Financial Disclosure: A closer look

Abstract

The central concern of this paper is the company's financial disclosure process. We briefly discuss this phenomenon. Furthermore, the research in this area is surveyed and discussed. Most of the research so far has been quantitative. Some early studies are discussed including their validity and their shortcomings. During the 90's some researchers started to investigate the financial disclosure process qualitatively. Some of this research, which may be complementary to the quantitative research, is identified and discussed in greater detail. The paper concludes with a discussion of how prospective research can contribute favourably to the understanding of this interesting but complex process.

1. Introduction

Management's policy regarding income measurement and disclosure is a popular research topic. Generally accepted accounting principles allow management wide latitude in the choice of accounting policies. Given adopted accounting principles, management faces discretionary accounting decisions, which are heavily oriented to a judgement process of determining amounts, rates, and timing. This situation enables management to greatly influence the figures disclosed.

In the recent literature and in practice, the generators of financial statements have been accused of income smoothing or, in a broader sense, earnings management. Earnings management is defined as the propensity to use the latitude in accounting principles and management's discretion to make sure the financial statements reflect the company's financial position in a way management sees fit. Such accusations however are not based upon a thorough investigation of the disclosure proces.

In our view, discretion in particular, is recognized in the translation of the management accounts (internal accounts) to the financial accounts (annual report). This translation process is influenced by several actors: generators of financial statements, users of financial statements, and the auditors.

Insight into the determinants of the disclosure process will contribute to an understanding of why financial statements take their current form and to the decision making capability of the aforementioned actors.

The central question is : Why do financial statements take their current form ? Related questions are:

* Who in the organization makes particular disclosure decisions?
* What determines the locus of this disclosure responsibility?
* What issues are considered when making disclosure decisions?
* What is the auditor's role in the disclosure process?
* What is the role of other external parties in the disclosure process?
* What is the impact of external disclosure rules on disclosure decisions?

We operationalize the disclosure process as the translation of the management accounts (internal accounts) to the financial accounts (annual report). The presumed relationships are presented in the following preliminary conceptual model:

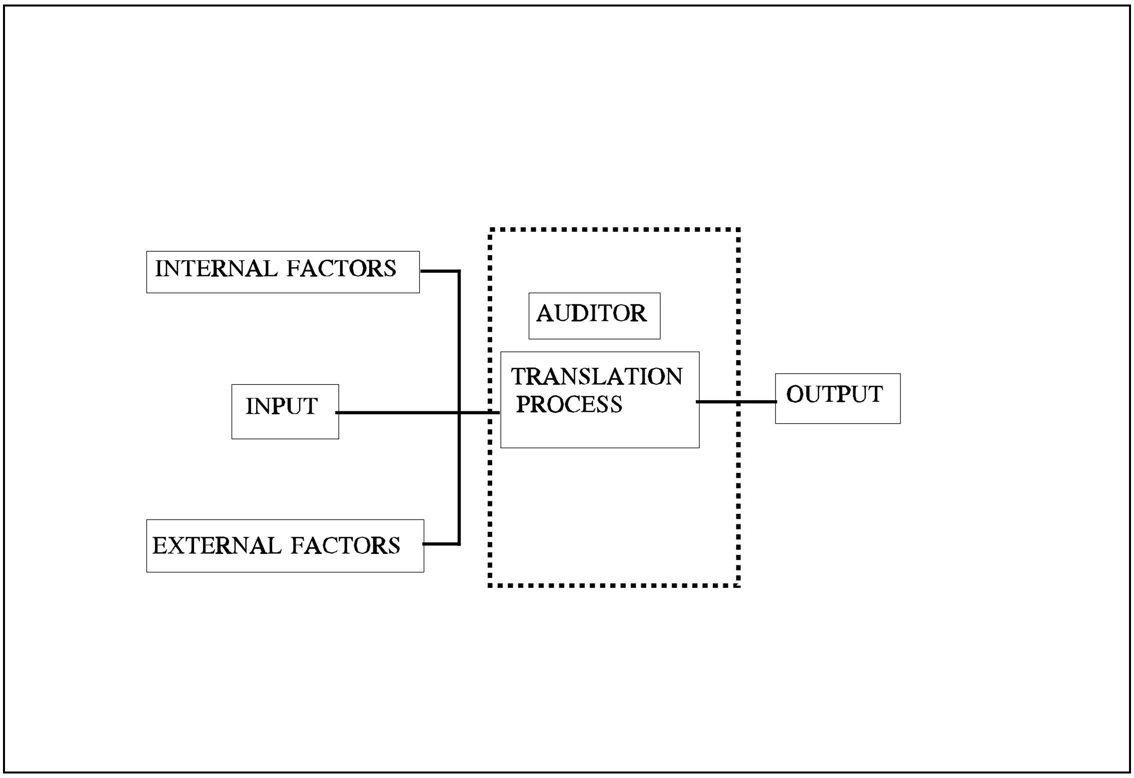

Figure 1

Internal factors:

-content of management accounts (trial balance)

-the company's disclosure culture
-management's attitude regarding disclosure
-disclosure issue and impact on figures
-expectations aroused by management
-habits in the industry
-assumed impact on users

External factors:

-the users' expectations
-involvement of the auditor and other external advisors

-accounting legislation and regulation
-existence and influence of pressure groups
-contracts and agreements

This listing may not be "all inclusive".

