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Qualifying for an EGC status in the post IPO phase under JOBS act Title 1: Opt in or opt out?

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Author: Julian Steenbergen*

Student number: 348120

Erasmus University

Erasmus School of Economics

Supervisor: Dr. Michael Erkens,

Assistant Professor of Financial Accounting

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*Graduate student in the MSc in Accounting & Auditing specialization at the Erasmus University Rotterdam.

Preface

This thesis is my final work of the Master in Accounting & Auditing at the Erasmus University Rotterdam. I have been enrolled in this Master from September 2015 up till December 2016. Underestimating the amount of work and time required for the finalization of the thesis on the one hand, and the combination of writing the thesis concurrently with working (subsequently) at Administratiekantoor Van der Voet B.V. [1]and EY[2] on the other hand, has led me to obtain a few months delay in finalizing my thesis. Nonetheless I am happy and proud to hand in this thesis now to finalize my Master, and to close off a rather busy period of my life.

First, I would like to thank Dr. Erkens for his guidance and patience. Furthermore, I would like to thank my family for support, confidence and advice in this hectic period. I hope you all enjoy reading this thesis.

[1] http://www.vdvoet.nl/
[2] http://www.ey.com/nl/nl/home

Abstract

This thesis investigates the research question "Why do firms declaim their EGC status prematurely after going public?" and is related to the Jumpstart Our Business Act (JOBS Act) of 2012. This US law formulates the emerging growth company (EGC) status. Companies that meet the requirements can adopt and retain this EGC status and benefit from the JOBS' pre- and post initial public offering (IPO) provisions for up till five years. These provisions reduce costs associated with IPOs and disclosure burdening in the period subsequent to the IPO for these firms. After five years the status is lost by reaching maturity. Therefore, the declaim of the EGC status within five years is referred to as being 'premature'. An EGC loses its status automatically prematurely if certain capital and/or size restrictions are exceeded. This results naturally from a firm's growth over time. This thesis focuses on the voluntary declaim of the EGC status. By doing so this thesis investigates the relation between voluntary disclosure and executive compensation and voluntary disclosure incentives (e.g. proprietary costs, capital market transactions and corporate control contest). The hypotheses are tested using pooled and sample per year multiple logit regression analyses. Of the EGC declaiming firms about two-third has lost its status. One-third has declaimed the EGC status voluntarily. The results of the regression analysis do not indicate a relation between executive compensation and voluntary EGC status opt out. The evidence regarding voluntary disclosure incentives is mixed. EGCs with high proprietary costs belonging to the pharmaceutical/biological industry are more likely to retain the EGC status. In addition, firms that are planning to increase public debt in the nearby future are likely to declaim their EGC status.

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1. Introduction

On April 5, 2012, the Jumpstart Our Business Start-ups (JOBS) Act was enacted by President Barack Obama to take down certain barriers for making initial public offerings (IPOs) to enhance the accessibility to the capital market for smaller companies (Barth et al, 2014). The underlying idea hereof is that more companies going public will eventually create jobs, as it is opined that public firms provide higher employment; hence, the fitting abbreviation. The JOBS Act formulates a new type of firm, the emerging growth company (EGC), and provides these EGCs with several regulatory exemptions based on provisions. These provisions should reduce the costs associated with IPOs and the compliance burdening that is associated with public firms following the IPO, to stimulate firms in their going-public decision. These provisions can be broadly categorized into de-risking and de-burdening provisions (Dambra et al., 2015). De-risking provisions affect the pre-IPO communication of an EGC. De-burdening provisions provide scaled disclosure requirements and exemption or delayed adoption of previous or future regulatory changes. These de-burdening provisions can be exploited by EGCs for up to five years following the IPO, after which the EGC status is lost by maturity. From the article of Berdejo (2014) however, it becomes clear that by the second fiscal year after the IPO already 40% of former EGCs stop qualifying for this status. This limits the expected ongoing benefits of the JOBS Act at the going public decision stage (Berdejo, 2014). Apparently, for this 40% of former EGCs, the benefits of the EGC de-burdening provisions either no longer outweigh its costs or these firms have for the EGC status. However, the remaining 60% of EGCs apparently still sees the JOBS Act benefits and is still eligible for the status. The purpose of this thesis is to analyse the causes of EGC status premature 'drop outs' to contribute to the overall evaluation of the effectiveness of JOBS Act. In this thesis "premature drop outs" as mentioned above refer to declaimers of the EGC status before the end of the fifth year following the IPO of the EGG, after which the status is lost automatically. The results of this research can benefit the SEC in evaluating the success of the JOBS Act as it is striking that so many of (former) EGCs don't fully exploit the JOBS Act possibilities. The research question that will be answered in this master thesis is as follows:

RQ: Why do firms declaim their EGC status prematurely after going public?

By answering this question, I hope to gain insight into why companies drop out their EGC status prematurely. To answer this question this thesis considers two options for declaiming the EGC status prematurely. First EGCs have the possibility to irrevocably opt out of the different provisions or of their EGC status at any time. Second, companies can lose the

status regardless their preference if capital/size boundaries are exceeded. Since the JOBS Act was only enacted four years ago, there will be no former EGC´s that have lost their status due to the passing of the full possible five years under JOBS. That is why the focus in this research is on premature (=before passing of 5 years) drop outs.

If a former EGC does not meet the requirements any more to continue qualifying as an EGC they automatically lose this status. Hence, this reason for declaiming the status just seems to result naturally from the development in the size and nature of a company through time. Therefore, more interesting to investigate are companies' reasons to choose to drop out of the EGC status. First, it is interesting to look which provisions of the JOBS Act drive a company's use of the EGC status. From the article of Berdejo (2014) on the adoption of JOBS' provisions it becomes evident that the main driver behind applying for an EGC status during the IPO stage is the option for confidential filing with the SEC. Companies only benefit from this during the IPO stage. In addition, the compliance costs regarding EGCs seem to not have decreased when comparing EGCs in the post-JOBS period to firms that would have qualified as EGCs the pre-JOBS period, according to this article. These findings imply why firms could elect to 'opt out' of the EGC status after the first year. They however do not explain why firms would prolong the EGC status after a year. This could be because of the additional provisions of the JOBS act. According to Berdejo (2014) one likely reason could be the provision regarding reduced executive compensation disclosure which is broadly embraced by EGCs. This provision lets EGCs disclose executive compensation for only the top three managers instead of five and takes away the obligation for an extensive compensation discussion and analysis (CD&A). This can be easily explained by the principal-agent theory which states that it is in management's best interest to have an informational advantage because they also serve their own goals (Garen, 1994). This provision therefore is a probable reason to retain the EGC status. Hence, it could be that firms that drop out of their EGC status pay their executives an average or below average compensation which makes that they don't see the benefit from reduced executive compensation disclosures. By disclosing this information, these companies want to *signal* they are doing well and/or that they have nothing to hide.

Contradictory to the article of Berdejo (2014), Dambra et al. (2015) find that compliance costs do decrease in the post-IPO period but that this is mainly the case for firms with high proprietary disclosure costs such as biological and pharmaceutical companies. Berdejo (2014) also finds that "*EGCs that take advantage of the scaled financial disclosure available under the JOBS Act are smaller, younger and more likely to belong to R&D-intensive industries, such*

as pharmaceuticals". Therefore, it could be that the specific characteristics of biological and pharmaceutical companies make it that they benefit more from the lessened disclosures than other businesses and that these are in fact the firms retaining their EGC status.

Furthermore, companies that choose to drop out of their EGC status prematurely or disclose information which they are not obliged to, due to the JOBS Act provisions, basically voluntarily disclose the additional information which would have been mandatory as a non-EGC. Therefore, the JOBS Act provides for a unique opportunity to test the voluntary disclosure theorem. Based on their review of voluntary disclosure literature, Healy and Palepu (2001) classify voluntary disclosure incentives into six categories. It is expected that companies that drop out of their EGC status prematurely are motivated by voluntary disclosure incentives. For feasibility purposes of this research, this research investigates only three of these incentives. These are the capital market transactions (1), the corporate control contest (2) and the proprietary costs (3) incentive. Firms voluntarily disclose more information to reduce information uncertainty when they expect to issue public debt or equity or to acquire another company in the nearby future (Lang & Lundholm, 2000). This way they reduce the cost of capital and increase their capital liquidity. The capital market transactions incentive thus implies that an EGC declaiming company (at t=0) is a company which increases its public debt or equity in the nearby future (at t=1). The corporate control contest incentive implies that managers voluntarily disclose information to explain away bad performance in a situation where the risk of job loss due to underperformance is significant (Warner et al., 1998; Weisbach, 1988). Hence, an EGC declaiming company is expected to be underperforming compared to the industry average for that year. Lastly the proprietary costs incentive. Management's decision to disclose information is influenced by the concern that such disclosures can damage their firm's competitive position in product markets (Dambra et al., 2015). Accordingly, when the proprietary costs of a firm are low, companies are more likely to disclose information. Finally, in a time where the disclosure burdening for public companies is very high, the JOBS Act provides with an exceptional opportunity to test for voluntary disclosure literature.

The different possible reasons for voluntarily opting out of the EGC status are tested using a multiple logit regression analysis, while controlling for firm size, leverage, insider ownership and profitability. This analysis is based on a pooled sample for all years as well as for samples per year relative to the IPO moment. This way the research does not only map the reasons for declaiming the status in general, but also the reasons for declaiming the EGC status

split by year relative to the year of the IPO. In these regression analyses the firms that have lost their EGC status as the result of the development in the size and nature of the firm through time are excluded.

The sample used in this master thesis consists of 300 US listed companies with EGC status. These 300 firms have been selected randomly from an entire population of 1500 US listed companies with this status that were available. These companies have all performed an IPO in the period surrounding and following the enactment of the JOBS Act in April 5 2012 and were hence eligible for and have chosen to apply for the EGC status. For these companies, all available initial S-1 filings and the following 10-K reports have been collected. This has resulted in observations for the fiscal years 2010 -2016. After filtering out firms with missing S-1 filings, missing 10-K reports in between two periods and after having subsequently filtered out firms with missing key identifier data and variable data during the merging with additional datasets, the final sample is reduced to 237 firms and 726 unique firm year observations.

Of these 726 unique firm year observations 601 contain firm year observations during which the observed firm had the EGC status. On the firm level there have been 65 EGC drop outs recorded at different moments, distributed over the year following the IPO until the fourth years after the IPO. Of these EGC drop outs, about two-third has lost its status due to exceeding the JOBS Act predefined capital/size restrictions. The other one-third of EGC drop outs has voluntarily declaimed its status (Table 5, p.31). The logit regressions are run on the sample excluding the firms that have lost their status.

