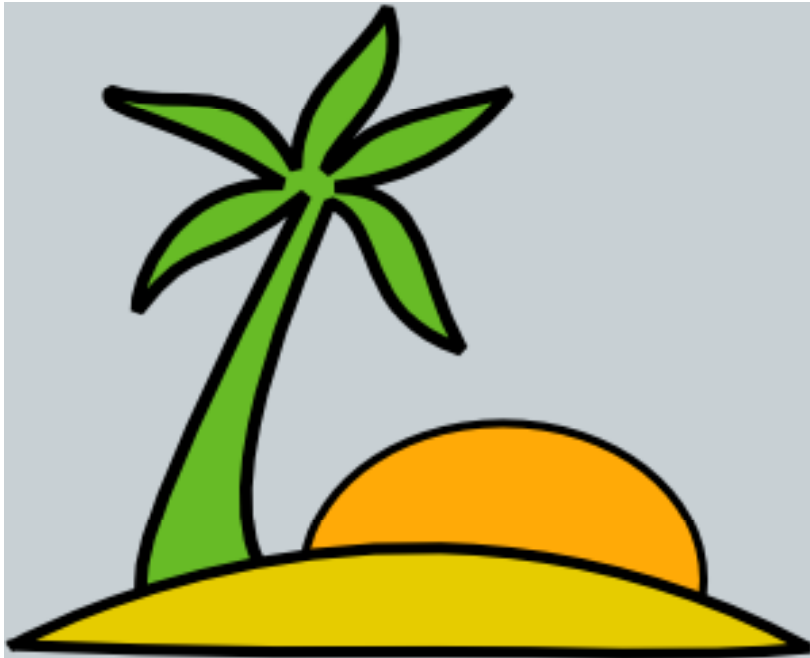


DISCUSSION OF “IS U.S.
MULTINATIONAL INTRA-FIRM
DIVIDEND POLICY
INFLUENCED BY CAPITAL
MARKET INCENTIVES?”
BLOUIN, KRULL, ROBINSON

- In February in Florida!



- In February in Florida (and I'm from Michigan)



- In February in Florida (from Michigan)
- Kids (Josie and Clark) are 2 and 4



- In February in Florida (from Michigan)
- Kids are 2 and 4...so will add a trip to Disney



- In February in Florida (from Michigan)
- Kids are 2 and 4 so will add a trip to Disney
- I am very interested in the topic of BKR's paper

- In February in Florida (from Michigan)
- Kids are 2 and 4 so will add a trip to Disney
- I am very interested in the topic of BKR's paper



**The Effect of Financial Accounting on the Location, Reinvestment, and Repatriation
Decisions of Multinational Companies**

John R. Graham
Duke University

Michelle Hanlon
University of Michigan

Terry Shevlin
University of Washington

Draft: September 02, 2008

BKR Research Question

9

- Do financial accounting costs affect dividend repatriations?
- Issues:
 - Measure repatriations?
 - Yes with BEA data
 - Measure financial reporting costs?
 - On one hand, this is difficult because one has to separate financial reporting costs from tax costs
 - On the other hand, there is a lot of prior literature in both tax and financial accounting that uses a variety of measures of “financial reporting costs” or “capital market pressure”.

I Am A Believer...

Table 4 - GHS

10

Survey responses to the question: In general, what factors are important in your company's decision to **reinvest foreign earnings outside of the U.S.**?

Factor	% important	% not important	Average rating	H ₀ : Average rating = 0
(1) Rate of return outside the U.S. is higher than that in the U.S.	58.4	19.9	2.58	***
(2) U.S. cash tax deferral	49.1	28.6	2.29	***
(3) Financial accounting expense deferral under APB23	44.9	31.9	2.18	***
(4) Foreign tax rate	40.8	26.7	2.15	***
(5) The need for cash to service foreign debt	27.8	54.9	1.48	***
(6) Other	16.5	70.0	0.95	***

Statistical Test of Differences in the Average Rating of the Factors

Comparison

<u>Factors</u>	<u>t-statistic</u>
(1) = (2)	3.12
(2) = (3)	1.13
(3) = (4)	0.30

Regression Model(s)

11

- $\text{Repatriations/Sales} = a + b\text{Tax Cost of Repatriating} + b\text{Public} + b\text{Public X Tax Cost of Repatriating} + b\text{Controls} + e$
- $\text{Repatriations/Sales} = a + b\text{HighPRE} + b\text{HighPRE X Tax Cost of Repatriating} + \text{same as above.}$

Data and Descriptive Statistics

12

- Use BEA data
 - Get actual repatriations
 - Accuracy levels...?
- Data on PRE/URE (financial statements)
 - Average ratio is 26%, median is 16%
 - Seems low (?) – especially if so many firms want to avoid accounting expense recognition

H1a

13

- ▣ H1a: Public firms are more sensitive to the tax cost of repatriating than private firms.
- ▣ Certainly a financial reporting cost differential.
 - Lots of prior literature

- ▣ Are private firms insensitive to tax costs?

