Stockholm School of Economics

Master's Thesis in Finance

EARNINGS MANAGEMENT AND CEO TURNOVERS-A STUDY OF SWEDISH CORPORATIONS

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Abstract

This paper aims to investigate whether CEOs undertake earnings management in association with CEO turnovers. There is a general perception illustrated in the Swedish press suggesting that newly appointed CEOs engage in earnings management in order to boost performance based salaries linked to accounting data. To this date there has been no academic study examining this phenomenon in a Swedish setting. This paper presents evidence of earnings being managed through the use of accruals management as well as write downs in Swedish corporations. These results are in line with studies performed outside Sweden on non-Swedish corporations and also in line with theories covering the subject. The paper cannot determine to what extent observed earnings management are due to managers behaving opportunistically at the expense of shareholders or due to necessary costs taken as a result of the firm's financial position. However, it is found that there are economically significant incentives for managers to manage earnings in order to boost the outcome of accounting-based compensation contracts. As a consequence, this paper suggests that it would be preferable to avoid the use of compensation contracts linked to accounting data.

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1 Introduction and Study Outline

This section provides a brief introduction to the subject followed by a study outline, were the reader can find a brief overview of the thesis.

1.1 Introduction

Over the past years an increasing focus has been directed towards the importance of correct and fair accounting. The interest in how companies pursue their financial reporting has grown in the wake of a multitude of large corporate scandals that has occurred world wide. Two of the best known examples of manipulation of accounting data and the consequences thereof are the collapses of Enron and World Com. To this date Sweden has been spared from accounting scandals of this magnitude but cases like Trustor and Prosolvia are indicators that manipulation of accounting data also occurs in Sweden, at least on a "smaller" scale.

Recently the focus of the fair accounting debate in Sweden has been centered on accounting practices in association to CEO turnovers. Criticism has been raised suggesting that performance based incentive programs linked to financial reporting in Swedish corporations create incentives for CEOs to engage in opportunistic behaviour at the expense of shareholders. Swedish press has claimed that newly appointed CEOs manage earnings in order to boost their compensation from accounting based incentive programs and in order to enhance appearance of their performance.[1] The press also illustrates the perception that, in practice, such earnings management is considered routine at the time of a CEO change.

> *"Newly appointed CEOs manipulate earnings in order to boost their salaries and to give a good impression of their work. This behaviour is common among large Swedish corporations."*[2]
>
> (Translated by the authors.)

[1] Svenska Dagbladet 2004-01-27, Uppdrag Granskning 2006-03-07
[2] Uppdrag Granskning 2006-03-07

Many of these claims are supported by anecdotic evidence rather than thorough academic studies. To the knowledge of the authors there seem to be few academic studies examining the occurrence of earnings management in a Swedish context and no academic research studying whether newly appointed CEOs in Swedish corporations engage in earnings management. Nevertheless, a general belief still exists, on the Swedish arena, that earnings management does occur in association with CEO turnovers and as will be discussed below there might be good reasons to believe so.

Extensive regulation covers accounting practices of firms. However, these regulations include a certain amount of flexibility in a sense that accounting regulation often permits a choice of policy, for example in respect to asset valuation. Moreover some areas within accounting are still not fully regulated. Regulation therefore provides room for CEOs to manage earnings.

One can argue that a firm which experiences unexpected accounting changes are likely to be engaged in some kind of manipulation of financial reports. However, it can be difficult to determine whether unexpected changes in accounting information in association with a CEO turnover are due to managers acting opportunistically at the expense of share holders or by accurate reporting of overall economic performance. Taking this into consideration this study introduces so called impressions management. Instead of focusing on management of accounting numbers, impressions management focuses on graphical presentation of financial information in financial reports. If indications of both earnings and impressions management are found in a corporation experiencing a CEO turnover, this is more likely to indicate on deliberate opportunistic behaviour rather than necessary changes due to underlying changes in the firm economy.

This paper aims to investigate whether CEOs undertake earnings management in association with CEO turnovers for Swedish corporations listed on the Stockholm Stock Exchange A-list (the A-list was removed in 2006. This paper examines the time period 1995-2004).

1.2 Study Outline

The thesis is divided into 11 sections. S*ection 2* presents the theoretical foundation on which the study is based. The section includes a brief overview of the principal agent theory, definitions of earnings management and impressions management as well as an overview of a number of incentives that may generate this kind of behaviour. The section also includes different circumstances around CEO turnovers that may affect incentives to manage earnings and impressions. The study is based on a number of hypotheses which are outlined in *Section 3* followed by *Section 4* where the methodological approach is described and motivated. *Section 5* reports and discusses the characteristics of the data as well as its sources. The results from the study are presented in *Section 6,* followed by an analysis presented in *Section 7*. The conclusions derived from the analysis are presented in *Section 8*. A methodological discussion can be found in *Section 9* and finally, in *Section 10* a set of suggestions for further research related to the topic is discussed. References are presented in *Section 11*. The interested reader can find additional information concerning the study in *Section 12*.

2 Theoretical Foundation

This section attempts to provide a comprehensive overview of the main theoretical arguments that provide the basis for the following analysis. The ultimate objective for the section is to give an understanding of the earnings management and impressions management concepts as well as the incentives that are said to exist for this kind of behaviour. The principal agent theory is used as a foundation for the argumentation.

2.1 Principal Agent Theory

The separation of ownership and control in modern corporations is the quintessential agency problem.[3] It has many advantages but it also creates information asymmetries that may lead to problems of moral hazard.[4] These problems stem from the high agency costs involved in

[3] Ross (1973), Jensen & Meckling (1976), Fama (1980)
[4] Brealy & Myers (2003)

order to monitor managers. Since both the principal and the agent are assumed to be utility maximizing there are strong incentives for the agent to not always act in the best interest of the principal.[5] Thus, there should be obvious reasons for the agent to engage in activities which are not in the owners' best interest. Looking at newly appointed CEOs, theory suggests that they have incentives to maximise their wealth at the expense of the shareholders. One way of doing this could be to behave opportunistically by manipulating earnings and impressions in financial reports in order to boost performance-based compensation linked to accounting data as well as to create a favourable image of their performance in general.

2.2 Earnings Management

Earnings management is a concept with many names. It is also referred to as income smoothing, creative accounting, earnings smoothing and cosmetic accounting. The preferred term in Europe is often "creative accounting". In the US on the other hand "earnings management" is the preferred term. Hence, this is also the term used in most of the literature on the subject and therefore also the term used in this paper. This paper uses the following definition of earnings management inspired by previous research:

> "Any action on the part of management which affects reported income and which provides no true economic advantage to the organization and may in fact, in the long-term, be detrimental."[6]

There has been extensive research in the area of earnings management, mainly in the US, in the form of income smoothing. This has primarily been done in contexts not specifically related to CEO turnovers.[7] However, several studies have taken a closer look on earnings management in association to CEO changes.[8] A number of these studies suggest that managers have incentives to manage earnings in order to diminish the chances that a sharp earnings increase will cause them to be burdened with difficult performance targets in

[5] Bergström & Samuelsson (2001)
[6] Merchant & Rockness (1994)
[7] Ball & Watts (1972), Merchant (1990), Jensen (2001)
[8] Pourcaui (1993), Murphy & Zimmerman (1993)

subsequent periods.[9] In accordance with many of these previous studies and in line with the principal agent theory there are reasons to believe that newly appointed CEOs in Swedish companies will behave opportunistically by managing earnings in a way that maximize the economic outcome of their accounting based incentive programs.

2.2.1 Different Forms of Earnings Management

There are many different ways in which earnings can be managed. For a variable to qualify as an instrument for earnings management, it must be at least to a partial degree at the discretion of management.[10] Even though there are extensive regulations covering the accounting practices of firms there are a considerable part of subjective elements involved. These regulations include a certain amount of flexibility in a sense that accounting regulation often permits a choice of policy, for example in respect to asset valuation (one example of this is that IAS permits a choice between valuing non-current assets at either revalued amounts or at depreciated historical costs). Depending on the choice of which accounting practice to use, the reported results may therefore come to differ in a substantial way. In addition, there are also some areas within accounting that are not fully regulated. Nevertheless, this somewhat subjective part has positive as well as negative implications of the effectiveness of financial reporting. A certain level of freedom of choice concerning accounting practises may in fact improve the efficiency of accounting procedures and the quality of the accounting information. However, if someone has incentives to manipulate accounting numbers in an opportunistic manner, this freedom in accounting practice provides opportunities to do so.[11]

The use of accruals is a natural tool for moving costs between periods. The simple case of accruals management through capitalization of expenditures illustrates several common characteristics of traditional earnings management practiced in many companies. First, the goal of accruals management is management of the income statement, i.e. earnings. Any additional effect on other financial statements, such as the effect on assets and liabilities, is

[9] Beidelman (1973), Ronen & Sadan (1981)
[10] Ronen & Sadan (1981)
[11] Healy & Wahlén (1999)

viewed by the manager as secondary. Second, accruals management is performed easily through accounting decisions, and does not require the creation of new business transactions. Third, and most important, accruals management is usually done by a single manager or a small group of managers. Nevertheless, the widespread use of accruals also creates an obvious problem for the interpretation of the results of this study since it is hard to distinguish between what is "normal" use of accruals and what is not "normal". In spite of this and in line with prior research accruals are considered as a highly relevant variable for this study since accruals are such important instruments for moving costs between periods and thus for managing earnings.[12] Thus, in order to circumvent the problem of what is considered "normal" accruals figures, this paper will focus on total expected accruals and how the observed accruals figure each year differs in relation to the expected ones. Exactly how this will be carried out is described in more detail in Section 4.

Taking on large write downs in the year of the change would be another way for a newly appointed CEO to blame predecessors for poor past performance and consequently to create a favourable platform for positive earnings development in years to come. However, it could also indicate on the failure of previous managers to act and to take the costs necessary.[13] Moreover, earnings management undertaken through this mechanism is relatively easy for financial statement users to identify in the year that is undertaken. Consequently, the realisation of benefits from opportunistic earnings management through large write downs may be limited.[14] Nevertheless, asset write downs are usually made on an irregular basis and then they make up a large part of abnormal and extraordinary items and may have a significant impact on reported earnings in the years succeeding the write downs. Hence, including write downs as a variable in this study is clearly justified.