The results of the regressions (Table 6, p.31 & Appendix C, p. 44) do not show a negative relation between firms with relatively higher executive compensation and EGC status declaim. As a result, the first hypothesis of this research is rejected. Although agents of a company are utility maximizers (Garen, 1994), the results of this study do not support the idea that overly paid executives would tend to disclose less information and retain the EGC status.

With regard to the second hypothesis, which investigates the influence of voluntary disclosure incentives on the EGC drop out decision, the evidence is mixed. The logit regression on the samples per year did not find any significant relations. For the logit regression on the pooled sample some significant relations have been found. First, a significant negative relation exists between the classification into pharmaceutical/biological firms and the EGC declaim decision. Consequently, it seems that these companies benefit more from the JOBS Act provisions than firms that do not belong to these industries. However, this could also mean that

pharmaceutical/biological firms are simply not growing as fast as other firms or that these firms were smaller at the IPO moment to begin with, which means they stay more often within the size requirements for retaining EGC status. Since the firms that have lost their EGC status due to exceeding the capital/size restrictions have been excluded in the regression, there could therefore be a sample selection bias because this excluded group contains only non-pharmaceutical/biological firms. Nonetheless, based on the results non- pharmaceutical/ biological firms seem more likely to voluntarily declaim the EGC status. The second proxy for the proprietary costs incentive measured by the relative amount of a firm's R&D compared to the sample year mean, did not show a significant relation with the EGC declaim decision. Thus, our evidence only partly supports the role of proprietary costs in the EGC retain or drop out decision. For the capital market transactions incentive, a significant positive relation is found between the rise in a company's debt in the year following the EGC status drop out (at t=+1) and the EGC drop out decision (at t=0). This indicates that firms that voluntarily drop their EGC status collect additional public debt following the EGC status drop out. This relation is not found with regard to public equity. Hence, the results regarding the capital market transactions incentive only support this incentive with regard to public debt. Lastly, the results with regard to the corporate control contest incentive and the relation of underperformance with voluntary disclosure are insignificant and are rejected.

This research contributes to the existing literature on the JOBS Act by providing the first results related to the declaiming decision that EGCs face. This can assist the SEC in the evaluation of the JOBS Act. Furthermore, this thesis contributes to the existing voluntary disclosure literature, as this research provides for a unique opportunity to test for voluntary disclosure incentives in a time where mandated disclosures are at an all-time high. Lastly this thesis contributes to the literature regarding the relation between agency theory and disclosures. The results indicate that the JOBS Act de-burdening provisions are better exploited by EGCs belonging to the pharmaceutical and biological industry. Firms belonging to these industries seem to continuously benefit from the JOBS Act provisions. No relation is found between excess executive compensation and the voluntary declaim of the EGC status. Further, the results support the voluntary disclosure theorem as significant relations are found for the proprietary costs incentive and the capital market transactions incentive with regard to the voluntary declaim of the EGC status.

There are several limitations to this research. First, the final sample used in the research is rather small which makes it difficult to draw solid conclusions. Future research should extend

our research with a bigger sample. Second, as this thesis wants to look at several reasons for declaiming the EGC status from a generic point of view, it did not breakdown the executive compensation variable into the different components, such as fixed salary, stock compensation, bonuses and others. Future research could investigate the relation between these components of executive compensation and the decision to retain or declaim the EGC status. Third, as described there are more voluntary disclosure incentives than the ones tested in this research (Graham et al., 2015; Healy &Palepu, 2001). Future research could extend our research by considering these other voluntary disclosure incentives.

This thesis is built up as follows. Chapter two provides a literature overview. The literature overview handles literature on IPOs, the JOBS Act, voluntary disclosure theorem and agency and signaling theory and is concluded by the research hypothesis development. Further, Chapter three discusses the research design. This paragraph elaborates on subsequently the dependent, independent and control variables of interest and the resulting empirical model. The third chapter is concluded with a discussion on the sample selection. Chapter four provides the results of this research. It provides the descriptive statistics and multicollinearity analysis and concludes with the results of the regression. Chapter five, the final chapter of this research, provides the research' conclusion and a discussion.

2. Literature Review

This chapter begins with exploring the literature regarding the IPO decision that companies face. Secondly, paragraph 2.2 will elaborate on the background of the JOBS Act, its provisions and previous research done regarding this matter. Paragraph 2.3 will discuss voluntary disclosure literature, the exceptional opportunity that the JOBS Act to contribute to this literature and companies' incentives to voluntarily disclose. Paragraph 2.4 discusses agency and signalling theory, two basic underlying key theories to the (voluntary) disclosure literature. Finally, paragraph 2.5 provides a synopsis of these paragraphs and the hypothesis development.

2.1 The IPO decision

To continue doing and expanding business a company needs capital. When a company's available capital falls short, additional capital needs to be acquired. A company has various ways to do this. It can acquire funding from private investors in exchange for ownership in the company, it can step into a loan agreement with a bank or another third party, or it can acquire funding by issuing equity in a public matter. When a company decides to choose for the last option for the first time this is referred to as a company's IPO. There are several reasons and occasions for which a company decides to perform their IPO.

Pagano et al. (1998) examine the reasons why companies go public among Italian companies. They found that most companies have made significant investments and that they are showing a high growth rate. At this point the companies have often already stepped into several loan agreements with banks, increasing their leverage. Pagano et al. (1998) state *"their decision to go public can be interpreted as an attempt to rebalance their balance sheet after large investments and growth."*. Hence companies issue public equity to polish their leverage position. Furthermore, Pagano et al. (1998) show that, after controlling for firm characteristics and leverage, credit terms between companies and banks post-IPO improve in the advantage of these companies. Furthermore, Pagano observes that it also becomes easier to issue debt or equity in the years following a company's IPO. Company owners that are looking to make money by selling their stakes in their company are also better off by going public (Zingales, 1995). Becoming public doesn't only attract more potential acquirers, it also increases the price that company owners would get from these acquirers since their bargaining position increases with the involvement of outside shareholders. By going public, a firm's management thus helps to facilitate the acquisition of their company for a higher value than the value they would get from an outright sale in the private sector (Ritter & Welch, 2002). Another possible motivation to go public is to get publicity and increase brand awareness (Brau et al., 2003).

When contemplating going public, management has to make a trade-off between the previously mentioned benefits and the costs associated with going and being public. These costs consist of regulatory compliance costs during and after becoming public, underwriters' gross spread, underpricing, loss of voting rights/power of the initial company's owners and indirect costs such as managerial time spent on the IPO-process (Berdejo, 2014; Brealey et al., 1977) and agency costs (Jensen & Meckling, 1976). A company's characteristics, such as their leverage position (Pagano et al. 1998), will influence their trade-off between the benefits and costs of the IPO, which will eventually lead them to either stay private, or go public. The JOBS Act (2012) tries to stimulate companies to go public by reducing several, namely regulatory, costs. The next paragraph will further elaborate on the JOBS Act.

2.2 JOBS Act

The Jumpstart our Business Startups (JOBS) Act was enacted on April 5, 2012. It consists of seven titles of which this thesis is only concerned with Title 1 Emerging growth companies (EGCs). The Jobs Act was employed to take down certain barriers for making initial public offerings to enhance the accessibility to the capital market for smaller companies (Barth et al, 2014). It does so by formulating a new type of firm, the EGC, and providing this EGC with several regulative exemptions. This was a response to the decline in the volume of IPOs since the beginning of the twenty-first century compared to the historical levels from before (Dambra et al, 2015). This decline in the number of IPOs was explained by practitioners and scholars as the result of the increase in regulatory compliance costs that came with the Sarbanes-Oxley Act of 2002 and the accompanying SEC-legislation. Especially smaller firms would have to 'think twice' before going public after SOX (Redner, 2002). By taking away or lowering some of these SOX-obligations for smaller firms, the JOBS Act tries to stimulate these firms to go public. The underlying idea of the JOBS Act is to increase these IPOs by smaller firms by removing certain barriers. It is thought that going public provides firms with additional business and that this creates *jobs*, hence the fitting abbreviation.

An EGC is defined under the JOBS Act as an issuer that had total revenues of less than $1 billion (adjusted for inflation every five years) during its most recent completed fiscal year, has not issued more than $1 billion in nonconvertible debt over the past three years, and is a non-accelerated filer under the Securities and Exchange Commission (SEC) reporting regulations and excluding all those issuers that completed an IPO on or before December 8, 2011. In practice, most companies that perform their IPO are eligible and can apply for an EGC

status. After qualifying as an EGC a company will lose this status as of the earliest as of (PWC, 2014):

1. the last day of the fiscal year during which it had total annual gross revenues of $1 billion or more;
2. the date on which it has issued more than $1 billion in non-convertible debt securities during the previous rolling three-year period;
3. the date on which it becomes a large accelerated filer (which generally occurs on the last day of the fiscal year in which its public float is at least $700 million as of the last business day of its second fiscal quarter – see Exchange Act Rule 12b-2); or
4. the last day of the fiscal year following the fifth anniversary of the first sale of the issuer's common equity securities in an offering registered under the Securities Act. Once EGC status is lost, it generally cannot be regained.

Many IPOs are unsuccessful and the stock often plunges after the IPO (Brill, 1997). This makes private companies wary to go public. Larger private companies that have more resources are usually more willing and better prepared for a public offering because they tend to have a better understanding of the market (Brill, 1997). Smaller companies are more uncertain about the degree of interest of the market in the stocks they consider offering. The JOBS Act provides several provisions for EGCs in an attempt to resolve some of the concerns involved with an IPO. Following Dambra et al. (2015) this research classifies these as either de-risking or de-burdening provisions. The de-risking provisions affect the pre-IPO communication of the EGC. The following de-risking provisions are provided by the JOBS ACT (Westenberg, 2012):

- *Expanded permitted communication with investors*. This provision, which is referred to as 'testing-the-waters' (Berdejo, 2014), enables small businesses to get an indication of interest from potential investors before actually incurring the costs and burdens of preparing an offering statement and filing it with the SEC. EGCs and their agents have more freedom to communicate with potential investors that are "qualified institutional buyers" (as defined in Rule 144A) or institutions that are "accredited investors" (as defined in Regulation D) (Westenberg, 2012).
- *Confidential filing:* Before the JOBS Act, firms were mandated to publicly file their registration statement (S-1 form) for an IPO. An EGC is permitted to submit a draft form S-1 (and amendments to this form) to the SEC for a confidential review. If the firm decides

to go forward with the IPO, the S1-form and its amendments must be publicly filed at least 21 days before the road show begins.

