

Firm structure, reporting incentives and international accounting research

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Presentation prepared for:

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Session 3: Saturday May 31, 9.30-10:00

Agenda

- Intro: harmonization of accounting standards
 - Worldwide ~ EU setting

- Harmonization effects on reporting uniformity
 - Accruals reporting process in EU15 countries
 - Time series evolution (1990-2007)
 - Pre vs. post-mandatory IFRS adoption

- Role of the Institutional / Information environment
 - Institutional enforcement/rule of law
 - Information environment: analysts/institutionals

- Conclusions and future research agenda

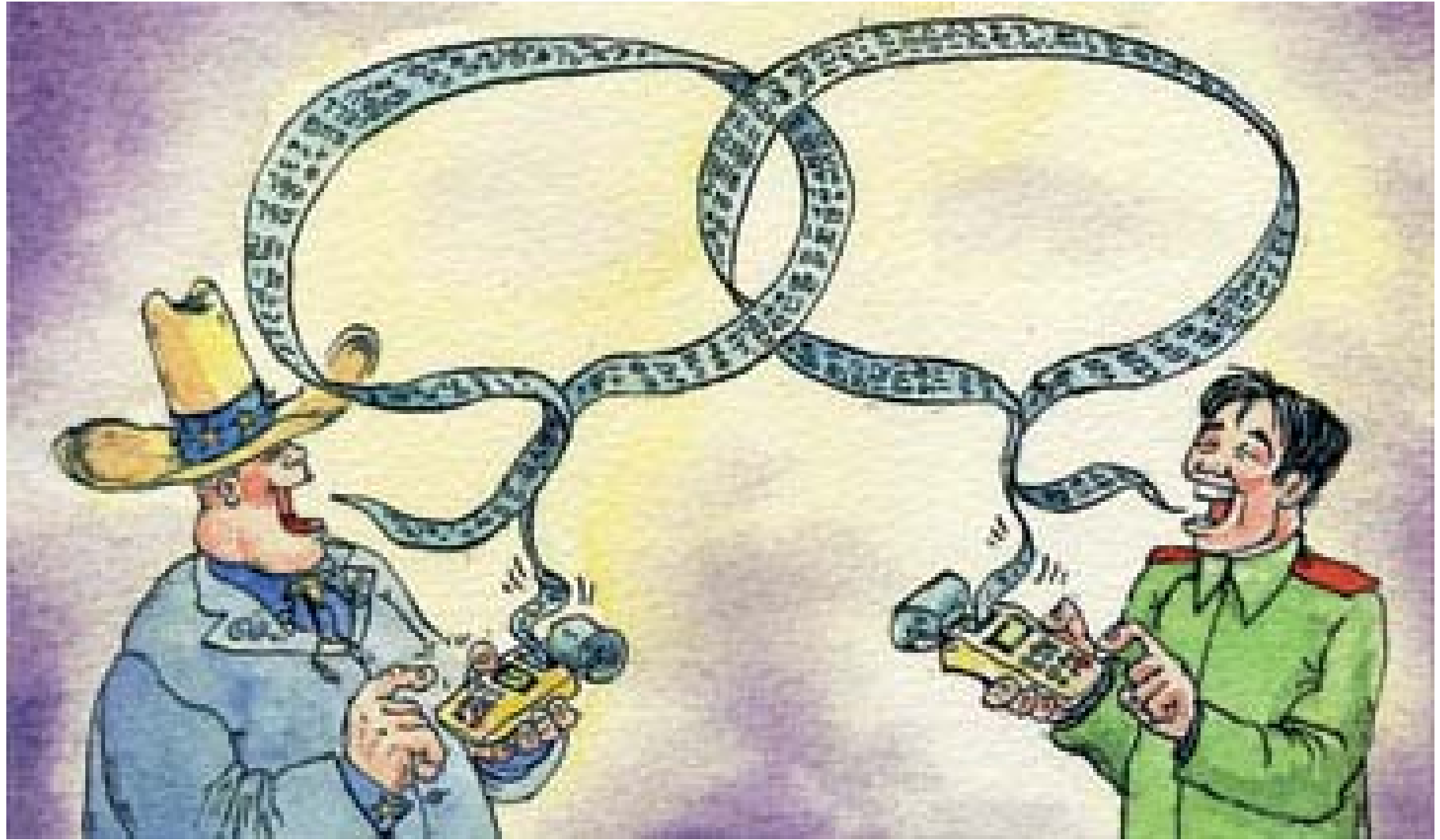
Accounting harmonization efforts

- International Accounting Standards (IAS)
 - 1973: IASC founded
 - 1995-99: core standards development
 - 2006: IFRS used in >100 countries

