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This study examines the relationship between earnings changes and MBOs. Using a different research design, the results show that earnings changes for the sample are significant. The results are consistent with the hypothesis that managers manipulated earnings downward prior to the MBO. An examination of pre-MBO earnings changes shows that preannouncements of earnings changes are systematically associated with pre-MBO earnings changes. Moreover, preannouncement declines in earnings are specific to MBOs. In the case of third-party takeovers, income did not decline in the preannouncement period. When this research design is applied to DeAngelo's (1986) sample, results consistent with earnings management are obtained. Taken together, the overall evidence favors the hypothesis that managers manipulated earnings downward prior to the MBO proposal. The potential benefit from earnings manipulation is estimated to be almost \$50 million on average for the sample firms.



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