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FIFTEENTH ANNUAL CONFERENCE WONDERS WHERE WERE THE PROFESSIONAL ACCOUNTANTS

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The CGA-ARC is located in Desmarais Building Room 7102.

News accounts over the past few years have recited tales of fraud, greed, misappropriation, negligence, deceptive accounting practices, broken internal control systems, theft and dishonesty at all levels of public organizations and in all sizes of business organizations. This Accounting Research Centre examined these issues at its twelfth annual conference. In this it's fifteenth and current conference the focus was aimed specifically at the accounting community, the accountants, auditors both internal and external, and the financial managers. These people seem to have been unable or unwilling to protect organizations and investors either by detecting or preventing undesirable behavior. This formed the theme for this conference.

The conference was held at the NAC on 20 October, 2006. Again, and some participants remarked on this, the conference played to a full house, with a topic of both concern and interest to accounting professionals, and with a panel of guest speakers who were recognized and international experts in their chosen fields.

The speakers were: Charles-Antoine St-Jean, Comptroller General of Canada; Vijay Jog, President, Corporate Renaissance Group; Mark Beasley, Professor, North Carolina State University; Gordon Thiessen, Chair, Canadian Public Accountability Board; and Irene Gordon, Professor, Simon Fraser University.

Joyce Evans, Chair of the Board of CGA Ontario welcomed the speakers and audience to the Conference. She had words of praise for Daniel Zeghal, Executive Director of the Centre and for the continued successes of the Centre.

While Professor Merridee Bujaki of the University of Ottawa again acted as moderator, she departed from that role a bit to introduce a study that had been conducted at her university. The study involved the survey of accounting professionals to see how they perceived the effectiveness of control systems. Those surveyed felt that the related monitoring

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Speakers and guest at the CGA-Accounting Research Centre conference: (left to right) Paul Faulkner, member of CGA-ARC's advisory council; Joyce Evans, chair ,CGA Ontario; Vijay Jog, President of Corporate Renaissance Group; Merridee Bujaki, Professor, University of Ottawa; Gordon Thiessen, chair, Canadian Public Accountability Board; Irene Gordon, Professor, Simon Fraser University; Mark Beasley, Professor, North Carolina State University and Daniel Zeghal, Professor, Executive Director CGA-ARC, University of Ottawa.



Distinguished speaker at the conference: (left to right) Gordon Thiessen, chair, Canadian Public Accountability Board; Irene Gordon, Professor, Simon Fraser University; Mark Beasley, Professor, North Carolina State University and Charles-Antoine St-Jean, Comptroller General of Canada.

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systems were most important to ensuring the effectiveness of the control system. This effectiveness could also be enhanced by training the participants better.

The keynote speaker for the conference was Charles-Antoine St-Jean. While he recognized that society has changed and that some things are acceptable now that were not in the past, he still feels that the concerns expressed in the topic of this conference are still important and valid. The concerns are as valid in the public sector as well as the private. Governments too have their problems with cheating and fraud. Hefty cost overruns and the sponsorship scandal are testimony enough to these problems. Some of the excuses used to try to explain why some of these things go undetected for so long range from "it's none of my business," or "I'm too busy" to "I'll use some creative accounting to get around it." Clearly, some changes are needed. These changes include: a clearer definition of the roles and responsibilities for all of those involved in the use of public funds; and a better definition of the role of the Senior Financial Officers. As needed as these are, these changes cannot guarantee that errors will not take place and this just makes the role of the audit function even more important.

