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TEACHING THE TEACHERS: A NEW COURSE IN AN ACCOUNTING MASTERS PROGRAM

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ABSTRACT

Faculty preparation in schools of business continues to offer little or no instruction on how to teach. Faculty members continue to rely on teaching methods they have always used. More often than not, the choice of instructional method is a habitual one rather than a reasoned decision based on instructional objectives of the course and content for the day. University instructors teach pretty much as they were taught.

A shortage exists in terminally-qualified accounting instructors. More and more professionally qualified, master's degree holders are entering the ranks of accounting educators. However, many have no experience in classroom instruction.

In 2009, a new accounting master's program was authorized and developed at our formerly undergraduate-only institution. During the design of the program curriculum, administrators informed us that no funding will be provided for graduate assistantships or tuition waivers. We knew from student surveys and advice from professionals that involvement in teaching and research processes was an important component of a sustaining program. So, the faculty initiated a course design called, "The Teaching of Accounting," to permit student-faculty interaction and mentoring. A course description of this elective course entered the graduate catalog.

In the second semester after the master's program launch, Spring 2011, two students independently approached the program coordinator and requested that they be permitted to take the course. So, we offered, ACCM 6900, The Teaching of Accounting, for the first time during Summer Session 2011. The course had two distinct components: (1) students serving as graduate assistants shadowing an experienced, excellent instructor and (2) students actively involved in a teaching of accounting seminar with another instructor. The seminar component was modeled after a master teacher program facilitated by the instructor during prior years.

This conference presentation will include the course outline, certain topic details, a bibliography of resources, outcome assessments provided by the two students and two instructors, and future plans. The presentation and discussions will encourage contributions from attendees.

THE ROTH IRA: HOW IT CAN INCREASE OUR UNDERSTANDING OF SOCIAL SECURITY

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ABSTRACT

Social Security has a serious budget problem. In 2010 President Barack Obama created the National Commission on Fiscal Responsibility and Reform to deal with the fiscal issues of Social Security, as well as with other governmental fiscal issues. The Commission recommended modifications that would generally decrease Social Security benefits although benefits would increase for the poorest quintile of recipients. The Commission noted that high earners were taking too many resources from Social Security. The purpose of this paper is to construct a Roth model for evaluating whether high earners are impoverishing Social Security. The data shows that high earners appear to be subsidizing the system since their contributions over time, with assumed levels of growth, would normally yield more wealth than the value of their social security claims.

Keywords: Roth IRA, National Commission on Fiscal Responsibility and Reform, Social Security

TOWARD A BETTER UNDERSTANDING OF THE CONTINGENT DETERMINANTS RELATED TO THE PERFORMANCE OF THE CAMEROONIAN MUNICIPAL PUBLIC SERVICES

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ABSTRACT

This paper aims to examine the nature of the contingency determinants related to the performance of the municipal public services of the Cameroonian municipalities. Its objective is twofold: the first consists to better understand the practices of performance measurement of the municipalities; and the second consists to identify the factors likely to influence the performance of the municipal public services. The study is based on a hypothetico-deductive approach. Two questionnaires were administered, one to the local elected officials and another to the managers of the different service departments visited. Subsequently, the data analysis clearly shows the existence of structural factors which influence the performance of the Cameroonian municipal public services.

INTRODUCTION

Performance measurement systems have considerably improved in the last few years in the areas of management control. Most organizations today must face new constraints and are increasingly asked to justify their actions depending on the public opinions, whether it concerns quality, fairness, cost transparency, or effectiveness regarding the objectives fixed to them (Alecian & Foucher, 1994). Local communities cannot escape this obligation to legitimize their actions since the public entity that conferred such a service for such a long time no longer exists; they must now demonstrate the effectiveness of the public services they provide. Thus, the communities' structure must now also include a means of reacting to the public (the end-users) demands. Performance measurement systems of the municipal public services therefore aim to rehabilitate local public services which are now facing a crisis of legitimacy and identity. It seems that Cameroonian people have more and more requirements. They see themselves as customers waiting on line for a service, whether of a civil matter or a technical one. In addition, the social and urban consequences in the current political-economic context will result in the emergence of new needs such as garbage removal, supplying potable water, and installing public lighting, at which the local communities will have to answer. Finally, Cameroonian people are increasingly advocating the reject of mediocre public services and they are more and more demanding about the quality of the public funds usage.

Without entering into a detailed analysis of the difficulties faced by Cameroonian municipalities, a certain number of questions underlie our problematic: we must question the nature of the measurement systems used for assessing the performance of the municipal public services in Cameroon. In other words, do the measures taken by Cameroonian authorities, such as the new decentralization plan, the balancing of public finances, and the implementation of a sector-based accounting plan, achieve the performance expected by the municipalities? Are there factors likely to influence the performance of the municipal public services of the Cameroonian municipalities? So the objective of this paper is to try to answer these questions. It is twofold: first, this paper brings a contribution to a better understanding of the contingency determinants related to the performance of the municipal public services; and second, it aims to identify the factors likely to influence the performance of the municipal public services.

The paper is structured as follows. In the first part of the paper, we present the performance measurement systems through structural contingency factors and we formulate the research hypotheses to be tested. In the second part, we describe the research methodology. And, in the last part, we present and discuss the main results got from a principal component analysis (PCA) as well as a multiple linear regression.

SPECIFICITIES OF THE PERFORMANCE OF MUNICIPAL PUBLIC SERVICES

Studies conducted on performance indicators in municipal offices in the United States show that such indicators are not created solely in themselves but in conjunction with their environment, such as contributions by elected officials, citizens, public servants, partners, and managers. With external support, local collectives complete *output* measurements along with *outcome* measurements (Wang X. and Berman E., 2001). The involvement of outside forces in establishing the indicators is necessary due to the complexity of local initiatives and the importance of end-user judgments in the measurement of local performance. The performance measurement system in local collectives is not limited to simply providing managerial information but also includes informing local end-users on the performance of local entities.

