

ACCT IS 971D
Empirical Research in Financial Reporting
Fall 2004

Class: 2:30 – 6:00 p.m. Wednesdays
2169 Grainger
Professor: Mark Kohlbeck
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Office Hours: Stop by or make an appointment

Course Objectives

The primary objective of this course is to develop a broad understanding of empirical accounting research in financial reporting. The intent is to focus the student on both the classics to provide a background and current research with a focus on the types of questions and innovative methods accounting academics are currently pursuing and developing. A second objective is for students to complete a substantial research project that may lead to publishable work and/or a dissertation.

Professor Information

Professor Kohlbeck's area of expertise is financial accounting and reporting. He is currently teaching financial accounting courses at the University. Mark previously taught at The University of Texas at Austin and Southern Methodist University. His primary research interests concern banking and financial institutions in the areas of intangible assets, regulation, accounting choice, and accounting disclosures. Previously, Mark was an auditor and management consultant for Deloitte & Touche in Dallas and Milwaukee. His professional experience includes restructuring troubled financial institutions, mergers and acquisitions, and litigation support. Mark is also a member of Beta Alpha Psi, Beta Gamma Sigma, the AICPA, and the AAA.

Required Text Books

Beaver, W. 1998. *Financial Reporting: An Accounting Revolution*. 3rd edition, Prentice Hall.

Campbell, J., A. Lo, and A. MacKinlay. 1997. *The Econometrics of Financial Markets*. 1st edition, Princeton University Press.

Watts, R. and J Zimmerman. 1986. *Positive Accounting Theory*, Prentice Hall.

Recommended Text Book

Kennedy, P. 2003. *A Guide to Econometrics*, 5th edition, The MIT Press.

Course Format

The course will be conducted in a seminar format addressing various capital markets and financial reporting issues. For each topic, a set of primary and background readings are presented. The student is expected to have read and understand the background readings prior to when the primary readings are discussed in class. Primary readings typically consist of three to four papers per session. *It is imperative that the required papers are read thoroughly prior to class.* All students will prepare a one-page critique of each paper that discusses its strengths and weaknesses. The critiques should be distributed via email the evening before class. In addition, one student will be designated as the discussion leader for each paper. The responsibilities of the discussion leader will include the following:

- Provide a summary of the paper to be distributed to the class (1 - 2 pages)
 - Research question
 - Primary research method
 - Findings
 - Contribution

- Lead the discussion of strengths and weaknesses

Each student should also identify at least one research idea related to each paper and compile the research ideas in a journal (I will review the journal periodically and provide feedback).

Grading

The following summarizes how you will be evaluated for this course.

Participation	30%
Referee Reports	10%
Literature Review Project	10%
Research Project	30%
Final Exam	<u>20%</u>
Total	100%

Participation – All students are expected to be prepared for each class and actively **contribute**. Participation also includes fulfilling discussion leader responsibilities, preparing critiques, and participating in the Accounting Department’s weekly research workshops.

Referee Reports – During the course of the semester, students are required to write two referee reports on anonymous working papers relevant to the course. The reports should be short and concise, focus on the “big” picture, and clearly convey an opinion on the research. The referee reports are due one week after the paper is distributed.

Literature Review – Each student will be assigned a topic to perform a review of the applicable literature. The student is responsible for synthesizing the applicable literature into a review of 10 – 15 pages. The literature review is due October 13, 2004.

Research Project – As discussed above, one objective of the course is to complete a research project. Your research topic should represent a new solo-authored project (no co-authorships or continuation of summer research projects are permitted) and involve archival research methodology. The final due date is firm – No Incompletes will be assigned.

Throughout the course of the semester, students will be required to meet the deadlines detailed below in completing the project.

	<u>Due Date</u>
Research question (preliminary)	9/8
Research question (final)	9/15
Three paragraphs (preliminary drafts)	9/22, 9/29, 10/6
Presentation of Preliminary Proposal	10/20
Preliminary Paper	11/24
Paper presentation	12/15
Final paper with response to reviewer	12/22

Final Exam – A final exam will be administered during the University’s final exam period. The exam will be similar to questions that the students may encounter on a preliminary exam.