- Europe:
 - Initial wave of harmonization:
 - 1978/83: 4th/7th Directive
 - > 1995: voluntary IFRS/US GAAP adoption
 - 2000: intention to mandate IFRS from Jan 2005 (listed firms)

- US-IASB: 2002 Norwalk Agreement
 - FASB convergence project of US GAAP and IFRS
 - 2008: no US GAAP reconciliation requirement for foreign registrants in US
 - Currently: draft on allowing IFRS (only) for US firms

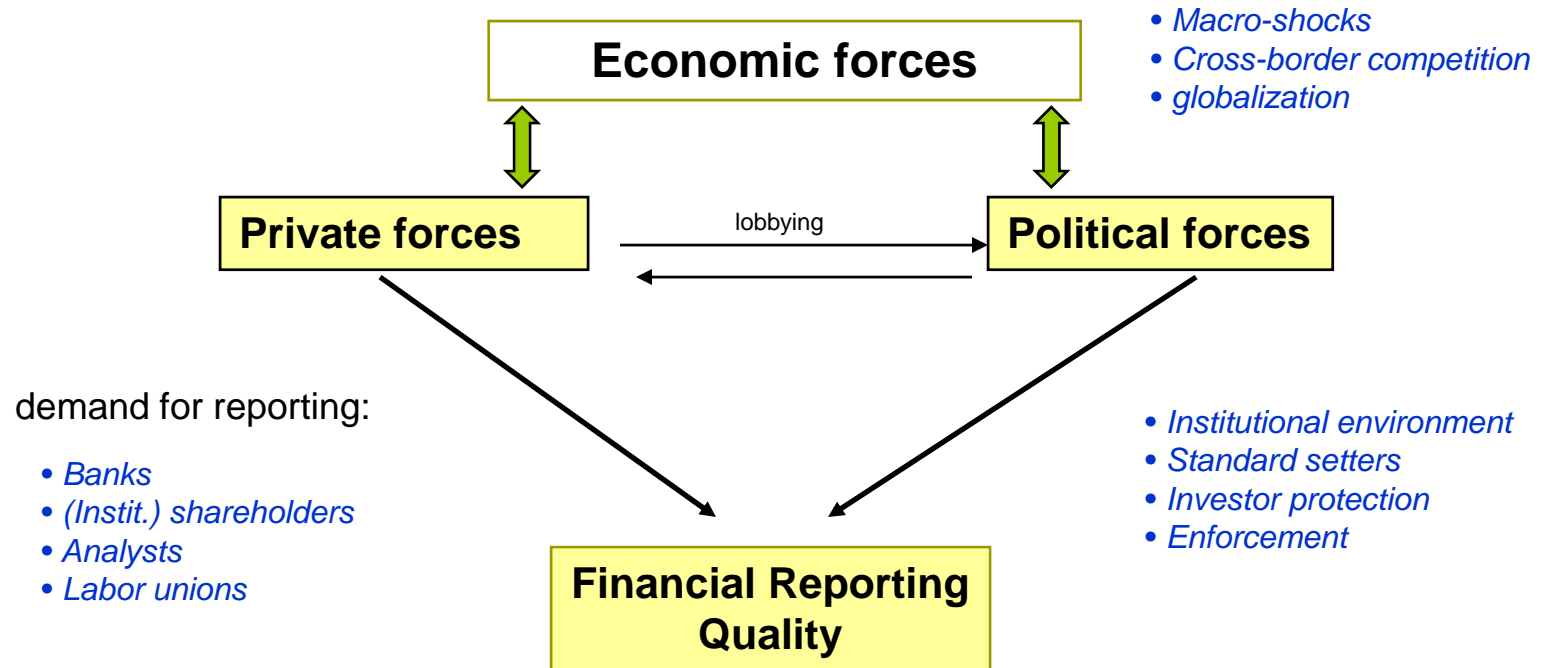
- "*Lingua Franca*" for financial reporting purposes?



