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Effects of Directors and Officers Liability Insurance on Accounting Restatements

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Abstract

This study investigates the relationship between directors and officers liability insurance (D&O insurance) coverage and the probability of accounting restatements. The results show that when managers are covered by relatively higher levels of D&O insurance, they are more likely to restate their financial reports. Moreover, the findings indicate that D&O insurance coverage is related to core earnings restatements and income overstatements, suggesting that managers' accounting policies are more aggressive when they have fewer legal liability concerns. Overall, these results provide consistent evidence that reducing managerial legal liability has the effect of encouraging managers to misstate reported earnings.

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