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## DETECTING EARNINGS MANAGEMENT: A TOOL FOR PRACTITIONERS AND REGULATORS

Corporate managers are expected to operate the company in the best interests of the shareholders. This expectation includes a focus on short-term value, using current market price as proxy for shareholders' wealth. This focus is often accomplished through earnings management activities. When this activity becomes aggressive, it changes the readers' perception of the story being told by financial statements. The study of earnings management, and methods to detect such, assist stockholders in analyzing corporate financial transparency.

Academic researchers usually wish to make general statements about earnings management from examining large samples of firms. A fundamental gap exists between the interests of academic researchers and non-academics (practitioners and regulators) whereby generalized statements made by academics do not assist non-academics in testing for the possibility of earnings management on a firm-by-firm basis. The prior research models are not hereby rejected or refuted. They are simply of no practical, useful benefit to non-academics since they have not been tested on a firm-by-firm basis.

Descriptive statistics using Microsoft Excel 2003, binary logistic regression using Small Stata version 8.0, and stepwise regression using SPSS version 15.0 were used in this study. Increase in the standard deviations from prior years to restatement year observations for the Miller Ratio and Modified Jones Model indicated volatility, suggesting possible earnings management. Binary logistic regression indicated neither the Miller Ratio, nor the Modified Jones Model, were effective in detecting the possibility of earnings management. Stepwise regression analysis indicated the Miller Ratio had some validity when regressed against leverage, growth, auditor quality, and

change in stock price. Stepwise regression determined the Modified Jones Model was not influenced by economic factors studied.

This study contributes to earnings management literature by moving research in the direction of utilizing acknowledged earnings management data in studying a new model. The Miller Ratio had been found to have some validity, indicating issues for further study. This validity was supported by the lack of correlation of the Miller Ratio and Modified Jones Model. The implication of this study is the development of a potentially useful tool for non-academics to use on a case-by-case basis to detect the possibility of earnings management.