Moreover, studies have suggested that earnings management comes in two basic forms: smoothing and falsifying.[15] Falsifying involves reporting erroneous data while smoothing simply concerns transferring profit or loss from one accounting period to another. This study

[12] Merchant (1990)
[13] Pourcaui (1993)
[14] Defond & Jiambalvo (1994)
[15] Merchant (1990)

will not consider the difference between the two, but will merely treat all kinds of manipulative behavior the same.

Moreover, something closely related to traditional earnings management, such as has been described above, is so called financial engineering. This has to do with the structure of financial transactions of the kind employed by Enron. This practice is more complex and might be requiring the formation of legal entities, and the creation of financing arrangements between the company, its lenders and new outside investors. Financial engineering may require an organizational commitment to earnings management and not only the commitment of a small group. It may require the commitment of senior management and the company's board of directors as well as management at lower levels of the organization in the decisions to create the needed financial commitments and structures. This kind of manipulation, however, will not be tested for in this paper.

In summation, this paper examines traditional earnings management variables and how these variables, accruals and write downs, change in the years surrounding CEO turnovers. In this way one ought to find evidence of whether CEOs of the largest Swedish companies engage in earnings management or not.

2.3 Impressions Management

Impressions management focuses on management's attempts to manage the interpretation of financial reports.[16] The communication of financial information through financial reports is the last resort in which management can affect impressions of their work assuming that financial reporting at least to a partial degree are at the discretion of management. A large part of the literature covering impressions management stresses the importance of graphs in the communication of financial data.[17] How users' perceptions are affected by graphs and the cognitive implications of presenting data in a graphical format are well documented.[18] A number studies within accounting research have confirmed that graphical presentation affects

[16] Gibbins et al. (1990), Graves et al. (1996)
[17] Steinbart (1989), Beattie & Jones (1992), Tufte (1983)
[18] Lewandowsky & Spence (1989)

the perceptions and decision making of the users of financial statements. The extent to which they are affected varies with the context and the type of decision.[19] Typically this research covers which graphs that are included in financial reporting and the distortion in the construction of these.[20] The performance based compensations of CEOs linked to accounting data will most likely not be affected by impressions management in the short run. These are based on changes in accounting data and graphical presentation will therefore not have an effect on the economic outcome of these contracts. Nevertheless, in the long run it is to the largest extent desirable for a utility maximizing CEO to appear as well-performing, independent of the actual result. To appear as well-performing is desirable since it is likely that current performance will build a foundation for a salary raise when negotiating in the future. With this in mind, this paper argues that CEOs will try to manage impressions of their work by the use of graphs.

2.3.1 Selectivity

This paper intends to examine so called selectivity variables. It refers to the use of graphs and what occurs when management selects the information to display and presents that information and other information in a manner that is intended to distort readers' perceptions of corporate achievements. Hence, the aim is to determine if firms changing CEOs are selective about the financial information they present in financial reports. Selectivity is concerned with whether the decision to include a graph, or a variable within a graph, is related to changes in firm performance. The study does not include all the graphed financial variables since this would yield too many observations that are more or less irrelevant and hard to evaluate. Instead this study will focus on a selection of key financial variables. In line with previous research covering the topic key financial variables are defined as sales, profit, earnings per share and dividends.[21] These variables have a clear earnings and revenue focus and hence there is a link to the earnings management variables. As well as downward earnings management are predicted in the year of the CEO change, management are predicted to try to give an unfavourable impression of the key financial variables presented in

[19] Schulz & Booth (1995)
[20] Steinbart (1989), Beattie & Jones (1992)
[21] Steinbart (1989)

that same year and a favourable impression in the year following the CEO turnover. In short, this paper recognizes graphs and the potential selective behaviour of managers as a variable worth investigating.

2.4 Combining Earnings and Impressions Management

It can be difficult to determine whether unexpected changes in accounting information in association to a CEO turnover are due to management opportunism or in fact due to accurate reporting of overall economic performance. There are a number of reasons why managers engage in earnings management as well as a number of methods to do so. Taking this into consideration and inspired by prior research impressions management is included in this study.[22] Looking at the graphs presented in financial reports and how they are presented may help to draw better conclusions about the underlying causes of potential earnings management. If graphical presentation of financial variables have been distorted in annual reports of companies where potential earnings management has been detected it is more likely that the observed changes in earnings are deliberate and discretionary rather then a consequence of an underlying change in the firm's economy (a manager that practises one form of manipulative behaviour is more likely to practice another).

2.5 Incentives for Earnings and Impressions Management

There are a number of reasons why newly appointed CEOs would engage in earnings and/or impressions management. These will now be described in more detail.

The separation of ownership and control in corporations may create diverse goals among the different stakeholders. One way in which the shareholders may achieve goal congruence throughout the organisation is to outline efficient *compensation contracts.* However, these contracts can also create obvious incentives for managers to manage earnings if the contracts are not outlined in a way that supports their purpose. [23] In fact, studies have shown on little relation

[22] Beattie & Jones (1992; 2000a)
[23] Anthony & Govindarajan (2005)

between incentive compensation contracts and performance.[24] The research covering this topic touches the core of the principal agent problem. The modern history of executive compensation research and incentives that may arise from compensation contracts began in the early 1980s and paralleled the emergence and general acceptance of the principal agent theory. There are numerous influential papers within this topic, and many studies have been made on the efficiency of compensation contracts.[25] Pay practices vary across firms and industries but most executive compensation programs include two fundamental parts, a base salary and some kind of performance based salary in the form of accounting based annual bonuses, stock options or long term incentive plans.[26] The base salary does not give any large incentives for manipulating financial data. Nonetheless, even in the complete absence of a variable performance based pay there may be incentives to manipulate financial results. For example, a CEO's current performance is likely to be evaluated when negotiating future rewards.[27] This is the reason for including impressions management in this study as mentioned in Section 2.3. Performance based salaries, though, provide clear incentives for managers to manage earnings and other accounting numbers in order to boost their salaries.[28] Financial performance is primarily measured in relation to earnings and this is one of the reasons behind the earnings focus of this study and others. Moreover, the incentives for managing earnings will most likely be enhanced by linking compensation directly to accounting data.[29] Furthermore, compensation contracts are to a large extent related to short term firm profitability which also might enhance CEO short term behavior and thus incentives for earnings management.[30] Hence, due to the structure of many management compensation contracts, there are clear incentives for CEOs, as agents, to engage in opportunistic and wealth maximizing behaviour at the expense of the shareholders by managing earnings and impressions.

Another source of incentives for earnings and impressions management that is closely related to that of compensation contracts is *the capital market* and its expectations. If managers

[24] Jensen & Murphy (1990a); (1990b)
[25] Merchant (1990), Jensen (2001), Anthony & Govindarajan (2005)
[26] Anthony & Govindarajan (2005)
[27] Wells (2002)
[28] Murphy (1999)
[29] Merchant (1990), Jensen (2001)
[30] Bergström & Samuelsson (2001)

strive to satisfy the capital markets by favouring short term profitability this could lead to underinvestment in strategically necessary long term investments.[31] Since the expectations of the capital market are often based on a firm's financial reporting, reported earnings are essential for companies to be able to attract investors. In short this may create incentives for earnings and impressions management. *Debt contracts* may also create incentives for earnings and impressions management.[32] General corporate finance theory claims that existing debt limits the firm's freedom to act. This is through restrictions, covenants, mainly on dividends, stock repurchases and the possibility to take on further debt. The covenants are often outlined in relation to accounting numbers. Therefore incentives to manage earnings may arise in order to satisfy debt contracts, to weaken potential debt covenants and in order to be able to attract additional debt funding.[33] However, one might expect debt holders to easily identify such earnings management. There are also *other contracts*, stated or non-stated, with other parties than creditors that might create incentives for earnings management.

Incentives that stem from compensation contracts linked to accounting data are what Swedish press in general have claimed as reasons behind earnings management. In a scenario when a company is changing its CEO, accounting-based compensation contracts and the desire to appear as well performing ought to be the most influential incentives for managers to engage in opportunistic earnings management. The other types of incentives mainly relate to funding issues. Nevertheless, what it boils down to in the end is that all of above mentioned incentives affect the corporate success and ultimately the CEO's appearance as well as compensation. Hence, there are clear incentives for earnings management that may or may not be beneficial for the company. With this in mind, the authors would like to remark that not all forms of earnings management are due to CEOs acting in self interest as is strongly implied in the text above.

[31] Bergström & Samuelsson (2001)
[32] Defond & Jiambalvo (1994)
[33] Brealy & Myers (2003)

2.6 CEO Turnovers- Routine versus Non-Routine

2.6.1 CEO Turnover Definition

This study defines a CEO turnover as an event when a CEO is leaving the position and a new person is taking this position. The definition assumes that it is unlikely that the outgoing CEO would sign a report taking responsibility for his successor's actions since this could result in unpleasant legal consequences. The exact date of the change is therefore of minor importance in this study. Instead focus has been placed upon when the new CEO gains control of the financial reporting. Hence, the year of the turnover is defined as the first year when the incoming CEO puts his signature on the annual report. In some cases both the outgoing and the incoming CEO sign the annual report. In these cases, according to the definition of this paper, the new CEO has not gained total control yet and the subsequent year will therefore count as the first year when the new CEO is in control.

2.6.2 Routine and Non Routine Turnovers

As presented in Section 2.5 there are clear incentives for CEOs to manage earnings and impressions in financial reports to create a favourable image of their performance. The strength of these incentives might be affected by the reasons behind the turnover. Reasons for CEO turnovers differ and one could say that each turnover is unique. This paper classifies the sample into routine and non-routine turnovers since prior research suggests that incentives for earnings management may differ depending on whether the change is routine or non-routine[34].

Routine turnovers are described as a well planned process in which the appearance of both the outgoing CEO and the incoming CEO are more or less interrelated. In a routine turnover the outgoing CEO and the incoming CEO are more likely to know each other and they are also more likely to share the same goals. As a consequence, incentives to attribute poor performance to predecessors and thus the incentives for opportunistic behaviour are likely to

[34] Pourciau (1993)

be reduced. [35] A typical example of a routine turnover is when the outgoing CEO stays on the board of directors and the incoming CEO is recruited internally. An empirical example of a routine turnover found in the sample is the turnover that took place in Assa Abloy in 2003. In the annual report of 2002 the company announced a necessary and expected CEO change in 2003.