To this effect, Melkers J. and Willoughby K.G. (2005) will conclude, after a quantitative study of a sample of 300 local collectives, that measurement systems are developed and contribute to improving the channels of communication between services, facilitating training, and confirming budgetary decisions derived from the information collected on the results, costs, and actions considered.

Analysis from various reports on performance measurement systems shows that the system must have four principal parameters:

1) The information from the performance evaluation should be used to review local efforts and to correct recorded anomalies. The integration of these indicators will not only be on the operational level but also extended to the strategic level: the review of local public policy in light of the results of the local performance evaluation. "The data should again be integrated in the corporate strategy to allow the hypotheses to be tested and therefore question again their actual perspectives"[1] The measurement system is well integrated in

the managerial procedure of municipal offices if it allows reformulating the local strategy and therefore the local public policies.

2) It must also integrate the performance indicators in budget appropriations. This parameter is partly realized: the established financial indicators are integrated since they are part of the accounting system that provides the principal informational outline of organizations. The question now arises on whether to use non-financial indicators in budget appropriations. Kaplan and Norton consider performance based remuneration of employees as an example of integrating non-financial indicators (innovation and competency) in budget appropriations.
3) Communicating on the inside the results of the performance evaluation constitutes a principal parameter in the measurement system. Waterhouse (1999) considers such communication originating from management to employees as a means of implementing the strategy, and thus encouraging employees to participate (Kaplan and Norton, 2001).
4) Communicating the results also can be done on the outside, principally to customers through numerous channels; for example, a marketing campaign that serves to show customers the performance and competency of innovative groups accompanied by a demonstration of the quality of the product proposed. In our opinion, outside communication seems to be a principal parameter in performance measurement systems for municipalities for the previously stated reasons, but also because the officials have the legal obligation to report to the public (citizens) and to justify their policy decisions. This parameter is an inseparable and irrefutable concept of "local governance" where elected officials must prove that they "govern the municipal entity by taking into account the wishes of the people."

DETERMINANTS OF THE PERFORMANCE OF MUNICIPAL PUBLIC SERVICES AND FORMULATION OF THE RESEARCH HYPOTHESES

Dependent Variables

Dependent variables are chosen by taking into account the specific organizational details of African municipalities. Considering the general reticence of African municipal officials to disclose their financial statements and particularly in Cameroon, we have measured the performance by using a combination of six criteria[2.] These criteria were assessed and personally evaluated by the department managers as a function of their importance on a 5-point Likert scale.

Independent Variables

The determinants of municipal performance are grouped into data sets of five exogenous variables. After having explained the theory for each of these explicative variables, we then introduce the respective related hypotheses.

Level of computerization of the activities

The degree of IT as a structural contingency factor has been the subject of numerous empirical studies in organizations, especially in SMB. Its use as a performance measurement in community settings needs no further explanation in the scope of our study. A study by Chapellier (1994) is one of the few that have tried to globally characterize the accounting practices of SMB, defined simultaneously in terms of preparing and using data by management, relative to four fields; namely, general accounting, management control, financial control, and control panels. Other studies, notably those of Lacombe-Saboly (1994) and Lavigne (1999), are more concerned with the particular field of general accounting. These research studies (Chapellier, 1994; Lacombe-Saboly, 1994; Lavigne, 1999), by entering the flow of contingency theory by including as much objective (structural) as subjective (behavioural) information, have shown the heterogeneity of SMB accounting information systems and have also identified certain determinants. According to Chapellier (1994), in the overall context of SMB, the structural contingency factors can be limited to a few fundamental characteristics that are cross-referenced with more general concepts of complexity and uncertainty.

In his research, Chapellier (1994) retains the size and age of the organization, the degree of management IT, and the nature of the activity. On the other hand, Germain C. (2000) shows in his study on SMB that there exists a significant link between the degree of IT on the organization's actions and the sophistication of the control panels. These results by Germain corroborate the research conclusions of those who looked at this relationship following the examples of Kalika (1987) and Chapellier (1994).

Therefore, it is a matter of verifying if the degree of information technology of municipal actions influences or not the organizational performance of public services. Thus, our research proposes to test the following hypothesis:

H1: The level of computerization of the activities has a positive influence on the performance of the municipal public services of the Cameroonian municipalities.

Size-effect

Among the work that was placed in evidence on the influence of size in an organization during the 1960's, the ASTON school (Pugh et al., 1969) is often cited as a pioneer in this field, notably in initiating comparative analysis whose aim is to uncover common and specific problems of all types of organizations. The principal results of the ASTON school affirm the notion that "the size of the organization constitutes a *major predictive factor* in its structure" (Desreumaux, 1992). Regarding the relationship between size and structure, numerous empirical works confirm the results of the ASTON group (Blau and Schoenherr, 1971; Child and Manfield, 1972…). Nevertheless, a study conducted by Meyssonnier F. (1993) on the use of control panels in 82 French communities shows that a large majority of municipalities do not use control panels to control the functioning of services and to direct municipal actions. Using the khi2 test to evaluate the hypothesis of independence between control panels and the size of communities, the author finds a khi2 value of 4.59 with a 2-degree spread and a probability of 9.85%. According to this author, "we cannot attest with certainty that size and use of control data are correlated, particularly since the nature of these control data can be variable". Considering the preceding work, regardless of the size of the organization, size seems to be a variable susceptible to influence the performance characteristics of municipal public services of Cameroonian communities. By placing us in the context of this study, along with other previous work, we propose the following hypotheses:

H2a: The size of the municipalities has a positive influence on the performance of the municipal public services of the Cameroonian municipalities.

