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A HISTORICAL PERSPECTIVE ON DUTCH AUCTION RATE PREFERRED STOCK

Lynda S. Livingston, University of Puget Sound

ABSTRACT

In February of 2008, the $330 billion auction-rate security market began to fall apart. Brokerage houses that managed the periodic auctions refused to support their issues, so that auctions failed and liquidity disappeared. Investors had a wake-up call: an asset they had thought was a money-market equivalent was in fact something much more risky. In this paper, we consider this current meltdown in light of the 1980s history of Dutch Auction Rate Preferred Stock (DARPS). We conclude that a significant contributor to the recent problems was the marketing of DARPS to individuals, when the security was designed for corporate investors.

JEL: G01, G32, K34

KEYWORDS: Preferred Stock, Auction, Dividends Received Deduction

INTRODUCTION

In early 2008, owners of billions of dollars' worth of auction-rate securities learned that the assets they had presumed to be as safe as money-market assets were, instead, not only quite risky, but also temporarily completely illiquid. The brokerage houses that had been standing behind the securities' rate reset auctions stopped supporting the market, and auctions failed—resulting in no liquidity for investors and in extremely high rates for some issuers. In late summer of 2008, some large brokerages began to promise that they would buy back the auction-rate securities of their retail investors; intervention by regulators soon encouraged other brokerages to do the same.

Retail investors whose accounts were frozen for months blamed brokers for misrepresenting the safety and liquidity of auction-rate securities. Mitigation efforts included demands by investor groups and by government regulators for clearer disclosure. Even now, issuers and investment bankers are scrambling to create acceptable new substitutes, while consumer advocates are demanding explanations.

The liquidity risks inherent in auction rate securities have been well known since their creation in the 1980s. However, they may not have been appreciated by the retail investors who have only recently entered the market. The auction rate market traditionally has been the exclusive province of corporate cash managers, who were able to benefit from the dividends received deduction (DRD). This preferential tax treatment has allowed corporate investors to exclude from taxes up to 85% of the dividends they received. Since corporate investors thus faced a lower effective tax burden on these securities, issuers could offer a lower pre-tax return on them. In short, everybody won. Dutch Auction Rate Preferred Stock (DARPS) was developed in the early 1980s to facilitate this tax benefit-sharing by allowing corporate cash managers to capture dividends with relatively little price risk. However, changing market conditions later in the decade threatened to make the security obsolete. A concerted effort by broker-dealers to extend the market to individual investors saved DARPS from extinction, but at the cost of selling it to investors for whom it was not designed. Coincidentally, as the market expanded to include retail investors, the share of potential benefits accruing to issuers greatly increased.

Since retail investors could not benefit from the DRD, they were simply using DARPS as a cash equivalent. This focus made them especially vulnerable to auction failure. They certainly seemed the

EVIDENCE ON EFFECTIVE TAX RATES IN THE CZECH REPUBLIC

Karel Brychta, Brno University of Technology

ABSTRACT

The paper describes the development of the effective tax of natural persons in the Czech Republic. The analysis covers the period from 1993 to 2009. Two categories of taxpayers are compared: the first a single childless taxpayer, the other a family with two children, where only one spouse earns incomes. The results of the analysis clearly show a gradual, but not steady, decrease in effective tax rates for both categories of taxpayers. For single taxpayers, the effective tax rate decrease is in direct proportion with the amount of tax base. For married taxpayers the effective tax rate decrease is relatively steady for the whole time interval.

JEL: H2; K3; P2

KEYWORDS: Effective tax rate, development, incomes from enterprise, natural person, Czech Republic

INTRODUCTION

The Czech Republic, a relatively small European country, has been classified as a transformation economy. At the beginning of the 1990s, the Czech Republic was a part of the Czech and Slovak Federative Republic. Since 1993 it has been an autonomous country. It has since undergone a number of significant social and economic changes. The ultimate result was transformation from a centrally planned economy to a free market economy. Žídek (2006, p. 4) points division of opinions on the appropriate classification of the previous economic system. Some argue it should be classified as a centrally planned economy, while others argue it should be classified as a biased free market economy. Nevertheless, the extent, importance, and impact these changes had on the Czech economy was, and remains, fundamental and indisputable.

