Moving the Bottom Line:
The Prominence of Net Income in Earnings Press Releases

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Abstract: This study explores the differences in quarterly earnings press releases of U.S. public companies based on their net profit and/or net loss. It compares earnings releases issued by companies that recorded a net loss followed by a net profit in consecutive quarters during 2003. Also compared is a sample of companies that recorded two consecutive losses and companies that recorded two consecutive profits during the same six-month period. The content analysis of 1,200 press releases shows significant differences in the headlines and text of releases during money-losing quarters and releases during money-making quarters. Social desirability theory suggests that many companies are likely to "play up" good news and "play down" bad news in hopes of appealing to internal and external audiences. The result of efforts to be socially desirable may be seen as attempting to mislead investors and the financial press.

Introduction

Imagine a press release from the Democratic National Committee with this headline: "Democratic presidential candidate receives 11.7 percent more votes in 2004 than 2000 candidate." Or this headline from the New York Yankees baseball team: "Yankees report more runs, more hits, fewer errors in 2004 American League Championship Series compared to 2003." Both headlines are accurate[1] but beside the point: Democrats lost the presidential race in both election cycles; the Yankees beat the Red Sox in 2003 but lost in 2004. Regardless of improvement in various subordinate statistical categories, Democrats and Yankee fans forever will remain fixed on the losses from their respective contests.

While these imaginary press release headlines seem far-fetched, some American publicly traded companies play a similar game when it comes to reporting financial results when those financial results are not positive. Companies must follow specific rules in official quarterly and annual reports filed with the U.S. Securities and Exchange Commission[2], and their filings must include financial data derived by following Generally Accepted Accounting

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[1] In the Democratic example, John Kerry received 56.3 million popular votes in 2004; Al Gore received 51 million votes in 2000. In the Yankees example, the team scored 50 runs in 2004, up 50 percent from 2003; recorded 75 hits in 2004, up 39 percent, and committed three errors, down 40 percent.

[2] For more information, start at the Securities and Exchange Commission's Division of Corporate Finance Web page, at http://www.sec.gov/divisions/corpfin.shtml.

Principles (GAAP) promulgated by the Financial Accounting Standards Board. But the SEC gives wider latitude to earnings press releases that companies issue to announce and to elaborate upon their financial statements. By choosing which financial statistics to use (or ignore) in the headlines and text of their earnings releases, companies can actively choose which financial data to highlight and which financial data to subordinate. Regardless of how many improvements in subordinate financial line items or the inclusion of pro forma information above or in place of GAAP information, stock analysts, investors, the Securities and Exchange Commission, and the financial press remain fixed on the bottom line – the GAAP "net income" (DeGeorge, Patel, & Zeckhauser, 1999).

Since investors and analysts remain focused on specific SEC mandated guidelines in assessing and evaluating the success of a company, ethical questions are raised when investor relations specialists and professional communicators choose to bury or even eliminate the mention of GAAP net earnings in their earnings press releases. As Atkinson (2002) reminds us, "There is a fine line between failing to disclose information and disclosing it in such a way as to hide its reality." (p. 212). Edgett (2002) offers 10 specific criteria for ethically desirable public relations advocacy. Within these 10 criteria, seven focus on issues related to honesty and transparency in the public relations process.

This exploratory study compares earnings press releases issued by U.S.-based publicly traded companies during the second and third quarters of the 2003 calendar year, looking for differences in headlines and text based upon the net income of the companies issuing the releases. This study is centered, in part, on the portions of Edgett's 10 criteria of advocacy in public relations that deal with issues of transparency and honesty[3] Unlike studies

[3] Among the "10 criteria for ethically desirable public relations advocacy," we consider veracity ("full truthfulness in all matters," validity ("all communication on behalf of the client or organization are

published in scholarly financial journals that focus on financial statistics or the stock-price ramifications of corporate news, this study focuses on the text of messages sent by companies toward audiences such as investors and journalists, who often are not as astute in corporate finance as accountants and investment analysts. The assumption is that journalists and many "regular" investors want to learn the company's quarterly bottom line as quickly and easily as possible. Popular press – ranging from *The Wall Street Journal* to daily general-interest newspapers – often devote little space to quarterly corporate reports except for total revenue, GAAP net income, and GAAP earnings per share. The Associated Press (2002) notes that it "traditionally focused such stories on 'net' income," which is the preferred practice unless "extraordinary charges or gains weigh so heavily on the results that using net earnings in the lead would ignore the news." A further assumption is that journalists and others prefer to see earnings releases written in "inverted pyramid," the journalistic style that places the most important information at the beginning of an article and less-important information at the bottom. Companies may not use that style in their press releases, but most journalists rewrite those press releases into inverted pyramid style for publication "because it meets the needs of media users" (Mencher, 1997).

This study shows that companies sometimes make it difficult for readers to find those three financial items within the text of their earnings press releases, which calls into question the ethical principal of veracity as mentioned by Edgett – a question that has become salient in the final community in the wake of accounting scandals involving Enron, WorldCom, HealthSouth, and other publicly traded corporations. This question of veracity becomes particularly salient for companies that lose money in one quarter and turn a profit in the next quarter.

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defensible against attacks on their validity"), and respect ("regard for audiences as autonomous individuals with rights to make informed choices….")

Background

Companies face strict penalties for failing to provide timely and accurate reports of their financial statements. However, as many studies and popular articles have discussed (e.g. Bhattachanya, Della Vigna, Gross, 2004), the Securities and Exchange Commission has fewer rules regarding financial earnings releases issued by companies. Earnings releases, such as news or press releases, contain "timely information about an activity of a public relations practitioner's organization, distributed in a ready-to-use form." (Wilcox, Ault, Agee, 1998, p. 551). Their public relations textbook advises practitioners that their releases should "[n]ever use excessively technical language in a release for a general audience. The objective is communication, not confusion" (Wilcox, Ault, Agee, & Cameron, 2001, p. 383). Although these guidelines are universal for all public communication efforts, it remains impossible to guarantee that these strategies are used by all communicators.