In the recent literature four methods to investigate earnings management have been distinguished. We feel this distinction between research methods can also be used for research on the broader issue of a firm's disclosure process:

1) Research which tries to explain management's propensity and behaviour by means of the results of this behaviour in the reported annual accounts.

2) Research which tries to explain management's behaviour by imitating it in a controlled laboratory experiment situation.

3) Research in which the auditor or other external advisors are interviewed.

4) Research which tries to explain management's propensity and behaviour by means of interviews and questionnaires.

So far, most researchers have used only the first method. With this method, only the suspect of the behaviour can be derived. As mentioned above, this research has not given sufficient insight into the firm's accounting policy decisions. This was already confirmed in 1983 by Holthausen and Leftwich who stated: "Further progress depends on innovation in theory and empirical tests rather than continued application of the current state of art."

Before reviewing research into the company's disclosure section 2 will discuss the earnings management phenomenon in greater detail.

2. EARNINGS MANAGEMENT

2.1 Introduction

We defined earnings management as the propensity to use the latitude in accounting principles and the discretion management has to make sure the financial statements reflect the company's financial position in a way management sees fit. Income smoothing, the most well known form of earnings management, can be defined as the effort to reduce fluctuations in reported earnings.

2.2 Income smoothing techniques

In this section, we will discuss the different ways management can smooth the reported income of their firm. For this purpose, a difference should be made between:

1) smoothing through real transactions (’real smoothing’)
2) smoothing through the recording of transactions (’accounting smoothing’)
3) smoothing through allocation over time (’intertemporal smoothing’)
4) smoothing through classification (’classificatory smoothing’).

	real smoothing	accounting smoothing
intertemporal smoothing	A	B
classificatory smoothing	C	D

Figure 2

Figure 2 indicates that both real smoothing and accounting smoothing can be intertemporal or classificatory. There are numerous examples of intertemporal real smoothing (A);

- -starting a Research and Development project or a large advertising campaign.
- -early or late disposal of machines to generate additional profit or loss.
- -advancing or delaying a sales transaction.

Intertemporal accounting smoothing (B) will dampen the fluctuations of reported profit through the choice and/or change of the applied accounting rules. For example;

- -stock valuation (FIFO, LIFO, actual costs).
- -depreciation method (straight line, double declining balance method).
- -capitalization or expensing research and development costs.
- -changing assumptions underlying the calculation of a provision.

When income variables other than net income (net of all revenues and expenses) are the object of smoothing, management can classify intra-income statement items in such a way that variations over time in those variables are reduced.
Nonrecurring revenues and expenses could be classified as ordinary or extra-ordinary to present a smoother appearance of the reported stream of ordinary income (classificatory accounting smoothing D).
In general, real smoothing has an intertemporal character. However, an example of classificatory real smoothing (C) is the sale of a subsidiary, which generates an extraordinary item instead of an operating item (earnings from subsidiaries).

A condition for accounting smoothing is, of course, that management's choice is in accordance with generally accepted accounting principles.

In previous studies of profit-smoothing practices the following classification of income smoothing also was recognized;

- Natural smoothing where the profit-generating process inherently produces a smooth stream of income.
- Real smoothing where management takes action to control underlying economic events directly effecting future profits.
- Artificial smoothing which represents accounting manipulations undertaken by management to smooth income.

2.3. Income smoothing process

Before actually performing income-smoothing activities, management should choose a smoothing object. This choice depends on the motive for smoothing the income. If a management compensation plan is stated in terms of accounting net income and this generates the most important motive for smoothing income the smoothing object is obviously net income. But the profit per share can also be a smoothing object resulting from the motive to satisfy the shareholders.
After determining the smoothing object management should have clear expectations of the non smoothed income pattern. It may be clear that wrong expectations about this pattern can cause even stronger fluctuations in reported income if the smoothing measures are taken.
Furthermore, management should decide which of the above mentioned smoothing actions should be taken. They have to consider the impact of this decision for the future and have to decide whether the actions will be reported in the financial statements.

2.4 Managing other aspects of disclosure

So far we have discussed the techniques and the process of income smoothing. In most cases, annual earnings will be the smoothing object. Information related to annual earnings is released to parties outside the firm in the form of financial statements. However, financial statements are not the only method of informing the outside world. Annual earnings can also be communicated through press releases, speeches, and interviews. These may relate to other kinds of disclosures such as advertising and public relations announcements.
Using the techniques discussed so far, the actual data (annual earnings) are managed. However, data are not the only aspect managed. Gibbens, Richardson and Waterhouse identify eight categories for disclosure management:

> *Data content,* the basic news or data. Annual earnings are a typical and widely studied "data content" aspect of managed disclosure.
>
> *Data organisation* refers to the format and classification of the data.
>
> *Prior and concurrent interpretation* by the discloser are attempts to influence how the receiver interprets information.
>
> *The medium* is the channel through which information content with interpretation is communicated to outside parties.
>
> *Timing* refers both to date and frequency of disclosure.