H2b: There is a significant relation between the use of control panels and the size of the Cameroonian municipalities.

Regularity of the controls

A diatomic vision of control and its consistency was studied by Mintzberg H. (1982, pg. 148-157). He makes the distinction between "performance control", its "consistency", and the "planning of actions". "The system of performance control is by nature general, and is interested in the consequences of actions; while the planning of actions occurs before their execution and is interested in specific actions". To that end, he specifies the objectives of the performance control system: measurement and motivation. As for the planning of actions, they emerge, according to Mintzberg, as the means by which non-routine decisions and actions in a function-structured organization can be achieved in an integrated fashion. The notion of control seems preferable to one of planning in the way it induces ambivalence with the terms "mastery" and "inspection". In order to specify the field of application to the notion of consistency of controls (Sharma D.S. and Ho, J., 2002), must we first inquire as to the motivations of non-profit organizations? If the case of non-profit organizations is relatively simple, we can state that profit can appear as the first objective of these entities. However, the case of local communities is more delicate to comprehend. Anthony R.N. and Young D.W. (1988) indicate that there is a double objective for these other forms of organizations. The first is to ensure a balance between resources and employees. The second is to maximize the services rendered to the collective within the constraint of minimizing costs. In this sense, the desire to place under control the local collectives is not a fruitless effort. In this framework, we can ask ourselves if the consistency of controls allows for a superior performance of municipal public services of Cameroonian communities. Such a question leads us to propose the following hypotheses:

H3: The more the controls are regular in the municipal public services of the Cameroonian municipalities, the more the performance is better.

H4: There is a positive relation between the size of the municipal public services and the regularity of controls.

H5: There is a positive relation between the control of the objectives by MINTAD[3] and the performance of the municipal public services.

RESEARCH METHODOLOGY

The methodology and the results are presented in the full paper.

References are available upon request.

ENDNOTES

1 P. F. DRUCKER, The information executives truly need, 1995

2 These criteria are: Q371_IMO (importance of the objectives 1 = users satisfaction); Q372_IMO (importance of the objectives 2 = to ensure the garbage collection); Q373_IMO (importance of the objectives 3 = to ensure recording birth and marriage certificates); Q374_IMO (importance of the objectives 4 = staff satisfaction); Q375_IMO (importance of the objectives 5 = drinking water supply); Q38_RO: to reach the objectives.

3 MINTAD: Ministry of the territorial administration and decentralisation.

MARKET REACTION TO RESTATEMENTS AFTER SARBANES-OXLEY

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ABSTRACT

Much has been written about the effects of the Sarbanes-Oxley Act (SOX). Some authors have noted the high cost of implementation, while others have focused on the proposed benefits of the Act. Research results have been conflicted, but in general, it has been determined that the market, at a minimum, has not been confused by the changes. Recent articles have examined the market reaction to restatements before and after SOX. In general, they find that the market reaction is less now that SOX is in effect, speculating that this means the market is less shocked by restatements than in the past.

It is possible, however, that these prior results may be confounded by the changes in behaviors during the implementation phase of SOX. In many other situations, it has been noted that management may opportunistically report exceptionally poor results when overall results are not good (the big bath). The idea is the market does not incrementally reduce returns more if the news is worse. Similarly, with the new 404 disclosures, it has been shown that management reported many problems during implementation, either because the increased scrutiny brought new items to light, or management felt that some system weaknesses would be expected by the market, and therefore, not penalized. Finally, the popular press actually talked about restatements during this period as being positive news that companies were cleaning up their problems.

Accordingly, we investigate whether the market reaction to restatements is different during the implementation period (2002-2003) compared to the current period (2004-2009). We find that there are differences. The reaction to management's discovery of errors leading to restatements is now more negative than during the implementation phase. In addition, core restatements are now viewed more negatively. Finally, companies currently making stealth restatements (not issuing a press release or 8-K) are viewed more negatively than during the implementation period.

Accordingly, it does seem that management received a buy during the implementation phase of SOX. More research is needed to see if this effect confounded the prior studies. In addition, more research is necessary to see if the restatement behavior of management has changed.

IS YOUR PORTFOLIO MANAGER SMARTER THAN A SECOND GRADER?

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ABSTRACT

As an educational experience and a testing of the Efficient Market Hypotheses, four teams of advanced undergraduate business students were each given the responsibility of investing and managing $10,000 in the stock market through a Scottrade.com account. Beyond structuring the initial investment, each team managed their account over a two month period beginning September 1, 2010. The intent of the exercise was to mimic the real world of institutional asset management where money managers strive to beat the S&P 500 index. In addition to competing against each other as they actively managed their portfolios, before the experience students picked randomly on a blank grid which was then populated with S&P 500 stock symbols. This random portfolio was also tracked over the investment period. The investigators' business school secretaries and the Dean's 7 year-old daughter also picked random portfolios. Lastly, recommendations from panelists and experts on Fox TV and CNBC's Mad Money program were also tracked.

Comparative results for all four team's actively managed portfolios are presented. Results from the team random selections as well as those from television experts and novices' random picks are also presented. While not a full test of the Efficient Market Hypotheses, there is sufficient evidence to raise the issue of the true value of paying a stock advisor versus broad based index buying for an investor.

INTRODUCTION

The modern version of the efficient market hypothesis (EMH), as originally developed by Fama (1965), argues that there is an inherent level of efficiency in financial markets. The EMH implies that it is impossible to consistently outperform the market index. This does not imply that the market cannot be outperformed from time to time, but rather, that is cannot be done on a consistent and ongoing basis. The theory has generated a considerable volume of comment and is one of the most widely tested theories in financial economics.

