

Does Discretionary Accruals Affect the Financing Behaviour of  
Firms? Evidence from Pakistan  
(A case of selected non-financial listed firms)



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**The Thesis titled**

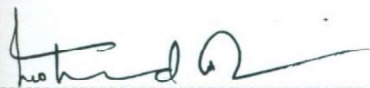
“Does Discretionary Accruals affect the financing behavior of firm? Evidence from Pakistan (a case of selected non-financial listed firms)”

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## Research Completion Certificate

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## Declaration

I Muhammad Rehan Siddique ID # 15002113004 Session 2015-2017, hereby certify that this thesis is being submitted in partial fulfillment of the requirements for the MS degree in Auditing and Control Systems.

This thesis is my original work, and the data/material presented herein has not been used for the acquisition of any other degree from any institution.

The Similarity Index is below the permissible limit.

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## **Abstract**

**Purpose-** In order to run organizations effectively and efficiently capital structure is considered as an essential element. Researchers often try to explain the determinants of capital structure. After the mega corporate scandals like Enron, WorldCom, financial reporting disclosures have become one of the most discussed topics. The prime objective of this research is to explore the relationship between discretionary accruals and financing behaviour of a firm.

**Design/Methodology/Approach-** Secondary research is done in this study in order to find out the relationship between discretionary accruals and financing behavior of a firm. This study covers a period from 2010 to 2015, further the proxy will be used to measure financing behavior is gearing ratio and discretionary accruals will be calculated by modified Jones model. In order to find out this relationship fixed effect regression model is applied.

**Findings –** Result explains that discretionary accruals have a significant and positive relationship with gearing ratio. This reflects that those firms that manage their earnings have a higher leverage. Whereas on the other hand Return on Assets (ROA) and size of a firm have a negative and significant relationship with gearing ratio. Furthermore tangibility has a positive and significant relationship with gearing ratio and Return on equity (ROE) has a negative relationship but this relationship is insignificant.

**Originality / Value-**This paper is useful for organizations, companies as well as for the Institute of Chartered Accountants of Pakistan. This paper is equally useful for academic institutions as well as for future researchers.

**Key Words –** Discretionary accruals, financing behavior, gearing ratio

**Paper type-** Research Paper

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## List of Abbreviations

TACC	Total Accruals
NDACC	Non Discretionary Accruals
DA	Discretionary Accruals
TA	Total Assets
REV	Revenue
REC	Receivables
PPE	Property Plant Equipment
GR	Gearing Ratio
ROA	Return on Assets
ROE	Return on Equity
TANG	Tangibility
FSIZE	Firm Size
VIF	Variance Inflation Factor

# **Chapter 1**

## **Introduction**

## **Introduction**

At present capital structure is considered as vital element in corporate finance. It not only affects the risk profile of a firm but also consider as matter of discussion among share holders. Linkage between financial reporting quality and capital structure is consider as most important issue in accounting and these issues are addressed by accounting standards (Lambert, Leuz, & Verrecchia, 2007) . Foster (2003) a member of a Financial Accounting Standard Board claims “More information always equates to less uncertainty and people pay for more certainty. In the context of financial reporting, the end result is that better disclosures results in a lower cost of capital.”

High quality financial reporting reduces the information asymmetry between management and shareholders. Furthermore information asymmetry affect the financial frication which results in to sub-optimal capital structure (Binsbergen, Jules, Graham, & Yang, 2010). Synn and Williams (2015) try to investigate the impact of financial reporting quality on capital structure; result reflects that by decreasing the financial reporting quality optimal capital structure also deviates.

Institutions should understand the role of earnings management in determining the capital structure as Leuz, Nanda, and Wysocki (2003) explain “...insider in an attempt to protect their private control benefits , use earnings management to conceal firm performance from outsiders”. Earnings management consider as important proxy for information disclosures (Ng, 2011).