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EVIDENCE OF EARNINGS MANAGEMENT FROM THE MEASUREMENT OF THE DEFERRED TAX ALLOWANCE ACCOUNT

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Abstract

Positive accounting literature has provided empirical evidence regarding firms' characteristics that cause their managers to make particular accounting decisions. The purpose of this study is to extend this line of research to the area of accounting for income taxes. The research is designed to identify accounting choice variables that influence managers' decisions to change the level of the deferred tax asset valuation allowance under SFAS No. 109. Specifically, the study presents an empirical examination of whether managerial discretion over the valuation allowance appears to be used for earnings management purposes. Evidence of earnings management motivations can provide insights into whether it is an appropriate accounting policy to

give management considerable discretion to choose the level of the valuation allowance.

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Notes

∗Statistically significant at the 0.10 level, one-tailed test.

∗∗Statistically significant at the 0.05 level, one-tailed test.

1. Given the nature of the leverage variable, any firm with a negative debt/equity ratio was given a debt/equity ratio of seven. In addition, the values of debt/equity ratios larger than seven were set to seven. The univariate and multivariate analyses were performed using a maximum of five, seven, and nine without a significant change in the estimated coefficients. The reported results use the maximum of seven.

2. The statistic value (z) for the skewness value is calculated as: If the calculated z value exceeds a critical value, then the assumption about the normality of the distribution is rejected. The critical value is from z distribution, based on the desired significance level [9].

Additional information

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