The public visibility of the various corporate scandals cannot help but have an impact on capital markets. This was the theme of the presentation made by Vijay Jog. Certainly, investors want an information efficient market which means that they want to be able to trust the information provided in corporate reports and financial statements. Illegal and/or unethical behaviour by corporate executives or senior financial officers can seriously impair the value of these corporate utterances. However, the speaker was quick to point out that despite these shortcomings the corporate statements can still provide clues as to possible illegal behaviour. Among the clues that he mentioned were: the behaviour of affiliates might give evidence of early revenue recognition; a growth in income not matched by a growth in assets; the behaviour of ratios such as the debt/equity one might provide evidence of improper accounting; and finally the behaviour of senior corporate executives might provide hints of improper or illegal activities. Some solutions to these kinds of activities were provided. While not everything can be legislated, certainly there can be a strengthening of the rules covering corporate governance. Also, the role and responsibilities

of corporate boards need to be strengthened and better defined as well as the improvement of the independence and frequency of audit. Trust is needed to make these improvements effective.

Mark Beasley also called for an improvement in corporate governance and in his presentation this improvement involved, among other things, the adoption of Enterprise Risk Management (ERM). (Readers of this Newsletter may recall that the topic of the ARC's last years' conference was ERM). The speaker stated that in order to provide an integrated and disciplined approach to the risks related to scandals and frauds Enterprise Risk Management was needed. Otherwise, without a clear definition and assessment of the risks, they will simply multiply. They will go unheeded because no one in the organization is responsible. While there may indeed be a host of management and financial controls, there is always the risk that they may be overridden. Indeed some 83% of corporate frauds have involved such control overrides by CEOs or CFOs. One counter-measure that can be effectively employed against this sort of risk is a program of ERM. Some of the components of ERM that help to combat fraudulent or illegal activities include an assessment of the risks of fraud. This activity involves more than just the auditors. It is a continuous process and includes a systematic review of corporate controls. In 2006, the Committee of Sponsoring Organizations of the Treadway Commission (COSO) issued a guide on the internal controls over financial reporting.

In this next presentation the point was made again that financial markets depend on good and trust worthy financial statements. Investors require reliable information to operate effectively. Because of the frauds and thefts of the past several years there has grown a lack of credibility in published financial reports. Some of the blame has fallen on the external auditors. They are not, it seems, ensuring the desired level of credibility. To counter this problem both the United States and Canada have created oversight agencies. In Canada, the Canadian Public Accountability Board was set up in 2003. Its chair, Gordon Thiessen, gave this presentation and described the role of the Board as; overseeing the external audit function, ensuring the enforcement of independence standards, and reviewing the quality of audit work. In the speaker's opinion the results of the Board's efforts have been very positive. A third round of evaluations of larger accounting firms has been completed. Early problems were discovered, many resulting from simply carelessness. However, substantial improvements have been made. Self-regulation proved not to be enough. It took the efforts of the Board's evaluations to result in the needed improvements, thereby reducing the probability of undetected fraud or error.

Irene Gordon wonders whether, given the propensity for corporate cheating, fraud and theft, accounting education is part of the problem or part of the solution. It seems that almost everyone is cheating. Apparently, some MBA students (our future executives) cheat. In Canada, 56% of MBA students acknowledge that they have cheated at one time or another. To try to see if accounting education and literature did anything to discourage immoral or unethical behaviour, she decided to do a study. She reviewed accounting textbooks and focused her attention to the following particular areas; ethics, professional judgement, social responsibility, governance and fraudulent activities. While admitting that her study might lack some of the scientific approach, it was conclusive enough to tell her that the books contained little reference to the above topics. Post-ENRON, the topics got a little more attention, but still not much. Students are not much exposed to these topics. To her, this is regrettable.

It was interesting that a number of the speakers felt that accounting standards needed to be stricter and subject to more discipline. Yet during the question period following the presentations, it was noted that standards were in fact becoming looser and the increasing popularity of fair value accounting was one prime example of this.

SAMPLE OF PUBLICATIONS

"Financial Reporting of Small Business Entities in Canada" by Michael Maingot and Daniel Zeghal, *Journal of Small Business Management*, 44(4), pp. 513-530, 2006.