Redundancy refers to the sequencing of disclosures and the selection of recipients.

Credibility is the trustworthiness of the disclosure in the eye of the recipient.

Subsequent interpretation refers to correcting recipients' interpretation.

2.5 Ethical aspects

The following question is a fascinating one: 'Is smoothing income ethically acceptable?'
In 1990 Rosenzweig and Fischer asked a sample group of management accountants this question. In a survey the practitioners gave accounting manipulation (in this survey defined as purposely influencing earnings through incorrect recording) an average rating between a moderate and a serious ethical fraction. Generally, they had few ethical qualms about operating decision manipulation, which can be considered equal to the earlier mentioned ways of real and accounting income smoothing. For this kind of manipulation the scores indicated an average rating between (fully) ethical and questionable. A salient feature of this survey was the fact that accountants with more experience and higher positions in the organization were more tolerant of income smoothing than accountants with less experience.

In general income smoothing is often considered 'misleading', 'cheating' or an 'immoral deed' of management. However, there are some considerations which may contradict those opinions.
Income smoothing can be considered as an indirect information supply of management's foreknowledge of future earnings and their distribution. After all, ad hoc attempts to adjust current income to minimize its difference from the preceding year's income may simply fail to produce long-run smoothing.
Sometimes even accounting standards promote income smoothing, for example the change from SFAS 8 to SFAS 52, relating to the translation of foreign currency. This change was dictated by the criticism on the application of SFAS 8 which stated that exchange rate results had to be recorded in the Profit and Loss account (leading to large fluctuations in reported profit). After the introduction of SFAS 52, those results could be recorded through equity.

Income smoothing does not necessarily have to be rejected, although caution is, of course, called for. The external auditor can play an important role. His task is to watch for the true and fair view of the financial statements. He can object a protest when accounting smoothing (e.g. discretionary accounting change) is misleading and he can lodge disclosure of the transaction in cases of real smoothing.

2.6. Conclusion

In this section we discussed the phenomenon income smoothing; the techniques, the smoothing process and various smoothing objects.
By discussing the ethical aspects, we also showed some other aspects of income smoothing.
This, we believe, is necessary to think systematically and productively about income smoothing and in a broader sense about earnings management. In the next section we will review research into the earnings management and income smoothing area.

3. PRIOR RESEARCH

3.1 Introduction

Early studies investigating the accounting policy choices of firms focused on the stock price behaviour of shares from firms that changed accounting policies. These studies investigated whether the stock market is systematically misled by the effect of accounting changes on reported earnings. These studies attempted to discriminate between two competing hypotheses on how stock markets react to reported earnings : The "mechanistic" hypothesis, which states that stock markets react mechanically to changes in earnings due to accounting policy changes, and the "efficient market" hypothesis, which holds that the stock market does not react to changes in earnings due to accounting policy changes unless the accounting changes reflect equivalent changes in the cash flows of the firm. Generally, research supports the latter hypothesis which raises the question: "If the stock market is not fooled by accounting changes, why do managers care about the accounting policy of their firm ? ".

3.2. Positive research

3.2.1 Introduction

This aforementioned central question is raised in many theories which are commonly referred to as "positive theories". Holthausen and Leftwich (1983) describe them as economic consequences theories. The theories are positive, as opposed to normative, though that is not their distinguishing feature. Much research in accounting is positive. Only a subset of that research investigates the economic consequences of accounting choice. Accounting changes have economic consequences if they effect the distribution of a firm’s cash flow or the claims of various parties on those cash flows. Economic consequences studies in general and earnings management studies in particular are driven by contracting and monitoring costs associated with firm’s contractual agreements.

3.2.2 Agency theory

3.2.2.1 Contracting and monitoring costs

In earnings management studies so far, economic behaviour is typically contractual assuming an agency relationship. Without going into too much detail some aspects of the agency theory will be explained. The agency theory views a firm as a nexus of contracts. These contractual agreements lead to contracting and monitoring costs. Contracting costs encompass the costs of evaluating, negotiating, writing and renegotiating the terms of a contract.

Monitoring costs are the costs of becoming informed about performance under contracts and evaluating compliance with the terms of the contracts. Once these costs are introduced, the choice of accounting measurement rules effects the firm's value and the wealth of various parties, because these costs prevent some users of accounting numbers from 'undoing' accounting changes at no cost.