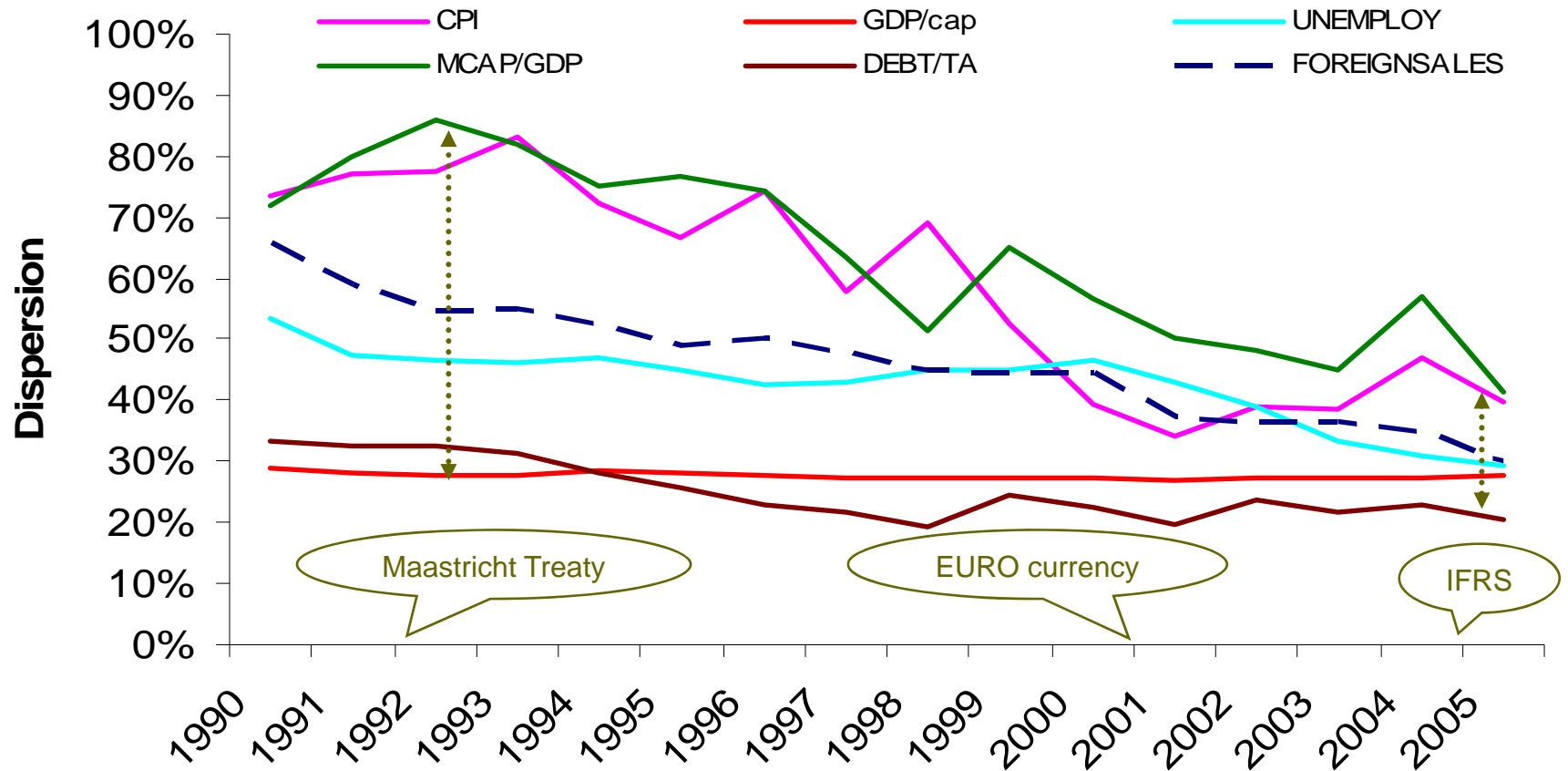
Reporting characteristics

- Issue = comparability of earnings
 - *"An economic transaction is measured and reported such that constituencies agree on the interpretation"*
- Key component of accounting earnings = accruals
 - Cash Flow + Accruals = Earnings
- 2 views on informativeness of accruals:
 - Decision relevance: Accrual accounting makes financial reporting more relevant
 - Opportunism: accruals management ~ estimations
- A large body of academic research, e.g.:
 - Jones (91): discretionary accruals
 - Ball et al. (03); Bushman/Piotroski (04): institutions, legal environment, incentives and reporting quality
 - Land/Lang (02); Leuz et al. (03): ACC-CFO correlation as an important quality characteristic

Framework



Research Setting: the EU context



$$\text{Dispersion} = \text{sdev}_{\text{EU15}}(X) / \text{avg}_{\text{EU15}}(X)$$