The de-burdening provisions provide scaled disclosure requirements and exemption or delayed adoption of previous or future regulatory changes. The de-burdening provisions provided by the JOBS Act are (Westenberg, 2012):

- *Reduced financial statement disclosure*. A non-EGC should present three years of audited financial statements and five years of selected financial data in their S-1 form. EGCs however are allowed to present only two years of audited financial statements and selected financial data in their registration statement.
- *Reduced Executive compensation disclosure*. Under this provision an EGC need not provide an extensive Compensation Discussion and Analysis (CD&A) section. In addition, compensation information is only required for the top three executive officers (including the CEO). Further only three of the seven compensation tables that are normally mandatory need to be provided. The Summary Compensation Table should cover two years, instead of three otherwise. Finally, a narrative disclosure of compensation policies and practices as they relate to risk management is not required.
- *Auditor Attestation opt-out*. EGCs are exempt from requirement 404(b) of the Sarbanes-Oxley Act that an independent registered public accounting firm should audit and report on the effectiveness of a company's internal control over financial reporting.
- *Delayed Application of New accounting standards:* EGCs do not have to comply with new or revised Financial Accounting Standards Board (FASB) accounting standards until they affect private companies. If an EGC decides to comply with a certain standard this is irrevocable.
- *PCAOB rulings opt out*. EGCs can opt out of future rules implemented by the Public Company Accounting Standards Board (PCAOB) unless the SEC determines that it is necessary in the public's interest that EGCs comply with the new rulings.
- *Exemption from Dodd-Frank Act requirements.* EGCs are exempt from Say-on-Pay, Say-on-Frequency, or Say-on-Golden Parachute nonbinding shareholder advisory votes as required by the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act and SEC rules. Thus, EGCs have more freedom in determining their compensation structure without stockholders interfering. The required disclosures on the relationship between executive compensation and financial performance and of the ratio between CEO

compensation and median employee compensation a by the Dodd-Frank Act also do not apply to EGCs.

Prior research on the JOBS Act has focussed on the achievement of the JOBS Act´s goal to increase the number of small firms going public and the reduction of disclosure costs. The evidence from these studies, regarding the volume increase in IPOs post-JOBS, is mixed. Berdejo (2014) found that there has not been a noticeable increase in the number of IPOs conducted for companies that qualify as an EGC that would have also qualified as an EGC pre-JOBS. However, he does find a shift in the characteristics of firms performing an IPO towards firms that belong to the more R&D intensive pharmaceutical companies. Dambra et al. (2015) however find that there is a significant increase in the number of IPOs conducted post-JOBS, and that this increase can be explained for a big part by the increase in the number of pharmaceutical and biotechnological firms. This is attributed to the fact that these companies would benefit more from the de-risking provisions of the JOBS Act because of their high proprietary disclosure costs. Berdejo (2014) did not find a decrease in the disclosure costs of EGCs post-JOBS and finds that some of the provisions might indirectly increase a company's costs. This is supported by the research of Barth et al. (2014) showing that the JOBS Act increases information uncertainty and with it the cost of capital. This increase seems to offset some of the benefits of the reduced disclosure costs. From the article of Berdejo (2014) it becomes clear that by the second fiscal year after the IPO already 40% of former EGCs stop qualifying for this status. Apparently, for this 40% of former EGCs, the benefits of the EGC de-burdening provisions either no longer outweigh its costs or these firms have for the EGC status. However, the remaining 60% of EGCs apparently still sees the JOBS Act benefits and is still eligible for the status. According to Berdejo (2014) one likely reason could be the provision regarding the reduced executive compensation disclosure which is broadly embraced by EGCs. It thus could be that firms that stay opt in to the JOBS Act exemptions share a certain executive compensation structure.

The focus in this paper will be on the de-burdening provisions since the de-risking provisions' benefits have faded in the years following the IPO. Hence these do not contribute to the analysis of the reasons why EGCs continue being an EGC after the first year and will not be discussed any further.

2.3 Voluntary disclosure literature

Companies are mandated by law and regulations to disclose certain information in their financial reports. When companies share additional information publically which they are not permitted to, they basically *voluntarily disclose* this information. The Financial Accounting Standards Board published a report called "Improving Business Reporting: Insights into Enhancing Voluntary Disclosures" in 2001. In this report the FASB defines voluntary disclosures as "disclosures, primarily outside the financial statements, that are not explicitly required by GAAP[4] or a SEC rule". The JOBS Act exempts companies that qualify as an EGC from several disclosures. Hence, companies that choose to drop out of their EGC status prematurely or disclose information which they are not obliged to due to the JOBS Act provisions, basically voluntarily disclose the additional information which would have been mandatory as a non-EGC.

Companies are reluctant to voluntarily disclose information. They want to avoid setting a precedent that will be difficult to maintain in the future (Madhani, 2008). Still, management has several incentives to voluntary disclose additional information. Graham et al. (2005) did a survey among managers on what their most important motives are for voluntary disclosure. According to the results, creating a transparent reputation is the most important reason for managers. Second is reducing the informational uncertainty and therefore the information risk that investors assign to a stock. The third most important motive according to this research is to share important information that is not included in financial statements.

Where the research of Graham is based on surveys among managers, other academic literature has come up with several own explanations for voluntary disclosure. Healy and Palepu (2001) have distinguished six motives for management to voluntarily disclose information, based on their review of existing disclosure literature. They acknowledge the following incentives:

1. Capital markets transactions incentive: Firms voluntarily disclose more information to reduce information uncertainty when they expect to issue public debt or equity or to acquire another company in the nearby future (Lang & Lundholm, 1997). This way they reduce the cost of capital and increase their capital liquidity.
2. Corporate control contest incentive: Managers that face bigger risks of job loss due to poor earnings and stock performance use information disclosure to reduce the likelihood of

[4] Generally Accepted Accounting Principles

undervaluation and to explain away poor earnings performance (Warner et al., 1998; Weisbach, 1988).

3. Stock compensation incentive: Managers disclose private information to: meet restrictions imposed by insider trading rules (Noe,1999 & Cheng, 2006); increase liquidity of the firm's stock if they intend to trade their own stock holdings (Aboody, 2000).
4. Litigation cost incentive: When managers face a bigger risk for litigation for inadequate or non-disclosure they are more likely to voluntarily disclose information. On the other hand, managers are also more likely to be sued when they have not met the promises they have previously made by voluntary disclosures. This is why especially forward looking information won't be voluntarily disclosed in such a situation (Skinner, 1997).
5. Management talent signalling incentive: Managers will voluntarily disclose information to show how skilled they are. They do this by making their future estimates publicly. This way the public can notice in the nearby future how skilled management is in making estimates. Trueman (1986) came up with this incentive.
6. Proprietary cost incentive: Management's decision to disclose information is influenced by the concern that such disclosures can damage their firm's competitive position in product markets (Dambra et al., 2015). Accordingly, when the proprietary costs of a firm are low, companies are more likely to disclose information.

Healy and Palepu (2001) conclude there is insufficient evidence for the management talent signalling incentive. The evidence they find on the litigation cost incentive is mixed and therefore difficult to prove. For the other four incentives Healy and Palepu have found clear and unambiguous evidence. The stock compensation incentive however, is determined as not feasible in terms of this research. Therefore, in the rest of this thesis the focus will be on the capital market transactions (1), the corporate control contest (2) and the proprietary costs (6) incentive. Finally, in a time where the disclosure burden for public companies is very high, the JOBS Act provides with an exceptional opportunity to test voluntary disclosure incentives.

The underlying reason for voluntary disclosure according to existing disclosure literature is the reduction of information asymmetry between management and outside stakeholders (Verrecchia, 2001 & Lambert et al., 2007). Verrecchia suggests that information asymmetry reduction is the starting point for disclosure literature. Two of the key theories that are in line with Verrecchia and that are heavily related to and explain the (voluntary) disclosure theorem and incentives are the agency theory (Jensen & Meckling, 1976) and the signalling

theory (Watts & Zimmerman, 1986). These will be further discussed in the next paragraph as this thesis contributes to the existing literature regarding these matters.

2.4 Agency and Signalling theory

The final accounting streams to which this master thesis contributes are the well-known principal-agent or agency theory (Jensen & Meckling, 1976) and the signalling theory (Watts & Zimmerman, 1986). These are heavily related to and form an explanation for (voluntary) disclosure theory and incentives. Both will be discussed.

2.4.1 Agency Theory

Agency theory classifies a firm's management as *agents* and all other stakeholders as *principals* (Jensen & Meckling, 1976). Between these groups there exists an informational asymmetry in the advantage of the agents. For instance, the shareholders of a firm (the principals) invest their money in the firm and trust management to do with it what is best for the firm. However, the agents also have a private agenda to pursue their personal objectives. The principals thus can never be completely sure about management's actions. Marschak (1955) states: "by definition the agent has been selected for his specialized knowledge and the principal can never hope to completely check the agent's performance". This misalignment is the result of the distinction between the owners of company (shareholders) and the ones in control (management) (Jensen & Meckling, 1976). The costs associated with this misalignment of interest and the expenses to reduce this misalignment are referred to as so called 'agency costs'. Agency costs include the costs of the principals' attempts to align agent's interests and actions with their own interest and the resulting costs of this misalignment (Jensen & Meckling, 1976). First the principals incur monitoring costs. These monitoring costs include not only the costs of the instalment of a monitoring authority but extend to budget restrictions, compensation policies, operating rules etc. designed by the principals to control agents' behaviour. Second, principals pay agents to induce behaviour that is in their benefit or to induce behaviour that ensures that their personal interests will not be harmed, so called "bonding costs". Lastly, the costs of the misalignment of interest. This "residual loss" represents the utility loss from the perspective of the principals as a result of the utility striving character of the agents that conflicts with the maximum utility for the firm and the side of the principals (Jensen & Meckling 1976).

As this agency relationship results from the separation of ownership between management and principals, the abovementioned agency costs decrease with increasing ownership from management in a company. The extreme being smaller companies where management owns 100 percent of the firm and where there are no agency costs at all (Ang et

al., 2000). Furthermore, Fama and Jensen (1983) propose that with the dispersion of ownership over a broad audience, the agency problem increases. More dispersion leads to more finger pointing among shareholders who expect someone else will take responsibility to monitor the agent, which is a costly business (Hart, 1995) On the contrary, companies of which significant amounts of stock are held by only a few stockholders have less agent-principal conflicts because these few stockholders more closely monitor and induce certain behaviour of managers. Hence, in companies where the stocks are widely dispersed there is more uncertainty for the principals.

By disclosing, management takes away some of this uncertainty for investors (Barth et al., 2014). Hossain (1994) has shown that the dispersion of stock ownership within a company is positively correlated with the amount of voluntary disclosure by a firm. In such firms the monitoring costs are higher due to the higher degree of uncertainty. Management tries to decrease these costs by voluntary disclosure.