3.2.2.2 Hypotheses

The agency-based theories generally try to explain the accounting choice using the following three hypotheses:

a) Bonus plan hypothesis
b) Debt/Equity hypothesis
c) political costs hypothesis

a) Bonus plan hypothesis

A management compensation plan is often stated in terms of accounting income. Thus, management's wealth can be effected by voluntary or mandatory changes in accounting numbers (assuming the compensation plan is not adjusted for such changes). Furthermore mandatory changes in accounting methods can lead to managers responding by altering the firm's investment and financing decisions to reduce any unfavourable impact on their compensation plan. This means that changes in accounting rules have economic consequences and there are incentives for managers to spend resources to voluntarily switch to different accounting principles, or to lobby for or against proposed mandatory accounting rule changes.

b) Debt/Equity hypothesis

An accounting rule causing a reduction in reported earnings or equity may put a firm into technical default under its loan agreement. This hypothesis assumes that the more unfavourable this ratio becomes, the more likely it is that the management of a firm has an incentive to choose accounting rules which will yield an increase in reported earnings. Besides preventing possible technical default this behaviour may reduce the cost of capital as the risk profile of the company will decrease.

c) Political costs hypothesis

A firm’s reported accounting numbers indirectly effect the extent to which the firm is either criticized or supported by consumers, employees, unions, politicians and bureaucrats. For example, large oil companies were castigated in the financial and popular press for reporting record profits during the oil ’shortage’.For politically visible firms, accounting numbers have economic consequences because changes in those reported numbers influence the probability of taxes being imposed or subsidies being granted.

Most studies did not test just one of the above hypotheses, but tested a combination of the hypotheses. Using the accounting technique as the dependent variable, the independent variables are proxies for contracting and monitoring costs. The most commonly used proxies are:

Bonus plan:	The existence of a management compensation plan tied to accounting earnings.
Debt/Equity:	Leverage of the company (debt/equity ratio)
Political costs:	The size of the company

In 1983 Holthausen and Leftwich reviewed research into the economic consequences of voluntary and mandatory choices of accounting techniques. In their paper they shortly discussed the results of 15 studies of which 9 examined the association between accounting technique choice and the proxies for
hypothised economic consequences. Holthausen and Leftwich summarised the results of these studies as follows:
"In general, it is hypothised that firms facing higher contracting and monitoring costs are more likely to choose accounting techniques that increase reported income, and firms that have high political visibility are more likely to choose income-decreasing techniques."

Hassink and Mertens (1992) reviewed three decades of research into the accounting technique choice. In an overview they indicated 63 research papers published in international economic magazines. Most of these studies (68 %) were published in Accounting Review, Journal of Accounting Research and the Journal of Accounting and Economics.

The results of these studies were summarised as follows:

	number of times examined	Percentage of tests which rejected the hypothese
Bonus plan	12	17 %
Debt/Equity	27	19 %
Political costs	28	36 %

No explanatory variables could be identified in 6 % of the studies.
The causal links these studies suggest are tentative. It is very difficult to test the influence of the separate hypotheses, as there may be a trade-off between them. However there is some evidence that companies choose their accounting rules based upon a combination of the determinants named above.

3.2.2.3 Further sophistication of the hypotheses

In 1989 Schipper stated that in earnings management studies the economical behaviour under consideration has been typically contractual. In her paper she considered earnings management from an informational perspective. Under an informational perspective, earnings are one of many signals which may be used to make certain decisions and judgements.
Holthausen further discussed the hypotheses mentioned above by contrasting three alternative, but not mutually exclusive, perspectives on accounting method choice: efficient contracting, opportunistic behaviour and information perspectives.
Efficient contracting was the general premise underlying some of the early work on economic consequences of an accounting choice. This work examined the incentives to choose among accounting methods because of the explicit and implicit contracts that relied on accounting numbers. It implies that accounting methods will be selected which minimize agency costs among the various parties.
The opportunistic behaviour perspective assumes that the accounting method choice and the form of financial statements is driven by the behaviour of managers who are maximizing their own utility.
Both the efficient contracting and the opportunistic behaviour perspectives can be considered as a sophistication of the agency theory explaining accounting method choices. They can be classified as contracting perspectives.
The information perspective assumes that if managers have a comparative advantage in providing information about their firms, they are expected to be compensated in part on the basis of their ability to provide information about the future cash flow of the firm. Thus, this perspective suggests that accounting methods are chosen to reveal the managers’ expectations about the future cash flow of the firm.

Both the contracting and the information perspective state that there is an association between accounting methods and cash flows, but they disagree on their causality. The contracting perspective suggests that the accounting method chosen effects the firm's cash flow (choose the most efficient methods to maximize the firm value or behave opportunistically to transfer wealth between shareholders, bondholders and management), while the information perspective suggests the methods chosen provide information about the future cash flow of the firm, but do not effect them directly.

3.3. Validity and shortcomings of the hypotheses

Empirical studies of the validity of all the above hypotheses (especially the agency theory) have statistically analyzed large cross-sectional samples of data (US firms). These studies showed that firms with management compensation plans and high debt/equity ratios were most likely to choose liberal accounting policies, and larger firms were likely to choose conservative accounting policies. No empirical research in this respect has been performed in the Netherlands yet. As also recognized in the US, today's understanding of the determinants of a firm's accounting policy choices and changes is still limited. Interpretation of the empirical evidence provided by studies so far is difficult because simple proxies have been used to test rich and complex hypotheses. Many research so far looked for evidence consistent with a certain theory, without seeking evidence for the assumptions underlying the theory. These studies did not focus on documenting actual cases of the phenomenon 'earnings management'.
This lead some researchers to undertake a descriptive analysis of a company's accounting policy choice and in a broader perspective, the disclosure process of a company. In the next section, we review qualitative research in this area. Qualitative research may result in a better understanding of financial disclosure.

