An International Comparison.
2011 AAA Annual Meeting

Do Investor Protection and IFRS Adoption Alleviate Earnings Management of Diversified Firms? Evidence From An International Comparison

Chiou, Jeng-Ren; Hsueh, Ming-Hsien; Lee, F. R.

Abstract

This paper examines how the institutional settings affect earnings management of diversified firms. The organization complexity of diversified firms increases the complexity of the information process which gives the opportunistic managers an opportunity to manipulate their performance for pursuing their personal interests. However, the managers' opportunism could be eliminated by institutional settings, including the legal system of the country, accounting standards, ownership structure. Our results show that outside investor right and IFRS adoption could lead shareholders to watch out for the cross-subsidization problem and scrutinize segment financial information. This behavior of shareholders will effectively limit the incentive of managers to manage earnings. Once discretionary accruals of each segment decrease while the cancellation effect of accruals remains, the level of discretionary accrual will even lower than that would be if only cancellation effect of segment accruals exist. Additional test provides some evidences of prerequisite for our inference.