Snapshot of analyses

□ EU14 differences in accruals recognition

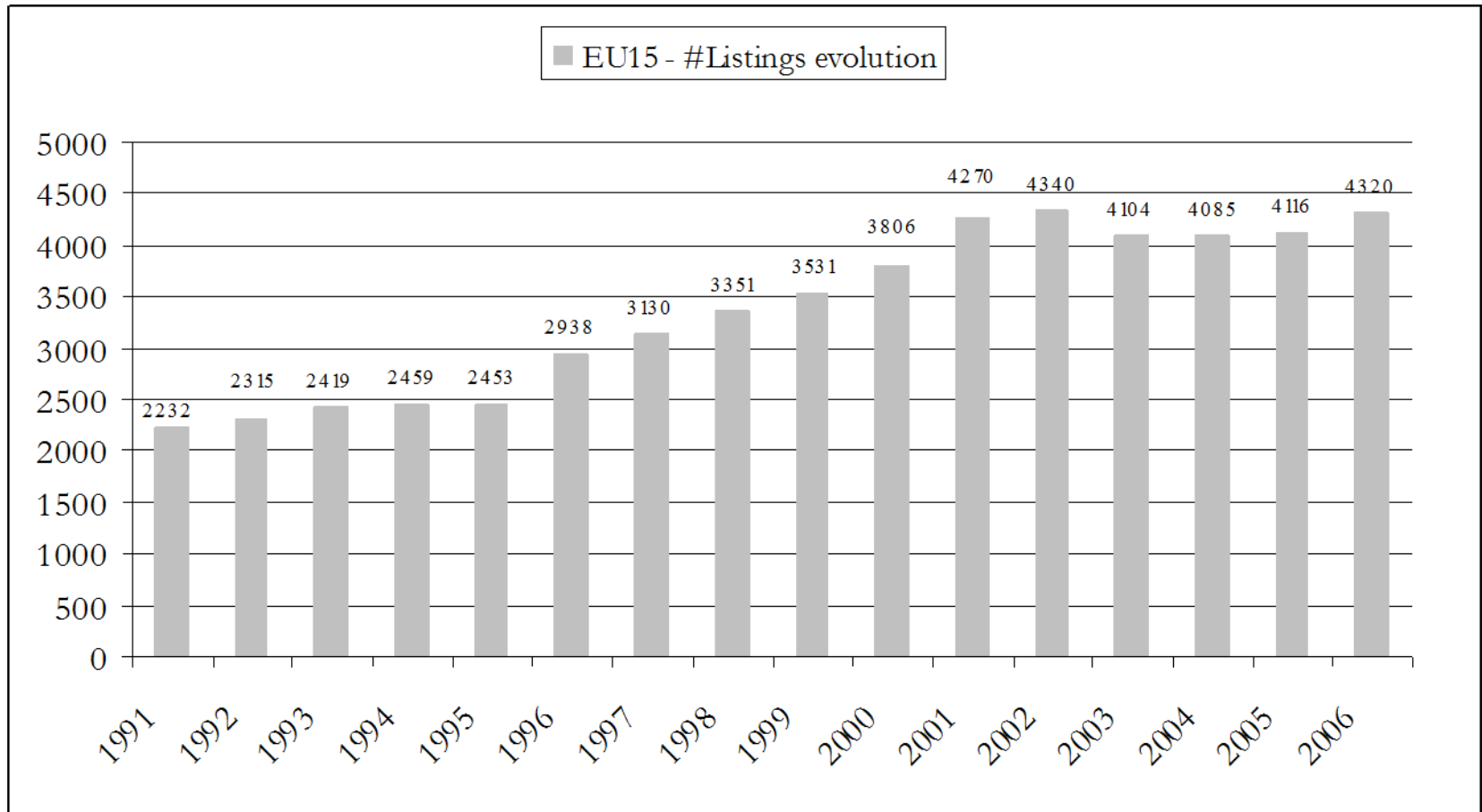
$$ACC = d(\text{cntry} \times \text{period}) + d(\text{cntry} \times \text{period}) \times CFO + \text{controls} + \varepsilon$$

- Country-average evolutions
- Between-country differences
- Different impact of expansion/recession periods