In contrast to routine turnovers, non-routine turnovers are described as relatively unplanned actions where the company does not have enough time to select a suitable successor. In these cases it is less likely that the successor is an insider and also that the departing CEO takes a place in the board of directors.[36] A typical example of a non-routine turnover is a situation where the outgoing CEO is fired because of poor performance and the firm recruits the incoming CEO externally under a relatively short period of time.

Hence, inspired by prior studies, routine CEO turnovers are defined as a process where the leaving CEO stays in the company, retires, or leaves the position on his own initiative.[37] It is also part of the definition that these turnovers are more or less anticipated. A non-routine turnover is characterised by the CEO being more or less forced to leave his position for various reasons, including being fired because of poor performance and health reasons are also included in the definition.

In some studies it has been found that newly appointed CEOs are more likely to engage in earnings management if the turnover was non-routine.[38] A possible explanation for this is the greater opportunities to engage in opportunistic behaviour in the somewhat more chaotic environment that arise in association with a non-routine turnover. Altogether, this is also why many of the previous studies within the subject have chosen to focus only on non-routine turnovers.[39] This paper, however, will not exclude the routine turnovers from the sample. Instead potential differences between routine and non-routine observations will be identified and analysed.

[35] Vancil (1987)
[36] Vancil (1987)
[37] Vancil (1987), Pourciau (1993)
[38] Wells (2002)
[39] Pourciau (1993)

3 Hypotheses

According to the discussion above there are incentives for managers to engage in earnings and impressions management. It could, therefore, be expected that an incoming CEO would manage financial reports in a way that would attribute poor performance to his or her predecessors. Doing this would also create a platform from where the CEO can start building future earnings and, thus, be in a better position to increase future performance based compensation linked to accounting data. When management engage in this kind of behaviour they are said to take a "big bath" or a "cost bath". Furthermore, this image of the new CEO as the company's saviour might be enhanced by a selective behaviour of the CEO concerning which variables to graph in the reporting of the financial performance. Based on the discussion above, there is nothing in the theoretical foundation that indicates that the newly appointed CEO has incentives to manage earnings and impressions in an opposite manner. In accordance with general economic intuition and the principal agent theory there should be no reason for an incoming CEO neither to attribute good performance to the outgoing CEO nor to manage earnings in order to create an impression of poor economic development when they are in charge. This is because each individual is assumed to be utility maximizing. Consequently, a number of one-sided hypotheses are formed and presented below.

In the year of the CEO change (year t) the following hypotheses are applied:

H1. Earnings Management

H1a. Firms report negative unexpected accruals in the year of the change reducing the result.

H1b. Firms report negative unexpected write downs in the year of the change.

H1c: Firms report revenues that are approximately equal to previous year.

H2. Impressions management

H2. Unfavourable selectivity in the year of the change through unfavourable changes in key financial variables graphed.

In the year following the CEO change (year t+1) the following hypotheses are applied:

H3. Earnings Management

H3a. Firms report positive unexpected accruals in the year following the change to increase the result of the firm.

H3b. Firms report positive unexpected write downs in the year following the change.

H3c: Firms report revenues that are approximately equal to previous year.

H4. Impressions management

H4. Favourable selectivity in the year following the change through favourable changes in key financial variables graphed.

H5. Routine versus Non Routine

H5. The hypotheses stated above are more pronounced for non-routine than for routine CEO turnovers.

4 Methodology and Model Specification

In this section the methodological approach is described in detail. First a method used to measure earnings management is presented. This method intends to examine the relation between CEO changes and earnings management. Second, another method is developed in order to measure potential impressions management. In accordance with what is stated above this is to make a better assessment of potential opportunistic management behaviour. Finally, a joint test is presented. This will simultaneously consider aspects of both earnings management and impressions management and thus, it examines the association between the two.

4.1 Earnings Management

4.1.1 Earnings

Earnings are the first variable to examine regarding earnings management. In line with what is stated above this paper argues that if CEOs engage in earnings management, i.e. taking a "cost bath" in the year of the change, one would expect to find lower earnings in that year than in the year prior to the change and the year following the change. Thus, earnings should show a V-shaped earnings figure over the observed time period. Such findings would indicate on either lower corporate revenues or higher expenses that year. Therefore, a first step in developing a model for earnings management involves looking at how company earnings change during the period. If earnings are reduced in the year of the CEO turnover due to a reduction in revenues of approximately the same amount this would most likely not indicate on earnings being reduced due to large unexpected accruals and or write-downs. However, if revenues stay the same or approximately the same over the period, even though profits decline in the year of the CEO turnover, increased costs would be the reason. I.e., this may indicate on the CEO taking a cost bath. When doing the tests earnings are deflated by lagged total assets to remove the effects from a potentially increasing asset base as well as to avoid heteroskedasticity and to facilitate inter firm comparisons. A non-parametric sign test is then used in order to test if earnings during the observed period are described by a V-shape or not.

4.1.2 Accruals

Accruals are a widely used tool for moving profit and loss between different accounting periods and it is probably the most frequently used earnings management practice.[40] This paper argues that accruals reflect the impact of changes in accounting estimates and, hence, serve as a tool for moving profit and loss between periods. This study intends to examine how accruals have changed over the years surrounding the CEO turnover. A way to measure this is by estimating so called unexpected accruals. Unexpected accruals are a proxy for the discretionary component of reported earnings or to which extent earnings management has

[40] McNichols (2000)

occurred. If accruals change over time and if negative unexpected accruals are found in the year of the change and positive unexpected accruals are found in the following year this could be evidence of earnings management. Thus, in accordance with previous research, the model makes a critical assumption that the examined variables for each firm remain constant between two reporting periods and consequently each observation point in time will have the prior year as a controlling variable.[41] In accordance with prior literature, unexpected accruals in year *t* are determined as follows. [42]

$$(Unexpected\ Accruals)_t = (Accruals)_t - (Accruals)_{t-1}$$

I.e., this year's unexpected accruals equal this year's booked accruals less last year's booked accruals, where:

$$(Accruals)_t = (Net\ Operating\ Profit\ After\ Interest\ and\ Tax)_t - (Cash\ Flow\ From\ Operations)_t$$

I.e., accruals for a year are defined as that year's net operating profit after interest and tax less that year's cash flow from operations. This definition states that cash flow from operations includes operating interest expenses and that financial interest expenses should be included in the financing and investment operations. It also assumes that interest and tax items, respectively, are extracted from the operations as well as accrued and also that no other items, like irregular items, have been excluded.

In accordance with Section 4.1.1 accruals are deflated by last year's lagged total assets in order to facilitate inter firm comparisons and to avoid heteroskedasticity.[43] Furthermore, a simple random walk model is used to describe the relation between earnings management and CEO-turnover. Even though you might expect the same results from both a parametric t-test and a nonparametric test both tests will be pursued since the t-test is only valid if the population is normally distributed. A flaw of the non-parametric test is the low power that the test might have. A potential difference between routine and non-routine CEO turnovers will

[41] DeAngelo (1986,1988), Eddey & Taylor (1999)
[42] DeAngelo (1988), Eddey & Taylor (1999)
[43] DeAngelo (1988), Jones (1991), Eddey & Taylor (1999), Wells (2002)

also be examined using t-tests and the Mann Whitney U-test. The Mann Whitney U-test is used since the objective of this test is to examine whether the central locations of the two distributions differ or not.

A common feature of all models testing for accruals management is their attempt to isolate and measure management's influence on the financial reporting. As indicated above an issue an earnings management researcher face is to estimate how reported earnings would behave without potential earnings manipulation. The method described above can be classified as a so called aggregate accruals model.[44] Two other test models frequently used in the earnings management literature is so called specific accruals models and the frequency distribution approach. These models will not be used in this paper since they are founded on assumptions that are not as empirically established. Moreover, a majority of the literature covering the earnings management concept has used aggregated accruals models. These models attempt to identify discretionary accruals based on the relation between total accruals, i.e. aggregated accruals, and hypothesized explanatory factors. Most of the aggregated accruals models use total accruals and change in total accruals, respectively, as measures of management's discretion over earnings.[45] Thus, earnings management exist if there is a significant difference between the total booked accruals of one point in time and the observation prior to this. Moreover, as stated above the aggregated accruals methods suffer from difficulties of identifying and separating discretionary components from nondiscretionary components. However, this is something all methods used in earnings management research suffers from. Later research on aggregated accruals models has introduced a regression approach, the so called Jones model, to control for nondiscretionary factors influencing accruals, specifying a linear relation between total accruals and change in sales and property, plant and equipment.[46] However, this approach requires substantial time-series or cross-section of data as well as a stationarity assumption, as opposed to the prior methods used that only assumes stationarity over two subsequent periods. Moreover, evidence has been presented indicating on firms with greater expected earnings growth are likely to have greater accruals which may result in possible misspecification of the Jones model.[47] Thus, the Jones model has been

[44] McNichols (2000)
[45] Healy (1985), DeAngelo (1986), Eddey & Taylor (1999)
[46] Jones (1991)
[47] McNichols (2000)

shown to have a rather low explanatory power and more research is needed to complement this model. In short, this paper chooses to use a non-regression approach when examining the occurrence of accruals management.

4.1.3 Write-Downs

Another variable to include in the study is restructuring costs. In accordance with the argumentation of Section 2.2.1 this study focuses on write-downs since write-downs is a frequently used tool for shifting future expenses to current periods.[48] If large write-downs are more abundant in the year of a CEO turnover this would indeed indicate on earnings management in the form of a big bath.[49] In accordance with the approach used when examining accruals this paper uses unexpected write downs as a measure of potential earnings management. Unexpected write downs in year *t* are defined as:

$$(\text{Unexpected Write Downs})_t=(\text{Write Downs})_t-(\text{Write Downs})_{t-1}$$

As for accruals and earnings, write downs are deflated with one year lagged total assets. To test if unexpected write downs are different from zero t-tests and non-parametric tests are used. Moreover, the differences in behavior between routine and non-routine turnovers will, as for accruals, be examined using t-tests and the Mann Whitney U-test.