Finally, relating agency theory to executive compensation, it is evident that managers are under heavy scrutiny and criticism towards their compensation. Berdejo (2014) found that the reduced compensation disclosure provision might be leading in a company's decision to retain the EGC status. Criticism towards excessive pay is far more likely than shareholders expressing that they find executive's compensation too low. It thus seems in management's own best interest to disclose less information on their executive compensation, especially when the public's perception might be it is excessive. In 1992 when the SEC was about to adopt regulations to increase the quality and quantity for executive compensation disclosures, there was a heavy and aggressive lobby from individual investor lobby groups to do so. Lo (2003) finds that this suggests that in the opinion of these stakeholders an extensive disclosure of executive compensation would contribute to an environment in which management is less likely to pursue its own goals. Hence, managers being utility maximizers, are less likely to voluntary disclose when they might appear to be self-centred (Garen, 1994).

2.4.2 Signalling theory

The second theory used to explain voluntary disclosures is signalling theory (Watts, 1986). This theory states that management uses voluntary disclosures to reduce the information uncertainty that investors have by sharing good news. Firms that perform relatively well will share certain information voluntarily to distinguish themselves from firms that do not perform as well in order to attract investments and a more favourable reputation (Campbell et al., 2001). Hence, they give a *signal* to the market by voluntary disclosing. They do this because of the "lemons problem" (Akerlof, 1970). Akerlof suggested that in a market where there exists an

informational uncertainty, the market will assign values to comparable products at equilibrium. Thus, bad products get overvalued by the public and crowd out the good products which get undervalued. The same principle applies to the capital market. Here investors assign values to companies based on the information that is made available to them. Consequently, it is in the interest of good companies to disclose additional information to reduce market uncertainty and to be valued higher by and become more attractive to investors compared to companies that do not disclose. It follows that nondisclosure can be an indicator of companies that are performing bad (Diamond, 1987).

2.5 Hypothesis development

In the previous sections the IPO literature, the JOBS ACT, voluntary disclosure literature and the agency and signalling theory have been discussed. Based on existing literature regarding these matters I have developed my research and the hypothesis that will lead me to the evaluation of the JOBS Act drop out motivations. Berdejo (2014) has shown that 40% opts out of the EGC status after the first year. These premature EGC drop outs can be either due to the loss of the EGC status as a result of exceeding the JOBS Act capital/size restrictions or by giving up the EGC status voluntarily. As the loss of the status results naturally from the growth of a firm through time it is more interesting to see what motivated former EGCs to voluntarily declaim the EGC status. This voluntary EGC status opt out can be triggered by several incentives. It could however also be that firms applied for the EGC status because of the de-risking provisions of the JOBS act that they don't benefit from retaining the EGC status and its de-burdening provisions. Following signalling theory (Watts, 1986) there is a downside in being an EGC. An EGC discloses less information, signalling a less transparent culture. In addition, less disclosures result in more uncertainty for investors, which can lead to more volatility in stock prices changes as a result of performance news (Lang and Lundholm, 1993). This counteracts management that normally pursues a continuous progressive growth. Therefore, after having exploited the JOBS Act de-risking provisions, there might be firms that declaim the EGC status after exploiting the de-risking provisions to pursue this goal. This could help explain the 40% drop out of former EGCs after year one that Berdejo (2014) found. However, more information can also lead to more volatility as there is more information for investors to respond to. Therefore, this argument does not seem to hold in explaining the decision to declaim the EGC status. Berdejo (2014) did not find any evidence of reduced disclosure costs in the years following the IPO. If an EGC status opt out is voluntarily and if

the cons of being an EGC or reduced disclosure costs are not the cause for retaining or declaiming the EGC status, then what is?

Following Berdejo (2014) the provision for reduced executive compensation disclosure is a probable cause in the decision to prolong or declaim the EGC status, as it is broadly adopted. As reduced executive compensation disclosure is an important feature of the JOBS Act provisions, it seems like one of the possible key motivators to adopt the EGC status. Therefore in this research, I follow Berdejo and expect that retaining or declaiming the EGC status is related to the level of executive compensation within a company. This is supported by the agency theory which states that it is in management's best interest to have an informational advantage because they also serve their own goals (Garen, 1994). I expect that companies with excessive executive compensation will retain their EGC status more often because these companies' management is more likely to get criticized for their personal salaries. Since agents pursue their own maximum utility, it seems logical that executives that get paid more than the market average after controlling for firm performance, will prefer using the JOBS Act exemptions and particularly those related to reduced executive compensation disclosures. Since the JOBS Act presents the opportunity to disclose the compensation of just three instead of five high executives, and takes away the obligation for an extensive CD&A, I expect that firms that don't want to disclose much information on executive payment will retain their EGC status and make use of this provision. This leads to the first hypothesis:

H1: Firms with higher executive compensation are more likely to prolong their EGC status

According to the disclosure theorem there could also be other incentives to retain or give up the EGC status. By giving up the EGC status companies basically voluntarily disclose information of which these companies would have been exempt if they retained their EGC status. Healy and Palepu (2001) have found several incentives to do so in academic literature. Since these incentives have not yet been tested in relation to declaiming the EGC status I have decided that I will examine this relation in this research more extensively. Of the incentives distinguished by Healy and Palepu (2001) I have determined that using the capital market transactions incentive, the corporate control contest incentive and the proprietary cost incentive are the most feasible to test for voluntary disclosure incentives as a cause for retaining or declaiming the EGC status. With regard to the use of the provisions of the JOBS Act, the capital market transactions incentive suggests that companies that have given up their EGC status after year one, might be firms that want to raise additional capital and hence disclose more

information to reduce the cost of capital (Barth et al., 2014). If firms have collected additional funds which make them exceed the JOBS Act capital/size restrictions, they are automatically forced out of their EGC status. However, based on this incentive it is expected that the same principle applies to firms that have voluntarily dropped out of their EGC status. The corporate control incentive implies that firms that opt out of the EGC status have performed worse than what was forecasted and hence make the additional disclosures of which they were exempt to explain away the poor performance in earnings and/or stock. The proprietary cost incentive might indicate that firms with higher proprietary costs maintain their EGC status. Both Berdejo (2014) and Dambra (2015) find an increase in biological and pharmaceutical companies that perform an IPO and qualify as EGC, indicating that these firms are more likely to benefit from the EGC status. This is in line with the proprietary cost incentive since these companies have high R&D expenditures. Based on the above the second research hypothesis is formulated:

H2: Opting out of the EGC status prematurely is related to voluntary disclosure incentives.

As several voluntary disclosure incentives are investigated, the evidence that will be obtained throughout this research with regard to the second hypothesis, can provide mixed results. Breaking down this hypothesis in the separate expectations related to the different voluntary disclosure incentives, the following sub hypothesis can be formulated with regard to the relations of the separate voluntary disclosure incentives with premature EGC status declaim:

H2a: Opting out of the EGC status prematurely is positively related to the capital market transactions incentive

H2b: Opting out of the EGC status prematurely is positively related to the corporate control contest incentive

H2c: Opting out of the EGC status prematurely is negatively related to the proprietary costs incentive.

Although all voluntary disclosure incentives could explain the use or the declaim of most of the JOBS Act provisions, some provisions are particularly relevant for the different incentives. Relating the specific JOBS Act provisions to the different voluntary disclosure incentives it seems that the exemption from an internal control auditor attestation is of specific interest when the corporate control contest incentive motivates management. Such an internal control auditor attestation can provide the manager of a bad performing firm with an excuse for disappointing results. Moreover, managers motivated by this incentive are especially likely to opt out of this

provision. In addition, this incentive might bring executives to disclose information on their compensation to show solidarity in their salary with firm performance, hence giving up exemptions that allow reduced executive compensation disclosure. If a firm is motivated by the capital market transactions incentive, it is likely that such a firm will give up the exemption to comply with the Dodd Frank Act requirement and exemptions related to financial statement disclosure. Investors will also be interested in the internal control auditor attestation so this exemption also seems likely to be declaimed when a firm wants to collect additional funds. If a firm is motivated by proprietary costs such a firm will particularly make use of the exemptions related to reduced financial statement disclosure, the delayed application of new standards and the PCAOB rulings opt out. In the next chapter the research design for the several hypotheses will be tested.

3. Research Design:

In this section the research methodology is described that is used to get an answer to the research question of this thesis. I start by distinguishing the dependent, independent and control variables to this research and their operationalisations. This will be followed by a brief discussion of the regression models that will be tested and the link between this empirical model and the hypotheses.

3.1 Dependent Variable

EGC Status

In this research, I look for reasons why companies declaim their EGC status. Therefore, the dependent variable in this research is whether the company is still an EGC or if it has declaimed its EGC status. More specifically, in our dataset this variable has been given the name Declaim_of_EGCstatus. This is a dummy variable which will be a 1 if a company has declaimed its status, and which will be a 0 if it has retained the EGC status. This variable will be obtained from either S-1 filings or subsequent annual reports.

3.2 Independent Variables

Based on the literature overview several factors can be distinguished to explain a firm's decision to declaim its EGC status. This paragraph elaborates on these explanatory independent variables.

3.2.1 Executive compensation

A possible reason according to Berdejo(2014) for declaiming or retaining the EGC status is executive compensation. Consistent with prior studies (Sapp, 2008; Bebchuck, 2010) this study focuses on the named executive officers (NEO's) rather than just on the CEO in measuring executive compensation. When companies adopt the JOBS Act provisions regarding reduced executive compensation disclosures, they are permitted to disclose executive compensation for only their top three NEO's. Therefore, in this study the focus will be on the top three paid NEO´s since these will be disclosed either way. It is expected that companies that pay their executives more than what is generally accepted, will more eagerly adopt this provision. To investigate this a new variable is introduced, namely Excess_com. If Berdejo(2014) is right, companies that pay their top NEO's more than the average will retain their status more often. Excess_com is a dummy variable which equals 1 if the top three NEO's get paid more than the average pay for the top three NEO's in that fiscal year, and 0 otherwise. This data will be obtained from either S-1 filings or the subsequent annual reports, if available.

3.2.2 R&D expenditures & industry

Proprietary costs as an incentive to retain the EGC status will be researched first by looking at the research and development (R&D) expenditures of a company. By choosing R&D as a proxy for proprietary costs within a company this research is in line with the research of Dambra et al. (2015) on the JOBS Act and its effect of post-JOBS IPO increase. Scherer (1983) measured the R&D expenditures of a company as the ratio of R&D expenditures divided by net sales, a ratio which he finds to be stable over time. Among the JOBS-applying first however are a lot of research related start-ups with zero revenues in the beginning years but with asssets. Therefore, in this research the R&D expenditures are measured as the ratio of R&D expenditures divided by total assets. Companies with above average R&D/total assets ratios will be expected to retain their status, while average or below average ratios are expected to drop out. This is a dummy variable which equals 1 if the ratio is average or below average and which equals 0 if it is above average. A second proxy for the proprietary costs incentive, based on prior JOBS research (Dambra et al., 2015; Berdejo, 2014), will be a dummy variable which equals 1 if a firm is a pharmaceutical or bio(techno)logical firm, and 0 otherwise.

