Impression Management Strategies in Disclosure Documents

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Firms use various corporate disclosure documents to communicate valuable incremental information to their investors about the firm's performance. Firms also use these documents opportunistically to manage or influence the perceptions of investors. This opportunistic behavior of firms in their disclosure documents is often referred to as impression management, which is a rapidly growing field of research in accounting. However, there is still little known about impression management practices of small, low-visibility firms. Moreover, there is lack of research on retail investors' direct attention to impression management strategies as prior research has mainly focused on stock market reaction.

This study analyzes several impression management strategies in the earnings press releases of TSX Venture Exchange firms to investigate whether, and how, low-visibility firms engage in impression management. It also explores the investor reaction to impression management strategies by supplementing stock market reaction with online investment discussion board reaction. This note is part of a sequence of three research notes. The first note (#PARG 2020-02RN) is about impression management strategies. The second note (#PARG 2020-03RN) is about firm perspective on impression management and provides findings on impression management practices of TSX Venture Exchange firms. The third note (#PARG 2020-04RN) is about investor perspective on impression management and shares findings on the consequences for investors of the use of various impression management strategies.
Impression management

First conceptualized by Goffman (1959) in social psychology, impression management is often described as a self-presentation process to appeal to target audiences and to manage others’ perceptions. Similarly, in the context of organizations, impression management can be defined as managing disclosures in a way that manipulates or distorts investors’ perceptions of the firm’s financial performance or other organizational outcomes (Davison, 2008; Guillamon-Saorin, Osma and Jones, 2012). Most of the time, impression management entails managing tone, highlighting or masking certain narrative portions of corporate disclosure documents, and manipulating readability or other rhetorical aspects.

Impression management may occur in a wide range of corporate disclosure documents such as Management Discussion and Analysis (MD&A), interim reports, presidents’ letters, chairmen’s reports, letters to stockholders, financial statement footnotes, prospectuses, and earnings press releases (EPRs). Each of these corporate disclosure documents provides a varying level of opportunity for the use of impression management. For example, while voluntary disclosure documents such as presidents’ letters allow for the use of impression management with great flexibility regarding content and organization, mandatory reports such as annual financial statements restrict the use of impression management to certain sections such as the wording used in notes. Unlike voluntary disclosures, mandated disclosures such as financial statements are audited and are regulated by governing financial bodies in terms of both content and structure of information contained in such documents (Healy and Palepu, 2001). Therefore, impression management is more likely to occur in voluntary disclosures rather than mandatory financial reporting documents.

Impression management strategies and analysis methods

There are several ways or techniques firms can use to engage in management strategies. In their review of prior literature, Merkl-Davies and Brennan (2007) identify seven major impression management strategies that can be classified into concealment and attribution strategies used by firms (see Table 1). They indicate that concealment strategies are generally achieved by either emphasizing good news (by tone management, visual and structural manipulation, performance comparisons, and choice of earnings number) or obfuscating bad news (by readability manipulation or rhetorical manipulation). Attribution strategies (attribution of performance), on the other hand, involve interpreting organizational events with a tendency to claim more responsibility for successes than for failures.
Tone management

Tone in narrative disclosures can be too positive or negative relative to concurrent performance results. As such, tone management can be defined as firms’ actions to control the tone of qualitative information in disclosure documents that cannot be warranted by current performance results (Huang et al., 2014).

Tone management studies are prevalent in the empirical impression management literature. These studies investigate various outcomes related to tone in the narrative disclosures and vary by approach taken to measure tone. Several studies have used a “bag-of-words” approach, which generally is based on the frequency of occurrence of each classified word, to measure tone in disclosures. While some of these studies use general words lists (for positive and negative words) in commonly used content analysis software packages such as the Linguistic Inquiry and Word Count (LIWC), General Inquirer (GI) and DICTION to quantify tone, others create custom word lists that are more suitable for describing tone in financial communication. Overall, findings from prior literature indicate that managers deliberately construct tone as part of their impression management in narrative documents.

Visual and structural manipulation

Firms engage in impression management through visual and structural manipulation with the primary purpose of emphasizing organizational outcomes (Davison, 2008). This impression management strategy involves the placement and repetition of words, phrases, and statements in narrative disclosure documents with the goal of attracting readers’ attention to specific information.

Visual and structural manipulation studies focus on the investigation of impression management within a single disclosure, and they apply mostly manual content analysis to identify impression management by repetition and placement of information. For example, Pesci, Costa and Soobaroyen (2015) perform a quantitative manual content analysis while considering the level of intensity of repetition. More specifically, Pesci et al. (2015) examine identical, similar, and accumulated repetition strategies which, the authors argue, have low, higher and the most intensive effect to create an impression, respectively. Pesci et al. (2015) admit the manual analysis is time-consuming; however, they argue that the inductive nature of identifying similar and accumulated repetition requires a more detailed and sophisticated analysis which can be better achieved by manual content analysis.

