EDITORIAL

Dear readers!

This issue of the journal is devoted to several issues of corporate governance.

Ilse Maria Beuren, Elza Terezinha Cordeiro Miiler verify how the Controllership institutionalization process takes place in corporate governance companies in Santa Catarina State – Brazil. Research was carried out by means of a multi-case study with a qualitative approach. Five companies were selected, but four answered the questionnaire, all listed in Bovespa's corporate governance. The research found only one company underwent a restructuring process in controllership. In this, the institutionalization process involved the system and sub-systems used in the company, encompassing every task and practice. The institutionalization of controllership assured the implementations, controls, performance, goals and levels of commitment of those involved.

Andrea Lolli shows that the financial situation of a company and its future evolution are legally relevant when the distribution of dividends are concerned and if the company wants to avoid –as an exception to the general rule- the application of fair value criteria. This I will argue is the case despite the fact that the EU has still not chosen to introduce a solvency test either as an alternative or as an additional system-to legal capital. The going concern principle as stated in Fourth Council Directive 78/660/EEC of 25 July 1978, and the financial information requested as part of the balance sheet by the EU Directive 51/2003, are the legal elements obliging the company to take into consideration the financial situation when the above mentioned decision is taken, in order to avoid liability for a decision which is inconsistent with the financial situation. The financial situation of the company is now particularly relevant for companies choosing to avoid the appliance of fair value criteria to financial instruments, as that choice presumes the ability to wait to sell that instrument on the market and that ability is very much dependent on the financial resources and the financial needs of the company.

Tzong-Huei Lin, Ching-Chieh Lin, Yueh Cheng, Wen-Chih Lee explores whether asset impairment loss as stipulated in International Accounting Standards (IAS) No. 36 provides an opportunity for finance industry to engage in earnings management, and whether corporate governance mechanism can deter such behavior. Using a sample of Taiwan finance industry, our results show that the amounts of asset impairment losses are related to "income smoothing" incentive rather than "big bath" motive. We also find that directors/managers recognize asset impairment losses basing on self-interest consideration and corporate governance mechanism have significant effect on asset impairment decision. The result also shows that financial holding company recognizes less asset impairment losses than non-financial-holding financial institution. Our conclusions are robust to different model specification, and are free from multicollinearity and outliers effects. This study contributes to understand the asset impairment behavior of finance industry and the behavior differences between financial holding company and non-financial-holding financial institution.

Michael J. Gombola, Amy Yueh-Fang Ho, Yi-Kai Chen investigate earnings management and long-term stock performance surrounding reverse stock splits. It is designed to provide evidence on the role of managerial pessimism and discretionary current accruals. Discretionary current accruals are used to measure earnings management. These discretionary current accruals are measured in our study using the balance sheet approach as well as the cash flow statement approach. We find consistent evidence of negative discretionary current accruals prior to reverse stock splits. Such negative discretionary accruals are consistent with managerial pessimism prior to a reverse stock split. Such pessimism is warranted by the observed negative market reaction to a reverse split announcement and the negative abnormal returns observed after reverse splits. Negative discretionary current accruals are also consistent with smoothing of earnings during difficult and challenging periods for the firm. Our study might provide an alternative to the opportunism explanation. It also provides additional evidence buttressing the role of managerial optimism and pessimism in explaining earnings management.

Yixi Ning, Massoud Metghalchi and Jonathan Du found that substantial changes in board size, either an increase or a decrease of three or more directors at one time, are permanent movements rather than temporary changes, but the large changes are followed by small reversal in the subsequent years. Empirical evidence shows that all types of directors (inside, affiliated, and independent) are strongly affected by board size expansions (or reductions). Large changes in board size provide a good opportunity for a firm to optimize its board structure by increasing board independence and retiring elder directors. Further analysis indicates that such substantial changes in board size are associated with more frequent board meetings, a higher likelihood of CEO transitions, and firm size expansions. However, we find no evidence that large decreases (or increases) in board size add (or destroy) firm value for shareholders in the long run.

Jorge A. Chan-Lau uses a stochastic continuous time model of the firm to study how different corporate governance structures affect the agency cost of debt. In the absence of asymmetric information, it shows that control of the firm by debtholders with a minority stake delays the exit decision and reduces the underinvestment problem. Such a governance structure may play an important role in diminishing conflicts between shareholders and debtholders.