3.2.3 Capital increase (Equity and Debt)

The capital market transactions incentive implies that an EGC declaiming company is a company which increases its public debt in the nearby future. Healy et al. (1999) found evidence that disclosures often correlate with subsequent public debt or equity offerings. Hence it is expected that a company which voluntarily opts out of its EGC status, increases its public financing in the subsequent periods. Hence, in our dataset two variables are introduced named Cap_increase_deb and Cap_increase_eq. These dummy variables equal 1 if the capital in the period t+1 is increased compared to the previous periods' existing debt or equity at t = 0 (the time of the declaim of the EGC status).

3.2.4 Underperformance

Another possible incentive for the declaim of the EGC status is underperformance. The corporate control contest incentive implies that managers voluntarily disclose information to explain away bad performance in a situation where the risk of job loss due to underperformance is significant (Healy and Palepu, 2001). Relating this to the voluntary declaim of the EGC status it is expected that such companies have shown worse earnings results than were forecasted. This is based on the industry average for the period. In this study the corporate control contest incentive thus translates into the variable Underperf which is also a dummy variable that equals 1 if a company has underperformed to the industry average for that year and 0 otherwise.

3.3 Control Variables

While investigating the possible explanatory variables for an EGC status declaim, several control variables should be taken into account. This paragraph elaborates on these control variables.

3.3.1 Size

The first control variable that should be considered is size. Prior research' findings have already shown a positive relation between firm size and the amount of (voluntary) disclosure of a company (Depoers, 2000; Hossain, 1995). This can be explained by the tendency of larger firms to have more external capital (Leftwich et al., 1981) and agency costs increase along with the increase in external financing (Jensen & Meckling, 1976). Hence, since larger companies have higher agency costs and management wants to reduce these, larger firms are more likely to voluntary disclose additional information. In addition, larger firms are subject to heavier scrutiny from the public (Lang & Lundholm, 1996). The proxy for size in this research will be the natural logarithm of total assets following King & Lenox (2001).

3.3.2 Leverage

The second control variable is leverage. Firms with higher leverage, put differently, that have relatively less equity and more debt in their capital structures have higher agency costs (Jensen & Meckling, 1976). Agency theory thus suggests that a higher leveraged company hence will make more disclosures to reduce monitoring costs and information uncertainty. The evidence in prior research is mixed. Bradbury (1992) found that firms that are more highly leveraged disclose more than lowly leveraged firms. However, several researches under which those of Depoers(2000) and Hossain et al. (1995) have not found any empirical results that affirm this relation. This study follows basic agency theory, expecting that a higher leveraged firm will declaim its EGC status more often. The proxy for Leverage is the debt on total assets ratio.

3.3.3 Ownership structure

Hossain (1994) finds that the dispersion of stock ownership within a company is positively correlated with the amount of voluntary disclosure by a firm. Hence companies in which stock ownership is widely spread will have more voluntary disclosures than companies with concentrated ownership. Chau and Gray (2002) agree with Hossain and show that the amount of disclosures decrease in the amount of insider ownership. As insiders become larger shareholders of a company, the amount of voluntary disclosures tends to decrease (Eng & Mak,

2003). In this research, insider ownership is used as proxy for concentrated ownership, where I expect that higher insider ownership leads to less disclosure.

3.3.4 Profitability

Following signalling theory (Akerlof, 1970), good performing firms will disclose more information to distinguish themselves from their competitors. In addition, it seems likely that profitable firms pay higher salaries to their top executives. The proxy for this control variable is a dummy variable based on a company's net income. As a company is making a profit (net income > 0) this variable will equal a 1. If a company is not making any profit (net income =< 0) this variable equals 0.

3.4 Empirical model

3.4.1 Regression model and proxies

In our empirical model as a whole, all the previously described variables should be addressed. The resulting ordinary least squares regression model looks as follows:

$$\textbf{Declaim\_EGC}_t = \alpha + \beta 1(\textbf{Excess\_com})_t + \beta 2(\textbf{R\&D\_exp})_t + \beta 3(\textbf{pharma/bio\_ind})_t + \beta 4(\textbf{Underperf})_t + \beta 5(\textbf{Cap\_increase\_eq})_{t+1}{}^* + \beta 6(\textbf{Cap\_increase\_ debt})_{t+1} + \beta 7(\textbf{Size})_t + \beta 8(\textbf{Leverage})_t + \beta 9(\textbf{Insider\_ownership})_t + \beta 10(\textbf{Profitability})_t + \varepsilon$$

Here the different proxies that influence the declaiming decision and the control variables are:

- Declaim_EGC = the dependent variable in our empirical model is a dummy variable that equals 1 if a company has declaimed the EGC status, and 0 if the company remains an EGC.
- Excess_com = dummy variable with Excess_com = 1 when the top three NEO's get paid more than the average and = 0 otherwise.
- R&D_exp = dummy variable which equals 1 if a company's R&D expenditures/Total Assets ratio is higher than the average of the sample, and 0 otherwise.
- Pharma/bio_ind = dummy variable that equals 1 if a firm is a pharmaceutical or bio(techno)logical firm, and 0 otherwise.
- Underperf = dummy variable with Under_Perf = 1 when the earnings have been lower than expected, and 0 when earnings are equal or higher than expected. This is benchmarked with the sample average based on the ROA.
- Cap_increase_eq$_{t+1}$ = a dummy variable which equals 1 when a company has raised additional equity following the IPO at t+1 and 0 if the company has not.
- Cap_increase_debt$_{t+1}$ = a dummy variable which equals 1 when a company has raised additional debt following the IPO at t+1 and 0 if the company has not

- Size = The natural logarithm of a company's total assets
- Leverage = the ratio of a company's total debt at FYE divided by a company's total assets at FYE.
- Insider_ownership = a continuous variable which falls between zero and 1. A 1 indicates dominate concentrated ownership by inside stakeholders and as this variable moves close to zero as insiders control a smaller part of the stakes. Measured as the percentage of shares owned by inside stakeholders.
- Profitability = this is a continuous variable which represents a company's profitability by using the ROA ratio.

3.4.2 Empirical model analysis

Analysing the empirical model with the two research hypotheses in mind, two separate parts within the regression model are distinguished:

1. A part linked to the executive compensation hypothesis, including variable β1(Excess_com)t; and
2. A part linked to the voluntary disclosure incentive hypotheses, including variables β2(R&D_exp)$_t$, β3(pharma/bio_ind)$_t$, β4(Underperf)$_t$, β5(Cap_increase_eq)$_{t+1}$* and β6(Cap_increase_ debt)$_{t+1}$.

Based on the hypothesis development, I expect the following coefficients/relations.

In line with H1 I expect that $\beta 1 < 0$. The Excess_comp variable being a 1 indicates that top management is being overpaid. However, this should lead to retaining the status. Hence the negative sign of β1.

In line with H2 I expect $\beta 2 < 0$ and $\beta 3 < 0$ and $\beta 4 > 0$, $\beta 5 > 0$ and $\beta 6 > 0$, indicating that voluntary disclosure incentives form an explanation for declaim of the EGC status. β2 and β3 relate to the proprietary cost incentive, β4 to the corporate control contest incentive and β5 and β6 to the capital market transactions incentive.

Considering the control variables a third part can be distinguished in the regression model, namely variables β7(Size)$_t$, β8(Leverage)$_t$, β9(Insider_ownership)$_t$ and β10(Profitability)$_t$. Here I expect $\beta 7 > 0$, $\beta 8 > 0$ and $\beta 10 > 0$ and $\beta 9 < 0$.

3.5 Sample

A random sample of 300 US listed companies with EGC status was selected from an entire population of 1500 US listed companies with this status that were available. These

companies have all performed an IPO in the period surrounding and following the enactment of the JOBS Act in April 5 2012 and were hence eligible for and have chosen to apply for the EGC status. From these companies I collect the initial registration statements (S-1 filings) as well as amended S-1 filings (S-1A's), together with the annual reports (10-K's) of the subsequent years following the IPO. This has led to the use of S-1 filings and annual reports for the fiscal years of these companies in the period 2010-2016. Both the S-1 filings and the annual reports have been collected through use of the EDGAR database. From these filings and reports the company's net sales, the type of company, used provisions, executive compensation data and the company's EGC status are hand collected per fiscal year. After the hand collection, those firms are filtered out that either did not have any reports available or that had missing 10-K's in between an S-1 filing and a later published 10-K filing. This leaves 293 unique firms. Through the COMPUSTAT database, data regarding a company's R&D expenditures, total debt, total equity, total assets, net income (loss) and industry are acquired for the firms of our sample for the 2011-2016 period using the CIK key identifier as CIK was present for the entire sample. 46 companies aren't found using the CIK key identifier and hence the sample is reduced to 251 companies. The two datasets are merged using CIK and fiscal year. During the merging of these two datasets, two additional firms have been filtered out because of duplicate errors. This decreases the resulting sample to 249 unique firms. Subsequently, a third non-specified dataset is created through the COMPUSTAT from which the industry average ROA and R&D/revenues ratios are calculated. These averages per firm year are merged into the former merged dataset of 249 firms using industry and fiscal year making a total of 1019 observations. Only the years of the IPO and the years following the IPO are of interest as a result of the research question. Hence, I drop firm year observations before firms' IPOs and keep 732 firm year observations. For the executive compensation variable, it is required to know how many NEO's are disclosed per firm year. This is easily calculated through excel. Importing this data and merging it with our file, results in a final sample of 726 unique firm year observations.

Classifying these firm year observations into the years relative to the IPO, the firm year observations of our sample are distributed as follows as follows: 237 firm year observations for the year of the IPO, 210 for the year following the IPO, 173 for the year after, 96 for the third year following the IPO and a mere ten firm year observations for the fourth year following the IPO (See Table 1).

Table 1

Sample distribution of firm year observations

Year relative to IPO	N	Percent.	Cum.
Year +0	237	32.64	32.64
Year +1	210	28.93	61.57
Year +2	173	23.83	85.40
Year +3	96	13.22	98.62
Year +4	10	1.38	100.00
Total	726	100	

Sample distribution of the firm year observations classified in the year relative to the moment of the IPO. The sample consists of in total 726 firm year observations. Column 1 shows the classification of years relative to the IPO. Column 2, 3 and 4 respectively indicate the number of observations per year relative to the IPO, the percentage and the cumulative percentage of the observations within the sample.

