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Carbon Performance and Classification Shifting: the Moderating Role of Financial Statement Comparability

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Abstract

This study investigates the mediating role of financial statement comparability in the relationship between carbon performance and classification shifting in UK-listed firms. Drawing on a panel of 5,436 firm-year observations from 2012 to 2023, the analysis explores how enhanced carbon performance influences managers' use of misclassification practices to inflate core earnings. The research leverages a threshold regression model to assess non-linear effects and applies 2SLS estimation to address endogeneity concerns. The findings reveal a negative association between carbon performance and classification shifting, suggesting that firms with superior environmental results are less likely to misclassify revenues. Furthermore, financial statement comparability strengthens this mitigating effect, acting as an effective constraint on earnings manipulation. These results highlight the disciplining role of comparability and underscore the importance of transparent carbon strategies in curbing opportunistic reporting behaviors. This study contributes to the literature on sustainability reporting and earnings quality by providing evidence on the interplay between environmental performance, information quality, and managerial discretion in financial reporting.

Keywords: Carbon Emissions; Classification Shifting; Comparability; Earnings Management; Sustainability