

# Employee Co-determination of German Private Companies: Smooth Earnings as a Job Protection Instrument?

Working Paper

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## Abstract

This study investigates the influence of employee participation on supervisory boards on firms' earnings patterns. Conditional on the company's legal form, industry and number of employees, employees obtain up to half the seats on the supervisory boards of German firms. Supervisory boards control management, as well as financial reporting, and also appoint the auditor. The results of this paper contribute to literature for several reasons. Employees seemingly view smooth company income as a job protection device, as co-determined supervisory boards have a significantly positive relationship with income smoothing. The positive influence increases with higher degrees of co-determination. To achieve their smooth earnings goals, co-determined supervisory boards also foster the creation of discretionary (abnormal) accruals. As these accruals have to be income-increasing as well as decreasing in nature, this leads to a significantly higher variability of discretionary accruals of co-determined companies.

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