4.2 Impressions Management

Impressions management involves looking at how firms are graphically presenting accounting material. As mentioned above the selection of so called key financial variables will be examined in this study. These are defined as sales, profits, EPS and dividends. The purpose of looking at these variables is to determine if firms changing CEO are selective about the information they are presenting in financial reports. The adopted method in this study compares annual reports in period *t-1* to those in period *t* in order to identify changes in

[48] Wells (2002)
[49] Wells (2002)

the choice of key financial variables graphed. This process is then repeated, comparing period *t* to period *t+1*. A selective change occurs if a key financial variable is graphed in period *t-1* but not in period *t*, or vice versa. If a change has occurred then this change will be classified either as favourable or unfavourable to the company. Adding a graph that shows a positive development or deleting a graph that would have shown a negative trend is defined as a favourable change. In addition, adding a graph that shows a negative development of performance or deleting a graph that would have shown a positive performance is defined as an unfavourable change. An empirical example of selectivity can be found in the annual reports of Skanska surrounding the CEO turnover in 1997. Throughout the observed time period revenues are constantly increasing. In the year of the turnover, the revenue graph is removed, thus showing on unfavourable selectivity. In the year subsequent to the turnover revenues are once again graphed, indicating on favourable selectivity. Each change will be awarded either *+1* or *-1* depending on if it is favourable or unfavourable. The total number of changes over an observation period is summed in order to obtain the total number of changes in the variables displayed. Thus, the aggregated favourable or unfavourable effect of selective behaviour is what is tested for. A t-test and a non-parametric sign test are used to be able to draw a statistically reliable conclusion about the potential selective behaviour of managers.

4.3 Combining Earnings and Impressions Management

A joint test will simultaneously consider both earnings management and impressions management. The joint testing will simply examine if companies where evidence of earnings management are found also has a higher probability of experiencing impressions management.

5 Data and Sample Collection

This section focuses on the data selection process. First, the choice of time period and the collection and categorisation of data crucial for the study are described in detail. Second, the selection procedure for choosing the sample will be described. Thereafter, a final sample will be presented and described in detail.

5.1 Data Selection

This paper concerns CEO changes in companies listed on the Stockholm Stock Exchange A-list over the time period 1995 to 2004. The A-list is chosen for three reasons. First, the general focus in the Swedish debate concerning CEO compensation contracts and the potential implications of these are centred on these larger firms. Second, this sample also constitutes a diversified sample of companies and this paper aims to examine the relation between CEO turnover and earnings management in large Swedish corporations in a general context. Finally, it is also likely that the behaviour of each of these larger corporations is norm setting for accounting practices in their particular industry.

Since the current debate on earnings management and management compensation focus on recent events it is desirable to include as current financial reports as possible in this study. The method used in the study requires financial reporting from one year after the CEO change. Hence, no observed CEO turnovers after 2004 can be included in the sample since there are no data available to extend the period further. Moreover, the study stretches over ten years from 2004 to 1995 and the intention of choosing a time span of roughly ten years is to reduce the impact from business cycles and general market trends. As mentioned above, this paper aims to measure the behaviour of CEOs in a current perspective. To further increase the time span and to add observations from earlier years would therefore be of little importance. There are a number of reasons not to increase the time span further, for example institutional and regulatory changes. Furthermore, one can argue that it is interesting to compare each company where a CEO turnover is observed with comparable companies in the same industry in that same time period in order to extract more reliable results. The reason

for this would be to control for industry cycles. However, doing this would yield a tremendous workload and the potential winning of doing this is not considered to be large enough in this study. This paper will therefore not make such a comparison which is in line with most of the previous research on earnings management.

5.1.1 CEO Turnover Data

For each firm on the A-list, the year book Owners and Power in Sweden's Listed Companies (1995-2004) was used to identify CEO changes that occurred during the chosen time period. These books publish lists of all CEO changes in companies on the Stockholm Stock Exchange. The sample that was obtained through compiling data from these books was then confirmed by using annual reports from the same firms. Furthermore, annual reports of those companies listed on the Stockholm Stock Exchange A-list but not listed in these books[50] were examined in order to determine whether a change took place or not during the relevant period.

The next step, in line with Section 2.6, was to classify each CEO turnover into either routine or non routine. Companies rarely state in press releases if there have been diverse opinions or if there have been conflicts involved when taking the decision of a CEO change. "Leaving to be able to spend more time with family" or "leaving for personal reasons" are two examples of frequently used statements when companies explain why they are changing their CEO. Thus, it is almost impossible to find the actual reason behind a turnover only by looking at press releases. Other sources of information were therefore needed in order to obtain more reliable information about the reason behind the turnover.

Although there are evident information asymmetries involved, this study first and foremost use company press releases and annual reports as a primary source of information in order to find the reason behind a CEO turnover. Press releases were found in the Affärsdata database and these were complemented with information from company web-sites. Based on this material a first classification into routine and non routine turnovers was made.

[50] ABB, Nokia, Tietoenator and Autoliv

In order to be able to draw more accurate conclusions about the reasons behind CEO turnovers the Affärsdata database was once again used in order to search for articles covering the turnovers. By studying articles published in some of the major Swedish newspapers and journals like Dagens Industri, Dagens Nyheter, Svenska Dagbladet and Affärsvärlden a more reliable view of the turnovers was found. These findings were then used to complement the information given in the press releases and a second and final classification of the sample was then made based on both sources of information. The subdivision of the total sample into routine and non-routine turnovers can be found in Table 2.

5.1.2 Accounting Data

Due to the chosen time period (1995-2004) and the fact that the chosen variables are measured one year prior to the change and one year following the year of change, accounting data from the period 1994 to 2005 was included. The data was collected from the financial reports for each company. Hence, more than 360 financial reports were collected, most of them were found in the archives of the SSE library (which is made up of the Six Trust non-electronic database) and the rest were obtained through direct contact with the firms included in the sample. Thus, a highly unique sample was created. At first, the intention of the authors was to use digital databases such as Six Trust, Orbis and DataStream in order to extract the accounting information. Unfortunately, that proved to be impossible due to the thorough level of accounting data needed and many of these databases lack data for the relevant time periods covering a number of the observed CEO turnovers.

Accounting data for some of the observed CEO changes was not available. This was in most cases due to companies no longer being listed. Some had been acquired by another company a few years back and some had ceased to exist. For this reason 20 observations were deleted from the sample due to lack of accounting data.

5.2 Final Sample and Sample Description

The initial sample consisted of 120 CEO turnovers reported by 90 firms. Due to the special nature of financial institutions (defined as banks and insurance companies) and the heavy regulations that apply for these firms they where excluded from the sample. A further reason to exclude financial institutions was the inapplicability of the variables and the model on their accounting practises. Since a period of three years are observed around each CEO turnover the incoming CEO have to stay on the post until the end of the second accounting year after the change in order produce the data needed. When two or more changes occur in a too narrow time span the last change is the only observation recorded. The reason for this is that data is needed for the years before and after the year of the actual change and also for consistency reasons. eight observations were excluded due to this reason. In line with similar previous studies and due to the nature of extraordinary events such as divestures, bankruptcy and CEO turnovers due to takeovers or mergers are excluded from the sample.[51] For these reasons, 32 more observations were excluded which gave a total 40 excluded firms from the sample. That left a final sample of 80 observations. Hence, 80 observed changes made in 63 corporations form the final sample examined in this study. The entire sample as well as excluded observations can be found in Appendices 12.A and 12.B respectively.

Descriptive statistics of the observed CEO changes are presented in Table 1 and 2. Table 1, Panel A, shows how the number of changes has evolved over the examined time period. Table 1, Panel B, displays the sample subdivided by industry. The industry classification is made using OMX guidelines. The sample consists to a large extent of the Industrials sector as well as the Financials sector. However, the categorisation used is rather wide and the OMX classification includes a number of industries in these two categories. Industrials, for example, includes most kinds of heavy engineering industries but also, for instance companies within transportation such as SAS, Linjebuss and Nordström & Thulin and consulting firms such as Ångpanneföreningen. The Financials category not only includes different forms of financial institutions and investment trusts but also real estate firms and companies like OMX itself. Panel B also includes the excluded companies and displays the total number of observed CEO changes that were made during the period 1995 to 2004.

[51] Pourciau (1993), Wells (2002)

Table 1

Summary of CEO turnover data

Panel A. Changes per year.

	CEO changes	
Financial Year	No.	%
1995	6	7.50%
1996	5	6.25%
1997	12	15.00%
1998	12	15.00%
1999	8	10.00%
2000	10	12.50%
2001	8	10.00%
2002	9	11.25%
2003	7	8.75%
2004	3	3.75%
Total	80	100.00%

Panel B. CEO turnovers divided by sector classification.[52]

Sector	No. of CEO changes	%	No. of Companies	%	No. of Companies (including excluded obs.)	%
Energy	1	1.25%	1	1.58%	1	0.84%
Materials	8	10.00%	7	11.11%	11	9.24%
Industrials	33	41.25%	26	41.27%	40	33.62%
Consumer Discretionary	12	15.00%	7	11.11%	14	11.76%
Consumer Staples	2	2.50%	2	3.18%	4	3.37%
Health Care	3	3.75%	3	4.76%	3	2.52%
Financials	12	15.00%	11	17.46%	31	26.05%
Information Technology	9	11.25%	6	9.53%	13	10.92%
Telecommunication Services	0	0.00%	0	0.00%	2	1,68%
Utilities	0	0.00%	0	0.00%	0	0.00%
Total	80	100.00%	63	100.00%	119	100.00%

[52] Classification made using the OMX Nordic Stock Exchange guide lines.

Table 2

Nature of CEO changes determined by reviewing press releases, annual reports and newspaper articles.

Nature of CEO Change	No. of changes	%
Routine	57	71.25%
Non-routine	20	25.00%
No info	3	3.75%
Total	80	100.00%

6 Results

This section presents the test results. First, in Section 6.1 the results from the tests examining earnings management are presented followed by Section 6.2 which presents the results from the tests examining impressions management.

6.1 Earnings Management

Table 3 presents descriptive statistics for the 80 firms included in the sample and the table shows significant differences between the firms. The sample includes small cap, mid cap as well as large cap companies.

Table 3 also shows how company earnings and revenues evolve over a three-year period surrounding a CEO-turnover. The data shows a general pattern of a reduction of mean earnings in the year of the change, year t, and increasing mean earnings in the year following the change, year t+1. Thus, earnings form a V-pattern which is graphically displayed in Figure 1 and also verified through a non-parametric sign test presented in Table 3, Panel B. The sign test examines whether earnings are more likely to display a V-pattern than the opposite and the test shows a highly significant p-value. Revenues on the other hand, although on average showing a slight decrease in the year of the change, seem to be fairly stable over the observed three-year period. This is verified through a non-parametric sign test

presented in Table 3, Panel B, showing highly insignificant values. Moreover, as mentioned in Section 4 the sample constitutes of observations equally spread over a 10 year period. This gives further strength to the observed V-pattern since business cycle factors are less likely to affect the result.

