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Original Articles

External Auditors, Audit Committees and Earnings Management in France

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Pages 429-454 | Published online: 29 Jun 2007

⚠ https://doi.org/10.1080/09638180701391030 **66** Cite this article

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accounting conservatism is consistent with the lower litigation risk offered by the French Civil Code (vs. the US Common Law system), which is likely to eliminate the deep pockets incentive for investors.

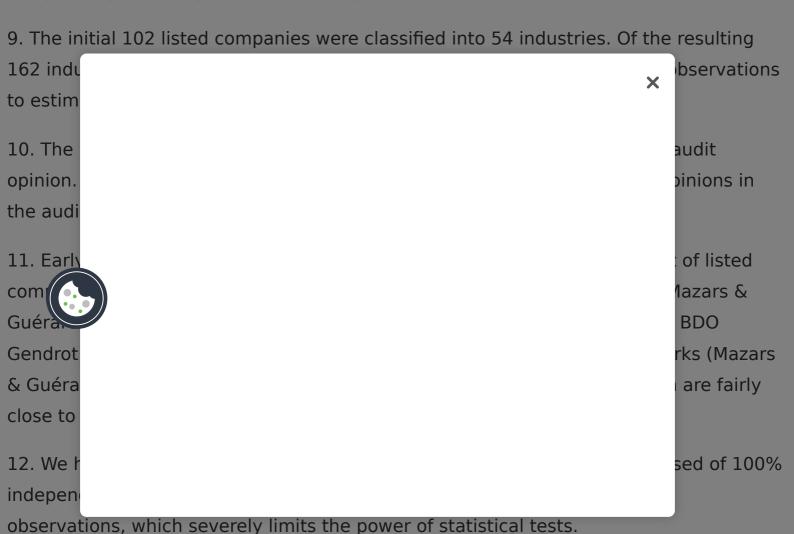
Acknowledgements

We thank the Research Alliance on the New Economy, funded by the Social Sciences and Humanities Research Council of Canada, as well as the Chair in Governance and Forensic Accounting at HEC Montreal, for their financial support. We are also grateful to workshop participants at the 28th EAA Congress in Gothenburg, the 25th Congress of the Francophone Accounting Association in Orléans, the Third International Conference on Governance and Forensic Accounting at HEC Montréal and the CERAG-Finance Group for their comments. Special thanks to C. Richard Baker, Claude Laurin and Călin Gurău for fruitful suggestions on previous drafts. Two anonymous reviewers have also contributed to the quality of this paper.

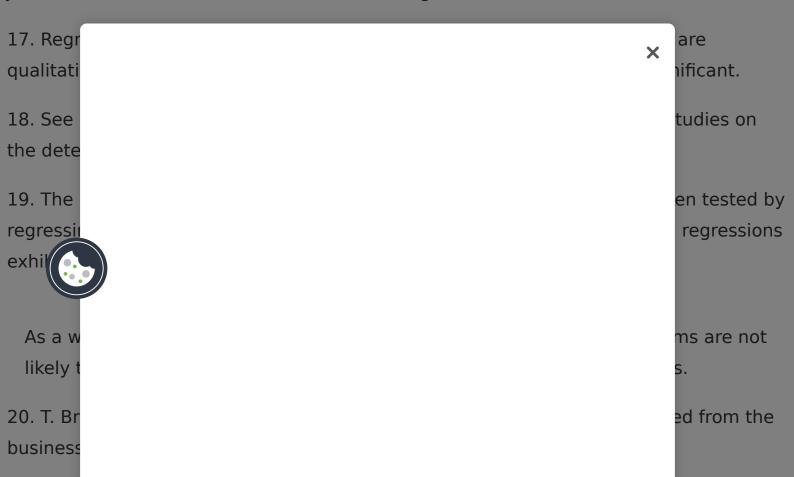
Notes

ecker et al. 1. See, f (1998),lein <u>(2002a)</u>, Kim et a 2. The e airs than in demons a strepe 3. It 1 his t can be mandate audited proved t compan 4. The fo

- 5. The methodology used for estimating abnormal accruals does not apply to financial companies.
- 6. Some authors (Peasnell et al., 2000b, Xie et al., 2003) posit that only the short-term component of accruals can actually be manipulated, and as such keep only these in their model. We prefer considering also the long-term component of accruals, because of the importance placed on provisions for risks and charges in the French accounting system. The indirect formula, based on balance sheet and income statement items, is preferred given that cash flow statements are not systematically supplied in the French Diane database at the time of our study. The items used in this formula are the ones prescribed by the French accounting format, replicated in Diane. English translations of these items are recommended by the authors so that the reader may be able to appreciate the equivalent in an Anglo-Saxon accounting system.
- 7. Long-term deferred expenses constitute amortisable entries in French financial statements; as such, they are added to the amortisable fixed assets.
- 8. If this coefficient is expected to be positive for industries where companies have a structural need for working capital, it should be negative for industries in which companies post a surplus in working capital.