Again, I Am A Believer...

Table 4 - GHS

14

Survey responses to the question: In general, what factors are important in your company's decision to **reinvest foreign earnings outside of the U.S.**?

Factor	% important	% not important	Average rating	H ₀ : Average rating = 0
(1) Rate of return outside the U.S. is higher than that in the U.S.	58.4	19.9	2.58	***
(2) U.S. cash tax deferral	49.1	28.6	2.29	***
(3) Financial accounting expense deferral under APB23	44.9	31.9	2.18	***
(4) Foreign tax rate	40.8	26.7	2.15	***
(5) The need for cash to service foreign debt	27.8	54.9	1.48	***
(6) Other	16.5	70.0	0.95	***

Statistical Test of Differences in the Average Rating of the Factors

Comparison

Factors	t-statistic
(1) = (2)	3.12
(2) = (3)	1.13
(3) = (4)	0.30

51% of public firms say APB23 is “important” only 15% of private firms

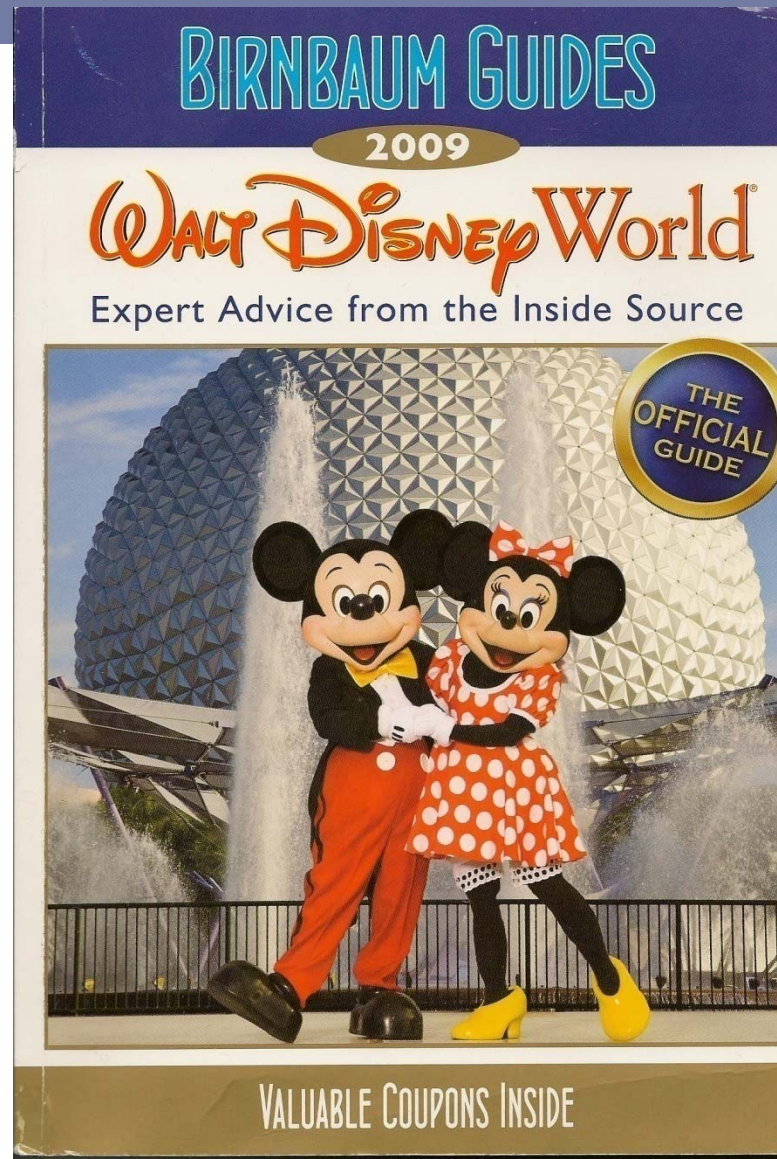
H1b

15

- ▣ H1b: Public firms with high amounts of permanently reinvested earnings are more sensitive to the tax cost of repatriation than other public firms.
- ▣ PRE = proxy for financial reporting costs

Clark on Mickey and Minnie...

16



H1b

17

- ▣ $\text{Repatriations/Sales} = a + b\text{HighPRE} + b\text{HighPRE} \times \text{Tax Cost of Repatriating} + \text{same as above.}$

- ▣ PRE = measure of financial reporting costs
 - More PRE then more likely high financial reporting costs

- ▣ But what else about PRE---

 - Is it circular? (by definition?)
 - Is it still a tax story?
 - Does PRE separate tax costs from accounting costs?

H2 – Quarterly analysis

- Fourth quarter repatriations will be different for public firms, especially those with high PRE.
 - Idea is that in fourth quarter might need to alter repatriations if need to meet reporting goals (i.e., by fourth quarter they have more information regarding overall earnings).
 - Would this affect actual repatriations or just “paper” designation of PRE?

