

# Syllabus ACCT 611

Stanford 2014

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## 1 Description

Accounting as a scientific discipline studies the provision, dissemination, and interpretation of information that takes place in capital markets and within firms. The accounting literature addresses this problem from two angles. The first one, referred to as the commitment approach, assumes that firms have the ability to commit to policies that are contingent upon information.<sup>1</sup> Throughout this class, we will assume that no such commitments are possible, so that firms' choices must be self-enforcing at any given point in time.

## 2 Methodology

The course consists of a series of lectures and student presentations (see calendar below). During each lecture, we will discuss seminal papers as well as recent theory developments in both the accounting and information economics literature.

Before each class, you will be required to read and work through a classic paper (labeled "assigned" in the calendar below). At the start, a student will be asked at random to prove on the blackboard (line by line) the main result of the assigned paper. There are two reasons why you may benefit from such an exercise, even if you plan to work on empirical issues: first, because being able to argue logically is more difficult than you think, but it is generally helpful. Second, because the subtlety and beauty of many theoretical results is often hidden in appendices.

## 3 Presentations

You will be required to present one of the papers listed below (marked with "\*") based on your preference (please let me know if you would like to present a different paper, including your own theoretical papers).

Student presentations last 60 minutes. The presenter is expected to "wear the hat" of the paper's author. This means he must motivate the question, defend the assumptions, and provide intuition for the results. During the presentation, the remaining students will be evaluated based on their capacity to articulate critical but thoughtful questions.

## 4 Content

### 1. The Value of Information (2 sessions)

- Risk [Rothschild and Stiglitz \(1970\)](#)
- Blackwell Informativeness [Blackwell \(1951, 1953\)](#)
- (Entropy) [Shannon \(2001\)](#)
- Impossibility of General Accounting Standards [Demski \(1973\)](#)

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<sup>1</sup>Compensation contracts based on firm's performance are a classic example of this approach

2. Disclosure of Verifiable Information (3 sessions)
  - Unraveling [Milgrom \(1981\)](#); [Grossman \(1981\)](#)
  - Proprietary Costs [Verrecchia \(1983\)](#); [Jovanovic \(1982\)](#)
  - Unknown Information Endowment [Dye \(1985\)](#); [Jung and Kwon \(1988\)](#)
  - Disclosure and Reputation [Jullien and Park \(2014\)](#)
3. Certification Intermediaries (2 sessions)
  - Monopoly Certifier [Lizzeri \(1999\)](#)
  - Certification and Investment [Albano and Lizzeri \(2001\)](#)
  - Dynamic Certification ?
4. Signaling and Earnings Management (EM) (3 sessions)
  - IPO Signaling [Leland and Pyle \(1977\)](#)
  - Earnings Management Motives [Dye \(1988\)](#)
  - Unknown Incentives [Fischer and Verrecchia \(2000\)](#)
  - Real Earnings Management [Stein \(1989\)](#)
  - Earnings Quality and Earnings Management ?
5. Cheap Talk: Soft Information and Trust (2 sessions)
  - Cheap Talk [Crawford and Sobel \(1982\)](#)
  - Multiple Senders [Battaglini \(2002\)](#)
  - Cheap Talk in Accounting [Gigler \(1994\)](#); [Melumad and Shibano \(1991\)](#)
6. Market Microstructure: Trading and Market Efficiency (3 sessions)
  - Impossibility of Efficient Markets [Grossman and Stiglitz \(1980\)](#)
  - Liquidity and Market Power [Kyle \(1985\)](#)
  - Bid-Ask Spread [Glosten and Milgrom \(1985\)](#)
  - Bubbles and Crashes [Abreu and Brunnermeier \(2003\)](#)
  - Market Efficiency with Disperse Information [Ostrovsky \(2012\)](#)
  - Cost of Capital and Information [Lambert et al. \(2007\)](#); [Bertomeu et al. \(2011\)](#)
7. Designing Information Systems (2 Sessions)
  - Bayesian Persuasion [Kamenica and Gentzkow \(2011\)](#)
  - Beeps [Ely \(2014\)](#)
  - Accounting Applications [Kanodia et al. \(2005\)](#)
8. Global Games and Market Transparency (2 Sessions)
  - Beauty Contests [Morris and Shin \(2002\)](#)
  - OLG and Price Drift [Allen et al. \(2006\)](#)
  - Mark-to-Market [Plantin et al. \(2008\)](#)

## 5 Grading

|                     | Percentage |
|---------------------|------------|
| Class Participation | 30%        |
| Presentation        | 40%        |
| Final Exam          | 30%        |

## 6 Calendar

| Date | Session | Assigned                         | Further Reading                      | Further Reading                               |
|------|---------|----------------------------------|--------------------------------------|---|
|      | 1       | Rothschild and Stiglitz (1970)   | Ganuzza and Penalva (2010)           |   |
|      | 2       | Demski (1973)                    | Blackwell (1951), Hirshleifer (1971) | Beaver and Demski (1979)                      |
|      | 3       | Milgrom (1981)                   |                                      |   |
|      | 4       | Verrecchia (1983)                | Jullien and Park (2014)              | Verrecchia (1990)                             |
|      | 5       | Dye (1985); Jung and Kwon (1988) | Acharya et al. (2011)                |   |
|      | 6       | Lizzeri (1999)                   |                                      |   |
|      | 7       | Albano and Lizzeri (2001)        |                                      |   |
|      | 8       | Dye (1988)                       | ?                                    |   |
|      | 9       | Fischer and Verrecchia (2000)    | Stein (1989)                         |   |
|      | 10      | Crawford and Sobel (1982)        | Fischer and Verrecchia (2000)        |   |
|      | 11      | Gigler (1994)                    | Battaglini (2002)                    |   |
|      | 12      | Grossman and Stiglitz (1980)     | ?                                    | Melumad and Shibano (1991)                    |
|      | 13      | Kyle (1985)                      | Albagli et al. (2011)                |   |
|      | 14      | Glosten and Milgrom (1985)       | Ostrovsky (2012)                     | Bertomeu et al. (2011); Lambert et al. (2007) |
|      | 15      | Gox and Wagenhofer (2009)        | Abreu and Brunnermeier (2003)        |   |
|      | 16      | Kanodia et al. (2005)            | Kamenica and Gentzkow (2011)         |   |
|      | 17      | Morris and Shin (2002)           | Ely (2014)                           |   |
|      | 18      | Plantin et al. (2008)            | Allen et al. (2006)                  |   |

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