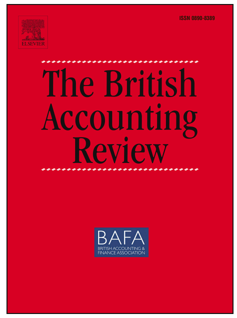
Accepted Manuscript



Earnings management in firms seeking to be acquired*

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PII: S0890-8389(14)00055-9

DOI: 10.1016/j.bar.2014.07.001

Reference: YBARE 669

To appear in: *The British Accounting Review*

Received Date: 9 October 2013

Revised Date: 10 May 2014

Accepted Date: 16 July 2014

Earnings management in firms seeking to be acquired[*]

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The British Accounting Review, forthcoming

Abstract

Empirical evidence regarding accrual-based earnings management around mergers and acquisitions has been setting-specific as far as target firms are concerned. This might be due to the fact that target firms cannot always anticipate an acquisition proposal, and thus lack the motive and the time necessary to manage their earnings in order to facilitate or impede the deal. In this paper, we provide clear evidence of downward earnings management by a sample of target firms that have both time and motive to engage in such actions. These are firms that publicly announce their intention to be acquired. Publicly 'seeking a buyer' represents a rather unusual corporate event, and we find that these firms engage in downward earnings management in the years surrounding the 'announcement year'. To some extent, this result is explained by overrepresentation of low performance and growth among these firms, and it can be interpreted under alternative explanations. Furthermore, we show that such downward earnings management negatively affects the probability for a 'seeking buyer' firm to secure an acquisition within a reasonable amount of time, a possible indication of efficient diligence by prospective buyers having a preference for firms 'seeking buyer' with no informationally obscure earnings.

JEL classification: M41, G34

Keywords: acquisition targets, takeovers, earnings management, income manipulation

[*] We are grateful to Professor Betty J. Simkins (Associate Editor), Professors Nathan L. Joseph and Alan Lowe (Joint Editors) and an anonymous reviewer for their helpful comments and suggestions. We are also grateful to Andrew Vivian and Yongtae Kim that have acted as discussants of the paper on separate occasions. The paper has benefited from the comments of participants of the European Financial Management Association (EFMA) annual conference, held in Reading, UK, 2013, the 35th annual congress of the European Accounting Association (EAA), held in Ljubljana, Slovenia, 2012, and the 18th annual meeting of the Multinational Finance Society (MFS), held in Rome, Italy, 2011. Any errors are the authors' sole responsibility.

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