The three postulated forms of the efficient market hypothesis are strong, semi-strong, and weak. Strong form efficiency states that stock prices accurately reflect all information available, from both public and private sources. This is rather difficult to empirically test given existing laws against insider trading and the difficulties with obtaining relevant information in private hands. Semi-strong market efficiency addresses this limitation by stating that stock prices reflect all publicly available information. Under this variant, markets respond quickly and accurately to any new information that is available. The weak form of EMH holds that all information contained in past stock prices is fully reflected in current prices. The implication of the weak form is that established trends cannot reliably be used to predict, and therefore beat, the market in the future.

While a number of researchers have tried to test the efficient markets hypothesis, the myriad of results and their implications do not lend to drawing a clear conclusion. For example, Haugen (1998, 1999), asserts that markets are inherently inefficient and therefore do not support the efficient markets hypothesis theory. On the other hand, others in academia, notably Fama (1997) provide extensive support for market efficiency.

When any investors, be it a student group, an individual, or a professional manager invest money in the stock market, their goal is generally to beat the market's performance. If not, they should simply place their funds in an indexed mutual fund and allow that fund to work to meet market expectations and performance. If a group of investors, in this case student groups, were to outperform the market once or twice, it would not provide definitive evidence against the efficient market hypothesis; however, if they were able to outperform the market repeatedly over time, it would lend some credence to a violation of market efficiency.

METHODOLOGY

Students enrolled in an upper-level undergraduate class on investment theory were split into four teams, tasked with investing and managing their initial $10,000 portfolios over a two month time span through active accounts. Teams were required to consider course information and theories and to develop a plan for managing their portfolios.
responsible for tracking.

Exhibit 1.
Random (I.E. Blind) Portfolio Selections by Teams and Novice Investors

			Student Teams				Novices	
S&P 500		GICS Sector	#1	#2	#3	#4	2nd Grader	School Staff
82	16.4%	Consumer Discretionary	10%	24%	7%	17%	20%	20%
81	16.2%	Financials	16%	21%	17%	17%	10%	10%
73	14.6%	Information Technology	10%	12%	20%	6%	10%	
58	11.6%	Industrials	19%	12%	10%	14%	10%	30%
51	10.2%	Health Care	19%	9%	20%	3%	10%	
41	8.2%	Consumer Staples	10%	9%	3%	9%	10%	20%
38	7.6%	Energy	3%		13%	11%	30%	10%
36	7.2%	Utilities	3%	9%	10%	6%		10%
31	6.2%	Materials	10%	3%		14%		
9	1.8%	Telecommunications Services		3%		3%		

Results in unshaded boxes represents overweights of at least 50% compared to entire S&P 500
Results in shade boxes represent overweights of at least 100% compared to entire S&P 500

In addition to their active management strategies, at the beginning of the course, before the project was explained to them and before they were placed into teams, each student was given a blank 500 space grid. They were instructed to place a mark in any 3, 4, or 5 spaces. Because of the potential bias that the center of a grid and the corners represent, these areas were omitted. Unbeknownst to the students the stock symbols of the S&P 500 had previously been randomly placed into the grid locations. The result was that once students were in their teams and the random selections had been matched to the underlying S&P 500, each team now had a randomly selected portfolio of stocks that they would be This random, or blind, selection process was also performed with two convenience samples, one – the two secretaries working in the school of business and second – the business school Dean's 7 year old daughter, Lilly, at the time in the second grade (see Exhibit 1).

Lastly, to allow comparisons of student team performance to other cohorts, two financial expert cohorts who regularly make stock recommendations were selected – Jim Cramer of CNBC's Mad Money television program (see exhibit 2) and guest panelists on the four television show block on Fox Television named the Cost of Freedom (see Exhibit 3). For both groups recommendations were taken from a specific program late in August 2010, near the date when the student teams would begin their portfolio management.

Exhibit 2: Stocks Recommended By CNBC Mad Money's Jim Cramer	
Ticker Symbol	Company
AGN	Allergan
HD	Home Depot
HOT	Starwood Hotels & Resorts
INTC	Intel
MRX	Medicis Pharmaceutical
NAL	New Alliance Bancshares
PEP	Pepsico
POT	Potash
TRV	Travelers Companies
WTW	Weight Watcher's
YHOO	Yahoo!

RESULTS

Exhibit 4 presents each student team's results, benchmarked against the S&P 500 performance over the specified two month interval. Each team was given $10,000 with a goal of beating the S&P 500 as well as the other teams in the course. As a group, the four teams were able to marginally beat the S&P 500, collectively earning a return of 13.0%. This was slightly better than the S&P 500's 12.8% return for September and October, 2010. As exhibit 4 indicates, while collectively the four teams did exceed their target benchmark, team 1 was primarily responsible for the overall performance, earning a stunning 20.4% return. Teams 3 and 4 generated positive returns in excess of the S&P 500 but marginally so. Team 2 did the poorest of the four teams with its returns dropping off precipitously during the last several weeks.

CONCLUSIONS

From a technical perspective, lessons learned by students involved with this project included: the importance of top-down macroeconomic analysis and diversification strategy, the ability to conduct fundamental investment research, signal monitoring of The Federal Reserve, consideration of transaction costs, sell disciplines, technical analysis, economic cycles, and more.

As to whether this classroom exercise could be considered a sufficient test of the efficient market hypothesis, the answer would have to be no. Beating market performance over time and not merely from time to time is the truest test of the theory. Currently, the "gold standard" is Warren Buffett. Even his longevity and performance over an extended period cannot be considered definitive evidence against the EMH. In early November of 2008 (CNNMoney.com, 2008) Mr. Buffett's Berkshire Hathaway Inc. reported a 77% drop in third-quarter earnings, hurt by declining insurance profits and a $1.05 billion investment loss. For those who like to point to Mr. Buffet as a point against the efficient market hypothesis, this announcement may give them some pause.