□ Information environment and effect on accruals recognition

- Analysts
- Institutionals

EU14 public firms

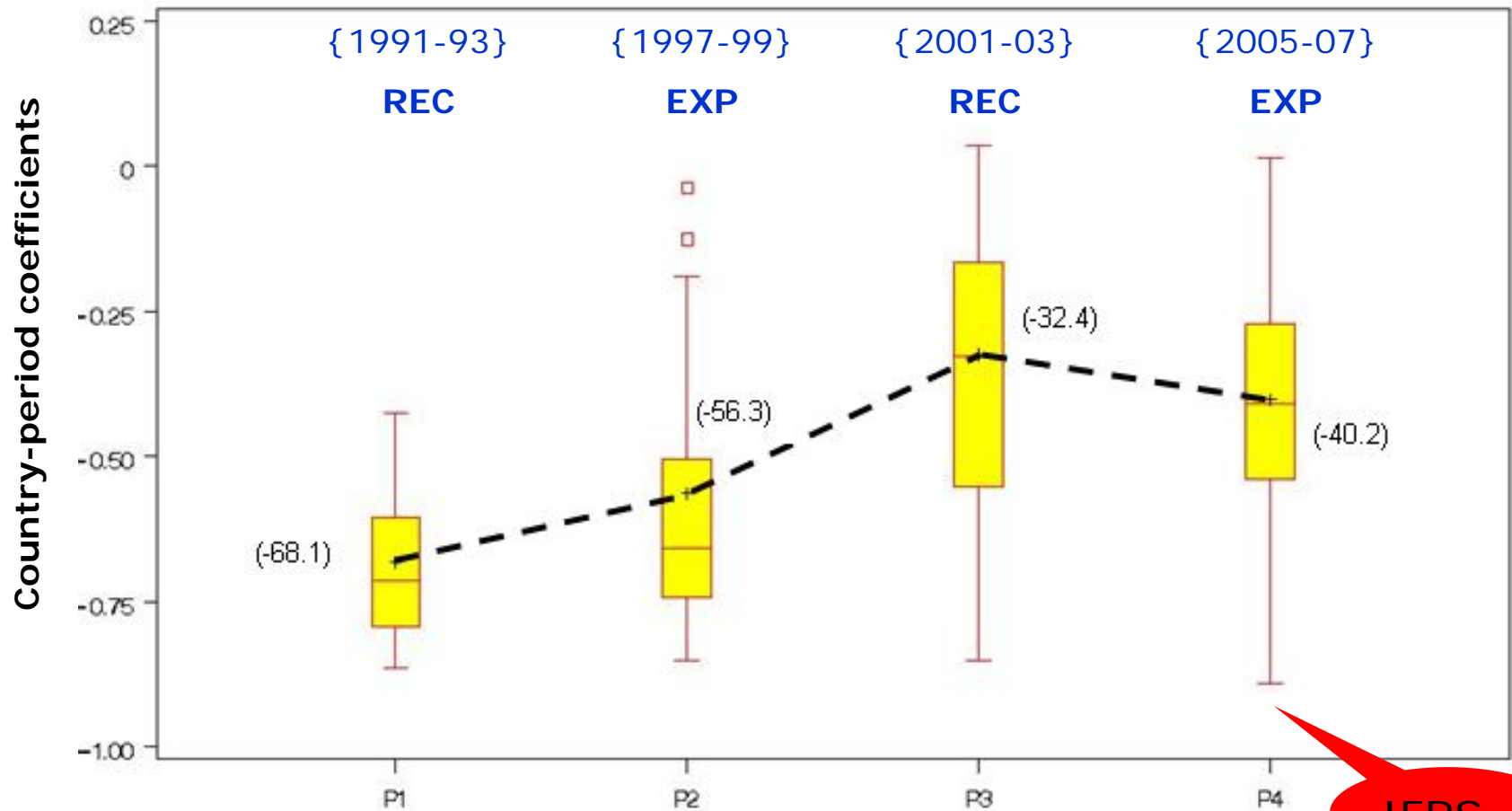


(Source: Thomson Reuters, May 2008)

