Earnings management before bankruptcy: a review of the literature
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In this article we will review the evidence on earnings management in distressed firms, in particular, during the periods before filing for bankruptcy. Knowing about the distortion of the accounting numbers through the failing firm is important for all stakeholders who make their decisions based on the firm’s annual reports. Over the last years, studies about the accounting behavior of failing firms have become able to present their findings in more detail which enables for better and more intelligible interpretations. In addition, on the basis of a higher level of available information for non-listed firms and the enhancements in the methods for detecting the earnings management, there are more and more options for investigations into the accounting behavior of bankrupt firms. However, the review will show that the results found in the literature about the accounting behavior in distressed firms in the periods before failing are ambiguous. So, as a result of the review, we will show to which extent the existing literature offers consistent findings, we will emphasize the obscure results and point out possible factors which could lead to the different results. In addition, we will identify gaps in research and will propose opportunities for further research on the earnings management in failing firms.

Keywords: earnings management, managerial crisis, bankruptcy, multi-period examination, accounting behavior

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