Exhibit 3: Fox TV Experts Stock Recommendations			
Ticker Symbol	Company	Fox Show	Person Recommending
AA	Alcoa Inc.	Forbes on Fox	Stephane Fitch
AEO	American Eagle Outfitters Inc.	Cavuto on Business	Charles Payne
AKAM	Akamai Technologies Inc.	Cavuto on Business	Charles Payne
ALL	Allstate Corp.	Forbes on Fox	Bill Baldwin
CMCSA	Comcast Corp.	Bulls & Bears	Jonus Max Ferris
CROX	Crocs Inc.	Bulls & Bears	Kristin Bentz
HRL	Hormel Foods Corp.	Bulls & Bears	Gary B. Smith
PGJ	PowerShares Gldn Dragon Halter USX China	Cashin' In	Wayne Rogers
PKX	POSCO	Cavuto on Business	Charles Payne
SYMC	Symantec Corp.	Forbes on Fox	Victoria Barrett
UL	Unilever ADR Reptg 1 Ord Shs	Bulls & Bears	Tobin Smith
VLO	Valero Energy Corp	Bulls & Bears	Eric Bolling
WACLY	Wacoal Holdings ADR Reptg 5 Ord Shs	Cashin' In	Jonathan Honig

The significant question that is raised by these results is the true value of advice paid for by consumers to investment professionals. Given the pattern of results observed in Exhibit 4 where random selection and buy and hold strategies were the most successful, the claims by many investment advisors of their historical returns should be better viewed compared to the performance of select indices over the same period. It is this, "valued added" by the advisor above and beyond more passive approaches to investing, that is a truer reflection of worth – and one for the individual investor to consider before buying such advice.

Exhibit 4.: Participant Performance Compared to S&P 500					
	Active Portfolio Management	Passive Portfolio (i.e. Buy& Hold) Management	Random(i.e. "blind") Selection Portfolio	Best Performing Strategy	Best Strategy Return Compared to S&P 500
Student Team #1	20.37%	25.92%	14.74%	Buy & Hold	1.93% pts.
Student Team #2	6.03%	9.34%	13.74%	Random Selection	0.93% pts.
Student Team #3	13.11%	12.97%	13.76%	Random Selection	0.95% pts.
Student Team #4	12.49%	12.49%	28.68%	Random Selection	15.87% pts.
2nd Grader Lilly			12.71%		(0.10) % pts.
Secretaries			8.80%		(4.01) % pts.
CNBC's Jim Cramer		12.03%			(0.78) % pts.
Fox TV Experts		10.08%			(2.73) % pts.

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THE RELATIONSHIP BETWEEN INVENTORY MANAGEMENT AND PROFITABILITY

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ABSTRACT

There are a lot of inventory management innovation case studies in business textbooks. However, there are few case studies to explain an efficiency of inventory management with financial terms. This paper examines the financial performance measurement data of 20 pairs of companies consisting of well-known companies with successful inventory management and other well-known companies in the same industry, for each pair. Relationship between inventory management efficiency and companies' profitability is investigated and we found that with lower days in inventory, higher returns on assets and inventories, a firm can increase its profitability.

A COMPARATIVE STUDY OF KOREAN GOVERNMENT ACCOUNTING STANDARD REFORM

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ABSTRACT

There has been a reform on governmental accounting standards in the 21st Century from cash accounting to accrual accounting. Korea (South) is one of the countries to adopt the accrual basis governmental accounting and to successfully implemented it. Comparison between Korea and U.S. governmental accounting standards is conducted through the governmental accounting reform procedure.

APPLYING THE APT MODEL TO A PORTFOLIO OF BSE STOCKS: AN EXPLORATORY STUDY

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ABSTRACT

The Capital Asset Pricing Model (CAPM) has been extensively tested in the context of the Indian stock market. However, the Arbitrage Pricing Theory (APT) model has not been fully tested on a portfolio of stocks in the Indian stock market. APT proposes that there are many sources of risk that cannot be eliminated by diversification.

In order to test the APT empirically, one has to use exploratory factor analysis. A set of sixteen macro economic variables were chosen for testing using the APT model and factor scores using principal component factor analysis were computed for these macro economic variables. Three of the macro economic variables had factor scores that were statistically significant and were used to test the APT model.

A cross sectional regression analysis for estimating asset sensitivity using the APT model with extracted factors from the factor analysis was run on a portfolio of 50 stocks on the Bombay Stock Exchange (BSE) for the time period 2004-07. The preliminary results suggest that the APT model is robust in explaining the risk-return relationship of the selected portfolio of stocks in the BSE.

INVESTIGATING PRESENTATIONAL CHANGE IN COMPANY ANNUAL REPORTS: AN EXTENSION

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ABSTRACT

Arguably the company annual report is one of the most accurate sources for information about the financial health and future prospects of a company (Lord, 2002). In addition, the company annual report is one of the most important tools that a company can utilize to impress shareholders and potential investors through voluntary disclosures, e.g. (Camfferman, 1997), (Lord, 2002), (Penrose, 2008) and (V. Beattie, 2008) (Dilla & Janvrin, 2010). In this practice, companies include extensive voluntary disclosures regarding financial and nonfinancial results, well beyond required financial disclosures. Voluntary disclosure includes, for example, carefully designed financial and nonfinancial charts and graphs, impressive pictures of products and leadership, and bold impressive words in print, such as, improved quality and growth.

This study extends previous work done by Beattie, Dhanani and Jones (2008) where the authors call for further longitudinal investigation into the nature of change in annual report design, specifically in the United States. Our research extends their work with a seven year (2004-10) longitudinal investigation of annual report design for Standard & Poor's (S&P) 500 companies. Our findings show a noticeable change has taken place in annual report design.

