

## Book Review of<Equity Concentration and Earnings Management Type Selection>

Yue HAN<sup>1, a \*</sup>

<sup>1</sup>Shandong University of Finance and Economics, Shandong 250014, China

<sup>a</sup>robbot@163.com

**Abstract**—Earnings management has received considerable attention in the accounting literature, but the prior literature research results there are two opposing views from various angles, the existing literature is not able to clearly show that the relationship between ownership structure and earnings management. The monograph “Equity Concentration and Earnings Management Type Selection” by Doctor Yuan Tangmei has solved the puzzle problem “There are two opposing views in research area of equity governance affect earnings management in all cases.” This paper describes the reform train of thought, research contents and research conclusions, main innovation, academic value of the monograph. The monograph research result is inconsistent with any previous common view that equity concentration affect earnings management, but not opposite to the before view, it give a new explanation from another angle for a variety of equity concentration focus on the uncertainty of the impact of earnings management. These results of the monograph study breakthrough some of the research results of this research field, it may shed a new light on the effect of equity concentration on earnings management, and has extended meaning.

**Keywords**—book review; equity concentration; earnings management; type selection.

### I. INTRODUCTION

The issue of “equity governance and earnings management” has always been a core question of mainstream research direction of “accounting information quality and the capital market” in international accounting profession. The promotion of research position of “accounting information quality and capital market” response greatly improved for the importance of capital markets in social life recent decades, it is the embodiment of the importance of financial accounting information in capital market. These area research results also made an important contribution to the development of capital markets, to strengthen the role of the accounting information in improving market efficiency, promote digestion of investor information, and reducing investment risk. Because of this, the issue of “accounting information quality and capital market” is a hot research field in the international accounting and finance academia area.

### II. PREVIOUS CORRELATIONAL STUDIES

Although earnings management has received considerable attention in the accounting literature, but the prior literature only documents a wide variety relationship between the complexity of ownership structure and earnings management. The research results there are two opposing

views from various angles, no general recognition of the unity of the final research conclusion, and the existing literature is not able to clearly show that the relationship between ownership structure and earnings management. In November 2015, Doctor Yuan Tangmei compose<Equity Concentration and Earnings Management Type Selection> pressed by the economic science. This monograph has solved the puzzle problem “there are two opposing views in research area of equity governance affect earnings management in all cases.

### III. REFORM THOUGHT OF THE MONOGRAPH

The monograph research the issue of “equity concentration effect on earnings management type selection” from the angle of earnings management type selection, and the economic results in different choice. The monograph research result is inconsistent with any previous common view that equity concentration affect earnings management, but not opposite to the before view, it give a new explanation from another angle for a variety of equity concentration focus on the uncertainty of the impact of earnings management. The results of the study have solved the problem that “there are two opposing views in research area of equity governance effect on earnings management in all cases. At the same time, it found an important factor of influence earnings management type selection. These results of the monograph study breakthrough some of the research results of this research field, it may shed a new light on the effect of equity concentration on earnings management, and has extended meaning. Concrete research reform thought is as follows:

First, the monograph divides earnings management into efficient earnings management and opportunistic earnings management according to its economic consequences. Earnings management is mainly used for measuring the quality of accounting information, but when talk about of earnings management, the common views regard it would harm to the firms future development, damage the firms health. However, the earnings managements are not all damage the firm future value. According to prior literature, there are two views of earnings management: one view thinks that earnings management was effective, earnings management can improve earnings in formativeness in communicating private information. The other view regard as earnings management is opportunistic, management using it to reports high earnings opportunistically to maximize his or her utility (Scott, 2000).

According to prior literature, many researches find that management preference REM (Real Earnings Management) but would be trade-off of AEM (Accrual Earnings

Management) and REM when out power restrain it. Roychowdhury (2006) propose “one important issue is how managers choose between real activities manipulation versus accrual manipulation when they have the flexibility to engage in both.” There are so many researches on order selection of real and accruals based earnings management, but literature concerning factors that influence the type of earnings management selections is quite rare. Previous empirical research only examines the equity concentration effect on earnings-management magnitude, and provides contradictory and inconclusive evidence on the role of different investors. So, whether different investors equity concentration influence on the management trade-off behaviors must be a valuable issue to do more research.

#### IV. RESEARCH CONTENTS AND RESEARCH CONCLUSIONS OF THE MONOGRAPH

After that, monographs examine the relationship between earnings management and firm future profitability and market value through empirical research method by using South Korea listed companies as samples. The content of this book includes three chapters. The following are research contents and research conclusions of each chapter:

The first chapter explore the relationship between different type corporate equity concentration and accrual based earnings management in South Korea market, then, examines if accrual based earnings management caused by different type ownership concentration have different impact on the stock returns. Using a large sample of listed firms in South Korea, Our study yields four major findings. (1) Find that as the control-ownership becomes larger, controlling shareholders tend to engage more in opportunistic earnings management to hide their behaviors, and control shareholders those aggressive earnings management behaviors reduce the minority shareholders stock returns. This result suggests that controlling shareholders expropriation of minority investors but covered by earnings management. (2) With the increase of total large shareholders holdings ratio, the magnitude of discretionary accruals is greater than controlling shareholders. The result indicates that there is conspiring relationship between other big shareholders and the controlling shareholders, rather than the supervision relations. Meanwhile, those aggressive earnings management behavior reduce the minority shareholders stock returns. Other large shareholders exacerbate the expropriation of minority investors by controlling shareholders with the control-ownership wedge widens. (3) As the institutional investors holding ratio increase, the firms manager tend to engage in non-operating accrual based earnings management, but not operating accrual. under this circumstances, when the institutional investors holding shares more than a certain level, minority shareholders stock gains would not decline with the increase of the degree of earnings management, but on the contrary, it increase. This is not consistent with any prior literature, but it also does not opposite to strategic alliance hypothesis and active monitoring role on earnings management. (4) Forth, the government and foreign investor shareholder concentration do not significantly effect on accruals-based earnings management and small shareholders

stock returns. This result suggests that government and foreign investors have no supervise role on earnings management and have no protection for small shareholders in South Korea. (5) Additionally, on the other side, large shareholders, institutional investors, government and foreign investors all have no monitoring role in South Korea firms. These results suggest that an increase in the proportion of large shareholders, institutional investors, government and foreign investors to strengthen monitoring is unlikely to be effective in South Korean firms. It is worth considering to strengthening corporate governance mechanism.

The second chapter discuss if the majority shareholder affect managers on manipulating real operating activities and then effect on the shareholders stock returns. It explore the relationship between the majority shareholders concentration and real operating activities manipulation in South Korea firms, then, examines if real operating activities earnings management caused by majority shareholders have different impact on the stock returns. The empirical research results of this chapter contribute to the literature on real activities manipulation research area in several ways. (1) The evidence in this chapter suggests that firms controlled by large investors are more likely to constrain managers to do operating activity manipulation. So the company managers manipulate earnings do not through manipulating normal operating activities (Sales manipulation; Reduction of discretionary expenditures; Overproduction manipulation). But there must be other channels. (2) Second, it find evidence that large shareholders have supervisory role to normal operating activities manipulation in South Korea firms. These results suggest that an increase in the proportion of large shareholders the firm decisions will likely to be made to benefit the firm normal operation and then maintain the firm value in South Korea firms. (3) Third, in fact, the empirical research, based on perspective of the real business operation activity manipulation, have not detect large shareholders hollowed behavior form enterprise and damage to the interests of small shareholders, from this aspect, it has not found evidence to support agency theory II. The monograph research results are not consistent with agency theory II. Especially, this study provides direct and robust evidence to support a negative association of corporate ownership concentration with real operating activity manipulation.

The third part discuss if the institutional investors effect on type of earnings management selected. It is to investigate whether institutional investors conduct efficient or opportunistic earnings management to the companies, using multiple regressions and large sample, this chapter finds evidence that institutional investors have significant influence on the type of earnings management selected in South Korea market. This part first examines that DAC has positive and significant related to the firms future profitability and firm's market value after controlling of the effect of REM, on the contrast, mostly REM (abn CFO, abn DEXP) have negative and significant related to the firms future profitability and firm's value, only the association between abn PROD and firms future profitability are not significant. Second, it explores the association between institutional investors and different types of EM. We find that as the institutional

investors holding ratio increase, the firms tend to engage in effective earnings management (AEM), and restrain the aggressive earnings management (-abn CFO). Third, it test the DAC caused by institutional investors concentration effect on the firms future market value and next year stock returns, the result show that earnings management incited by institutional investors is positive related with both future market value and next year stock returns when institutional investors concentrate more than a certain level(such as: INST>40%) . Those evidences indicate that institutional investor effect on type of earnings management selection. Institutional investor affect managers conduct effective earnings management (DAC) and constrain opportunistic earnings management (-abn CFO), then, benefit firms health development and stock holders returns. This evidence is inconsistent with any previous common view that institutional investors active monitoring or strategic alliance. So, the institutional investors are probably a protector to minority shareholders. Developing institutional investors may be a good way to safeguard minority interest. This may shed a new light on the effect of institutional investors on earnings management research area.

#### V. MAIN INNOVATION OF THE MONOGRAPH

The main innovation points of the monograph can be summarized as the following two points:(1) Break through the original literature simple research logic of just to verify the relationship between ownership concentration and earnings management, the monograph focus on earnings management type selection for various circumstances equity concentration based on depth theoretical analysis.(2) The monograph has solved the puzzle problem “there are two opposing views in research area of “equity governance affect earnings management” in any cases.

#### VI. ACADEMIC VALUE OF THE MONOGRAPH

The research Angle of this work expanded the scope and research train of thought of the field. It breaks through the limitations of research on the relationship between equity concentration and surplus management. The monograph research result is inconsistent with any previous common view that equity concentration affect earnings management, but not opposite to the before view, it give a new explanation from another angle for a variety of equity concentration focus on the uncertainty of the impact of earnings management. The results of the study have solved the problem that “there are two opposing views in research area of equity governance effect on earnings management in all cases. At the same time, it found an important factor of influence earnings management type selection. These results of the monograph study breakthrough some of the research results of this research field, it may shed a new light on the effect of equity concentration on earnings management, and has extended meaning. It further advances this research direction.

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