Performance comparisons

Performance comparisons as an impression management strategy involves the use of numerical performance comparisons such as benchmark earnings numbers and previous performance referents that show the firm’s current performance in the best possible way (Merkl-Davies and Brennan, 2007). Performance comparison in disclosure
documents has also been examined by researchers as a sign of emphasis in the form of reinforcement. For example, Guillamon-Saorin et al. (2012) investigate a performance comparison strategy in the headlines of EPRs. Their approach to identifying reinforcement involves manual coding of EPR headlines in which performance figures are accompanied by a benchmark. Guillamon-Saorin et al. (2012) find that firms only use positive performance comparisons in the headlines of their EPRs, i.e. they use comparisons only when performance has improved relative to a prior period.

Choice of earnings number

Choice of earnings number as an impression management strategy entails selecting or emphasizing certain earnings figures and omitting others to portray firm performance (Merkl-Davies and Brennan, 2007; Guillamon-Saorin, 2006). Guillamon-Saorin et al. (2012) examine the degree of selectivity of earnings numbers in the headlines of earnings press releases from the face of the profit and loss statement. They use a manual coding approach that involves coding quantitative items in the profit and loss account and matching those items with earnings numbers included in the headlines of EPRs. Consistent with prior research (Aerts, 2005; Bowen, Davis and Matsumoto, 2005), Guillamon-Saorin et al. (2012) find that firms emphasize positive performance by highlighting the most favorable earnings numbers.

Readability manipulation

Readability manipulation entails managing the verbal complexity of disclosures to obfuscate performance results. The Fog index, Flesch index, and Smog index are widely used readability measures which consider metrics such as sentence length, number of complex words per sentence, and some measure of verbal complexity such as syllables per word to assess readability. A sizeable literature has found that poorly performing firms obfuscate their disclosures using textual complexity. However, other researchers have argued that this relationship between readability and firm performance does not exist (Rutherford, 2003).

Rhetorical manipulation

Studies on rhetorical manipulation mainly investigate how firms manage rhetorical features such as communication style, narration, and verbal structure in narrative portions of their disclosure documents (Jameson, 2000; Yuthas, Rogers and Dillard, 2002; Aerts and Yan, 2017). Brennan, Guillamon-Saorin and Pierce (2009) study how firms rhetorically reinforce sentences using qualifiers to emphasize arguments in hostile takeover defense documents. They argue it is not possible to derive contextual meaning by computer assisted methods that assess keywords or statements analysis. Thus they manually analyze the narrative content of the disclosures to examine the use of qualifiers in sentences that attack the bidding firm and sentences that defend the target firm.
Attribution of performance

Several studies have documented strong evidence that firms engage in impression management by attributing positive performance to internal factors and negative performance to external factors (Kimbrough and Wang, 2014; Aerts and Yan, 2017). A sizeable literature applies content analysis techniques to examine whether, and how, firms attribute positive/negative organizational outcomes to their own actions/external factors.

Studies on attribution of performance rely on manual coding to identify positive and negative outcomes and classify attributions to identified outcomes. For example, Kimbrough and Wang (2014) read EPRs to identify statements explaining current period performance. Then, they code the cause in each sentence as having either favorable or unfavorable impact on performance, as cited by a disclosing firm. Finally, the authors classify the sentences to be attributed, by the firm, as either an internal or external cause. Other studies using manual content analysis perform similar analyses to this approach. To date there has been no study that uses computer-based methods to determine performance attribution in disclosure documents.

Summary of impression management strategies and analysis methods

The seven impression management strategies discussed above have been widely studied in prior impression management research which investigated various corporate disclosure documents. The choice of manual versus computer-assisted methods of analysis is primarily determined by the impression management strategy investigated. Computer-assisted methods enable research to analyze vast amounts of content efficiently; however, they may not be applicable in situations where the study requires a sophisticated analysis which can be better achieved by manual methods. Table 1 summarizes the seven impression management strategies identified by Merkl-Davies and Brennan (2007) and recaps the disclosure content management actions involved when engaging in each impression management strategy.

The investigation of each perspective (firm and investor) entails the analysis of six (out of the seven) impression management strategies shown on Table 1 using computer-assisted content analysis methods. The performance attribution strategy is not included because, as prior literature shows, this impression management strategy can only be reliably analyzed using manual methods.
Table 1 - Summary of impression management strategies

<table>
<thead>
<tr>
<th>Impression Management Classification</th>
<th>Impression Management Strategy</th>
<th>Involved Action</th>
</tr>
</thead>
<tbody>
<tr>
<td>Concealment – Emphasis on good news</td>
<td>Tone management</td>
<td>Using optimistic and pessimistic words</td>
</tr>
<tr>
<td></td>
<td>Visual and structural</td>
<td>Placing information and managing visual aspects</td>
</tr>
<tr>
<td></td>
<td>manipulation</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Performance comparisons</td>
<td>Using numerical performance comparisons</td>
</tr>
<tr>
<td></td>
<td>Choice of earnings number</td>
<td>Selecting main performance number for highlighting</td>
</tr>
<tr>
<td>Concealment – Obfuscation of bad news</td>
<td>Readability manipulation</td>
<td>Manipulating verbal complexity</td>
</tr>
<tr>
<td></td>
<td>Rhetorical manipulation</td>
<td>Managing rhetorical styles and verbal structure</td>
</tr>
<tr>
<td>Attribution</td>
<td>Attribution of performance</td>
<td>Associating performance with internal and external factors</td>
</tr>
</tbody>
</table>

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References


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