"Board Structure and Firm Technical Efficiency: Evidence from Canadian State-Owned Enterprises" by R.Bozec et M.Dia, *European Journal of Operational Research*, 177 (3): 1734-1750, 2007

"La gestion des résultats comptables lors des prises de contrôle : Une analyse dans le contexte Suisse." by Missonier-Piera, F., and W. Ben Amar., *Comptabilité Contrôle Audit*, accepted, 2007

"A study of earnings-management motives in the Anglo-American and Euro-Continental Accounting models: The Canadian and French Cases" by H. Ben Othman and D. Zeghal, *The International Journal of Accounting*, 41(4), pp.406-435, 2006.

"Use of Earning Information for Stock Pricing in Different Market Cycles: The Effect of Discretionary Accruals" by A. Daneshfar and D. Zeghal, *Journal of Business & Economics Research*, accepted.

"Enterprise Risk Management: Rethinking risk in the 21st Century" Proceedings of the 14th Annual Conference, by D. Zeghal and K. Lajili Editors, 119 pp., 2006.

"The Ownership-Efficiency Relationship and the Measurement Selection Bias", by R.Bozec, M. Dia, and G. Breton, *Accounting and Finance*, 46 (5): 733-754, 2006

"Effet de la structure des droits de vote sur la qualité des mécanismes internes de gouvernance : Cas des entreprises canadiennes" by Ameur Boujenoui and Daniel Zeghal, *Canadian Journal of Administrative Sciences*, 23(3), pp. 183-201, 2006.

"Separation of Ownership from Control and Acquiring Firm Performance: The Case of Family Ownership in Canada" by W.Ben Amar and P. André, *Journal of Business Finance and Accounting*, 33 (3&4), 517-543, 2006

"An Analysis of the Factor Affecting the Adoption of International Accounting Standards by Developing Countries" by K. Mhedhbi and D. Zeghal, *The International Journal of Accounting*, 41, pp. 373-386, 2006.

"Revisiting Agency and Transaction Costs Theory Predictions on Vertical Financial Ownership and Contracting: Electronic Integration as an Organizational Form Choice" by K. Lajili and J. Mahoney, *Managerial and Decision Economics*, Vol. 27, pp. 573-586, 2006.

RESEARCH ABSTRACTS

1. "A Study of Earnings Management Motion in the Anglo-American and Euro-Continental Accounting Models: The Canadian and French Cases" by D. Zeghal and H. Ben Othman.

The purpose of this study is to investigate factors which potentially influence earnings management policy with reference to the Anglo-American and Euro-Continental accounting models. Canada and France, respectively, belong to those different socio-economic environments. Earnings management practices detected in those two countries are expected to be affected by the specific socio-economic features of the two environments. Earnings management practices are explained by incentives provided in the literature to



Keynote speaker Charles-Antoine St-Jean, Comptroller General of Canada.

reveal which motives are prominent within each environment. Earnings management motives were tested using appropriate panel techniques. Over 1674 Canadian and 1470 French firm-year observations were used.

The results provide evidence that incentives for earnings management for French firms are specifically linked to contractual debt costs and effective tax rate. However, Canadian firms show specific incentives matched with a dynamic capital market. Issuing equity is a strong motive for earnings management in Canadian firms.

2. "Board Structure and Firm technical Efficiency: Evidence from Canadian State-Owned enterprises" by R. Bozec and M.Dia.

The objective of the study is to analyze the board-performance relationship for a group of 14 Canadian SOEs. This context is unique because SOEs do not have major control devices other than the board. As the interaction effect, if any, between the board and other corporate governance structures is expected to be low, we do not have to fully control for the potential impact of different control devices, or to disentangle them completely from influencing board composition. The performance is also measured using data envelopment analysis (DEA), a linear programming method used for the first time in this research area. As such, this study contributes to the operational research literature while applying DEA method to untraditional fields of research.

The results from the multivariate analysis suggest that board size and board independence are positively related to firm technical efficiency only when SOEs are exposed to market discipline. In other words, product market competition is a precondition for boards to be effective.

3. "The Factors Affecting the Adoption of International Accounting Standards by Developing Countries" by D. Zeghal and K. Mhedhbi.