Course Schedule

<u>Week</u>	<u>Topic</u>
9/8	Introduction, Discussion of Summer Research, Discussion of Reviews / Responses (JAAF example), Developing Research Questions
9/15	Valuation (Price and Returns)
9/22	Valuation (RIM)
9/29	Earnings Information (Earnings Announcements)
10/6	Earnings Information (ERCs)
10/13	Non-Earnings Information I
10/20	Presentation of Research Question
10/27	Non-Earnings Information II
11/3	Market Anomalies and Market Efficiency (Drift)
11/10	Market Anomalies and Market Efficiency (Other)
11/17	Accounting Choice (Voluntary Disclosure)
11/24	Accounting Choice (Economic Consequences)
12/1	Accounting Choice (Earnings Management)
12/8	Accounting Choice (Contracts / Compensation)
12/15	Presentations
TBA	Final Exam

See attached list of readings.

Professional Conduct Policy

To foster a more professional learning environment and to develop habits that lead to success in the business work, all participants in must engage in professional behavior, including:

1. Taking responsibility for individual actions.
2. Attending each class session, including arriving promptly and leaving at the designated time.
3. Being attentive and an active participant in group activities and class discussions.
4. Respecting diversity in the classroom and treating everyone involved in the class in a civil manner.
5. Planning outside activities to avoid conflicts with the activities outlined in the syllabus.
6. Agree to abide by the academic misconduct rules and procedures and code of ethics discussed below.
7. Acknowledging the importance of clarity of expression in written and oral communication and understanding that the course grade will be affected by your ability to communicate.

Academic Misconduct Policy

UW conduct rules describe academic misconduct as "... an act in which a student: (a) Seeks to claim credit for the work or efforts of another without authorization or citation; (b) Uses unauthorized materials or fabricated data in any academic exercise; (c) Forges or falsifies academic documents or records; (d) Intentionally impedes or damages the academic work of others; (e) Engages in conduct aimed at making false representation of a student's academic performance; or (f) Assists other students in any of these acts."

Charges of academic misconduct are taken seriously and actions that can be taken against a student include failure in the course and permanent record in the student's file.

Student Conduct and Disciplinary Rules <http://www.wisc.edu/cac/res/sdg/summary.htm>

Tentative Reading List

Date	Primary Readings	Background Readings
Summer	<p>Beaver. 1998. <i>Financial reporting: an accounting revolutions</i>, 3rd edition, Prentice Hall.</p> <p>Watts and Zimmerman. 1986. <i>Positive accounting theory</i>, 1st edition, Prentice Hall.</p> <p>Kothari, S. 2001. Capital Markets Research in Accounting. <i>Journal of Accounting & Economics</i> (September) 31: 105-232.</p>	NA
9/8	<p>Beaver, W. 2002. Perspectives on recent capital markets research. <i>The Accounting Review</i> 77 (April): 453-474.</p> <p>Lev, B. 1989. On the usefulness of earnings and earnings research: lessons and directions from two decades of empirical research. <i>Journal of Accounting Research</i> 27 (Supplement): 153-201.</p>	Campbell, Lo, and Mackinlay. 1997 – Chapters 1 and 5.
9/15	<p>Beaver, W., and S. Ryan. 2000. Biases and lags in book value and their effects on the ability of the book-to-market ratio to predict book rate of return on equity. <i>Journal of Accounting Research</i> 38 (Spring): 127-148.</p> <p>Collins, D. E. Maydew and I. Weiss. 1997. Changes in the value-relevance of earnings and book values over the past forty years, <i>Journal of Accounting and Economics</i> 24 (December): 39-67.</p> <p>Collins, D., M. Pincus, and H. Xie. 1999. Equity valuation and negative earnings: the role of book value of equity. <i>The Accounting Review</i> 74 (January): 29-61.</p> <p>Lev, B. and P. Zarowin. 1999. The boundaries of financial reporting and how to extend them. <i>Journal of Accounting Research</i> 37 (Supplement): 353-387.</p>	<p>Campbell, Lo, and Mackinlay. 1997 – Chapter 7</p> <p>Barth, M., W. Beaver, and W. Landsman. 2001. The relevance of the value-relevance literature for financial accounting standard: another view setting. <i>Journal of Accounting & Economics</i> (September) 31: 77 - 104.</p> <p>Beaver, W., C. Eger, S. Ryan, and M. Wolfson. 1989. Financial Reporting, Supplemental Disclosures, and Bank Share Prices. <i>Journal of Accounting Research</i> 27 (Autumn): 157-178.</p> <p>Easton, P. 1985. Accounting earnings and security valuation: empirical evidence of the fundamental links. <i>Journal of Accounting Research</i> 23 (Supplement): 54-77.</p> <p>Holthausen, R. and R. Watts. 2001. The relevance of the value-relevance literature for financial accounting standard setting. <i>Journal of Accounting & Economics</i> (September) 31: 3 - 76.</p> <p>Kothari, S. P. and J. Zimmerman. 1995. Price and Return Models, <i>Journal of Accounting and Economics</i>, (September), 155-192.</p>