In the context of the abovementioned changes, new opportunities opened for natural persons in the in the form of enterprise and practice of independently gainful activities. Frequent and crucial changes took place during the development, not only in the categorization of these incomes for the purposes of the Trades Licensing Act (see Act No. 455/1991 Coll., on Trade Licensing), but also in the follow-up financial laws, particularly in the Act No. 586/1992 Coll., on Income Taxes (hereinafter Act on Income Taxes). A feature of the latter act, which represents the basic rights and obligations of taxpayers concerning the income taxes of natural persons and legal entities, is its high frequency of changes including changes in nominal tax rates, nontaxable parts of the tax base and tax abatements.

This paper is concerned with the development of the effective tax rate, which represents the impact of relevant regulation on a taxpayer. It is an undisputable fact that a taxpayer primarily perceives the nominal tax rates most dramatically. However, due to other factors such as nontaxable parts of the tax base or eventual tax abatements, nominal tax rates say very little about the amount of real tax burden.

The paper is divided into several parts. The first section gives a brief introduction. Section 2 contains the findings from the literature research that has been carried out regarding the so-called effective tax rate and other related questions. Section 3 gives a general introduction of the Czech Act on Income Taxes. Section 4 lists starting points for the constructed mathematical models, on the base of which the amount of effective tax rate for the taxable periods and the defined categories of taxpayers in focus has been

STABILITY OF RENTS AND RETURNS AS A SOURCE OF INTERNAL FINANCING: EVIDENCE FROM APPALACHIAN COAL PRODUCERS

C. W. Yang, Clarion University of Pennsylvania
Ken Hung, Texas A&M International University

ABSTRACT

The role of steam coal was constrained by the Kyoto Protocol and the Copenhagen Climate Summit which call for reduced emissions of green house gases and related measures. These agreements increase the importance in properly managing emissions. Coupled with rapidly increasing demand from China and India, a study on the rents of the Appalachian coal mines is as important as it is timely. In this paper, we show that response surfaces of producers' surpluses are nonlinear with respect to changes in any parameters. They are closely related to a given flow pattern in which only m+n-l positive coal flows prevail. Only when the flow patterns change does the response surfaces of the producers' surplus undergo structural changes. Production taxes decrease supplier's welfare. Furthermore the result of the Friedman test indicates that the relative welfare position, measured in terms of producers' rents, differs significantly in our simulation.

JEL: B41; C15; H2; M48

KEYWORDS: Appalachian coal producers, rents and returns, internal financing, simulation technique, non-liner response function

INTRODUCTION

A major source of internal finance for producing firms in the Appalachian coal market is the generated rents or producer surplus. Some of the Appalachian areas were economically depressed especially before the era of skyrocketing oil price. Some had bounced back when crude oil price hit close to $150 a barrel. On the other hand, steam coal burning does generate substantial amount of pollution and has been considered one of the culprits of global warming. The main thrust of the Kyoto Protocol and Copenhagen Climate Summit is on the reduction of carbon dioxide emission and imposition of emission fees in terms of carbon tax or related measures. On the global level, a computable general equilibrium model may shed a light on the issue. On national level, however, such a simulation both mathematically consistent and price responsive, is lacking. One approach found successful for analyzing rents on a regional basis is that of spatial allocation modeling. The impact on location rents of Appalachian coal producers, due to changes in taxation policies or economic parameters (environments) in the framework of the spatial equilibrium model (Takayama and Judge 1964, 1971) has not been studied thus far due to the complex nature of the problem. Most of the applications were on shipment pattern of the commodity especially steam coal. In this paper, we first analytically investigate this problem; then we perform some simulations on the stability of rents or returns of the Appalachian steam coal producing regions. The analysis is based on an estimated spatial equilibrium model (Labys and Yang, 1980) from which "optimum" shipments between Appalachian producers and eastern utilities are determined. It is capable of generating a set of optimal coal productions, consumptions, coal flows, and prices which, in turn, permit a calculation of producers' surplus. With the computational aid of a software package (Cutler and Pass, 1971), such simulation can be made conveniently. It is encouraging that we discover some anomalies which contradict the long recognized classical result in the space-less models. Further, in view of current financial stringency at regional levels, the relationship between different taxes and interconnected spatial rents is worthy of a careful evaluation.