4. Empirical Results and Tests

In this section the empirical results of our research are described. I start by looking at the descriptive statistics. In this section the distribution of the used provisions is given for the firms per year relative to the IPO. Second, the regression analysis results of this research are described to see whether the EGC drop out decision is influenced by one of the factors under investigation in this Master's thesis. Finally, robustness and sensitivity tests are performed to test if the results from the regression analysis are reliable and the effect of control variables on our findings is discussed.

4.1 Descriptive Statistics

In this chapter the descriptive statistics will be discussed. As the point of interest of this research relates to the motivations of firms for declaiming and retaining the EGC status it is interesting to observe which part of (former) EGCs drop their status in the years following the IPO. Table 2 shows the amount of EGCs per firm year observation (relative to the IPO year).

Table 2
EGC status distribution

Year relative to IPO	N	EGC status	EGC status
Year +0	237	237	100.00
Year +1	210	183	87.14
Year +2	173	123	71.10
Year +3	96	55	57.29
Year +4	10	3	30.00
Total	726	601	

Sample distribution of firm year observations with EGC status and without EGC status. The total sample of firm year observations consist of 726 firm year observations. 601 of these firm year observations contain observations with EGC status. Column 1 shows the classification of years relative to the IPO moment. Column 2, 3 and 4 respectively indicate the number of observations, the amount of firm year observations with EGC status and the percentage that has EGC status for the years relative to the IPO.

In our sample, 13% of the firms drop their EGC status the year following the IPO year, a remarkable lower portion than the fourty percent opt out as described by Berdejo (2014). After the second year following the IPO, another 16% of former EGCs drop out, resulting in about

70% of EGCs that have retained their status after two years. For the firm year observations collected relating to the third year following the IPO year, only 57% of former EGCs still claim this status. Only 30% of former EGCs holds their EGC status until the fourth year following the IPO.

According to prior research (Berdejo, 2014; Dambra et al, 2015) the reasons for companies to apply for the EGC status relate to, either or both, the de-risking and de-burdening provisions. For this research, only the de-burdening provisions are of interest, as this research tries to find an answer to why certain companies retain and certain companies drop out of their status after the year of the IPO. In Table 3 the adoption of the provisions is given for the firm year observations relative to the IPO year (for elaboration on the specific provisions in Table 3, see Appendix A). The results relating to year 4 relative to the IPO should be ignored as there are only 3 firm year observations where firms have retained their EGC status.

The main adopted provisions by EGCs according to the findings relate to the exemption of an internal control auditor attestation, the exemption of Dodd Frank Act requirements and reduced executive compensation disclosure. The average adoption for these provisions approaches 90% for all years relative to the IPO and hence it seems that these provisions could be the motivation to retain the EGC status. The provisions related to financial statement disclosure reduction appear mixed. The provision that lets firms disclose two instead of three years, is widely adopted by 61,2% of EGCs in the year of the IPO. In the first year following the IPO only around 20% of EGCs choose to prolong the use of this provision and disclose less than 3 years. This can be easily explained as it takes just a little effort from management to include the financial statement numbers of two years back in the financial statements which are published the year following the IPO, as these had been made public the prior year already. The provisions that exempts companies from the obligation to disclose financial statement data for

the last five years is adopted by 71,3% of EGCs in the year of the IPO and progressively decreases to adoption of this provision of 49,1% in the third year following the IPO. The provision that exempts EGCs from the application of new accounting standards is adopted by a mere 16,9% of EGCs in the IPO year and stays around 20% in the following years. The provision that exempts EGCs to comply with future rulings implemented by the PCAOB is

Table 3

EGC Jobs Act provision adoption overview

		Reduced FS disclosure			Delayed application new standards	PCAOB ruling opt out	Reduced executive compensation disclosure				Auditor Attestation Opt out	Exemption Dodd Frank Act require-ments
Year_relative to_IPO	Nr of EGC's	**Provisions**										
		Prov 1.1	Prov 1.2	Prov 1.3	Prov 2	Prov 3	Prov 4.1	Prov 4.2	Prov 4.3	Prov 4.4	Prov 5	Prov 6
Year +0	237	43,0%	61,2%	71,3%	16,9%	35,9%	92,4%	88,2%	87,8%	95,8%	93,2%	92,0%
Year +1	183	10,4%	20,2%	68,3%	16,9%	29,5%	93,4%	93,4%	89,1%	90,7%	96,2%	92,3%
Year +2	123	11,4%	22,0%	61,8%	18,7%	33,3%	92,7%	94,3%	88,6%	83,7%	96,7%	92,7%
Year +3	55	12,7%	27,3%	49,1%	21,8%	30,9%	94,5%	90,9%	92,7%	85,5%	98,2%	94,5%
Year +4	3	0,0%	0,0%	0,0%	0,0%	33,3%	66,7%	0,0%	33,3%	33,3%	100,0%	66,7%
Total	601	23,6%	37,3%	66,1%	17,6%	32,9%	92,8%	90,8%	88,5%	90,5%	95,3%	92,3%

The above table shows an overview of the adoption rate with regard to the provisions that EGC's can use (Westenberg, 2012) under use of the JOBS Act. Column 1 contains the distribution of firm year observations relative to the IPO. Column 2 shows the number of EGCs within the sample that are left per year relative to the IPO. For the different provisions, several features have been checked. In Column 3 up till Column 13, the adoption has been recorded with regard to these features. The classification in grey on the top of these column indicates which provision features measured belongs to which provision (Appendix A).

adopted by 35,9% in the IPO year and the percentage of EGCs using this provision in the years following shows no big differences.

in the above it has not been considered that firms that classify as a smaller reporting company (SRC) due to their size, can already benefit from certain provisions without being an EGC due to existing legislation to support SRCs (Shirodkar & Darnell, 2011). The reduced executive compensation disclosure and the reduced financial statement disclosure provisions that the JOBS Act offers to EGCs, are already available to smaller reporting companies. Therefore, for these provisions the descriptive statistics are rerun, while controlling for EGCs that are also SRCs (Appendix B). For a description of the provisions, see Appendix A. When compared to the previous table there are only small differences for the year of the IPO and the first and the second year after. The third and fourth year stay the same. The small noted differences are not remarkable however.

4.2 Multicollinearity analysis

An important underlying assumption of the regression model is that there shall be no perfect linear relationship between non-dependent variables. If two independent predictive variables approach such a relation, this can give rise to multicollinearity problems. These problems can be broadly categorized into: an unreliable *b* coefficient, limitation of the *R* size and it can become more difficult to determine the individual effect of the predictive variable(s) on the dependent variable (Field, 2009, p. 220-224).

To determine multicollinearity for the variables in the research regression, the variance inflation factor(VIF) analysis is performed (see table 4, next page). The VIF estimates how much the variance of a coefficient is "inflated" because of linear dependence with other predictors. It is assumed based on the rule of thumb as described by O'brien(2007) that variables with a VIF higher than 10 and tolerance results smaller than 0.1 are highly multicollinear.

In table 4, only the variable size_log has a VIF higher than 10. Hence, multicollinearity problems exist for the size proxy. However, this variable is a control rather than a predicting variable. All other independent variables have VIF's far below 10 and tolerance results greater than 0.1. Based on VIF and tolerance results, it can be concluded that there are no multicollinearity issues between predictor variables in my sample.

Table 4
VIF-analysis

Variable	VIF	Tolerance
size_log	11.51	0.09
Profitability	5.62	0.18
PharmaBio	3.17	0.32
Insider_Ownership	2.90	0.34
equity_incr	2.32	0.43
RD_AT_high	1.74	0.57
Underperf	1.61	0.62
Excess_comp	1.39	0.72
debt_incr	1.32	0.76
Leverage	1.14	0.88
Mean VIF	3.27	

In the above table the Variance inflation factor(VIF) analsysis is performed for the logit regression that will be run on the dependent variable EGC status declaim. Column 1 contains all the independent and control variables of the key regression model. In Column 2 and 3 respectively the VIF and Tolerance results are shown for these variables. The results are ordened with the variables with the highest VIF (=lowest tolerance) on the top and the variables with the lowest VIF (=highest

4.3 Results

In this chapter the results of the hypotheses discussed in the beginning of this thesis will be elaborated on. These hypotheses will be discussed by comparing them not only with the literature in our research but also with similar studies conducted so far. By discussing these hypotheses, an answer will be given for the research question:

RQ: Why do firms declaim their EGC status prematurely after going public?

There are two options regarding the premature EGC status declaim of a firm. The declaim results either from the loss of the status because a firm's size or capital amount exceed the predefined EGC restrictions, or by the decision to give up the EGC status. To measure if a firm has lost the EGC status, a dummy variable called noStatus_Loss was created. This dummy variable equals 1 if total revenue is below 1 billion and if a firm is not a large accelerated filer, implicating that drop outs that meet these conditions have voluntarily declaimed their EGC status. If either one of these conditions is not met, the value of this dummy variable becomes zero, indicating that the EGC status is lost due to exceeding the prescribed EGC capital/size restrictions. Table 5 shows the EGC drop out distribution for our sample. It becomes obvious

that almost two-thirds (63.08%) of declaiming firms in our sample lose their status as they either exceed the revenue barrier and/or by becoming a large accelerated filer. This however results naturally from the growth of a company overtime. Our research intends to find why companies decide to drop out of the EGC status and hence our regression excludes firms that have lost their EGC status and firm year observations that follow an EGC status declaim year.

Table 5

EGC Drop out overview

EGC Drop out due to	Nr. Declaiming	Percent	*Status loss due to	
			Rev > 1 billion	Large accelerated filer
Status loss*	41	63.08	6	38
Status give up	24	36.92		
Total	65	100.00		

The above table shows the initial EGC drop out distribution, split out in "Status loss" and "Status give up". Both variables are based on a dummy variable noStatus_loss. This dummy variable is created to distinguish between voluntary EGC status opt outs and EGC status losses. This variable equals 1 if the value of the annual_gross_revenue variable is below 1 billion AND if a firm is not a large accelerated filer(L_acc_filer variable = 0), indicating that there is a voluntary EGC status declaim. If either one of these conditions is not met, the value of this dummy variable becomes zero, implicating that the EGC status is lost due to exceeding the prescribed EGC capital/size restrictions (PWC, 2014). Columns 2 and 3 respectively represent the amount of EGC drop outs due to Status loss or Status give up, and the percentage of the total drop outs. Column 4 and 5 demonstrate due to which exceeded capital/size restrictions the EGC status is lost.

Declaim of the EGC status is regressed on the relative height of executive compensation (H1) and on the relative amount of R&D expenditures for a year, a company being a (non) pharma-/biological companies, underperformance to the industry year mean and equity and debt increase at t+1 (H2), while controlling for: firm size, leverage, the amount of insider ownership and profitability. The table below (Table 6) reports the pooled sample regression results of the OLS, showing the predicted sign of the relation with the dependent variable, the coefficient demonstrating the actual relation, the standard error, the z score and the significance levels.