Date

Primary Readings

Background Readings

<p>9/22</p>	<p>Dechow, P., A. Hutton, and R. Sloan. 1999. An empirical assessment of the residual income valuation model. <i>Journal of Accounting and Economics</i> 26 (January): 1-34.</p> <p>Lo, K. and T. Lys. 2000. The Ohlson model: contribution to valuation theory, limitations, and empirical applications. <i>Journal of Accounting, Auditing, & Finance</i> 15 (Summer): 337-367.</p> <p>Penman, S., and T. Sougiannis. 1998. A comparison of dividends, cash flows, and earnings approaches to equity valuation, <i>Contemporary Accounting Research</i> 15 (Fall): 343-383.</p>	<p>Feltham, J. and J. Ohlson. 1995. Valuation and Clean Surplus Accounting for Operating and Financial Activities, <i>Contemporary Accounting Research</i>, (Spring), 689-731.</p> <p>Ohlson, J. 1995. Earnings, Book Value and Dividends in Security Valuation, <i>Contemporary Accounting Research</i> (Spring), 661-687.</p>
<p>9/29</p>	<p>Atiase, R. 1985. Predisclosure information, firm capitalization and security price behavior around earnings announcements. <i>Journal of Accounting Research</i> (Spring), 21-36.</p> <p>Easton, P. and M. Zmijewski. 1989. Cross-Sectional Variation in the Stock Market Response to the Announcement of Accounting Earnings, <i>Journal of Accounting and Economics</i>, (July), 117-141.</p> <p>Francis, J., K. Schipper, and L. Vincent. 2002. Expanded disclosures and the increased usefulness of earnings announcements. <i>The Accounting Review</i> 77 (July): 515-546.</p>	<p>Campbell, Lo, and Mackinlay. 1997 – Chapter 4</p> <p>Ball, R. and P. Brown. 1968. An Empirical Evaluation of Accounting Income Numbers, <i>Journal of Accounting Research</i>, (Autumn), 159-178.</p> <p>Bamber, L. 1987. Unexpected Earnings, Firm Size, and Trading Volume around Quarterly Earnings Announcements, <i>The Accounting Review</i>, (July), 510-532.</p> <p>Beaver, W. 1968. The Information Content of Annual Earnings Announcements, <i>Journal of Accounting Research</i>, (Supplement), 67-92.</p>
<p>10/6</p>	<p>Ali, A. and P. Zarowin. 1992. Permanent versus transitory components of annual earnings and estimation error in earnings response coefficients. <i>Journal of Accounting and Economics</i> (June/September), 249 – 264.</p> <p>Easton, P. and T. Harris. 1991. Earnings as an Explanatory Variable for Returns, <i>Journal of Accounting Research</i>, 19 -36.</p> <p>Freeman, R. and S. Tse. 1992. A Nonlinear Model of Security Price Responses to Accounting Earnings. <i>Journal of Accounting Research</i>, 185-209.</p> <p>Dhaliwal, D., D. Guenther, and M. Trombley. 1999. Inventory accounting method and earnings-price ratios. <i>Contemporary Accounting Research</i> 16 (Fall): 419-436.</p>	<p>Collins, D. and S. Kothari. 1989. An Analysis of the Intertemporal and Cross-Sectional Determinants of Earnings Response Coefficients, <i>Journal of Accounting and Economics</i>, (July), 143-181.</p> <p>Freeman, R. 1987. The association between accounting earnings and security returns for large and small firms. <i>Journal of Accounting and Economics</i> (July), 195 – 228.</p> <p>Kormendi, R. and R. Lipe. 1987. Earnings Innovations, Earnings Persistence, and Stock Returns. <i>Journal of Business</i> (July), 323-346.</p>