4. QUALITATIVE RESEARCH

4.1 Introduction

As explained in the previous section qualitative research can contribute favourably to a more thorough understanding of a firm's financial disclosure. There are some interesting qualitative research papers in this area, which provide some very useful insights.

4.2 Corporate financial disclosure

4.2.1 Introduction

Among several usefull qualitative research papers the report by Michael Gibbens, Alan Richardson and John Waterhouse, is a very interesting one. Using the grounded theory, the authors developed an empirically derived structure to explain and predict corporate financial disclosure. Financial
disclosure is defined in this paper as any deliberate release of financial information, whether numerical or qualitative, required or voluntary, or via formal or informal channels.
Their approach developing a structure for disclosure is based on grounded theory. An inductive theory is said to be "grounded" when its development is based on a phenomenon. Through interviews (approximately twenty were conducted) the authors developed a vocabulary of constructs and variables to describe disclosure processes and to identify relationships among these constructs and variables.

4.2.2 Disclosure position

The interview data were used as a framework for corporate financial disclosure. Based on the results of their research, the authors state that one of the distinguishing features of a firm is its disclosure position. Firms develop a stable two-dimensional internal preference for managing disclosure. The first dimension results in an apparently uncritical acceptance of rules and norms, which is referred to as a ritualistic disclosure position. The second results in a propensity to seek a firm-specific advantage in the disclosure of financial information, which is defined as an opportunistic disclosure position. This preference appears to develop as a result of market factors as well as firm-specific factors (such as internal politics). The attributes of disclosure which are managed are set out in more detail in section 2.4. The information itself, its timing, and interpretation are included in the discussion.

Apart from the firm's disclosure position, structure, both in the organisation itself and in the external demands for information, has an important influence on disclosure outputs. Internal structure, the structure within the organisation itself, is the extent to which responsibility for the management of the disclosure process is assigned to particular positions within the organisation and/or it is guided by clearly understood policies and procedures. Well-defined internal structures may exist for both ritualistic and opportunistic disclosure positions. External structure is the extent to which external demands for information are channelled through organisations that claim to represent third-party interests.
Besides the factors mentioned above, disclosure outputs are also influenced by external mediators and consultants and, not least, perceived opportunities and norms in the situation at hand.

4.2.3 Method

The method used is fairly new in the disclosure area. A framework has been developed by first developing a vocabulary (constructs, variables) in order to describe and analyze disclosure processes, after which the authors induced some relations among the constructs identified in the data. Interviewees were selected making sure the population addressed consisted of people with different perspectives on the disclosure process (intimately involved or involved as outside consultants, internal versus external involvement, product market versus capital market).

4.2.4 Results

As a result of their work, the authors are able to present a more sophisticated model, which also indicates that the disclosure process involves generating disclosure outputs in response to external and internal stimuli. The nature of the outputs is a function of those stimuli and of the firm's predisposition and existing response structure. Reference is made to section 4.2.2 in which these factors are dealt with.
The following figure clearly defines the relations between the independent and the dependent variables in the disclosure process.