Table 6
Pooled sample logit regression results

Variables	Predicted. Sign	β	Std. Error	z	P>z
(Constant)		5,399	1,934	2,790	0,005
Excess_comp	-	0,362	0,684	0,530	0,597
RD_AT_high	-	-0,109	0,734	-0,150	0,882
PharmaBio	-	-1,832	0,795	-2,300	0,021
Underperf	+	-0,228	0,612	-0,370	0,709
equity_incr	+	0,949	0,636	1,490	0,135
debt_incr	+	2,071	0,627	3,300	0,001
size_log	+	-0,896	0,168	-5,330	0,000
Leverage	+	-0,063	0,156	-0,400	0,686
Insider_Ownership	-	-0,031	0,012	-2,520	0,012
Profitability	+	0,659	0,708	0,930	0,352

For a (former) EGC: Declaim_EGCt = α + β1(Excess_com)t + β2(R&D_exp)t + β3(pharma/bio_ind)t + β4(Underperf)t + β5(Cap_increase_eq)t+1 + β6(Cap_increase_ debt)t+1 + β7(Size)t + β8(Leverage)t + β9(Insider_ownership)t + β10(Profitability)t + ε. The dependent variable is EGC status declaim. The firm year observations included in the regression consist of all EGCs or initial EGC declaiming observations. If a firm year observation has a declaimed EGC status, the year subsequent to that year is dropped from the regression. The total amount of firm year observations run in the regression is 606. Excess_comp is a dummy variable that equals 1 if a firms top three NEOs get paid more than the average of the top three NEOs for that year. RD_AT_high is a dummy variable that equals 1 if a firms R&D divided by Total Assets is above the average ratio for that year. PharmaBio is dummy variable that equals 1 if a firm is a Pharmaceutical or Biological company. Underperf is a dummy variable that equals 1 if the roa of a company is below the industry roa for that year. equity_incr is a dummy variable that equals 1 if a company's equity at t=0 is bigger than the company's equity at t-1. debt_incr is a dummy variable that equals 1 if a company's debt at t=0 is bigger than the company's equity at t-1. size_log is a continous variable which is the log of the total assets of a company. Leverage is Total Debt/Total Assets for that year. Insider Ownership is continuous and size ranges between 0 and 1. Profitability is a dummy variable that equals 1 if a company's Net Income is possitive. Because of the dummy variables the performed regression with these variables is a logit regression for the entire sample. Column 2 shows the expected sign of β based on the hypothesis development and research design. Column 3 and 4 show respectively the actual β and the standard error. Column 5 and 6 show the z value and the significancy of the relation. The regression analysis is performed with the broadly used significance level of 0.05

The first hypothesis aims to find if average or below average executive compensation leads to a premature EGC status declaim decision and its supporting voluntary disclosures, supported by agency and signalling theory. Although the resulting coefficient is positive, it is insignificant.

H2a Opting out of the EGC status prematurely is positively related to the capital market transactions incentive

H2b Opting out of the EGC status prematurely is positively related to the corporate control contest incentive

H2c Opting out of the EGC status prematurely is negatively related to the proprietary costs incentive.

The second hypothesis looks for a relationship between voluntary disclosure incentives and premature EGC status declaim. The results regarding the second hypothesis are mixed since several voluntary disclosure incentives are investigated. For this hypothesis, significant results are found for the PharmaBio (H2c) and debt_incr (H2a)variable. There is a significant negative relation between companies that are classified as pharma-/biological and companies that

declaim their EGC status (β=-1,832, z=-2,3). Hence, companies that classify as a pharmaceutical or a biological company tend to retain their EGC status for longer periods. This way they have to disclose less (sensitive) information for the years where they qualify as an EGC. This finding supports the proprietary costs incentive (H2c) which states that a firm's decision to disclose information is influenced by the concern that such disclosures can damage their firm's competitive position in product markets (Dambra et al., 2015). Hence, this finding supports H2. The findings are in line with the researches of Dambra et al. (2015) and Berdejo (2014) who both already found evidence that companies in the R&D intensive industries, more specifically, the pharmaceutical and biological companies are benefiting more from the JOBS Act environment. The other measurement proxy for the proprietary cost incentive is the RD_AT_high variable and indicates if a firm has a relative high amount of R&D expenditures. The found relation is insignificant. For the corporate control contest incentive, the measuring proxy was underperformance compared to the year mean for ROA. The found relation is insignificant and hence no evidence is found for this voluntary disclosure incentive (H2b). The capital market transactions incentive predicts that companies that declaim their EGC status raise more capital in the year following the declaim. The regression has split this capital increase in an equity and a debt increase variable and shows a positive correlation for both of these capital market transaction incentive indicators (respectively β=0,949, z=1,49 and β=2,071, z=3,3). Hence, firms that are planning to raise capital in the nearby future might toss their EGC status and thus voluntarily disclose information, to reduce their cost of capital and to increase their capital liquidity for the planned capital raisings (Lang & Lundholm, 1997). Our findings however only show a significant result for the debt increase variable. Hence, no conclusions can be made regarding planned increases in public equity following the declaim of the EGC status (H2c).

As the OLS results for the regression on the pooled sample have just been discussed it is also interesting to see the results of the OLS regression results per year relative to the moment of the IPO. As Berdejo (2014) found that 40% of former EGCs no longer qualify as an EGC after year 1, it seems of value to run the regression on the sample for the different years (relative to the IPO). The results of the OLS logit regression for the sample from the year of the IPO until the fourth year after the IPO moment separately however, show no significant relation with any of the independent variables whatsoever. Hence these results are not extensively discussed and no conclusions can be made with regard to the moment of a firm's declaiming decision relative to the year of the IPO. The results are included in Appendix C of this paper.

In conclusion, the results indicate evidence of the proprietary costs incentive and the capital market transactions incentive as reasons for companies to voluntarily disclose, e.g. to declaim their EGC status. For the first hypothesis regarding a relation between executive compensation and dropping out of the EGC status, no evidence is found. For the second hypothesis, concerned with voluntary disclosure incentives behind declaiming, the results are mixed. For the proprietary costs incentive the results indicate a significant negative relation for firms that belong to the pharmaceutical or biological branch and the EGC status declaim decision. The results do not indicate such a relation for firms with relatively high R&D expenditures and the EGC status declaim. Consequently, the results can only be generalized for as far as Dambra et al. (2015) have done this before, namely a relation between the pharmaceutical/biological branch and the decision to maintain the EGC status. For the corporate control contest incentive the results are insignificant. The findings related to the capital market transactions incentive show a significant positive relation between the rise in a company's debt in the year following the EGC status drop out and the EGC drop out decision.

5. Conclusion and Discussion

5.1 Conclusion

This research investigates the relationship between the EGC drop out decision and executive compensation and voluntary disclosure incentives. The results of this thesis may contribute to the overall evaluation of the JOBS Act effectiveness as well as too agency and voluntary disclosure theorem. The research question of this paper is:

RQ: Why do firms declaim their EGC status prematurely after going public?

This thesis focuses mainly on the executive compensation incentive (based on agency and signalling theory) and on the proprietary costs, the capital market transactions and the corporate control contest incentive (based on voluntary disclosure theorem) as factors influencing the EGC drop out decision. This paper purposely does not elaborate on executive compensation components, as this paper does not aim to be a paper on executive compensation but rather about EGC drop out motives from a more generic point of view.

The first hypothesis of this paper is concerned with the relation between executive compensation and the EGC declaim decision. The results in this paper do not show a negative relation between firms with relatively higher executive compensation and EGC status declaim. The found correlation is in fact positive but the results are insignificant. Hence, the found results can be ignored. As a result, the first hypothesis of this research is rejected. Although agents of a company are utility maximizers (Garen, 1994), our results do not support the idea that overly paid executives would tend to disclose less information.

With regard to the second hypothesis, which investigates the influence of voluntary disclosure incentives on the EGC drop out decision, the evidence is mixed. For the proprietary costs incentive, a significant negative relation between firms that belong to the pharmaceutical or biological branch and the EGC declaim is found. Consequently, it seems that these companies benefit more from the JOBS Act provisions than firms that do not belong to these industries. However, this could also mean that pharmaceutical/biological firms are simply not growing as fast as other firms or that these firms were smaller at the IPO moment to begin with, which means they stay more often within the size requirements for retaining EGC status. Since the firms that have lost their EGC status due to exceeding the capital/size restrictions have been excluded in the regression, there could therefore be a sample selection bias. Nonetheless, based on the results non- pharmaceutical/biological firms seem more likely to voluntarily declaim the EGC status.

As a second proxy for the proprietary costs incentive the relative height of a firm's R&D was used. The results regarding this proxy were insignificant. As a result, it seems the role of proprietary costs in the EGC drop out decision is only partly supported. For the capital market transactions incentive, a significant positive relation is found between the rise in a company's debt in the year following the EGC status drop out and the EGC drop out decision. It thus seems that firms that drop their EGC status collect additional public debt following the EGC status drop out. The positive relation between EGC status declaim and the rise of public equity in the year following the EGC status declaim is insignificant and hence this relation is not supported. Lastly the results with regard to the corporate control contest incentive and the relation of underperformance with voluntary disclosure are not significant and are thus rejected.

5.2 Discussion

The results of this research have several implications for the existing literature on the JOBS Act, voluntary disclosure theory and the agency theorem. With regard to the literature on the JOBS Act, our research does not find a 40 percent drop out of EGCs in the year following the IPO as Berdejo (2014) did, but rather a continuous EGC declaim rate of 13% in the first, second and third year following the IPO. Based on these findings it does not seem firms merely adopted the EGC status to benefit from the JOBS Act de-risking provisions as the results of Berdejo might have suggested. Rather, EGCs seem to ongoingly take advantage of the JOBS Act provisions. In addition, of the declaiming companies about two-thirds lost their EGC status due to exceeding the restrictions to maintain the EGC status. Hence, The biggest part of declaiming firms does not voluntarily give up their status. With regard to the declaiming decision that EGCs face, our research indicates that firms belonging to the pharmaceutical or biological industry are more likely to retain their status. These findings support the ideas of Berdejo (2014) and Dambra et al. (2015) that these companies would benefit more from the JOBS Act provisions. These results support existing literature on the proprietary costs incentive as motive in a (non)disclosure decision.

There are several limitations to this research. First, the final sample used in the research regression consists of 237 firms. This makes it difficult to draw solid conclusions. Future research should extend our research with a bigger sample. Second, as this thesis wanted to look at several reasons for declaiming the EGC status from a generic point of view, it did not breakdown the executive compensation variable into the different components, such as fixed salary, stock compensation, bonuses and others. Future research could investigate the relation between these components of executive compensation and the decision to retain or declaim the

EGC status. Third, as mentioned before there possible exists sample selection bias within the sample used for the regression, as the firm year observations have been excluded of firms that have actually lost their EGC status due to exceeding the size/capital restrictions. Future research could extend this research and control for this matter. Finally, there are more voluntary disclosure incentives than the ones tested in this research (Graham et al., 2015; Healy &Palepu, 2001). Future research could extend our research by considering these other voluntary disclosure incentives.