Date**Primary Readings****Background Readings**

10/13	<p>Barth, M. 1991. Relative Measurement Errors among Alternative Pension Asset and Liability Measures, <i>The Accounting Review</i>, (July), 433-463.</p> <p>Barth, M., and G. Clinch. 1998. Revalued financial, tangible, and intangible assets: associations with share prices and non-market-based value estimates. <i>Journal of Accounting Research</i> 36 (Supplement): 199-233.</p> <p>Dechow, P. 1994. Accounting Earnings and Cash Flows as Measures of Firm Performance: The Role of Accounting Accruals, <i>Journal of Accounting and Economics</i>, (July), 3-42.</p> <p>Lev, B. and T. Sougiannis. 1996. The Capitalization, Amortization, and Value-Relevance of R&D, <i>Journal of Accounting and Economics</i>, 107-138.</p>	<p>Barth, M. 2000. Valuation-based Accounting Research: Implications for Financial Reporting and Opportunities for Future Research. <i>Accounting and Finance</i> 40: 7-31.</p> <p>Barth, M., W. Beaver and W. Landsman. 2001. The Relevance of the Value Relevance Literature for Financial Accounting Standard Setting: Another View, <i>Journal of Accounting & Economics</i>, (September), 31: 77-104.</p>
10/20	3 paragraph presentations	NA
10/27	<p>Amir, E. and B. Lev. 1996. Value-Relevance of Nonfinancial Information: The Wireless Communications Industry, <i>Journal of Accounting and Economics</i>, (August-December), 3-30.</p> <p>Ittner, C. and D. Larker. 1998. Are Non-financial Measures Leading Indicators of Financial Performance? An Analysis of Customer Satisfaction. <i>Journal of Accounting Research</i> 36: 1-35.</p> <p>Jennings, R., P. Simko and R. Thompson. 1996. Does LIFO Inventory Accounting Improve the Income Statement at the Expense of the Balance Sheet? <i>Journal of Accounting Research</i>, (Spring), 85-109.</p>	<p>Ittner, C. and D. Larker. 2001. Assessing Empirical Research in Managerial Accounting: A Value-based Management Perspective. <i>Journal of Accounting & Economics</i> (December) 32: 349-410.</p>