Our investigation shows two distinct design trends in annual report design. First, we find companies are providing very specific financial and nonfinancial information to the shareholders. The design trend is to include Securities & Exchange Commission (SEC) Form 10-K, which includes a complete set of financial statements and extensive nonfinancial information in the annual report to the shareholders. Second, the practice of voluntary disclosures appears to be changing. We find that companies selectively use voluntary disclosures or have eliminated completely voluntary disclosures in satisfying SEC reporting requirement to shareholders.

Overall, we conclude corporate America has improved the quality and presentation of nonfinancial and financial information in annual reporting. Including SEC Form 10-K with the annual report to the shareholder provides the user with a complete set of financial statements, plus a wealth of very useful nonfinancial information. Prior to this design trend, a shareholder would have to seek out Form 10-K separately. In addition, we identify a design trend where companies no longer use a wide spectrum of voluntary disclosures to mask the true performance in the annual report to shareholders. The advantage to shareholders is that they no longer have to wade through useless information to complete a quality company analysis. With this trend in design, the informed consumer of the annual report can gain a clear picture of performance, liquidity and financial position.

LITERATURE REVIEW

Research in annual report design generally follows two tracks. Beattie, Dhanani and Jones (2008) (hereafter, BDJ) investigate specific trends in annual report design. Related research inquiries identify trends in annual report design, with particular attention to voluntary disclosures, such as charts and graphs and other material designed to impress the shareholder and/or potential investor.

Specifically, BDJ (p. 217) find companies continue to move in the direction of preparing a design-orientated document in compliance with the annual report. A design-orientated document in this context means financial reports alone do not dominate the annual report. Voluntary disclosures, as discussed above, appear to dominate the annual report (V. Beattie, 2008). The normalization trend appears to be that design and presentational attributes of nonfinancial information is increasing in the annual report. This finding supports previous work by Lee (1994) and McKinstry (1996). BDJ (p. 219) conclude future research should investigate the normalization of annual report design practices in other countries, such as the United States, with longitudinal studies.

S&P 500 DATA ANALYSIS

The authors' sample comes from companies listed on the S&P 500, for the years 2004-2010. The S&P 500 was used because, it is widely regarded as the best single gauge of the U.S. equities market. The D&P 500 focuses on the large cap segment of the market, with approximately 75% coverage of U.S. equities, and it is also an ideal proxy for the total market. The sample consists of 468 useable company annual reports for the years 2004-2010. A company must provide annual reports to the shareholder for the entire sample period to be included in the study.

The authors' study consists of segmenting company annual report to shareholder reporting practices into six categories. The "full" annual reports (Category A) includes the chair's letter, financial highlights (table or graph form), marketing material and a complete set of financial statements, including the management discussion and analysis (MD&A) section, designed beyond the standard structure found in SEC Form 10-K. Marketing material consists of impressive pictures or words about company product or services, such growth, profitability and more designed to impress the annual report reader. Additional marketing material includes bold looking pictures of leadership and/or any other material in the annual report designed to impress the reader. The financial statements carry an enhanced format, compared to the pure black and white financial statements found in SEC Form 10-K. Although the financial values are the same as that found in the 10-K, the statements' format is typically easier to read and interpret with spacing and font design enhancements. The reader can think of the full annual report to shareholders as a high gloss report, printed on quality paper (or in PDF form appearing as if on high quality paper), stuffed with pretty pictures, chart, graphs and words that exude quality. Typically, the report communicates success long before the reader sees the financial statements.

Categories B – F reflect different reporting practices. Category B includes similar material to Category A except the company includes SEC Form 10-K to satisfy the financial statement reporting requirement. Category C includes the chair's letter, financial highlights and SEC Form 10-K in compliance with the annual report to shareholder requirement. Category D includes the chair's letter, marketing material and SEC Form 10-K. Again, marketing material consists of pictures and suggestive works, such growth, profitability and more designed to impress the annual report reader. Category E includes the chair's letter and SEC Form 10-K. In Category F, a company simply provides SEC Form 10-K in compliance with the annual report to shareholders requirement.

The authors' analysis consists of tracking two levels of change to company financial reporting practices for the period 2004-2010. The first level identifies the overall change to reporting practices. The second level tracks the pattern of change. We exam the specific change in reporting practices for those companies that changed from Categories A - F to some other form of reporting.

FINDINGS

Exhibit 1 recaps the first level of data analysis. The findings show a distinct change to how companies comply with the SEC annual report to shareholders requirement. In 2004, 201 Category A companies provided shareholders with a full annual report. By 2010 the number dropped to 98. Between 2004 and 2010 Category A reporting design structure declined by 54% ((201-92)/201).

The findings show an increase in Category B reporting practices. In 2004, 169 companies provided shareholders with Category B annual reports. By 2010, the number increased to 194. This reflects a 15% ((194-169)/169) increase. All of the remaining categories show an increase in reporting frequency as well. Category C increases by 16%. Category D increases 36%. Category E increases by 147%. Category F increases by 148%.

Exhibit 1: Overall Change to Reporting Practices

Annual Report Structure		Annual Report Reporting Practices						
Category		2004	2005	2006	2007	2008	2009	2010
A	Full annual report	201	178	166	141	111	98	92
B	Chair's letter, financial highlights, marketing material, and Form 10-K	169	179	183	193	195	194	194
C	Chair's letter, financial highlights, Form 10-K	25	28	26	33	36	36	29
D	Chair's letter, marketing material, Form 10-K	25	30	29	29	32	33	34
E	Chair's letter, Form 10-K	19	19	33	36	39	44	47
F	Form 10-K only	29	34	31	36	55	63	72
Total		468	468	468	468	468	468	468

Exhibit 2 recaps specific company pattern of reporting trends. We discuss this topic by comparing 2004 reporting category (horizontally listed) compared to 2010 reporting category (vertically listed). We find that 51% of the companies have the same reporting category in 2004 compared with 2010 ([(86+103+11+10+16+11)/468] = 51%).