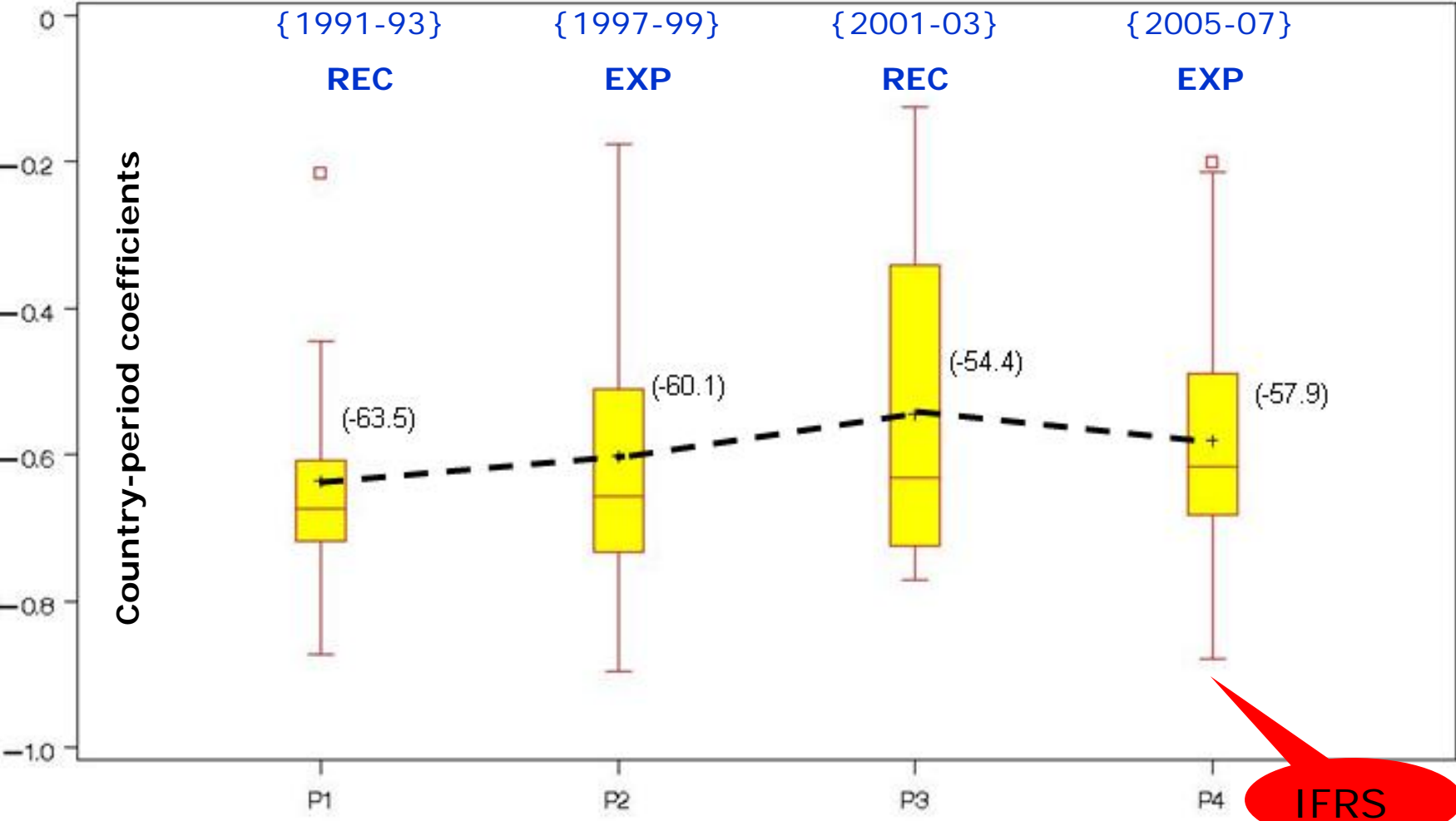
Sample

Country	Full sample				Constant, >15-year sample			
	Firm years		Firms		Firm years		Firms	
	N	%	N	%	N	%	N	%
AUT	846	2%	113	2%	211	2%	13	2%
BE	1,100	2%	128	2%	436	4%	27	4%
DK	1,453	3%	148	2%	570	5%	35	5%
FI	1,202	3%	159	2%	182	2%	11	1%
FR	7,566	16%	972	15%	2,321	19%	145	20%
DEU	6,446	13%	990	15%	482	4%	30	4%
GRC	2,209	5%	321	5%	341	3%	22	3%
IRE	803	2%	129	2%	112	1%	7	1%
IT	2,150	4%	307	5%	562	5%	35	5%
NL	1,610	3%	167	2%	751	6%	46	6%
PT	801	2%	104	2%	191	2%	12	2%
ESP	1,422	3%	135	2%	759	6%	46	6%
SW	2,679	6%	407	6%	502	4%	31	4%
UK	17,707	37%	2,601	39%	4,549	38%	275	37%
ALL	47,994	100%	6,681	14%	11,969	100%	735	100%

Accruals recognition, EU differences



Accruals recognition, EU differences (Constant sample)



Impact information environment?