Table 3

Characteristics of Earnings

Panel A. Descriptive Statistics of Company Earnings.

	Mean	Median	Max	Min
Year t-1				
Net Profit After Tax mSEK	1089.90	380.40	13041.00	-19013.00
Total Assets mSEK	32718.37	8870.50	320766.32	97.65
Year t				
Net Profit After Tax mSEK	897.79	270.00	12130.00	-10844.00
Total Assets mSEK	33270.46	9077.50	335083.80	48.23
Year t+1				
Net Profit After Tax mSEK	1625.55	394.65	21018.00	-7946.12
Total Assets mSEK	33577.26	9611.50	305961.88	53.17
	Mean	Median		
Year t-1				
Net Profit After Tax Deflated by Total Assets t-2	0.05686	0.04944		
Revenues Deflated by Total Assets t-2	1.17337	1.04157		
Year t				
Net Profit After Tax Deflated by Total Assets t-1	0.03528	0.04435		
Revenues Deflated by Total Assets t-1	1.16977	1.12014		
Year t+1				
Net Profit After Tax Deflated by Total Assets t	0.05572	0.04759		
Revenues Deflated by Total Assets t	1.17848	1.11209		

Panel B. Non-parametric sign test of how earnings and revenues evolve over a period of three years surrounding a CEO turnover. The test examines if the earnings and revenues from year t-1 to t+1 form a "V-pattern".

		z-statistic (p-value)
Net Profit After Tax (Pattern) $n_{V\text{-shape}}$: $n_{\Lambda\text{-shape}}$	32:17	(0.00454)
Revenues (Pattern) $n_{V\text{-shape}}$: $n_{\Lambda\text{-shape}}$	19:28	(0.9566)

Figure 1

Graph of the V-pattern illustrating fluctuations in mean deflated net profits for the years surrounding the CEO change.

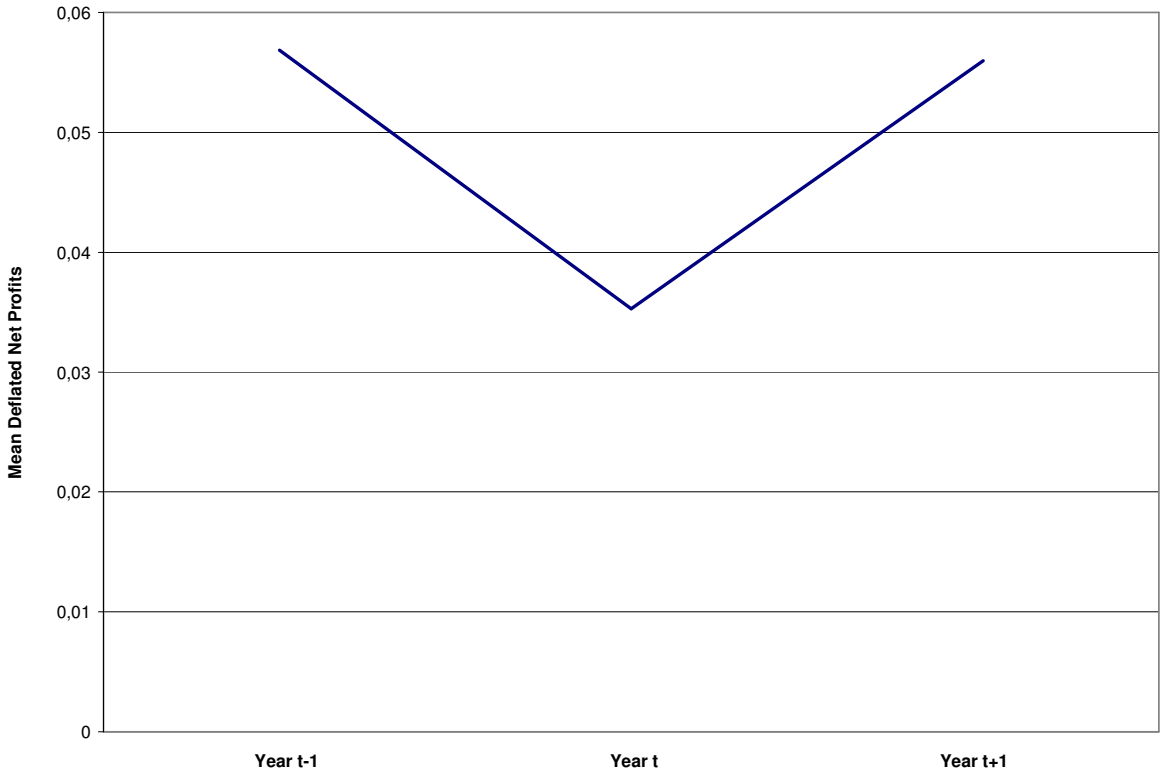

Table 4 summarizes the data and the tests performed on accruals in association with CEO turnovers. The data presented in Panel A shows that, on average, unexpected accruals is negative in the year of the change, year t, and positive in the year following the change, year t+1. The median values also describe this pattern as negative unexpected accruals are found

in the year of the change and positive unexpected accruals are found in subsequent year. The t-tests as well as the Wilcoxon Rank Sum tests presented in Table 4, Panel A, verify this impression as they all show highly significant results. These results indicate on accruals management generating negative unexpected accruals in year t and positive unexpected accruals in year t+1. Furthermore, as can be seen in Panel A, more observations are showing negative unexpected accruals than positive ones in the year of the turnover. The reverse is found in the year following the change.

In Table 4, Panel B, the firms have been divided into either routine or non-routine CEO turnovers. The mean and median values for the two sub samples are opposite to the results one could expect from hypothesis h5 stated in Section 3. The mean and median unexpected accruals are lower for the routine sub-sample than for the non-routine sub-sample in year t the and higher in the following year. Furthermore as can be seen in Table 4, Panel B, none of the Mann Whitney U-tests shows significant values. These tests are used to determine if the mean of unexpected accruals in year t is more negative for the firms experiencing a non-routine turnover than for the companies experiencing a routine change and if the opposite is true for year t+1.

Table 4

Summary of Unexpected Accruals

Panel A. Descriptive statistics of unexpected accruals.

	Mean	Median (p-value)	t-statistic [a] (p-value)	z-statistic [b]
Unexpected Accruals$_t$ Deflated by Total Assets	-0,02345826	-0,02428512	-1,931351558 (0.0286)[d]	
Unexpected Accruals$_{t+1}$ Deflated by Total Assets	0,045075183	0,012930068	2,409255984 (0.0092) [d]	
Positive: Negative$_t$	31:49			-2,49886563 (0,0064) [d]
Positive: Negative$_{t+1}$	48:32			-1,98086661 (0,0239) [d]

Panel B. Unexpected Accruals, Routine vs. Non-routine.

	Mean	Median	t-statistic [a] (p-value)	z-statistic [c] (p-value)
Routine				
Unexpected Accruals$_t$ Deflated by Total Assets	-0,034802479	-0,03023788		
Unexpected Accruals$_{t+1}$ Deflated by Total Assets	0,057144316	0,01229471		
Non-Routine				
Unexpected Accruals$_t$ Deflated by Total Assets	0,003752416	-0,02144929		
Unexpected Accruals$_{t+1}$ Deflated by Total Assets	0,00744092	-0,00052348		
Testing the difference of sample means Routine versus Non-Routine				
Routine: Non-Routine$_t$			Not significant [d]	Not significant [d]
Routine: Non-Routine$_{t+1}$			Not significant [d]	Not significant [d]

[a] Tests that mean unexpected accruals <0 (>0).
b Calculated from the non-parametric Wilcoxon Rank Sum Test. Tests that the number of positive (negative) unexpected accruals is greater than the number of negative (positive) unexpected accruals.
[c] Calculated from the non-parametric Mann Whitney U-test examining the hypothesis that the central location of the two populations differ.
d One-tailed significance levels.

Table 5 describes the data and the tests performed on write-downs made in relation to CEO-turnovers. As can be seen from Panel A unexpected write downs are on average negative in the year of the turnover, year t, and positive in the year following the change, year t+1. The median, however, shows a less pronounced difference between these values. The t-tests as well as the non-parametric Wilcoxon Rank Sum tests support this impression as they all show highly significant values. Moreover, the data shows that the number of observations showing negative unexpected write downs in year t is almost four times as many as the number of observations showing positive unexpected write downs. In the following year the number of observations showing positive unexpected write downs is almost twice as many as negative ones.

A Mann-Whitney U-test is performed in order to find potential differences between routine and non-routine turnovers concerning the use of write-downs. The results from these tests are presented in Panel B showing non-significant values. Furthermore, looking at the t-tests for the two sub samples the mean values clearly describes a pattern of negative unexpected write-downs in the year of the change and positive write downs in the year following the change. However, as opposed to hypothesis h5 stated in Section 3 the mean values of the routine turnovers show a much more pronounced difference between the two years than the mean values of non-routine turnovers. Nevertheless, the median values presented in panel B describe just the pattern anticipated by hypothesis h5.

Table 5

Summary of Unexpected Write-Downs

Panel A. Descriptive statistic of unexpected write downs.

	Mean	Median	t-statistic[a] (p-value)	z-statistic[b] (p-value)
Unexpected Write Downs$_t$ Deflated by Total Assets	-0,016040531	-0,000466979	-2,599679753 (0.0057)[d]	
Unexpected Write Downs$_{t+1}$ Deflated by Total Assets	0,014640702	0	2,202027325 (0.0153) [d]	
Positive: Negative$_t$	11:41			-4,608099856 (0,00) [d]
Positive: Negative$_{t+1}$	32:18			-2,756542363 (0,0029) [d]

Panel B. Routine vs. Non-routine

	Mean	Median	t-statistic[a] (p-value)	z-statistic[c] (p-value)
Routine				
Unexpected Write Downs$_t$ Deflated by Total Assets	-0,019203838	0		
Unexpected Write Downs$_{t+1}$ Deflated by Total Assets	0,014971538	0		
Non-Routine				
Unexpected Write Downs$_t$ Deflated by Total Assets	-0,00867815	-0,002536704		
Unexpected Write Downs$_{t+1}$ Deflated by Total Assets	0,014327644	0,002866698		
Testing the difference of sample means Routine versus Non-Routine				
Routine: Non-Routine$_t$			Not significant [d]	Not significant [d]
Routine: Non-Routine$_{t+1}$			Not significant [d]	Not significant [d]

[a] Tests that mean unexpected accruals <0 (>0).
[b] Calculated from the non-parametric Wilcoxon Rank Sum Test. Tests that the number of positive (negative) unexpected accruals is greater than the number of negative (positive) unexpected accruals.
[c] Calculated from the non-parametric Mann Whitney U-test examining the hypothesis that the central location of the two populations differ.
[d] One-tailed significance levels.