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Attachments

Appendix A

Appendix A

JOBS Act provision classification

De-burdening provision categories	Provision classification	Provision measured by looking in S1-filings and 10-K reports for:
Reduced FS disclosure	Prov 1.1	Explicitly mention reduced FS requirements
	Prov 1.2	Reduced FS years (<3 years)
	Prov 1.3	Reduced FS data years (<5 years)
Delayed application new standards	Prov 2	Expl. mention delayed application of new accounting standards
PCAOB ruling opt out	Prov 3	Expl. mention exemption to comply withnew PCAOB rulings
Reduced executive compensation disclosure	Prov 4.1	Expl. mention reduced executive compensation disclosures
	Prov 4.2	Absence of a Compensation Discussion and Analysis paragraph(CD&A)
	Prov 4.3	Disclose executive compensation for less than 5 NEO's
	Prov 4.4	Disclose executive compensation for <3 years
Auditor Attestation Opt out	Prov 5	Expl. mention exemption of internal control auditor attestation
Exemption Dodd Frank Act requirements	Prov 6	Expl. mention exemption of Dodd-Frank Act requirements

Appendix B

Appendix B

EGC provision adoption - SRCs excluded

		Reduced FS disclosure			Reduced executive compensation disclosure			
Year relative to IPO	Nr of EGC's	*Provisions* Prov 1.1	Prov 1.2	Prov 1.3	Prov 4.1	Prov 4.2	Prov 4.3	Prov 4.4
Year +0	229	43,7%	59,8%	70,7%	92,4%	89,1%	87,8%	95,6%
Year +1	180	10,6%	18,9%	67,8%	93,4%	93,3%	89,4%	90,6%
Year +2	122	11,5%	21,3%	61,5%	92,7%	94,3%	88,5%	83,6%
Year +3	55	12,7%	27,3%	49,1%	94,5%	90,9%	92,7%	85,5%
Year +4	3	0,0%	0,0%	0,0%	66,7%	0,0%	33,3%	33,3%
Total	589	23,9%	36,2%	65,6%	92,8%	91,2%	88,6%	90,4%

The above table shows an overview of the adoption rate with regard to the provisions that EGCs can use (Westenberg, 2012) under use of the JOBS Act. The reduced executive compensation disclosure and the reduced financial statement disclosure provisions that the JOBS Act offers to EGCs, are already available to smaller reporting companies. Therefore, for these provisions the descriptive statistics are rerun, while controlling for EGCs that are also SRCs. Column 1 contains the distribution of firm year observations relative to the IPO. Column 2 shows the number of EGCs within the sample that are left per year relative to the IPO. For the different provisions, several features have been checked. In Column 3 up till Column 9, the adoption has been recorded with regard to these features. The classification in grey on the top of these column indicates which provision features measured belongs to which provision (Appendix A).

Appendix C

Appendix C

Sample per year logit regression results *Year relative to the IPO = 0*

All observations are EGC at year relative to the IPO=0, so there are no EGC declaims

Year relative to the IPO = 1

	Predicted. Sign	β	Std. Err.	z	P>z
(Constant)		6,818	2,680	2,540	0,011
Excess_comp	-	-1,077	1,000	-1,080	0,282
RD_AT_high	-	0,017	0,901	0,020	0,985
PharmaBio	-	-0,786	0,881	-0,890	0,372
Underperf	+	-0,006	0,725	-0,010	0,993
equity_incr	+	-0,854	0,789	-1,080	0,279
debt_incr	+	0,835	0,765	1,090	0,275
size_log	+	-0,869	0,225	-3,870	0,000
Leverage	+	1,918	1,063	1,800	0,071
Insider_Ownership	-	-0,027	0,014	-1,860	0,063
Profitability	+	0,934	0,894	1,050	0,296

For a (former) EGC: $Declaim\_EGC_t = \alpha + \beta1(Excess\_com)_t + \beta2(R\&D\_exp)_t + \beta3(pharma/bio\_ind)_t + \beta4(Underperf)_t + \beta5(Cap\_increase\_eq)_{t+1} + \beta6(Cap\_increase\_debt)_{t+1} + \beta7(Size)_t + \beta8(Leverage)_t + \beta9(Insider\_ownership)_t + \beta10(Profitability)_t + \varepsilon$. The dependent variable is EGC status declaim. The firm year observations included in the regression consist of all EGCs or initial EGC declaiming firm year observations per year relative to the IPO. This means this regression is run on several samples. If a firm year observation has a declaimed EGC status in prior year, in the year subsequent to that year the firm year observation for that firm is dropped from the regression. The total amount of firm year observations run in the regression is 201. Excess_comp is a dummy variable that equals 1 if a firms top three NEOs get paid more than the average of the top three NEOs for that year. RD_AT_high is a dummy variable that equals 1 if a firms R&D divided by Total Assets is above the average ratio for that year. PharmaBio is dummy variable that equals 1 if a firm is a Pharmaceutical or Biological company. Underperf is a dummy variable that equals 1 if the roa of a company is below the industry roa for that year. equity_incr is a dummy variable that equals 1 if a company's equity at t=0 is bigger than the company's equity at t-1. debt_incr is a dummy variable that equals 1 if a company's debt at t=0 is bigger than the company's equity at t-1. size_log is a continous variable which is the log of the total assets of a company. Leverage is Total Debt/Total Assets for that year. Insider Ownership is continuous and size ranges between 0 and 1. Profitability is a dummy variable that equals 1 if a company's Net Income is possitive. Because of the dummy variables the performed regression with these variables is a logit regression. Column 2 shows the expected sign of β based on the hypothesis development and research design. Column 3 and 4 show respectively the actual β and the standard error. Column 5 and 6 show the z value and the significancy of the relation. The regression analysis is performed with the broadly used significance level of 0.05

Appendix C (Continued)

Appendix C (continued)

Sample per year logit regression results *Year relative to the IPO = 2*

note: RD_AT_high != 0 predicts failure perfectly, hence RD_AT_high is dropped and 33 obs are not used
PharmaBio != 0 predicts failure perfectly, hence PharmaBio dropped and 35 obs not used
Underperf != 0 predicts failure perfectly, hence, Underperf dropped and 14 obs not used

	Predicted. Sign	β	Std. Err.	z	P>z
(Constant)		16,962	18,386	0,920	0,356
Excess_comp	-	3,825	5,655	0,680	0,499
RD_AT_high	-	0,000	(omitted)		
PharmaBio	-	0,000	(omitted)		
Underperf	+	0,000	(omitted)		
equity_incr	+	5,341	4,596	1,160	0,245
debt_incr	+	11,972	8,828	1,360	0,175
size_log	+	-2,299	1,816	-1,270	0,206
Leverage	+	-2,176	4,719	-0,460	0,645
Insider_Ownership	-	-0,016	0,117	-0,140	0,892
Profitability	+	-6,891	8,363	-0,820	0,410

Note: 5 failures and 0 successes completely determined

For a (former) EGC: $Declaim\_EGC_t = \alpha + \beta1(Excess\_com)_t + \beta2(R\&D\_exp)_t + \beta3(pharma/bio\_ind)_t + \beta4(Underperf)_t + \beta5(Cap\_increase\_eq)_{t+1} + \beta6(Cap\_increase\_debt)_{t+1} + \beta7(Size)_t + \beta8(Leverage)_t + \beta9(Insider\_ownership)_t + \beta10(Profitability)_t + \varepsilon$. The dependent variable is EGC status declaim. The firm year observations included in the regression consist of all EGCs or initial EGC declaiming firm year observations per year relative to the IPO. This means this regression is run on several samples. If a firm year observation has a declaimed EGC status in prior year, in the year subsequent to that year the firm year observation for that firm is dropped from the regression. While running the regression for year relative to IPO=2, RD_AT_high, PharmaBio and Underperf predict EGC_declaim perfectly and are omitted from the results. The total amount of firm year observations left, run in this regression consists of 44 firm year observations. Excess_comp is a dummy variable that equals 1 if a firms top three NEOs get paid more than the average of the top three NEOs for that year. RD_AT_high is a dummy variable that equals 1 if a firms R&D divided by Total Assets is above the average ratio for that year. PharmaBio is dummy variable that equals 1 if a firm is a Pharmaceutical or Biological company. Underperf is a dummy variable that equals 1 if the roa of a company is below the industry roa for that year. equity_incr is a dummy variable that equals 1 if a company's equity at t=0 is bigger than the company's equity at t-1. debt_incr is a dummy variable that equals 1 if a company's debt at t=0 is bigger than the company's equity at t-1. size_log is a continous variable which is the log of the total assets of a company. Leverage is Total Debt/Total Assets for that year. Insider Ownership is continuous and size ranges between 0 and 1. Profitability is a dummy variable that equals 1 if a company's Net Income is possitive. Because of the dummy variables the performed regression with these variables is a logit regression. Column 2 shows the expected sign of β based on the hypothesis development and research design. Column 3 and 4 show respectively the actual β and the standard error. Column 5 and 6 show the z value and the significancy of the relation. The regression analysis is performed with the broadly used significance level of 0.05

Appendix C (continued)

Sample per year logit regression results	*Year relative to the IPO = 3*

outcome does not vary --> No EGC declaimers due to other reasons than becoming a Large accelerated filer or having a revenue > 1 billion

	Year relative to the IPO = 4

outcome does not vary --> No EGC declaimers due to other reasons than becoming a Large accelerated filer or having a revenue > 1 billion

For a (former) EGC: $Declaim\_EGC_t = \alpha + \beta1(Excess\_com)_t + \beta2(R\&D\_exp)_t + \beta3(pharma/bio\_ind)_t + \beta4(Underperf)_t + \beta5(Cap\_increase\_eq)_{t+1} + \beta6(Cap\_increase\_debt)_{t+1} + \beta7(Size)_t + \beta8(Leverage)_t + \beta9(Insider\_ownership)_t + \beta10(Profitability)_t + \varepsilon$. The dependent variable is EGC status declaim. The firm year observations included in the regression consist of all EGCs or initial EGC declaiming firm year observations per year relative to the IPO. This means this regression is run on several samples. If a firm year observation has a declaimed EGC status in prior year, in the year subsequent to that year the firm year observation for that firm is dropped from the regression. While running the regression for year relative to IPO=3 and IPO=4 the results indicated that the outcome does not vary. After looking closely there are no declaimers after filtering out declaimers that have lost their EGC status.