Exhibit 2: Specific Reporting Trend

Categories	2004						
2010	A	B	C	D	E	F	Totals
A	86	4	-	-	1	1	92
B	68	103	11	7	3	2	194
C	7	8	11	1	2	-	29
D	11	13	-	10	-	-	34
E	10	17	2	2	16	6	53
F	19	24	1	5	6	11	66
Totals	201	169	25	25	28	20	468

Evaluating the upper right and lower left of the diagonal provides insight regarding the specific pattern in changes to reporting practices. Values in the upper right signal companies are moving to more voluntary disclosures. Values in the lower left signal companies are moving to less voluntary disclosures. Exhibit 2 shows the number of companies moving into the lower left section of Exhibit 2 is far greater than the upper right diagonal.

CONCLUSION AND SUGGESTIONS FOR FUTURE INQUIRY

Our findings point to two design normalizations underway in our sample. First, SEC Form 10-K appears to play a much larger role in the annual report to the shareholders. Second, the pattern of evidence recapped in Exhibit 3 suggests voluntary disclosures are decreasing.
The reasons for the changes need to be answered. Does, in fact, SEC Form 10-K provide helpful insight? Are more institutional investor using SEC Form 10-K, and do not need or use other forms of reporting?

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AUTHORS' NOTE

Professors Zeller and Stanko (Chair) teach financial accounting in the Department of Accounting and Business Law. Their research investigates financial reporting and analysis.

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EARNINGS MANIPULATION IN ACQUIRING COMPANIES: AN OVERVIEW

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ABSTRACT

This study addresses earnings manipulation actions under certain circumstances. Many studies have shown that bidding companies experience abnormal negative returns after undertaking bids. This anomaly requires an explanation from an accounting perspective, as a linkage between accruals and stock returns would yield insight into such observations. This paper addresses earnings manipulation in general and in the context of takeover bids, describes potential factors related to mergers and acquisitions, and suggests a methodology to provide empirical evidence to explain the decline in bidding companies' performance post takeover that causes abnormal negative returns. This study seeks to extend earnings manipulation studies using a takeover perspective and suggests a link between accounting policies around a takeover and stock return behaviour during the same period.

Keywords: Earnings management, Accounting Policies, Efficient Market Hypothesis, Mergers and Acquisitions.

INTRODUCTION

There is an understanding among many accounting researchers (e.g. Healy 1985, DeAngelo 1986, and Jones 1991) and among users of financial statements that management deliberately manipulates earnings for certain events. Healy (1985) studies the earnings manipulation assuming that the management compensation plans is the incentive for this action, DeAngelo (1986) argues that the motivation buyout, and Jones (1991) assumes that tax relief is the motivation. Earnings manipulation is assumed to be a practice employed by management in pursuit of self-interest either by selecting accounting procedures or by manipulating accruals in order to increase or decrease reported earnings. Certain economic and contractual variables provide an additional incentive for this practice. In addition to afore mentioned studies, Defond and Jiambalvo (1994) suggest that debt contracts provide management with incentives to manipulate earnings. This approach does not violate the perspective that managers, on average, smooth earnings to enhance their quality. The studies of Subramanyam (1996) and Chaney et al (1996), among others, indicate that managers, on average, smooth income to enhance the quality of earnings. Shubita (2011) reveals mixed results for income smoothing in the Gulf Corporation Council Capital Markets. This study will provide a review of the motivations for earnings manipulation under certain circumstances. The event that will be analyzed is merger and acquisition.

The remainder of this study is organised as follows. Section 2 discusses the incentives of managers prior to takeover bids. Section 3 discusses consequences of earnings manipulation for bidder companies. Section 4 presents additional factors to explain earnings manipulation prior to takeover bids. Finally, section 5 contains a summary and conclusions.

DISCUSSION OF MANAGERS' INCENTIVE TO MANIPULATE ACCRUALS PRIOR TO TAKEOVER BIDS

Acquiring another company can be considered a major strategic decision for the acquiring company. Thus, it requires the management of the acquiring company to prepare in advance before making a decision to undertake a bid. It is unlikely that such an important decision will be undertaken without sound and early planning. Managers of acquiring companies, like all rational managers, seek to minimise the cost of bids as much as possible to benefit their company and its shareholders, as this will reduce the cost of the financing operation.

There have been several UK studies, in addition to many other international studies, that have investigated the stock market performance of acquiring companies around takeover bids. Gregory (1997) examines the long-term performance of UK acquiring companies after a takeover. His results indicate that the post-takeover performance of acquiring companies is unambiguously negative, particularly in the case of equity offers. His explanation for this observation is that acquiring companies use over-valued equity to buy target companies. Further, he contends that share-for-share acquisition is simply one way of issuing over-valued equity to the market. Moreover, Limmack (1991) shows that bidder companies obtain positive abnormal returns in the six months before bid announcement. On the other hand, bidding companies obtain negative returns for the post-bid period. Further, Limmack (1991) demonstrates that the outcome of the bid does not have an impact on the trend of the results. In the same vein, Franks and Harris (1989) show that bidding companies achieve negative returns for the post-bid period.

In summary, existing evidence indicates that bidding companies achieve positive abnormal returns in the pre-bid period and negative abnormal returns in the post-bid period, regardless of the outcome of the takeover bid (Limmack 1991). Dechow et al (1996) found that, among other motivating variables, the most important motivation for management to manipulate earnings is the desire to attract external financing at a low cost. As indicated earlier, acquiring another company involves a financing decision, and when one takes into account the findings of Dechow et al. (1995) that the main incentive for manipulating earnings is to reduce financing costs, it is clear that there is a great motivation for the managers of bidding companies to increase their earnings prior to takeover bids by opportunistically manipulating their accruals in order to convince the market that their companies are performing efficiently. This is done with a view to boosting their share price in order to allow them to finance their companies at lower cost by acquiring other companies using overvalued shares. A potential consequence of such manipulation is that accruals are expected to reverse in the following years (the bidding year and subsequent years). Accrual manipulation prior to takeover bids and its reversal after making bids may provide an explanation for the recent positive returns for bidding companies prior to takeovers and abnormal negative returns for the post-bid period.

