Washington University in St. Louis
OLIN BUSINESS SCHOOL

ACCOUNTING RESEARCH CONFERENCE

2017 Schedule

Thursday, November 9, 2017

12:00 p.m. Lunch, Charles F. Knight Executive Education Center, Anheuser Busch Dining Room, 3rd floor.

1:00 Welcome to Olin, **Mark Taylor**, *Dean, John M. Olin School of Business*, Bauer Hall, Room 210.

1:15 "Changes in Lending Practices and Borrower Reporting Quality: Evidence from Chinese State Bank Privatizations" Presented by **Sugata Roychowdhury**, *Boston College*.

Discussion led by **Allison Nicoletti**, *University of Pennsylvania*.

Abstract: "How do developments at lending institutions that alter the way they grant and monitor loans influence their borowers' financial reporting quality (FRQ)? We examine this question by investigating the influence of Chinese stated owned bank (CSB) privatization on the quality of their borrowers' financial statements. Using a difference-in-difference research design which compares changes in CSBs that issued initial public offerings (IPOs) to those that did not, we find that bank-lending terms, including loan maturity, guarantee requirement, and interest rate became more sensitive to borrower return on assets (ROA) after a bank IPO. More importantly, we find that pursuant to the IPOs by their lending banks, various measures of borrowers' FRQ improve banks. Further analysis reveals that the imporvements in borrower FRQ are more pronounced for those IPO-issuing banks that exhibit a decline in political connections and those that experience an increase in board financial expertise. These results suggest that post-privatization, 1) CBSs increased their reliance on borrowers' operating performance for setting loan terms; 2) this increased reliance contributed to an improvement in the quality of the financial statements that provide the performance measures. Our results are robust to controlling for confounding factors in the cross section and in the time series."

2:25 Break

2:40 "How Well do Machines Mimic Readers?" Presented by **Jared Jennings**, *Washington University*.

Discussion led by **Salman Arif**, *University of Pennsylvania*.

Abstract: We examine whether support vector regressions (SVR), supervised LDA (sLDA), random forest regression trees (RF), and 'tone' extract narrative content from conference calls that correlates with what a human reader would identify. We find that each narrative-content measure (along with a composite measure) explains a portion of analyst-forecast revisions for quarter q+1 issued after the conference call in quarter q. Correlation with analyst-forecast revisions improves when the composite measure adapts to context (positive/negative returns; high variance/low variance) and ignores sparse words. The correlation is comparable and incremental to that of financial signals (cash-flow changes, earning surprises, and management forecasts), suggesting that the narrative content of conference calls as extracted by readers is economically significant. Our results suggest that models of narrative content

have reasonable construct validity and that this validity is likely to be improved by further thought on the unique characteristics of text.

3:50 Break

4:05 "Accounting Versus Prudential Regulations," Presented by **Jeremy Bertomeu**, *University of California, San Diego*.

Discussion led by **Henry Friedman**, *University of California, Los Angeles*.

Abstract: We develop a framework to study how accounting measurement and prudential regulation interact to affect a bank's incentives to originate credit. Our main result is that the accounting measurement system and bank leverage are policy tools that should be used in tandem, generating more value than systems that rely either on accounting regulation or on prudential regulation. An important application of our analysis is on the current debate on the appropriate loan loss provisioning model. We show that while banks engage in excessive risk-taking under an incurred loss model, an expected loss model can lead to excessive liquidations. More interestingly, we show that as credit conditions in the economy improve, the optimal measurement system moves towards an expected loss model. Conversely, as credit conditions deteriorate, the optimal measurement regime tilts more towards an incurred loss model.

5:30 Ph.D. Poster Session and cocktails, Whittemore House.

6:30 Dinner, Whittemore House.

<u>Friday, November 10, 2017</u>

7:30 a.m. Continental Breakfast, Bauer Hall, Room 210.

8:00 "Regulatory Spillovers in Common Audit Markets," Presented by **Michael Minnis**, *University of Chicago*.

Discussion led by **Nathan Marshall**, *University of Colorado, Boulder*

Abstract: We find that Sarbanes-Oxley (SOX) had large, persistent effects on how nonpublic entities access the audit market. Private companies reduced their use of attested financial reports in bank financing by 12%. For nonprofit organizations (NPOs), audit fee increases and the rate of switching to smaller audit firms more than doubled. We trace these effects to a shortage of audit labor by studying exogenous variation in audit labor availability across otherwise similar clients. Moreover, we find the audit supply structure changed. Both the audit supply concentration and Big 4 market share of the nonpublic market dropped in half. These changes in supply structure are persistent through 2014. Our results demonstrate how public company regulation causes spillovers for nonpublic entities and identifies significant consequences of regulations that expand beyond audit and disclosure requirements for public firms.

9:10 Break

9:25 "Discretion in Forecast Exclusions: Accuracy Enhancing and Opportunism," Presented by Xiumin Martin, *Washington University*.

Discussion led by **Andy Call**, *Arizona State University*.

Abstract: The earnings consensus forecasts provided by Thomson Reuters I/B/E/S, commonly referred to as "Wall Street Estimates," have been widely used by investors and researchers as market expectation of earnings. We examine I/B/E/S' discretionary decision to exclude forecasts from the consensus to understand the economic forces that shape this process. We find that on average exclusions improve I/B/E/S consensus accuracy. The probability of exclusions increases with both analyst EPS forecast errors and forecast optimism after controlling for both the accounting basis and timeliness of the forecast. These potitive relationships are robust to instrumenting EPS forecast accuracy and optimism by the corresponding analysists' reveue forecast accuracy and optimism. In addition, the positive association of exclusion likelihood with forecast optimism becomes stronger when firm managers have higher incentives to meet or beat consensus earnings benchmark (hereafter MB) and when firm information assymmetry is higher. Furthermore, investors respond to consensus revisions resulting for forecast exclusions and these reactions do no reverse subsequently. Lastly, at earnings announcements investors react to earnings surprises benchmarked against the I/B/E/S consensus but not excluded forecasts. Collectively, the evidence is consistent with a model in which I/B/E/S exercises discretion to remove inaccurate forecasts based on private information received from managers, which improves price efficiency on one hand, and on the other hand this discretion also yields opportunity for managers to improve their ability to meet or beat the street consensus by persuading I/B/E/S to remove optimistic forecasts.

10:35 Break

10:50 "Does Auditor Regulatory Oversight Affect Corporate Financing and Investment Decisions?" Presented by **Nemit Shroff,** *MIT*.

Discussion led by **Carlo Maria Gallimberti**, *Boston College*.

Abstract: This paper examines the real effects of auditor regulatory oversight on companies' financing and investing policies. Using the Public Company Accounting Oversight Board's (PCAOBs) international inspection program as a setting to generate within-country variation in auditor oversight, I find that companies respond to the increase in auditor oversight by issuing additional external capital amounting to 0.5% of assets and increasing capital expenditures by 0.3% of assets. These effects are larger for financially constrained companies and weaker for companies whose auditors' are criticized by the PCAOB for having deficient engagement practices. This paper documents the importance of auditor oversight in mitigating external financing frictions.

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