Date**Primary Readings****Background Readings**

11/3	<p>Bernard, V. and J. Thomas. 1990. Evidence that Stock Prices Do Not Fully Reflect the Implications of Current Earnings or Future Earnings. <i>Journal of Accounting and Economics</i> (December), 305-340.</p> <p>Ball, R., and E. Bartov. 1996. How naive is the stock market's use of earnings information? <i>Journal of Accounting and Economics</i> 21: 319-337.</p> <p>Bartov, E., S. Radhakrishnan, and I. Krinsky. 2000. Investor sophistication and patterns in stock returns after earnings announcements. <i>The Accounting Review</i> 75 (January): 43-63.</p>	<p>Campbell, Lo, and Mackinlay. 1997 – Chapters 2 and 6.</p> <p>Bernard, V. and L. Thomas. 1989. Post-Earnings-Announcement Drift Delayed Price Response or Risk Premium, <i>Journal of Accounting Research</i>, (Supplement), 1-36.</p> <p>Foster, G., C. Olsen and T. Shevlin. 1984. Earnings Releases, Anomalies and the Behavior of Security Returns, <i>The Accounting Review</i>, 574-603.</p>
11/10	<p>Abarbanell, J. and B. Bushee. 1998. Abnormal returns to a fundamental analysis strategy, <i>The Accounting Review</i>, (January): 19-45.</p> <p>Collins, D., and P. Hribar. 2000. Earnings-based and accrual-based market anomalies: one effect or two? <i>Journal of Accounting and Economics</i> 29 (February): 101-123.</p> <p>Lev, B. and R. Thiagarajan. 1993. Fundamental Information Analysis, <i>Journal of Accounting Research</i>, 190-215.</p>	<p>DeBondt, W. and R. Thaler. 1987. Further Evidence of Investor Overreaction and Stock Market Seasonality, <i>Journal of Finance</i>, (July), 557-581.</p> <p>Ou, J. and S. Penman. 1989. Financial Statement Analysis and the Prediction of Stock Returns, <i>Journal of Accounting and Economics</i>, (November), 295-330.</p> <p>Sloan, R. 1996. Do stock prices fully reflect information in accruals and cash flows about future earnings? <i>The Accounting Review</i> 71, 289 – 315.</p>
11/17	<p>Botosan, C. 1997. Disclosure Level and the Cost of Equity Capital. <i>The Accounting Review</i> 72: 323-350.</p> <p>Lundholm, R. and L. Myers. 2002. Bringing the future forward: the effect of voluntary disclosure on the returns-earnings relation. <i>Journal of Accounting Research</i> 40 (June): 809-840.</p> <p>Miller, G. 2002. Earnings performance and discretionary disclosure. <i>Journal of Accounting Research</i> 40 (March): 173-204.</p> <p>Skinner, D. 1994. Why Firms Voluntarily Disclose Bad News. <i>Journal of Accounting Research</i> (Spring): 38-60.</p>	<p>Healy, P. And K. Palepu. 2001. Information Asymmetry, Corporate Disclosure, and the Capital Markets: A Reviw of the Empirical Disclosure Literature. <i>Journal of Accounting & Economics</i> (September) 31: 405-456.</p> <p>Penman S. 1980. An Empirical Investigation of the Voluntary Disclosure of Corporate Earnings Forecasts. <i>Journal of Accounting Research</i> (Spring), 132-160.</p> <p>Verrechia, R. 1983. Discretionary disclosure. <i>Journal of Accounting and Economics</i> 5, 179 – 194.</p>

Date**Primary Readings****Background Readings**

Date	Primary Readings	Background Readings
11/24	<p>Beatty, A., S. Chamberlain, and J. Magliolo. 1995. Managing financial reports of commercial banks: the influence of taxes, regulatory capital, and earnings. <i>Journal of Accounting Research</i> 33, 231 – 261.</p> <p>Warfield, T., J. Wild, and K. Wild. 1995. Managerial ownership, accounting choices, and informativeness of earnings. <i>Journal of Accounting and Economics</i> 20: 61-92.</p> <p>Subramanyam, K. 1996. The pricing of discretionary accruals. <i>Journal of Accounting and Economics</i> 22, 249 – 281.</p>	<p>Lev, B. 1979. The impact of accounting regulation on the stock market: the case of oil and gas companies. <i>The Accounting Review</i> (July): 485-503.</p> <p>Fields, T., T. Lys, and L. Vincent. 2001. Empirical research on accounting choice. <i>Journal of Accounting and Economics</i> (September), 255 – 308.</p>
12/1	<p>Burgstahler, D. and I. Dichev. 1997. Earnings management to avoid earnings decreases and losses. <i>Journal of Accounting and Economics</i> (December), 99 – 126.</p> <p>Dechow, P., R. Sloan, and A. Sweeney. 1995. Detecting earnings management, <i>The Accounting Review</i> (April), 193 – 255.</p> <p>Defond, M. and J. Jiambalvo. 1994. Debt covenant violation and manipulation of accruals. <i>Journal of Accounting and Economics</i> 17, 145 – 176.</p>	<p>Jones, J. 1991. Earnings management during import relief investigations. <i>Journal of Accounting Research</i> 29, 193 – 228.</p>
12/8	<p>Dechow, P. A. Hutton, and R. Sloan. 1996. Economic consequences of accounting for stock-based compensation. <i>Journal of Accounting Research</i> (Supplement), 1 – 20.</p> <p>Healy, P. 1985. The effect of bonus schemes on accounting decisions. <i>Journal of Accounting and Economics</i> (April), 85 – 107.</p> <p>Holthausen, R., D. Larcker, and R. Sloan. 1995. Annual bonus schemes and the manipulation of earnings. <i>Journal of Accounting and Economics</i> 19, 29 – 74.</p>	<p>Watts, R. and J. Zimmerman. 1991. “Positive Accounting Theory: A Ten Year Perspective.” <i>The Accounting Review</i> (January): 131-156.</p> <p>Holthausen, R. 1981. Evidence on the effect of bond covenants and management compensation contracts on the choice of accounting techniques. <i>Journal of Accounting and Economics</i> (March), 73 – 109.</p>
12/15	Presentations	NA