The paper is composed of three parts: (1) Mathematical Analysis of the Sensitivity of the Rent, (2) Nonparametric Analysis of the Rent Response Surface via Friedman's Test (M. Friedman, 1937), and (3)

FINANCIAL COMMUNICATION ON THE WEB EVIDENCE FROM BELGIUM

Laetitia Pozniak, University of Mons

ABSTRACT

The ambition of this research is to identify the determinants of internet financial communication of small- and medium-sized firms quoted on non-regulated markets in Belgium. First, a scoring was established to determine the intensity with which firms use the internet as a vector of financial communication. To do this, an analysis grid was built on the basis of a review of the literature, highlighting the rules for disclosure of information through the Web. The score was then regressed via ordinary least squares on variables presented in the literature as determiners of the firms' financial communication. The main results of the findings bring to light three fundamental determiners of this score: membership or not in the information technology sector, the performance of the company and the market on which the company is quoted.

JEL: G10, M15, C31, O32.

KEYWORDS: financial communication, non-regulated financial markets, Web site, Small- and medium-sized firms.

INTRODUCTION

In recent years, the internet has become a privileged channel for current and potential investors to collect financial information. For year 2006, Léger (2008, p. 91) notes that 83% of individual investors were internet users, versus 57% in 2002. The proportion of potential investors and shareholders surfing the web in search of financial information has thus increased exponentially. Internet, a real tool for managing the investor relationship, therefore allows the financial community and the public investor to evaluate companies by providing financial information to them (Barredy and Darras, 2008, p. 3). Almilia and Budisusetyo (2008) even assert that traditional company reports on paper are outmoded.

The originality of the study presented here resides in its research object. Our analysis concerns small- and medium-sized firms quoted on the unregulated markets in Belgium: Alternext and the Free Market. Those markets are relatively recent and, to our knowledge, have not yet been the topic of such a research project. Inspired by the English Alternative Investment Market ("AIM"), Alternext Paris was launched in May 2005. Alternext Brussels followed in June 2006. The Free Market was elaborated in November 2004 by Euronext Brussels on the model of the Free Market established in the Paris Stock Exchange in 1996.

The Free Market et. alternext have been legally considered MTFs (multilateral trading facilities) since November 1st, 2007. They are unregulated markets in the sense of the European directives and Belgian financial legislation. Companies listed on these markets are not forced to publish their accounts in the IAS / IFRS standards or to conform to the Belgian Code of Governance.

The Free Market of Euronext Brussels includes twenty-eight companies. It was created to answer the accessibility difficulties of companies that did not have a minimal market capitalization of 50 to 75 million euros. "No precondition, no anteriority of the accounts and no minimal percentage of distribution are required for registration on the Free Market" (Goldberg-Darmon, 2006). In matters of communication, companies listed on this market are subject to more flexible rules (Euronext, 2008). Alternext Brussels counts nine firms. On this unregulated but organized market, certain conditions have to be met for

MARKET CONCENTRATION MEASURES AND INVESTMENT DECISIONS IN MEXICAN MANUFACTURING FIRMS

Antonio Ruiz-Porras, University of Guadalajara
Celina López-Mateo, University of Guadalajara

ABSTRACT

We study how different measures of market concentration explain investment decisions of Mexican manufacturing firms. The Herfindahl-Hirschman Index is the traditional measure of market structure concentration. The Dominance Index is a competition measure used by Mexican regulators. The econometric assessments suggest that investment decisions of Mexican firms can be better explained by the Dominance Index than by the Herfindahl-Hirschman Index. Thus our results suggest that the Mexican Dominance Index might be useful as a measure of market structure and competition. The results also suggest that market concentration reduces investment. These conclusions are based on several econometric assessments.

JEL: L40; L22; L60

KEYWORDS: Dominance Index, Herfindahl-Hirschman Index, Investment, Mexico, Manufacturing

INTRODUCTION

Traditional economic theory indicates that the maximization of profits explains the behavior and decisions of firms. Particularly, from the view of financial economics, firms are considered as flows of financial streams that depend on investments. Such view explains why the study of optimal investment decisions and their determinants is considered an important research field for economists.

Here we study the determinants of investment decisions in Mexican manufacturing firms because studies for emerging economies are relatively scarce. Particularly, we focus on how market concentration, as a proxy of market structure and competition, influences investment decisions. The assumption underlying our study is that Mexican firms face constraints imposed by its competitors and by nature.

In the literature, competition constraints are analyzed with market concentration indexes. In this study we follow this practice. The Herfindahl-Hirschman Index (HHI) is the usual measure of competition. However it is not the only one. An alternative measure is the Dominance Index (DI) proposed by Garcia Alba (1990). The main difference between these measures is that the DI explicitly accounts the size of firms to measure competition.