H2 – Quarterly analysis

19

- ▣ What else?
 - I asked one of our respondent companies from GHS survey.
 - Avoid December transactions like the plague.
 - Too hard to assimilate and figure out how to report.
 - Many statutory audits of foreign jurisdictions are in the spring. Often repatriate after that – have more information (about the subsidiary)

- ▣ Results

H3- Investment – repatriation relation

- H3a: The association between repatriation decisions and investment behavior is lower for public firms than for private firms.
- H3b: The association between repatriation decisions and investment behavior is lower for public firms with high levels of PRE than for other public firms.
- Idea from Hartman (1985) that repatriations map into U.S. investment (or PRE maps into foreign investment). Well...

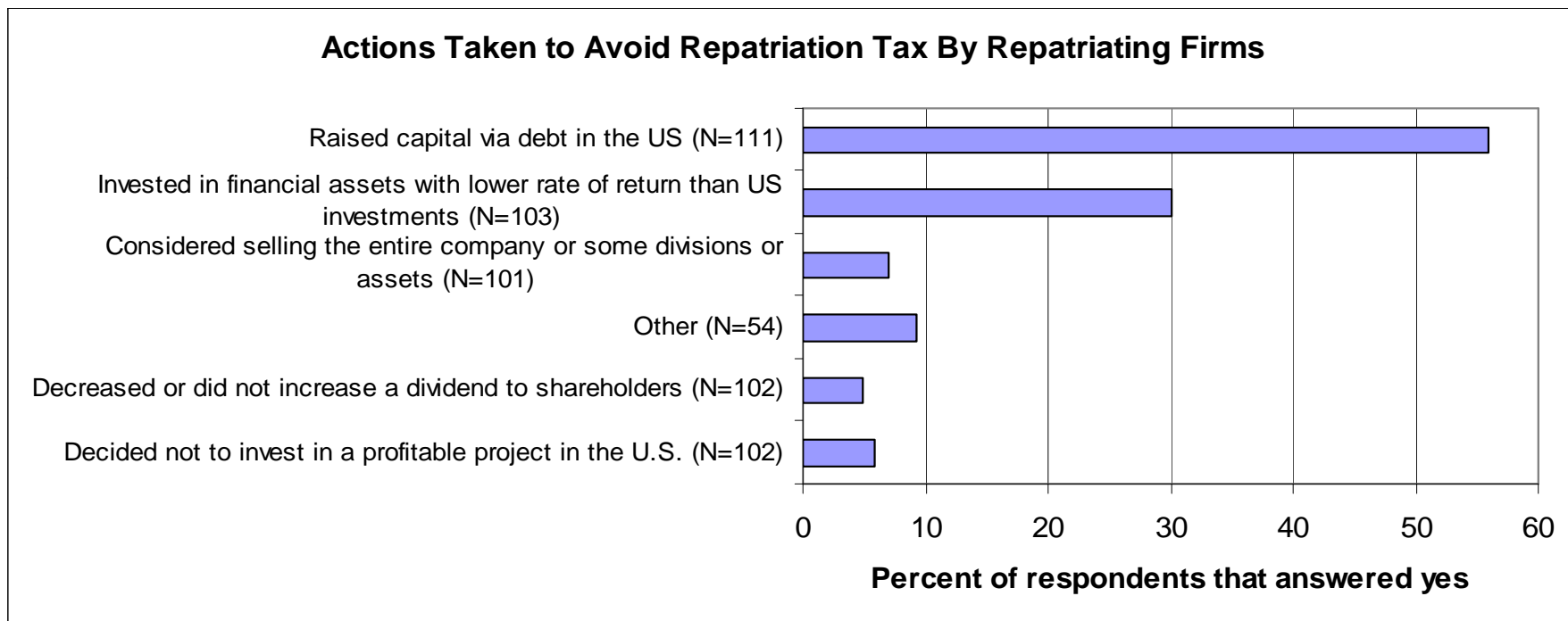
H3- Investment – repatriation relation

21

- ...Hartman (1985) is more of a way to start thinking about how things work...not really that representative of how things do work.
- Relation between repatriation and investment only strong if financially constrained and cannot get alternative financing for investment.
- Evidence in...
 - ...Blouin and Krull (2008)
 - ...Graham, Hanlon, and Shevlin, of course 😊

H3- Investment – repatriation relation

22



Graham, Hanlon, and Shevlin (2008-Barriers to Mobility)

H3- Investment – repatriation relation

23

- Do public firms have easier access to capital?
- Condition on PRE – again could be tax.

- I have no doubt financial accounting costs play a role...but...

Does Life Get Any Better? (aka Conclusions)

24

- In February in Florida (from Michigan)
 - Could be warmer... it was 40 degrees last night!
- Kids are 2 and 4 so will add a trip to Disney
 - Disney could be cheaper!!!
- I am very interested in the topic of BKR's paper
 - Paper could be better (like all of our papers)
 - This is good news!
 - Double check econometrics.
 - Provide more support that PRE is a proxy for financial reporting costs and not tax costs or something else.
 - Reconcile to Krull (2004) a little more—4th Q tests