The recommended approach that could be adopted as the methodology of this event study is that of Defond and Jiambalvo (1994). The argument here is that managers of acquiring companies plan in advance for takeover by boosting reported earnings, particularly, in the year immediately preceding the takeover. This may explain the findings of Limmack (1991) that bidding companies achieve abnormal positive returns for the pre-bid period as a result of positive earnings manipulation in an effort to fool the market. Consequently, the increase in accruals will be reversed (offset) in the following year(s); this may explain why bidding companies achieve abnormal negative returns for the post-bid period, as accrual reversal occurs due to the technical requirements of double-entry accounting. The market thus revises its expectations downwards by having negative returns in the post-bid period as a reaction to the decline in earnings after the takeover. This scenario provides a logical accounting explanation for the results of the Gregory (1997) study.

CONSEQUENCES OF EARNINGS MANIPULATION FOR BIDDER COMPANIES

Madura and Wiant (1994) analysed abnormal returns of acquiring companies over the long term after a takeover. They found that, in a US sample of 152 acquisitions taking place between 1983 and 1987, average cumulative abnormal returns of acquires were negative during the 36-month period following the merger announcement. Additionally, abnormal returns were negative in nearly every month. Acquirer losses around the time of the announcement may reflect a loss of wealth from an overly generous merger price. Negative abnormal returns in months after the announcement may be due to the market revising its expectations for the merger downwards. The clear results of Madura and Wiant (1994) support the conclusion reached by Gregory (1997), Limmack (1991), and Franks and Harris (1989), as mentioned earlier.

The clear evidence regarding negative abnormal returns for bidding companies post-takeover raises the question of the reason. In light of the Efficient Market Hypothesis (EMH) that indicates that share price is a valid and creditable benchmark for company performance, and in light of the market mechanism to detect any manipulation, a potential explanation for negative returns is that the reported Earnings per Share of the bidding companies is an inflated figure used chiefly to convince the target shareholders to accept the takeover offer. This explanation is predicted on the assumption that the managers of bidder companies plan for the takeover ahead of time by utilizing discretionary accruals to inflate earnings. Based on the EMH, such behaviour cannot continue over the long run. Furthermore, the accruals' nature is to reverse to correct any manipulation-inflated action(s) based on accruals.

The linkage between the negative abnormal returns for the post-bid period that have been revealed in many studies mentioned previously and the accrual-based studies that indicate the possibility of earnings manipulation, especially under certain circumstances, shows that there is a chance to employ accruals to manipulate earnings prior to the takeover bid in order to minimize financing costs.

ADDITIONAL FACTORS TO EXPLAIN EARNINGS MANIPULATION PRIOR TO TAKEOVER BIDS

Following the discussion in the previous sections, one may assume that the takeover event is sufficient motivation for earnings manipulation. Thus, it is quite important to consider additional factors associated with the takeover event that may lead to better understanding of the management behaviour of bidding companies prior to takeover bids.

The following list describes additional factors that may explain to extend of earnings manipulation prior to takeover bids and the expected trend of the relationship between these factors and the engagement of earnings manipulation:

Type of offer

This factor is expected to have an impact on the extent of earnings manipulation by the management of a bidding company prior to a takeover bid. Based on the analysis of the Datastream listing of the takeover, the most common offer types are the following:

- Cash offer
- Equity offer
- Cash offer with equity alternative

- Equity offer with cash alternative

Gregory (1997) shows that negative abnormal returns were significant in the case of equity offers. Thus, considering the type of offer enables a better understanding of manipulation pre- and post-takeover.

Outcome of offer

Offers may be classified as either:

- Successful or
- Unsuccessful

Despite the finding in studies that abnormal returns in the post-bid period did not indicate clear evidence of any differences due to the outcome of the bid, this factor should be considered, as the outcome of the bid is expected to be a function of the preparation for the bid.

Attitude of the offer

Takeover bids can be classified as either:

- Friendly or
- Hostile

Martynova and Renneboog (2006) describe greater price reaction for a hostile takeover compared to a friendly offer. Thus, it is worth investigating the potential impact of this factor on the extent of earnings manipulation.

Value of the offer

Finally, the value of the bid may explain the motivation for earnings manipulation. In this regard, it is expected that the extent of earnings manipulation is higher when the value of the bid increases.

Overall, the above factors may support the initial argument in this section that the managers of bidding companies manipulate accruals prior to takeover bids. As a consequence of this manipulation, results show that there is a decline in unexpected accruals in the post-bid period. Such an argument may explain the positive abnormal returns in the six months before bid announcement for bidding companies, as noted by Limmack (1991), as well as later negative, as presented in most of the studies in this field (as discussed previously).

SUMMARY AND CONCLUSIONS

This study provides theoretical background for earnings manipulation based on a small-sample approach. The major advantage of the sample is in providing a methodology of analysis based on a homogeneous sample with an event that gives the manager the incentive to manipulate accruals in order to reduce external financing costs. Further, this study provides the expected trend of the results.

Other potential factors have been presented in order to provide better explanations of earnings manipulations prior to takeover. These factors are the type of offer, attitude of the offer, outcome of the offer, and value of the offer.

In the further, it is recommended that researchers seek a link between stock-returns behaviour and accounting policy based on accruals around takeover bids.

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