We analyze how these two measures of market concentration may explain investment decisions of Mexican manufacturing firms. We focus on micro, small, medium and large size firms. We control for certain firm characteristics that capture the constraints that firms face by nature. They include firm size, cash flow, capital intensity and investment opportunities.

The contributions of this research focus on two areas. The former contributions relate to the literature on investment determinants. Traditional studies focus on developed economies, not in emerging ones. The second contribution is methodological. To the best of our knowledge, econometric comparisons of the HHI and the DI as market concentration measures do not exist.

ADDITIONAL EVIDENCE ON UNIVERSITY RANKINGS BY COST OF LIVING ADJUSTED FACULTY COMPENSATION

Terrance Jalbert, University of Hawaii at Hilo
Mercedes Jalbert, The Institute for Business and Finance Research
Lucila Zarraga, Universidad de Caribe

ABSTRACT

This paper ranks 500 universities and colleges based on compensation paid to their faculty. The analysis examines universities both on a raw basis and cost of living adjusted basis. This work extends the previous literature by examining a broader group of schools. This research includes private universities and community colleges. Most previous literature is limited to the examination of public universities. Similar to previous papers, the results here show that cost of living adjusted salaries differ dramatically from raw salary figures. The results suggest that administrators should design compensation packages that reflect cost of living realities in their area. Faculty seeking employment opportunities should carefully consider cost of living issues.

INTRODUCTION

Faculty in the academic job market must assess a number of factors when evaluating a job offer. Faculty must aggregate information on these factors using their own weighting scheme to make an informed decision. One important factor is financial compensation. Comparing salary offers from multiple institutions is difficult at best due to differences in benefits, work demands, and cost of living. Cost of living varies considerably across the United States and internationally. Despite the importance of cost of living issues in evaluating job offers, few studies examine costs of living adjusted salaries offered by universities. The focus of this paper is to compare cost of living adjusted salaries.

Figlio (2002) found a positive relationship between salary levels and the quality of teachers hired at U.S. public schools. The evidence suggests that universities receive benefits by paying higher salaries. As such administrators have a strong motivation to develop compensation plans that appropriately balance compensation paid with faculty quality desired.

Study of the impact of differential costs of living (COL) salary values was pioneered by Boothe (1933) and Winakor (1943). More recently researchers have examined COL adjusted salaries within a locality or university (See Stoops 2007, and Foster 2002, and Guilkey, Mroz, Rhode and Salemi, 2009). In a recent study, Jalbert, Jalbert and Hayashi (2010), produced a comprehensive study COL adjusted salaries at U.S. universities.

This paper extends the work of Jalbert, Jalbert and Hayashi (2010) by including a broader group of schools. The Jalbert, Jalbert and Hayashi (2010) study was limited to examining salaries at public U.S. universities that offered at least a bachelor degree. This study uses a different dataset that includes both public and private schools. In addition, the study here includes schools at both the university level and community college level. Finally, the study here includes specialized schools within universities, such as medical and law schools. While Jalbert, Jalbert and Hayashi (2010), examined both salary and benefit data in the aggregate and by faculty rank, the study here is limited to an examination of salary information and is not separated by faculty rank.

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RATIO OF DEFERRED TAX LIABILITIES TO SHARES AS A PREDICTOR OF STOCK PRICES

Kevin A. Diehl, Western Illinois University

ABSTRACT

This research examines whether deferred tax ratios predict US stock prices. The importance of deferred tax ratios stems from the existence of two separate reporting systems. US financial reporting is subject to managerial discretion, but US tax reporting is not. Investors may prefer to review tax numbers which are free from earnings management. However, only financial numbers are publicly disclosed. Deferred tax items enable investors to translate the financial results into less subjective numbers. Deferred tax liabilities also indicate successful tax planning. Correlation and regression establish the ratio of deferred tax liabilities over shares is more related to price than traditional ratios, such as basic earnings per share, earnings per share including extra items, cash flow per share, and book value per share.

JEL: M40

KEYWORDS: Deferred tax liabilities over shares, ratios, US stock prices, deferred tax items

INTRODUCTION

This research seeks to show that deferred tax liabilities to shares (DTL/Sh.) is so related to price that price to DTL/Sh. could replace price to earnings and other ratios in determining whether a stock is overpriced or underpriced. No ratio currently utilized seems entirely effective in ascertaining whether a stock is priced adequately. This study uses a data set of 3,016 US stocks, which allows us to draw statistically robust conclusions. Correlation and regression identify the statistical significance of the relationship between DTL/Sh. and price.