- 13. The question of the shareholder linkage is not addressed in detail in the Viénot Reports of 1995 and 1999. The Bouton Report (2002, p. 10) stipulates that 'Beyond a threshold of 10% in capital or in voting rights, it is suitable that the board, based on the report of the nomination committee, should systematically inquire into the independent qualification, taking into account the capital structure of the company and the potential for conflicts of interest.' By default, all the directors who hold more than 10% of the capital or voting rights are not considered to be independent; the same applies to the representatives of other companies that pass one of these thresholds.
- 14. The results reported are potentially biased by the arbitrary dichotomy used. It is also possible that the relation between a high tenure and a loss in audit quality is not linear. Furthermore, considering only the tenure of the leading auditor inevitably causes a loss of information. In order to integrate the joint-auditorship, these tests were replicated with the average tenure of co-auditors, and the results were insignificant.
- 15. Given the strong contingency between the presence of an audit committee (AC = 1) and the presence of a committee independent in majority (ACInd50 = 1), hypotheses H3 and H4 are tested separately.
- 16. This control variable is included only when abnormal accruals are derived from the Jones Model. The control for cash flows is endogenous when the CFO Model is used.



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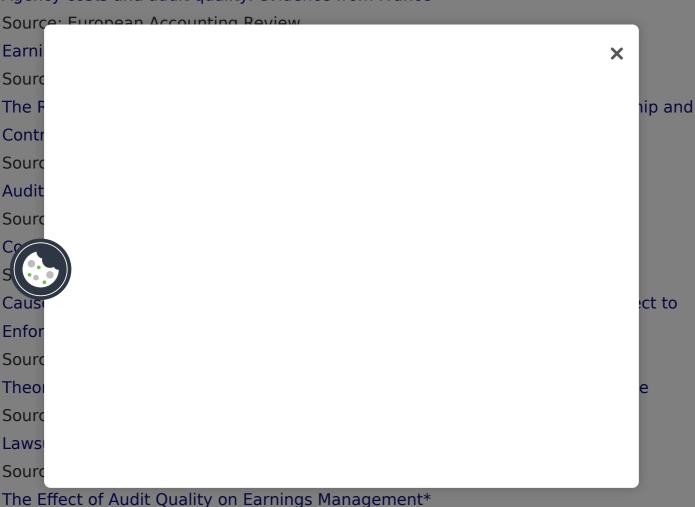
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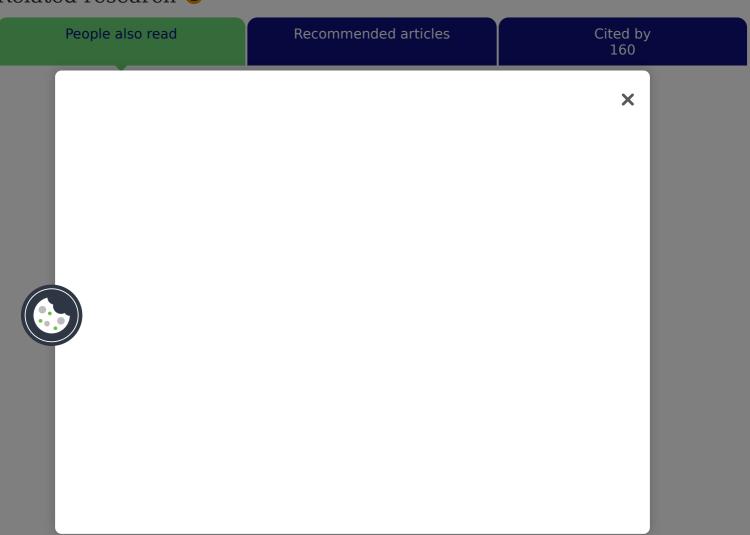
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