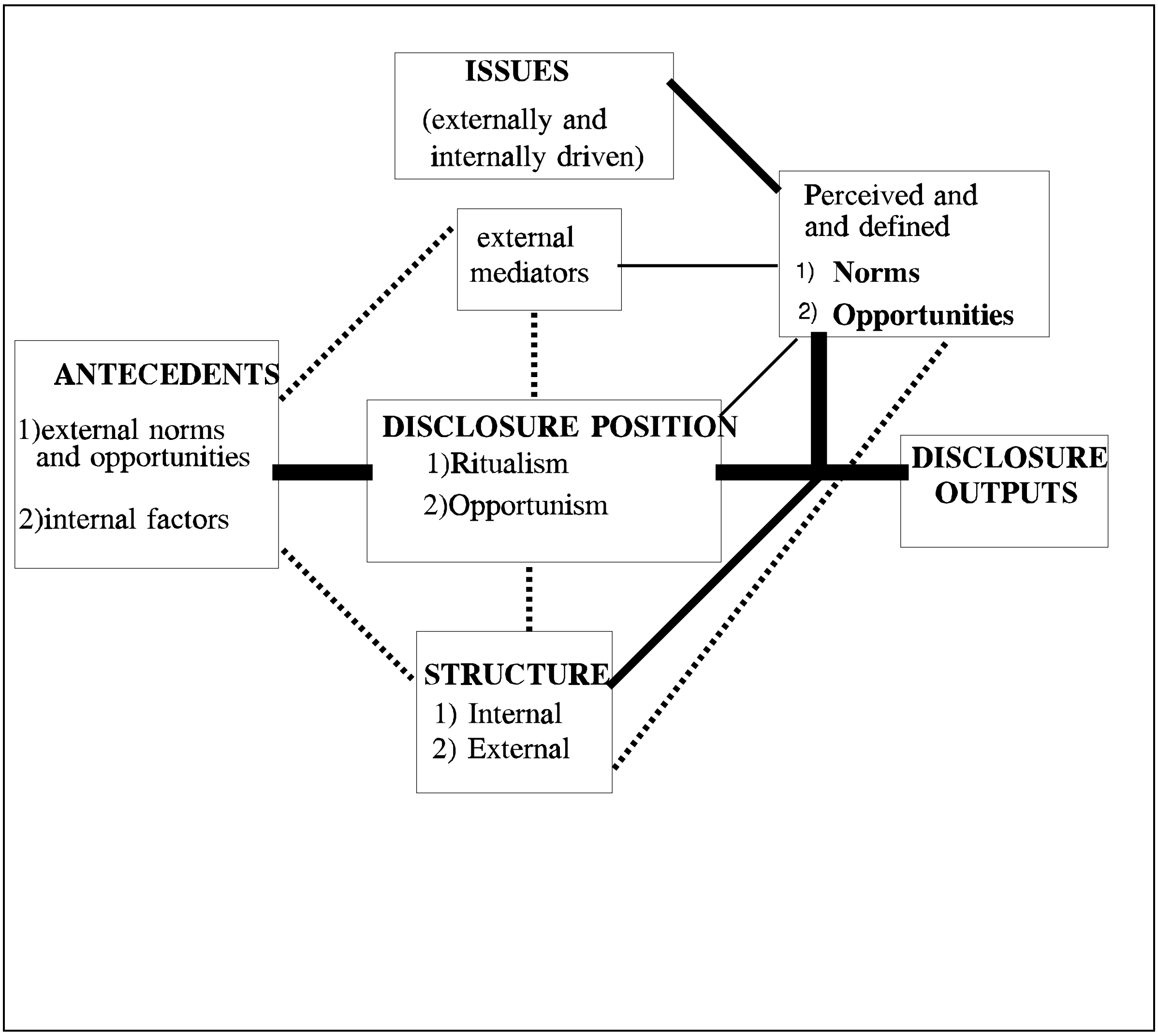

Figure 3

The firm's readiness to disclose is a function of its developed disclosure position, the existence of internal or external structures for handling disclosure, and the presence of auditors, consultants or other external mediators. Of course, the specific disclosure issue to be considered will be relevant to perceived and defined norms and opportunities.

The relations which were mainly discerned in the authors' analysis are the effects of antecedents on disclosure position (e.g., external norms and opportunities and internal factors) and the effects of perceived norms and opportunities, disclosure position and structure on output.

In the study, six categories of components that firms attempt to manage were

identified: information set, content, redundancy, timing, ex ante interpretation, and ex post interpretation.
The five independent variables identified are: the firm's disclosure position, antecedents of the firm's disclosure position, the specific disclosure issues faced by the firm, external consultants and advisors, and structure.

4.2.5. Contribution

The authors thus developed a theoretical structure relating to corporate financial disclosure, which involved both the general position of firms with respect to disclosure and the observed disclosure behaviours and outputs, including the use of external consultants. The model arrived at is considered to be explanatory and a sound basis for further research. The authors are well aware that the components of the framework need to be tested before the model is generally accepted.

4.3 The manager's accountability and disclosure

4.3.1 Introduction

In the research paper, "Theoretical proposals and a case study on the manager's accountability and the firm's financial disclosure", the authors, Gibbens and Ikäheimo, examine the generation of financial disclosures by the firm as a function of the accountability experienced by the firm's managers. Their perspective is that of a manager within the firm who perceives accountability pressure from outside or inside the firm and who can influence the firm's disclosures in response to that pressure. It should be noted that contrary to the researchers' position in the paper, "The management of corporate financial disclosure: Opportunism, Ritualism and Processes", which has been dealt with in the previous section, their focus is on individual managers, not on the firm behaving as if it were able to act by itself. In doing so, the authors are able to expand the accounting research explanation of financial disclosure. Of course, financial disclosure is prompted by other factors, and there are more responses to accountability pressure than disclosure (or managing or at least influencing disclosure).

We consider their approach to be especially meaningful since it uses a well known theme, accounting as an instrument for discharging accountability and links this theme to financial disclosure as a managerial activity involving economic and social incentives, contingencies and choices. In introducing the individual manager's perspective, they also incorporate a sociological perspective of accountability.

4.3.2 Manager's accountability

Gibbens and Ikäheimo identify two main contributions to understanding disclosures by means of their accountability perspective.

1. It points out that financial disclosure is associated with the sorts of behaviours expected of accountable people.
2. It views disclosures as an outcome of an accountability-influenced contingent process, thereby introducing reputation, culture, structure, and strategy as components of disclosure.