Even though the relevant literature shows relationships between the deferred tax accounts and earnings, no known research harnesses these relationships into some useful ratio. This relatively simple but powerful finding has heretofore been undiscovered likely for two reasons. First, the US market overemphasizes earnings and therein earnings per share. Second, despite the research demonstrating otherwise, market participants continue to misunderstand the predictive power of deferred tax accounts.

Deferred tax liabilities (DTLs) and deferred tax assets (DTAs) are the important considerations. The true benefits of DTLs tend not to be understood. There are two separate reporting systems in the US: the financial reporting system and the tax reporting system. In the US financial reporting system, managers have significant discretion over reported numbers. The US tax system does not provide that flexibility. Thus, investors may prefer to review tax numbers that are free from earnings management. Unfortunately, only the financial reporting numbers are publicly disclosed. However, investors can utilize the financially reported deferred tax items to reconcile the two systems. In fact, they enable investors to translate the financial results into numbers less subject to discretion and therein produce higher quality information to predict what US stock prices should be.

The research here shows that, DTL/Sh. explains price significantly more than previous research on deferred tax assets (DTAs) and deferred tax liabilities (DTLs). The research here provides significant value in establishing two findings: 1) the superiority of price to DTL/Sh. over price to earnings, and other ratios and 2) greater significance in the relationship between DTLs and price than has been found in previous research.

AUDIT COMMITTEE EFFECTIVENESS IN THE LARGEST US PUBLIC HOSPITALS: AN EMPIRICAL STUDY

Wen-Wen Chien, Nova Southeastern University
Roger W. Mayer, New York City Health and Hospitals Corporation
John T. Sennetti, Nova Southeastern University

ABSTRACT

Most research focuses on the role of audit committees in the private sector and less in the public sector, especially public hospitals. Therefore, we investigate the role and quality of public hospital audit committees in controlling problems in financial reporting and in major Federal award programs. We investigate all publicly available Office of Management and Budget Circular A-133 audit reports on internal controls over Federal reporting for public hospitals. We then conduct a follow-up study on the administrators of these reporting units. We find the presence of a committee and the committee's specific quality characteristics of independence, financial expertise, and increased activity, positively correlate with reduced frequencies of internal control problems. In addition, we find audit committees with financial expertise associated less frequently with material weaknesses over financial reporting and over major Federal programs. Our findings extend corporate governance research to the public health care sector, provide additional support for the Sarbanes-Oxley Act of 2002 and the Office of Management and Budget Circular A-123 requirements, and answer questions found in prior research on non-profit hospitals given by Vermeer et al. (2006) and Pridgen & Wang (2007).

JEL: M4, H5, H7

KEYWORDS: Audit committee; internal control; Office of Management and Budget Circular A-133 audit; material weakness.

INTRODUCTION

Audit Committees (ACs) serve an important monitoring mechanism in corporate governance. In the aftermath of highly publicized corporate scandals, such as Enron, WorldCom, and Tyco, the Sarbanes-Oxley Act of 2002 increased the committee's responsibility in providing greater transparency and an internal control structure over financial reporting in private sector. In like manner, the public sector also increased the committee's responsibilities. The U.S. Government Accountability Office (GAO) recommends that public sector entities consider the benefit of using ACs in governmental units (George, 2005; Hardiman, 2006).

Because of the investigations of ACs operating in the private sector and the correspondingly few studies about the role and effectiveness of ACs in the public sector, especially in public health care, (e.g., DeZoort et al., 2002; Hermalin & Weisbach, 2003; Vermeer et al., 2006), we extend the prior corporate governance research to the public health care sector. We do this by examining the impact of ACs in Federally funded public hospitals and healthcare systems (hereafter public hospitals).

Every year, more than 10 million people in the United States (U.S.) receive health care from public hospitals. More than 80% of public hospitals provide many essential community-wide services, such as primary, trauma, and neonatal intensive care to uninsured patients (Zaman et al., 2004). The indigent and uninsured population is growing, with more than 47 million uninsured Americans and illegal aliens (Gilmer & Kronick, 2005; Adamy & Meckler, 2010). To address this gap in healthcare coverage, U.S.

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Contact Information

Mercedes Jalbert, Managing Editor
The IBFR
P.O. Box 4908
Hilo, HI 96720
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