6.2 Impressions Management

Table 6 presents the descriptive statistics from the sign test for the impressions management variable selectivity. The p-value for negative selectivity in year t is not significant and, thus, does not indicate on unfavorable impressions management in the year of the turnover. In the year following the CEO change, year t+1, a significant p-value for positive selectivity in graphed key financial variables is found indicating on favorable impressions management in that year. In the left column the number of favorable as well as unfavorable changes out of the total sample of 80 observations made for each year is presented. In the right column of the table one can find the p-values. As can be seen in the left column only 21 respectively 16 out of the total 80 observations each year engage in some kind of selective use of graphs. Due to the small number of companies actually changing their graphs of key financial variables no subdivision into routine and non-routine CEO turnovers is made when examining impressions management.

Table 6

Impressions Management

The table displays the results from a non-parametric Sign Test made on key financial variables graphed and selectivity. A total of 80 observations were used each year.

		z-statistic[a] (p-value)
Favourable:Unfavourable$_t$	8:13	0,1376
Favourable:Unfavourable$_{t+1}$	12:4	0,0227

[a] Calculated from the non-parametric Sign Test.

7. Analysis

In this section the results presented in Section 6 are analyzed using the theoretical foundation presented in Section 2. The section begins with an analysis of potential earnings management. Thereafter potential impressions management is analyzed.

7.1 Earnings Management

The results presented in Table 3 in Section 6.1 clearly display that earnings are reduced in the year of the turnover and increased in the year following the turnover, forming a V-pattern. Although revenues show a slight tendency of forming a similar pattern revenues cannot be held as the main explanatory variable for reduced earnings in the year of the CEO turnover. Compared to the year prior to the change mean net profits deflated by one year lagged total assets are reduced by approximately 38%. In the same time period mean revenues deflated by one year lagged total assets are reduced by less than 0.5%. In the year following the turnover mean net profits deflated by one year lagged total assets show an increase of almost 58%. During the same period revenues increase by approximately 0.7%. These findings therefore support hypotheses h1c and h3c suggesting that revenues are held fairly constant over the observed time period. By dividing the change in revenues deflated by one year lagged total assets for one year by the change in earnings deflated by one year lagged total assets for that same year one can extract the proportion of observed change in earnings that can be explained by fluctuations in revenues. Thus, approximately 17% of the earnings drop in the year of the turnover and 43% of the increased earnings in the subsequent year can be explained by fluctuations in revenues. In short, earnings are reduced by 31.5% [(1-0.17)*0.38] due to costs taken in the year of the CEO turnover. Earnings increase in the year subsequent to the CEO turnover by 33% [(1-0.43)*0.58] due to cost reductions. These results are interesting since there seems to be great potential for earnings management through moving costs between the two periods and thus to affect the outcome of performance based compensation contracts linked to accounting data. Since, on average, approximately 30% of earnings have been found altered by managing costs and keeping in mind that changes in earnings affect the compensation of CEOs, such discretionary practice must be seen as

economically significant for CEOs to engage in. In Sweden pay practices between companies and their CEOs are not public data. It is therefore hard to estimate the exact economic magnitude this kind of behaviour might have. However, it is empirically established that a large part of the total compensation paid to CEOs comprises of performance-based compensation linked to accounting data.[53]

In line with hypotheses h1c and h3c revenues do not seem to show the pronounced V-pattern that earnings do. This is also verified by a non-parametric sign test performed on revenues presented in Table 3, Panel B, examining the occurrence of a V-pattern. The sign test shows a highly insignificant value. Hence, from the discussion above there seem to be an earnings reducing effect that can be derived from the cost side in the year of the change which may indicate on the CEOs taking an "earnings bath" that year. To further investigate this, accruals are examined in relation to CEO turnovers. According to hypothesis h1a, large negative unexpected accruals should be found in the year of the change contributing to reduced earnings. The values presented in Table 4, Panel A, support the hypothesis as the mean unexpected accruals are negative and highly significant in the year of the turnover, using both a parametric t-test and a non-parametric Wilcoxon Rank Sum Test. Furthermore, hypothesis h3a suggests that unexpected accruals should be positive in the year following the turnover, thus contributing to increased earnings. The data presented in Table 4, Panel A, also support this hypothesis as the mean unexpected accruals are positive and highly significant using both a parametric t-test and a non-parametric Wilcoxon Rank Sum Test. In fact, accruals seems to be a widely used tool for attributing costs to different accounting periods among the firms included in the sample and, thus, accruals seems to be a widely used tool for managing earnings. This is in line with prior non-Swedish studies that have found accruals to be an important tool for earnings management.[54] Empirical evidence, mainly found in the US has indicated that incoming CEOs are managing accruals in order to decrease earnings in the year of the CEO change followed by upwards earnings management in the years that follow to give a more favourable impression of their performance.[55] One

[53] Jensen (2001)
[54] Merchant (1990), Jones (1991), Pourcaui (1993), McNichols (2000)
[55] Watts & Zimmerman (1978), Murphy & Zimmerman (1993)

outcome of this kind of behaviour is a potential increase in their performance based compensation linked to accounting data.[56]

Hypothesis h1b suggests that unexpected write downs will reduce earnings in the year of the change. This hypothesis gains support from Table 5, Panel A. The table presents results from a t-test and a non-parametric Wilcoxon Rank Sum Test that both show significant values, indicating that firms actually use unexpected write downs to reduce earnings in the year of the change. In the year subsequent to the CEO turnover the results are as anticipated by hypothesis h3b. Table 5 shows statistically significant values indicating positive unexpected write-downs that year. However, it also shows mean values of unexpected write-downs deflated by lagged total assets that are considerably lower than mean unexpected accruals deflated in the same manner even though Section 2.2.1 implies that it would be the other way around. An explanation for this might be that only approximately 75 percent of the firms included in the sample actually used write downs during the period. According to the accruals definition of this paper all firms use accruals. Furthermore, as can be seen in Table 5 the sample median for write downs is zero. Since firms not using write downs are still included in the sample this has an effect on the mean unexpected write downs by reducing the values. Hence, although not as widely used as accruals, write downs seems to be a frequently used tool for managing costs and, thus, earnings among the firms included in the sample. In short, Table 5, Panel A, presents evidence consistent with downward earnings management at the time of the CEO turnover and upward earnings management in the following year. These findings are also in line with several US studies that have found increasing write downs in association with CEO turnovers.[57] These studies suggest that taking on large write downs in the year of the change is a way for a newly appointed CEO to blame predecessors for poor past performance and consequently to create a favourable platform for positive earnings development in years to come. However, as suggested above, earnings management undertaken through this mechanism should be relatively easy to identify in the year that it is undertaken compared to accruals. Potential benefits from this

[56] Watts & Zimmerman (1978), Merchant (1990), Jensen (2001)
[57] Moore (1973), Strong & Mayer (1987), Elliot & Shaw (1988)

kind of behaviour should therefore be more limited. [58] One would therefore not expect CEOs to use write downs as the primary tool for discretionary earnings management.

Previous research has pointed out that the probability of a CEO change occurring increases significantly as corporate performance is relatively poor.[59] This constitutes a problem for the interpretation of the results. When a company is performing poorly there are potential needs for restructuring and taking on considerable restructuring costs might be necessary which will affect earnings negatively. Therefore, by looking at a restructuring situation, it is hard to draw reliable conclusions whether costs are taken by the newly appointed CEO as a remedy for prior poor economic performance or because of management opportunistic behaviour. Moreover, in a scenario when a company is performing poorly revenues will most likely on average be a major cause of reduced earnings. However, as illustrated in Table 3, firms included in the sample seem to be rather well-performing throughout the entire observation period. Panel A shows positive mean values for earnings after tax. During the same time period revenues stay relatively stable and only a small portion of the earnings decrease can be attributed to reduced revenues. Furthermore, one can argue that companies engaging in earnings management in order to smooth earnings would do so by increasing costs in the year of the change, thus taking a cost bath, without reducing revenues. Reducing revenues involves operations that are hard to reverse and could be detrimental for the company. The reduction in mean revenues that is seen in the year of the change is therefore probably an effect derived from companies included in the sample that actually performs poorly. Moreover, as illustrated in Table 3, a cost reduction as well as a slight revenue increase is detected in the year following the turnover. The cost reduction is hard to evaluate. If necessary restructuring costs were taken by the newly appointed CEO in the year of the change, costs would most likely have peaked during this year. Hence, the new CEO would thus be better at tracking costs and a cost reduction would therefore be expected in the year following the CEO turnover. If costs were taken in order to deliberately manage earnings in the year of the turnover, this will most likely generate a similar cost reduction in the year subsequent to the change. Either way, costs are expected to decrease and revenues to increase from the previous year making it hard to distinguish between discretionary earnings

[58] Defond & Jiambalvo (1994)
[59] Murphy & Zimmerman (1992), Coughlan & Schmidt (1985), Warner et al. (1988), Weisbach (1988).

management and restructuring costs taken in association with the appointment of a new, more capable CEO.