Accountability is defined as the manager's perception of responsibility to another party or parties either inside or outside the firm to inform such parties about activities taken and results achieved. Accounting as an instrument for discharging accountability, clearly coming from an agency theoretical approach. However we feel the scope has been broadened since the individual manager's perception may include far more than the principal in the agency theory. This is noted since it gives rise to more and different sources of accountability pressure. Accountability relationships may involve whatever legal, contractual, hierarchical, social, or moral obligations the manager perceives and experiences.

4.3.3. Disclosure process

The disclosure process can be broadly characterized as follows:

- Among others an incentive structure, including managers being accountable for their behaviour is included in the analysis.
- The individual accountable manager decides what to do in response to the perceived stimulus. This analysis focuses primarily on the individual manager and not on the group and organizational dynamics involved.

Basically, it can be said that accountability involves perceived pressure to act in ways others expect, and to defend actions not thought to meet such expectations. It should be noted here that managers may try to manage financial disclosure as a way of disclosing information that leads to believing exactly what managers feel stakeholders expect. On the other hand, managers may even try to work on the expectations of stakeholders. As a board member of a Dutch publicly listed firm stated when interviewed by us "Expectations, especially those of investors should be closely monitored and preferably be the same as those of management. Therefore management should be aware of any deviations in expectations and endeavour to use its richer information and its management position in order to keep expectations from drifting apart."

4.3.4 Accountability relationships

Accountability is manifested and supported through a variety of relationships such as economic, political, ethnocentric and intellectual ones. The relationships identified can be briefly explained as follows:
- Economic: the familiar principal-agent model. Such stewardship reporting is judged to be fundamental to financial disclosure. Economic accountability may also extend to employees and customers.
- Political: relationships involve both formal and informal norms that extend, complicate or contradict economic pressures. Such norms may arise from legislation. More informal norms are based on cultural pressures among the managers involved in disclosure.

- Ethnocentric: relates to closer level of personal networks, informal groups and friends. Ethnocentric accountability may matter informally, not just inside the organization, but also to outside parties.
- Intellectual: arises from professional groups to which managers belong or from beliefs about rational or ethical behaviour.

The different relationships are unlikely to be as distinct as described above. They will more likely evolve into each other. The theoretical view can therefore best be described as a potentially dynamic system, with disclosure decisions being made within a nexus of relationships that influence each other and that the individual manager may also influence through the very disclosure choices he makes or through other actions.

4.3.5 Disclosure management

As mentioned earlier, the accountable manager has to decide what to do in response to perceived stimuli. This decision is referred to as "disclosure management" and implicitly presumes that the manager’s and firm’s disclosure actions are not entirely determined by regulations or other constraints. The individual manager’s decision may very well be directed towards effort minimizing and approval maximizing. The possibilities for the manager to manage disclosure for discharging accountability are effected by other managers in the organization and by contingencies like organization size, structure, strategy, culture, and external forces represented in various markets. Reference is made to section 4.2.4 in which a more general model for the disclosure process has been included. This model also takes into account the contingencies referred to.

Gibbens and Ikäheimo summarise their analysis of accountability responses and relationships and their potential connection to disclosure management in the following framework. The figure is rather complex, but in each disclosure it is likely that only some aspects of the framework are employed.