The purpose of this study is to identify the factors that could explain the adoption of international accounting standards by developing

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countries. The following factors were selected: economic growth, education level, the degree of external economic openness, cultural membership in a group of countries, and the existence of a capital market.

The results of the study indicate that developing countries with the highest literacy rates, that have capital markets, and that have an Anglo-American culture are the most likely to adopt international accounting standards.

4. "Separation of Ownership from Control and acquiring Firm performance: The Case of Family Ownership in Canada" by W.Ben Amar and P. André.

This study investigates the relationship between ownership structure and acquiring firm performance. A large proportion of Canadian public companies have controlling shareholders (families) that often exercise control over voting rights while holding a small fraction of the cash flow rights. This is achieved through the concurrent use of dual class voting shares and stock pyramids. Many suggest that these ownership structures involve larger agency costs than those imposed by dispersed ownership structures and that they distort corporate decisions with respect to investment choices such as acquisitions. We find that average acquiring firm announcement period abnormal returns for our sample of 327 Canadian transactions are positive over the 1998-2002 period. Cash deals, acquisitions of unlisted targets and cross border deals have a positive impact on value creation. Governance mechanisms (outside block holders, unrelated directors and small board size) also have a positive influence on the acquiring firm performance. Further, the positive abnormal returns are greater for family firms. We do not find that separation of ownership and control has a negative impact on performance. These results suggest that, contrary to other jurisdictions offering poor minority shareholder protection or poor corporate governance, separation of control and ownership is not viewed as leading to value destroying mergers and acquisitions, i.e., market participants do not perceive families as using M&A to obtain private benefits at the expense of minority shareholders. We do find a non monotonic relationship between ownership level and acquiring firm abnormal returns. Ownership of a majority of the cash flow rights has a negative impact on announcement returns. This is consistent with the view that large shareholders may undertake less risky projects as their wealth invested in the firm increases.

5. "Revisiting agency and transaction costs theory predictions on vertical financial ownership and contracting: electronic integration as an organizational form choice" by K.Lajili and J.Mahoney.

This paper provides an organizational economics foundation to guide managers in matching the comparatively more efficient organizational mode with transactional characteristics such as: (1) the degree of (human capital) asset specificity involved in the transaction, (2) the degree of uncertainty surrounding the transaction, and (3) the number of trading partners (suppliers and buyers) in the vertical supply chain. The key role of technology, and more specifically the e-business infrastructure and its effects on organizational mode choice, is highlighted. The main results from this analysis suggest that changes in information technology are changing the nature of transaction costs leading to more efficient management through an electronic integration solution thus favoring contracting and outsourcing than would have been technologically possible when Williamson's Markets and Hierarchies (Markets and Hierarchies: Analysis and Antitrust Implications. Free Press: New York, 1975) was published. It is emphasized that the transaction cost economics principles are durable but that the breathless advances in information technology, especially in the past decade, have comparatively favored lower transaction costs of markets over hierarchies.



Once again the annual CGA-ARC conference boasted a capacity crowd of more than 250 executives, professional accountants and academics.

DISTINGUISHED SPEAKER SERIES

The Accounting Research Centre sponsored the following presentations by distinguished speakers:

- "The Use of Signs with Management Accounting" by Gary Spraakman, Professor of Accounting, York University.
- "Erroneous Accounting and the efficiency of Industry Investment" by Artyom Durnev, Professor of Finance, McGill University.
- "Analyst Forecast Accuracy on GAAP vs. Non-GAAP Financial Measures; Case of real Estate Investment Trusts" by Steve Fortin, professor, McGill University

OTHER NEWS

The Executive Director of the Accounting Research Centre, Dr. Daniel Zeghal, has been honoured by a number of appointments:

- He has been appointed as a member of the editorial board to the [Journal of Accounting & Business Research](#);
- He is now a member of the CGA-Canada Research Board Committee; and
- For the next three years, he will serve as Associate Editor to [Accounting Perspectives](#).

FOR MORE INFORMATION

To learn more about the CGA-ARC visit our web site at the following address: www.cga-arc.uottawa.ca

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