Other Articles of Interest

Model Specification and Econometric Issues

- Barth, M. and S. Kallapur. 1996. The Effects of Cross-Sectional Scale Differences on Regression Results in Empirical Accounting Research, *Contemporary Accounting Research*, (Fall), 527-567.
- Bernard, V. 1987. Cross-Sectional Dependence and Problems in Market-Based Accounting Research, *Journal of Accounting Research*, (Spring), 1-48.
- Christie, A. 1987. On Cross-Sectional Analysis in Accounting Research, *Journal of Accounting and Economics*, (December), 231-258.
- Ohlson, J. and P. Shroff. 1992. Changes versus Levels in Earnings as Explanatory Variables for Returns, *Journal of Accounting Research*, (210-226).
- Acharya, S. 1993. Value of Latent Information: Alternative Event Study Methods, *Journal of Finance*, (March), 363-385.
- Brown, S. and J. Warner. 1980. Measuring Security Price Performance, *Journal of Financial Economics*, (September), 205-257.
- Brown, S. and J. Warner. 1985. Using Daily Stock Returns: The Case of Event Studies, *Journal of Financial Economics*, (March), 3-32.
- Cheng, C., W. Hopwood, and J. McKeown. 1992. Non-Linearity and Specification Problems in Unexpected Earnings Response Regression Model, *The Accounting Review*, (July), 579-598.

Literature Reviews

- Beaver, W. 1996. Directions in Accounting Research: NEAR and FAR, *Accounting Horizons*, 113-124.
- Bernard, V. 1989. Capital Markets Research in Accounting During the 1980's: A Critical Review, *The State of Accounting Research as We Enter the 1990's* (University of Illinois), 172-120.
- Lev, B. 1989. On the Usefulness of Earnings and Earnings Research: Lessons and Directions from Two Decades of Empirical Research, *Journal of Accounting Research* (Supplement), 153-201.
- Lev, B. and J. Ohlson 1982. Market-Based Empirical Research in Accounting: A Review, Interpretation and Extension, *Journal of Accounting Research* (Supplement), 161-234.
- Schipper, K. 1995. Academic Accounting Research and the Standard Setting Process, *Accounting Horizons* (December), 61-73
- Foster, G. 1980. Accounting Policy Decisions and Capital Market Research, *Journal of Accounting Research* (March): 29-62.
- Beaver, W. and J.S. Demski. 1974. The Nature of Financial Accounting Objectives: A Summary and Synthesis. *Studies of Financial Accounting Objectives: Supplement to Vol. 12 of the Journal of Accounting Research*.
- Gonedes, N. J. and N. Dopuch. 1974. Capital Market Equilibrium Information-Production and Selecting Accounting Techniques: Theoretical Framework and Review of Empirical Work. *Studies of Financial Accounting Objectives, Supplement to Vol. 12 of the Journal of Accounting Research*.