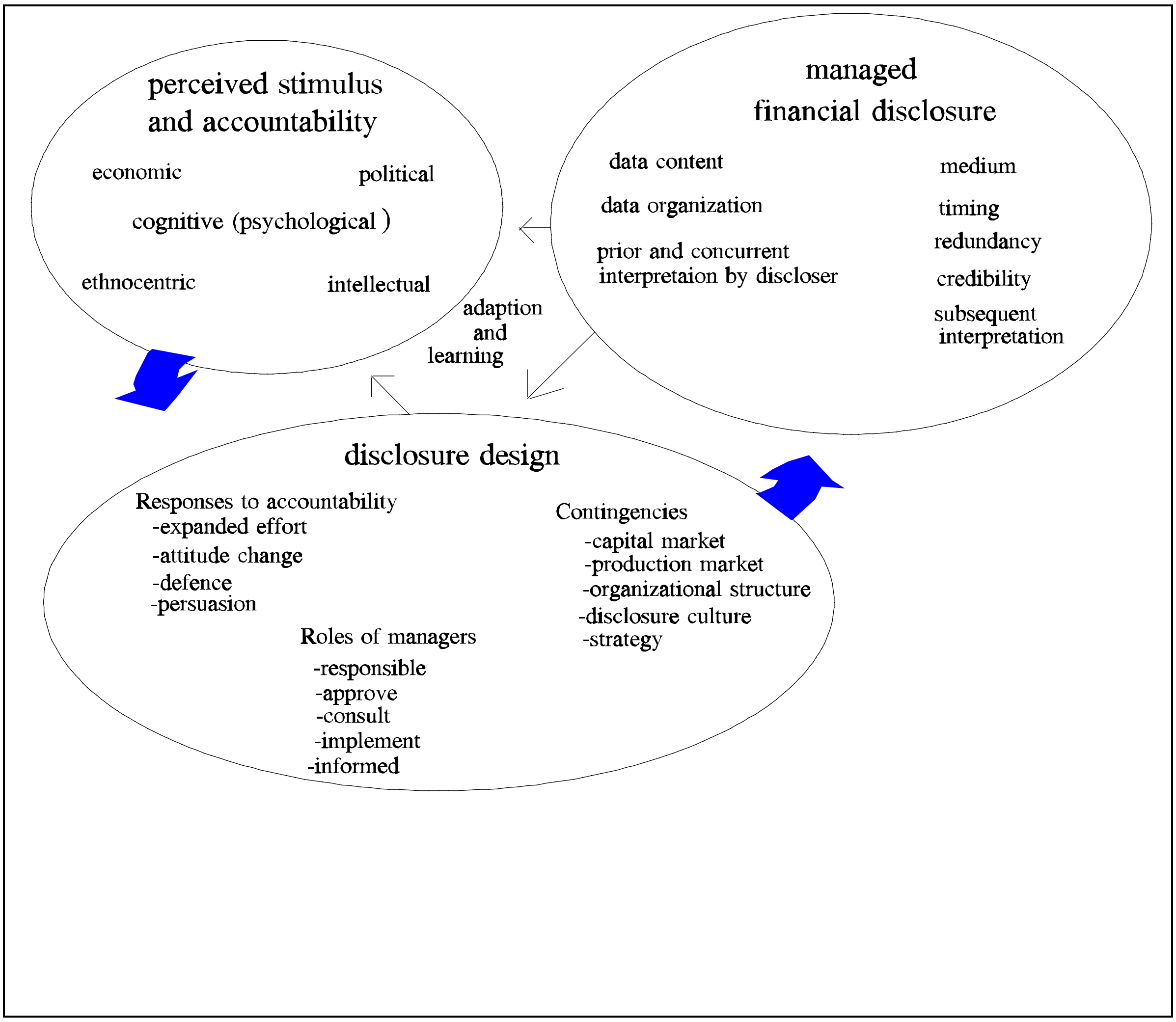

Figure 4

Gibbens and Ikäheimo also incorporated the results of a case study on disclosure management. They conducted some 16 interviews with 14 interviewees, including the chief executive officer, the accounting director, the company lawyer, the public relations manager, several division and product managers and the company's auditor.

In their case study, six real life disclosures and their management were involved, namely interim report, financial analyst's visit, press releases on project deliveries, subsidiary company report and reply, preliminary earnings and dividend increase.
In each disclosure, accountability pressures were identified. All four kinds, econ-

omic, political, ethnocentric and intellectual, as explained in section 4.3.4 were experienced. Financial disclosure management was presented as a consequence of the company's management of these pressures.
Based on their results, Gibbens and Ikäheimo state that traditional agency theory provides a narrow perspective of the financial disclosure management. The relationship between accountability and financial disclosures is more complex and ambiguous than the stated economic one. Financial disclosure management also involves political, intellectual, and ethnocentric structures which are not just superficially different but in fact reflect economic accountability. They are translators and creators of other kinds of accountability pressures and disclosures. Different kinds of accountability procedures are interlinked and economic and hierarchical accountability pressures provide only a partial and insufficient explanation of how accountability-influenced financial disclosures are managed.

However, economic stewardship accountability is important though this accountability pressure changes into other kinds of accountability pressures and thus the end result may change. In general, their research report supports the concept that financial disclosures are context-dependent and subjectively designed to create a basis for discharging accountability.

Further research

Most of the research so far has been quantitative. Since this quantitative research alone does not explain the rich and complex characterictics of the process in full, we feel qualitative research can be complementary. Great emphasis is therefore placed on qualitative research in this paper.

In our opinion, the conclusions arrived at by the researchers in the papers discussed in section 4, clearly provide a sound basis for further empirical research in the Netherlands. Primarily focusing on the conceptual framework set out in Figure 3, section 4.2.4, we will perform a descriptive analysis of the disclosure process of a number of Dutch publicly listed firms as a first step. We will operationalize the disclosure process as the translation of the management accounts (internal accounts) to the financial accounts (annual report), which is defined as the disclosure output. An in depth analysis, including interviews with key personnel and examination of source documents directed towards the determinants of the disclosure process within these firms will enable us to formulate new hypotheses. As a second step these newly derived hypotheses can be tested quantatively.

Conclusion

Although the financial disclosure process research already started some decades ago, today's understanding of the determinants of the firm's financial disclosure process is still limited. Most of the, especially, quantitative research describes how companies may react on certain external and internal stimuli, but these studies do not explain the rich and complex characteristics of the process. This can only be reached by undertaking also qualitative research in which the financial disclosure process of a single or only a few companies is investigated in great detail. Although this kind of research has some methodological weaknesses, which are not discussed in this paper, we believe such research may contribute favourably to the understanding of the determinants of this interesting but complex process.

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