance.

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