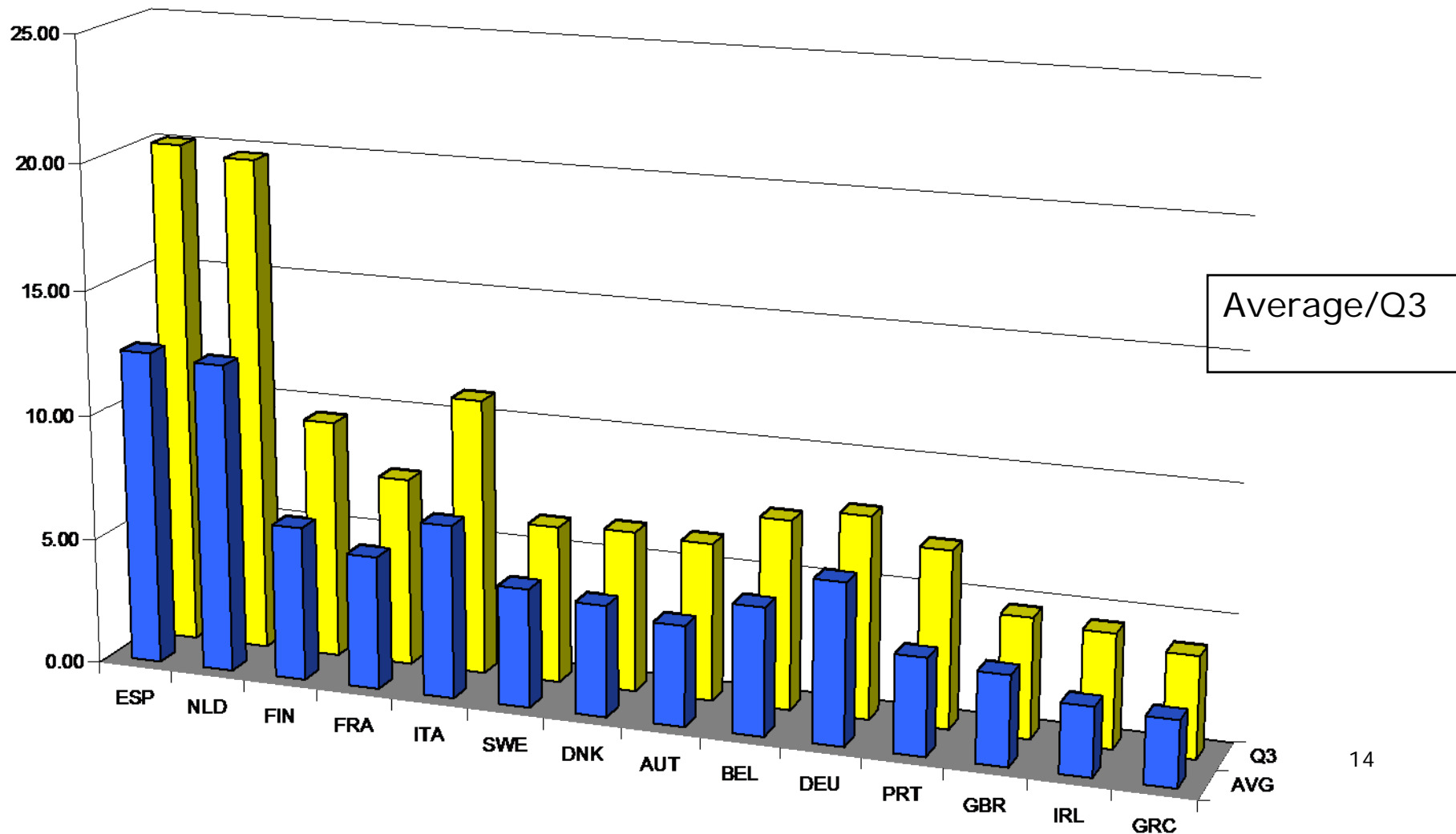
□ Analyst following

- Variation across countries – within countries
- Lang/Lins/Miller (2004):
 - Less analyst following when family is blockholder
 - Stronger effect in low investor protection countries
 - Positive firm valuation effect of analyst following
- EU: *IBES* files

□ Institutional investors

- Variation across countries – within countries
- Bradshaw et al. (2004): international firms exhibiting US GAAP conformity => higher US institutional ownership
- EU: *Amadeus* ownership files

1. Analyst coverage



2. Institutional investor base

(Year=2006)		Nr. Institutional holdings				% Institutional holdings			
Country	N	mean	median	q1	q3	mean	median	q1	q3
AUSTRIA	39	4.4	3	1	6	4.3	2.1	0.2	7.0
BELGIUM	74	4.2	2	1	5	9.5	2.7	0.2	11.9
DENMARK	72	4.8	3	2	7	21.0	14.0	5.5	32.6
FINLAND	91	12.8	10	4	18	17.8	15.7	8.8	25.5
FRANCE	452	3.6	2	1	5	9.2	4.4	0.2	12.3
GERMANY	442	3.6	1	0	5	7.5	1.4	0.0	9.8
IRELAND	51	9.4	7	2	16	24.3	17.1	4.3	38.2
ITALY	143	5.1	3	1	8	5.9	4.5	0.6	9.0
NETHERLANDS	79	6.6	7	1	10	22.0	15.4	2.2	31.7
PORTUGAL	39	4.6	4	0	7	8.6	5.0	0.0	15.4
SPAIN	83	13.3	11	5	21	14.6	11.5	3.6	20.4
SWEDEN	190	8.1	6	2	12	20.1	16.4	4.4	30.7
UK	1071	9.0	7	3	13	31.4	27.4	13.3	46.2

Excess analyst coverage and accruals reporting

- Analysts:
 - Monitoring versus increase market pressure (Yu, 2008)?
 - Improving reporting quality vs. inducing earnings management?

