Department of Accounting
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Ph.D. Qualifying Exam- Financial Accounting
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PART 1

1. (30%)

The argument of Wynn (2008, AR) associated with voluntary disclosure is as the following:

This paper examines whether legal liability coverage, as measured by excess Directors' and Officers' (D&O) liability insurance coverage and excess cash for indemnification, is associated with the quantity and the quality of a firm's voluntary disclosures. Using Canadian firms whose D&O insurance data are publicly available, I find that firms with higher excess coverage are less likely to report bad news forecasts for the sample firms that are cross-listed in the U.S., and that the number of bad news forecasts decreases for large cross-listed sample firms having high litigation risk. The results are consistent with the litigation cost argument for the disclosure of bad news. I also find that higher excess liability coverage leads to disclosures of more precise bad news for the cross-listed sample firms and less timely disclosures of bad news for large cross-listed sample firms. Further, excess cash for indemnification is a more significant determinant of disclosure decisions.

Similarly, there are some arguments related to voluntary disclosure in Penno (1997).

(1) Propose the conclusions in Penno (1997).

(2) What are the assumptions in Penno (1997)

(3) If you take Wynn's arguments into account, what are your comments/suggestions on Penno (1997)?

2. (20%)

McNichols and Stubben (2008, AR) examine whether firms manipulating their reported financial results make suboptimal investment decisions. They examine fixed asset investments for a large sample of public companies during the 1978-2002 period and document that firms that manipulate their earnings -- firms investigated by the SEC for accounting irregularities, firms sued by their shareholders for improper accounting, and firms that restated financial statements -- over-invest substantially during the misreporting period. Furthermore, following the misreporting period, these firms no longer over-invest, consistent with corrected information leading to more efficient investment levels. They find similar patterns for firms with high discretionary revenues or accruals. Their findings suggest that earnings management, which is largely viewed as targeting parties external to the firm, can also influence internal decisions.

From another perspective, Bagnoli and Watts (2000) also discuss about earnings management by analytical method.

(1) What is the information structure in Bagnoli and Watts (2000)?

(2) Propose various issues including potential topics, hypothesis, and research design related to earnings management.