Thus the V-pattern illustrated in Figure 1 might have to possible explanations. First, as already discussed above is the one of opportunistic managers engaging in earnings management in order to affect accounting data and thus to boost their performance-based compensation. Another possible explanation might be that the departing CEO has been performing poorly and is replaced by a better suited successor, more capable of running the company by for example tracking and cutting costs. This is somewhat contradicted since the sample in this study consists largely of routine turnovers and one could doubt for example the likelihood that the board of directors would wait for the old CEO to retire if they could find a better suited person in advance. Prior research has examined the effect of a CEO turnover on firm performance subsequent to the turnover. Some research has found negative relationship between CEO turnovers and performance. An explanation for this would be that changing CEO causes disruptive effects on an organization's processes and routines, which affect performance negatively.[60] Other researchers have suggested that changing CEO is a critical mechanism of organizational adaptation. It provides an occasion to replace decision makers with others who are better suited for dealing with the firm's critical issues.[61] A third view on the subject suggests that changing CEO has no effect on the firm performance since firm performance is a function of the firm-specific processes which to a large extent is outside the control of managers.[62] Finally, complementing these views on the subject, a study argues that the degree of organizational disruption created by the circumstances around the predecessor CEO's departure (e.g. non-routine versus routine turnover) and the potential for organizational change existing within the company are important factors affecting firm performance subsequent to the turnover.[63] Based on the discussion above there is little evidence that newly appointed CEOs in general can affect the corporate performance solely based on their competencies. Moreover research has presented evidence in recent years that corporations increasingly are seeking CEOs who are charismatic, well known and whose

[60] Grusky (1963)
[61] Pfeffer and Salancik (1978)
[62] Gamson and Scotch (1964)
[63] Khurana & Nohria (2000)

personality impresses analysts.[64] Thus, the task of finding CEOs whose experience and abilities are right for companies' specific needs has become less important. In short, there is little evidence supporting the hypothesis that newly appointed CEOs in general are more capable of running the company and thus acts as the company's saviour when appointed. Consequently, it is not likely that the earnings pattern observed in the years surrounding the CEO turnovers examined in this study can be explained by the competence of the newly appointed CEO.

For the 57 turnovers classified as routine, mean accruals deflated by total assets as well as mean write downs deflated in the same manner show the anticipated V-pattern. This is illustrated in Tables 4 and 5. However, as can be seen from the same tables, mean accruals deflated by total assets do not show this pattern for non-routine turnovers. Moreover, the difference between the two samples are not consistent with hypothesis h5, suggesting that earnings management should be more pronounced for turnovers classified as non-routine. The t-tests as well as the non-parametric Mann-Whitney U-tests provide further evidence presented in Tables 4 and 5 against hypothesis h5. This does not concur with previous research suggesting that incentives for earnings management are greater for non-routine turnovers than for routine.[65] However, the results presented in this paper may suffer from flawed data. For example, the size of the sample may be too small to subdivide. To a large extent the total sample consists of routine turnovers and the non-routine sub-sample is therefore very small. The non-routine sample consists of only 20 observations which imply that single observations will have high impact on the results. Moreover, the 20 observations form a sample that is too small for extracting data in order to draw reliable statistical conclusions about non-routine turnovers in general. Another explanation for the results presented in Tables 4 and 5 might be that CEOs are as likely to engage in earnings management under routine circumstances as under non-routine circumstances. Moreover, taking into account that more than 70 percent of the sample consists of routine CEO turnovers, this suggests that poor performance is not the underlying cause of most of the turnovers included in the sample. Thus earnings management seem to be a frequently used

[64] Khurana (2002)
[65] Pourciau (1993)

practice in association with routine turnovers although not recognised by some prior research.[66]

7.2 Impressions Management

This paper includes so called impressions management variables in order to be able to draw better conclusions about whether observed accounting behaviour are due to management opportunism or in fact by accurate reporting of overall economic performance. Section 3 presents two hypotheses, h2 and h4, suggesting that companies engage in impressions management through selective use of key financial indicators graphed in annual reports. An unfavourable selection of graphed indicators in the year of the change will weaken the image of the firm performance (h2). A favourable selection of graphed indicators in the year subsequent to the change will strengthen a favourable image of the firm performance (h4). The results presented in Table 6 support these hypotheses to some extent as they show a significant value for year t+1. However, the p-value for year t is not significant. As can be seen from Table 6 the results are extracted from less than 25 percent of the total sample and these values should therefore be interpreted with scepticism. In fact, these findings imply that roughly 75 percent of the companies included in the sample have not made any changes in variables graphed. Nevertheless, the companies that made changes did so at least in period t+1 to a large extent in the way predicted by the hypothesis. However since the number of companies changing their graphs is so small that could be purely coincidental. As stated earlier only 21 companies in the year of the change and 16 companies in the subsequent year out of the total sample of 80 companies did some kind of change in their key financial variables graphs. Taking this into consideration the test results for selectivity loses much if not all of their significance. Hence, the results show little support for hypotheses h2 and h4 and the pattern suggested by the theoretical foundation in Section 2.3. Although there seem to be evidence for earnings management taking place among the firms that constitute the sample, managing impressions by being selective in the graphs presented seem to be a less employed practice. A number of possible explanations for these findings are discussed below.

[66] Pourciau (1993)

When looking at the results presented in Section 6 it seems like the importance of impressions management has been overrated. How graphs effect financial statement users' perceptions is, however, a well documented area.[67] Looking at the general conclusions presented in these studies they all state that the choice of graphs presented and potential distortions of these have significant impact on the impressions of management's performance. The extent to which impressions are affected varies with the context and the type of decision.[68] Still, graphical presentation of financial information seems to have negligible effects on users of financial statements published by Swedish corporations. Compared to many studies made abroad these findings differ. One study made on U.S. firms concluded that these firms were more likely to include graphs of key financial variables as performance improves.[69] However, more recent papers do not find such an association.[70] Other studies made in a U.K. context also found a relation between selective management behaviour and performance.[71] An explanation for the rather mixed findings could be that impressions management have the greatest impact on laymen and not on professional investors acting in the market. The large institutional investors make up a majority of the market and these are probably more likely to base their investment decisions on facts and will not be fooled by impressions of graphs presented in annual reports. The rather weak findings on selectivity as an impressions management variable in Sweden could also be explained by that there might be other forms of impressions management practises are preferred to selectivity. Moreover, since these findings show little support for hypotheses h2 and h4, the evidence found on earnings management could in fact indicate on actual restructuring work than managers trying to boost performance-based salaries linked to accounting data. If the companies also had managed their graphs it would have been easier to argue that fluctuations in earnings and in underlying variables affecting earnings are due to discretionary behaviour. In short, the relatively weak findings of impressions management also makes it impossible to perform a meaningful cross sectional analysis that will simultaneously consider both the earnings and impressions management concepts. Even if

[67] Lewandowsky & Spence (1989), Steinbart (1989), Beattie & Jones (1992)
[68] Schulz & Booth (1995)
[69] Steinbart (1989)
[70] Frownfelter & Fulkeson (1998)
[71] Beattie & Jones (1992; 2000a)

the results of period t+1 would be considered significant, 12 firms is not enough to constitute a statistically reliable sample.

8 Conclusions

This paper aims to investigate whether CEOs undertake earnings management in association with CEO turnovers for Swedish corporations listed on the Stockholm Stock Exchange A-list during the years 1995 to 2004. It presents strong evidence of earnings management in the form of accruals management as well as in the form of write downs management both in the year of the CEO turnover and in the year following the turnover. However, this paper cannot with certainty determine whether observed earnings management are due to managers behaving opportunistically at the expense of the shareholders in order to boost accounting-based compensation or if observed earnings management are due to necessary costs taken as a result of the financial position of the company. Moreover, impressions management in the form of selective usage of key financial variables graphed cannot be empirically verified in this paper. Since little evidence of impressions management are found, the cross-sectional analysis that was intended to jointly analyse earnings and impressions management in relation to CEO turnovers could not be pursued.

This paper also examines whether earnings management is more frequently used in association to non-routine CEO turnovers than to routine CEO turnovers. The study finds no empirical evidence supporting this hypothesis. This is somewhat contradictory to what could be anticipated by theory and previous research which could be explained by the small data sample for non-routine turnovers. Nevertheless, the little evidence found of differences in accounting behaviour between routine and non-routine CEO turnovers give indications on that there are in fact no considerable differences present. The fact that earnings management is found even though the sample consists to a large extent of routine turnovers is interesting since it indicates that routine turnovers are well worth investigating in an earnings management context.

This is the first study specifically examining earnings management in association with CEO turnovers in Swedish corporations. The findings are interesting since they indicate that earnings are being managed as a CEO turnover takes place. This is in line with studies performed outside Sweden and also in line with theories covering the subject. The study has shown that a significant part of the corporate results can be altered. Since, a large part of the compensations enjoyed by CEOs are based on accounting measures, mostly related to earnings, managers do benefit from managing earnings. It is therefore to a large extent advisable to avoid the use of compensation contracts linked to accounting data.

9 Methodological Discussion

This paper investigates the occurrence of earnings management in association with CEO-turnovers in Swedish corporations listed on the Stockholm Stock Exchange A-list. The results presented indicate on existing earnings management. However, similar to all prior studies the results presented in this paper suffers from the problem of differentiating between what is "normal" earnings management and what is deliberate and discretionary earnings management. A significant element of the models trying to measure potential discretionary earnings management is a strong prediction about the behaviour of earnings around the target which is not plausibly due to nondiscretionary forces. The rather simple classification of unexpected accruals used in this study is correct and widely used. However, the definition is dependant on a number of assumptions stated in Section 4.1.1 above. Furthermore, there is a gap between our institutional knowledge and empirical procedures. For instance, even with a general characterization of the behaviour of accruals absent discretion, there is far more richness in the behaviour of accruals than simple models allow.[72] There is the potential to reduce this gap through the use of better research designs and measures of discretionary behaviour which condition on more information than the prior literature has attempted. However, the models developed in this paper as well as in others are still too simple.

Finally, this paper focuses on examining earnings management in a general Swedish context. Therefore the whole sample has been studied without subdividing it into smaller groups

[72] McNichols (2000)

based on for example size or industry. This is in line with several other studies. Some, however, have divided the sample after size arguing that size will affect the opportunity to manage earnings. Moreover, most studies have excluded financial institutions because of their nature and a few studies have divided the sample by industry. Dividing the sample by industry would be justified because firms with greater earnings growth have been found to be more likely to have greater accruals.[73] Moreover, firms operating in different industries might be affected by industry cycles, which might be necessary to control for. Thus with a more thorough classification this paper might have found additional insights about the occurrence of earnings management in specific industries. This could plausibly have provided information facilitating the detection of potential discretionary behaviour.

10 Suggestions for Further Research

This paper has attempted to provide a comprehensive analysis of the earnings management concept in association with CEO turnovers in a Swedish setting. Despite the large amount of research related to the area, there still remain several aspects to be investigated, especially put into a Swedish context. In future studies one could further develop this thesis' findings in mainly three areas discussed below.