- Model reporting behavior in light of excess analyst coverage:
 - Step 1: #Analysts=f(size, past performance, growth, leverage, centry/year effects)
 - Step 2: Error term from step 1 (*excess coverage*) in explaining the accruals reporting decision

- Plus: partition for institutional environments
 - high – low enforcement (Hope [2003] classification)

- Similar analyses for NIH/PIH

Excess analyst coverage and accruals reporting

<i>Dependent=Accruals</i>	(1)	(2)	
Constant	-0.051 ***	-0.036 ***	
High Enforce		-0.016 ***	
Excess Coverage	-0.002 ***	-0.001 ***	
Enforce*excessCov		-0.001 ***	
CFO	-0.427 ***	-0.593 ***	
Enforce*CFO		0.280 ***	Less smoothing when analysts following increases...
ExcessCov*CFO	0.019 ***	0.012 ***	
Enforce*ExcessCov*CFO		0.006 ***	+ Effect is more pronounced in high enforcement countries...
Controls	Yes	Yes	
Industry fixed effects	Yes	Yes	
Year fixed effects	Yes	Yes	
OBS	40,888	40,888	
adjR2	42.2%	51.5%	

Excess analyst coverage and accruals reporting

<i>Dependent=Accruals</i>	(1)	(2)	Period by period			
			P1	P2	P3	P4
Constant	-0.051 ***	-0.036 ***	-0.017 ***	-0.007 *	-0.077 ***	-0.041 ***
High Enforce		-0.016 ***	0.011 ***	-0.007 ***	-0.017 ***	-0.009 ***
Excess Coverage	-0.002 ***	-0.001 ***	-0.001 ***	0.000	-0.003 ***	-0.001 **
Enforce*excessCov		-0.001 ***	0.000	0.000	0.001 **	-0.001 **
CFO	-0.427 ***	-0.593 ***	-0.685 ***	-0.686 ***	-0.456 ***	-0.556 ***
Enforce*CFO		0.280 ***	0.037 **	0.226 ***	0.242 ***	0.216 ***
ExcessCov*CFO	0.019 ***	0.012 ***	0.007 ***	0.002	0.024 ***	0.003
Enforce*ExcessCov*CFO		0.006 ***	-0.007 **	-0.001	-0.003	0.013 ***
Controls	Yes	Yes	Yes	Yes	Yes	Yes
Industry fixed effects	Yes	Yes	Yes	Yes	Yes	Yes
Year fixed effects	Yes	Yes	No	No	No	No
OBS	40,888	40,888	5,528	7,548	8,801	4,713
adjR2	42.2%	51.5%	74.5%	62.9%	43.1%	51.3%

Plus: similar effects for institutional holdings analyses (not tabulated)

Conclusions / future research

Conclusions

- Reporting in EU during 90s: indicative of earnings smoothing
 - However, tendency towards less smoothing over time
- Substantial variation across countries (e.g. SWE vs. GRC)
- Mandatory IFRS:
 - No sudden switch to similar reporting behavior
 - Institutional/firm-specific incentives...
- Firm information environment affects reporting decisions
 - Both through analyst following and institutional holdings
 - Effect is strongest across high enforcement countries (all years)
 - IFRS (P4) contributes, but only in high enforcement settings

Thank you

Amadeus: own% info providers

7.3. List of Information Providers (IPs)

Banks:	Fitch	Japan:	Teloku Databank
Insurance companies:	TFIS	Korea:	KISS
Companies worldwide:	Zephus	Latvia:	Creditreform Latvia
Belgium:	National Bank of Belgium	Lithuania:	Patikimo Verslo Sistema
Bulgaria:	Creditreform Bulgaria	Netherlands:	LexisNexis
China:	Huaxia	Norway:	Creditinform AS
Croatia:	Creditreform Croatia	Poland:	InfoCredit
Czech Republic:	Albertina data	Portugal:	Coface Mope
Denmark:	Købmandstandens Oplysningsbureau	Romania:	Chamber of Commerce & Industry of Romania
Estonia:	KredidInfo	Russian Federation:	Creditreform St Petersburg
Finland:	Suomen Asiakastieto Oy - Finska	Slovenia:	Coface Intercredit
France:	Coface SCRL	Spain:	Informa
Germany:	Verband der Vereine Creditreform	Sweden:	UC
Greece:	ICAP	Switzerland:	Graham Associates
Hungary:	Creditreform - InterInfo	UK:	Jordans
Iceland:	LT-Icecredit	USA:	SEC NASDAQ
Ireland:	CFI Online	Serbia and Montenegro:	MID Group
Italy:	Novocredit		