First, as stated above there might be interesting insights to gain by subdividing the sample by firm size and industry. This could plausibly yield a better understanding of the entire earnings management concept by looking at potential differences between companies of different scales and industries. However, subdividing the sample would probably yield too small sub-samples. Doing this would therefore require a bigger initial sample by for example including firms from the former O-list.

Second, in general there is a need for further research on the factors that motivate managers to manipulate earnings, and for this understanding to be better reflected in our empirical methods as discussed in Section 9. This paper have illustrated evidence of earnings management in Swedish companies in association with CEO turnovers without being able to

[73] McNichols (2000)

determine with certainty the kind of incentives behind this kind of behaviour. A better understanding of why managers manipulate earnings will allow researchers to assess the power of alternative earnings management tests, and ultimately strengthen our understanding of the implications of earnings management for investors and other contracting parties.

Finally, are earnings management entirely bad for a firm or are there positive effects that can be derived from earnings management? Swedish press has illustrated an impression of earnings management as a phenomenon that is only of negative nature for the specific firm. However, as stated in Section 2.5, managers also have incentives to manage earnings in ways that in fact benefits the company. For example, earnings management is good for the company if it achieves any of the standard goals of corporate finance like raising capital at the lowest cost, reduce the risk exposure and make funds available for value creating projects. Consequently, do the positive effects from earnings management outweigh the negative ones? The non-academic research might in fact be skewed regarding this issue. Of course some firms suffer from non-beneficial earnings management as a consequence of opportunistic management behaviour. This study has approached the problem from perspective based on the principal agent theory, thus from a shareholder-manager perspective. From a shareholder point of view opportunistic earnings management is for the most part detrimental, assuming that managing earnings is not in line with the corporate goals. However, as stated above, it is hard to distinguish between what is opportunistic earnings management and what is not when managing earnings is in line with the corporate goals as well as in the best interest of the CEO. Thus, a more thorough investigation of the aggregated effect of earnings management is justified.

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12 Appendices

A. Data Sample

Table A.1

Summary of CEO changes made on the A-list 1995-2004 included in the study.

Company	List on OMX	New CEO	Replaced CEO	Year of change	Reason for leaving
ABB	A	Göran Lindahl	Percy Barnevik	1996	routine
ABB	A	Jürgen Dormann	Jörgen Centerman	2000	routine
ABB	A	Jörgen Centerman	Göran Lindahl	2002	routine
Aga	A	Lennart Selander	Marcus Storch	1996	routine
Allgon	A	Jan Edhäll	Torsten Körsell	1998	reason uncertain
ASG	A	Jörgen Ekberg	Gunnar Malm	1997	non routine
Assa Abloy	A	Bo Dankis	Carl-Henric Svanberg	2003	routine
Assi Domän	A	Gunnar Palme	Lennart Ahlgren	1999	non routine
Atlas Copco	A	Guilio Mazzalupi	Michael Treschow	1997	routine
Atlas Copco	A	Gunnar Brock	Giulio Mazzalupi	2002	routine
Avesta Sheffield	A	Stuart Pettifor	Per Molin	1996/97	routine
Bilia	A	Kjell Åkesson	Mats Jansson	1999	routine
Bilia	A	Heinrich Blauert	Kjell Åkesson	2003	non routine
BPA	A	Johan Karlström	Rolf Akerlind	1995	reason uncertain
Bure Equity	A	Peter Sandberg	Roger Holtback	2003	routine
Cardo	A	Kjell Svensson	Lennart Nilsson	1997	non routine
Castellum	A	Lars-Erik Jansson	Thomas Alexandersson	2000	routine
Celsius	A	Olof Lund	Åke Plyhm	1995	routine
Celsius	A	Lars G Josefsson	Olof Lund	1997	routine
Custos	A	Christer Gardell	Lars Öberg	1996	routine
Electrolux	A	Michael Treschow	Leif Johansson	1997	routine
Electrolux	A	Hans Stråberg	Michael Treschow	2002	routine
Ericsson	A	Kurt Hellström	Sven-Christer Nilsson	1999	routine
Ericsson	A	Carl-Henric Svanberg	Kurt Hellström	2003	non routine
Esselte	A	Jan Kvarnström	Bo Lundquist	1997	routine
Esselte	A	Anders Igel	Jan Kvarnström	1999	routine
Evidentia	A	Kent Gravesen	Dag Klerfeldt	1998	non routine
Finnveden	A	Tommy Boork	Sten Thunberg	2002	routine
Gambro	A	Sören Mellstig	Mikael Lilius	2000	routine
Getinge Industrier	A	Johan Malmquist	Carl Bennet	1997	routine
Hennes&Mauritz	A	Fabian Månsson	Stefan Persson	1998/99	routine
Hexagon	A	Ola Rollén	Börje Andersson	2000	routine
Holmen	A	Göran Lundin	Per Ericson	2001	non routine
Holmen	A	Magnus Hall	Göran Lundin	2004	routine
Hufvudstaden	A	Ivo Stopner	Tomas Billing	1999	routine
Industrivärden	A	Anders Nyrén	Clas Reuterskiöld	2001	routine
Investor	A	Marcus Wallenberg	Claes Dahlbäck	1999	routine
JM	A	Carl Eric Stålberg	Sven Larsson	1995	routine
JM	A	Johan Skoglund	Carl Eric Stålberg	2002	routine
Kalmar Industries	A	Christer Granskog	Jonas Svantesson	1998	non routine
Kinnevik	A	Vigo Carlund	Stig Nordin	1999	routine
Klövern	A	Lars Sköld	Ronald Magnusson	1995	routine
Lindex	A	Jörgen Johansson	Hans Johansson	2000/01	routine

Munksjö	A	Per Rodert	Rolf Ekedahl	2000	non routine
NCC	A	Alf Göransson	Jan Sjöqvist	2001	non routine
Nobel Biocare	A	Heliane Canepa	Jack Forsgren	2001	non routine
OM Gruppen	A	Per E Larsson	Olof Stenhammar	1996	routine
Perstorp	A	Åke Fredriksson	Gösta Wiking	1997/98	routine
Platzer	A	Birger von Hall	Claes Levin	1998	routine
PLM	A	Fredrik Arp	Rolf Börjesson	1996	routine
Sandvik	A	Lars Pettersson	Clas Åke Hedström	2002	routine
SAS	A	Jörgen Lindegaard	Jan Stenberg	2001	non routine
SCA	A	Jan Åström	Sverker Martin Löf	2002	routine
Scandiaconsult	A	Kristina Larsson-Götzén	Olof Hultén	1997	non routine
Scribona	A	Lennart Svantesson	Örjan Håkansson	2000	routine
Scribona	A	Tom Ekevall	Lennart Svantesson	2003	routine
Seco Tools	A	Håkan Bergström	Jan Erik Forsgren	2000	routine
Seco Tools	A	Kai Wärn	Lars Renström	2004	routine
Senea	A	Anette Brodin Rampe	Christer Carlsson	2000	non routine
Siab	A	Lars Wuopio	Jan Jepsson	1995	reason uncertain
Skanska	A	Claes Björk	Melker Schörling	1997	routine
Skanska	A	Stuart Graham	Claes Björk	2002	non routine
SKF	A	Peter Augustsson	Mauritz Sahlin	1995	routine
SKF	A	Sune Carlsson	Peter Augustsson	1998	non routine
SKF	A	Tom Johnstone	Sune Carlsson	2003	routine
SSAB	A	Torsten Sandin	Leif Gustafsson	1998	routine
SSAB	A	Anders Ullberg	Torsten Sandin	2000	routine
Stena Line	A	Bo Severed	Bo Lerenius	1998	routine
Swedish Match	A	Lennart Sundén	Göran Lindén	1998	routine
Swedish Match	A	Sven Hindrikes	Lennart Sundén	2004	routine
Sydkraft	A	Lars Frithiof	Göran Ahlström	1998	routine
Ticket	A	Dag Tveterås	Anders Holst	2000	routine
Ticket	A	Mats Frid	Dag Tveterås	2003	routine
Trelleborg	A	Fredrik Arp	Kjell Nilsson	1998	non routine
TV4	A	Torbjörn Larsson	Krister Forsström	1998	non routine
TV4	A	Jan Scherman	Thorbjörn Larsson	2001	non routine
WM-data	A	Lars Harrysson	Tord Wilkne	1997	routine
WM-data	A	Crister Stjernfelt	Lars Harrysson	2001	routine
Volvo	A	Leif Johansson	Sören Gyll	1997	routine
Ångpanneföreningen	A	Jonas Wiström	Gunnar Grönkvist	2002	non routine

B. Firms Excluded from the Data Sample

Table B.1

Summary of CEO turnovers made on the A-list 1995-2004 excluded from the study and the reasons for exclusion.

Company	List on OMX	Year of change	Reason for excluding observation
Stadshypotek	A	1995	2
J&W	A	1996	4
JP Bank	A	1996	2
Skandia	A	1996	2
United Tankers	A	1996	1
Linjebuss	A	1996	4
Nordström&Thulin	A	1996	4
Evidentia	A	1996	3
Spectra Physics	A	1996	1
Autoliv	A	1996	1
Allgon	A	1997	3
Graphium	A	1997	4
SEB	A	1997	2
Stora	A	1997	1
Sifab	A	1997	1
Hufvudstaden	A	1997	1
Ericsson	A	1998	3
JP Bank	A	1998	2
Scancem	A	1998	4
Ratos	A	1998	4
Föreningssparbanken	A	1999	2
Hemköp	A	1999	4
Seco Tools	A	1999	3
TietoEnator	A	1999	1
Allgon	A	2000	3
Nordea	A	2000	2
Svedala	A	2000	1
Telia	A	2000	1
Holmen	A	2000	3
Axfood	A	2000	1
SHB	A	2001	2
Bure Equity	A	2001	3
Bergman&Beving	A	2001	1
Nordea	A	2002	2
Telia Sonera	A	2002	1
Föreningssparbanken	A	2003	2
Skandia	A	2003	2
Skandia	A	2003	2
OM HEX	A	2003	1
Lindex	A	2004	3

Reason for excluding		Nr excluded
Merger, acquisition or divesture	1	13
Financial institution	2	12
Too many changes	3	8
Lack of data	4	7
Total		40