As corporate accounting scandals have rocked the financial world in the past few years, researchers and other have addressed the underlying ethical concerns involved with the creation and distribution of earnings releases. Atkinson (2002) discussed the ethics behind the perception and use of press releases and the role of corporate communicators within this process. Additionally, DeGeorge, Patel, & Zeckhauser (1999); Edgett (2002), and Francis (1990) remind public communicators and investor relations specialists of the importance in maintaining positive, consumer-driven information campaigns to maintain the trust and loyalty of the audience.

In December 2001, the Securities and Exchange Commission (SEC) warned both companies and consumers about the inclusion and use of pro forma results in prepared earnings reports (Release Nos. 33-8039, 34-45124, and FR-59). "Investors are likely to be deceived if a company uses a 'pro forma' presentation to recast a loss as if it were a profit, or to obscure a material result of GAAP financial statements, without clear and comprehensible explanations of the nature and size of the omissions." (SEC, 2001). Similar statements by Financial Executives International (2001) and the National Investor Relations Institute (2004) shortly followed this warning announcement.

> Earnings press releases should include "reported" results for the period presented under generally accepted accounting principles (GAAP)…. Reconciliation between GAAP and pro forma results should be treated in similar fashion for comparable periods. In other words, elements of the reconciliation should not be presented in one period without including similar elements in pro forma results of comparable periods. (Financial Executives International, 2001).

In addition to the comments by the SEC and professional organizations, academic studies have evaluated the use and ethical implications by the continued use of pro forma data within the traditional earnings release. Barbarash (2001) warned investors that the pro forma results they may be reading were the equivalent of financial hypotheticals. Amernic (1998) reminded faculty and instructors that "the corporate annual report and all its attendant systems and process, are a rhetorical device" (Amernic, 1998, p. 89). Additionally, other researchers (Hirshleffer and Teoh, 2003 and Louge & Marquardt, 2004) add further concerns about the potential for companies to use earnings releases to misguide or distort financial reporting.

Research and dialogue relating to the corporate earnings releases does not end with pro forma reporting. Issues relating to reporting "bad news" after the market has closed on Friday afternoons (Damodaran, 1989; DellaVigna & Pollet, 2004; and Gross, 2004), timing (Stice, 1991; Francis, Pagach, & Stephan, 1992; and Francis, Schipper, & Vincent, 2002), and the impact of news placement of stock prices (Thompson, Olsen, & Dietrich, 1987 and Patell & Wolfson, 1982) have all received attention in both academic journals and the media.

Social desirability theory, as defined by Crowne & Marlowe (1964) offers insight into why companies seek to accentuate positive financial news and subordinate negative news. Phillips and Clancy (1972) define social desirability as "a response determinant that refers to the tendency of people to deny socially undesirable traits or qualities and to admit to socially desirable ones." (p. 923). This phenomenon, usually discussed within the realm of survey construction (Zerbe & Paulhus, 1987) has also been explored in the study of mass communications phenomenon. The social desirability theory was designed to assess adults; however, the theory seems to apply to corporations and the people who run them.

The research of this project builds upon the structure of both Phillips and Clancy (1972) and Lougee and Marquardt (2004), whose analysis of earnings press releases showed that companies with low GAAP earnings were more likely than other companies to include pro forma data in their press releases. Similar to the work of Lougee and Marquardt (2004), a content analysis of earnings releases was conducted to evaluate the tendency and frequency of companies highlighting good news by placing this information higher in earnings releases.

Hypotheses

Previous research, non-quantified observation[4], and social desirability theory suggest the following hypotheses:

> H1: Companies that lose money in a quarter are more likely to wait longer in their earnings releases to make a first mention of net income than companies that make money in a quarter.

This hypothesis is based upon the notion that individuals or companies tend to delay delivering bad news, as well as literature suggesting that companies with poor GAAP net

[4] One of the authors of this study is a business editor at a daily newspaper. His duties include reading press releases issued by publicly traded companies and rewriting earnings releases.

incomes will highlight pro-forma earnings and place GAAP information in a subordinate position in the press release.

> H2: Companies that lose money in a quarter tend to wait longer in their earnings releases to offer a comment from a corporate officer than companies that report a positive net income in a quarter.

This hypothesis is based upon social desirability theory, which posits that individuals do not like having their names associated with bad news but enjoy being the bearer of good news.

> H3: Companies that lose money in a quarter are less likely to state their net loss in a headline than companies that make money.

Closely related to H1 is the notion that companies that lose money will be more likely to delay mention of net income than companies that make money.

Methodology

Data were collected from 1,282 press releases issued during 2003 by 641 companies. Choosing companies began with use of Standard & Poor's Research Insight, a computer database of financial statistics compiled for roughly 20,000 North American companies. Researchers narrowed the list by identifying companies with shares traded on the New York, American, Nasdaq, or Over-the-Counter market stock exchanges. The group was narrowed to 592 companies that reported a negative net income (using GAAP standards) in the April-to-June 2003 quarter and a positive net income in the July-to-September quarter. These time periods were chosen in hopes of capturing companies that were not reporting fourth-quarter and full-year results, which could affect how companies report earnings.[5] The group was further narrowed to American-based companies that were most likely to be subject to the

[5] A hypothesis not tested here is that companies with "bad" fourth quarters might lead their press releases with full-year results instead of quarterly results.

reporting rules of the U.S. Securities and Exchange Commission. Researchers also eliminated from analysis companies that did not issue press releases in both quarters, were acquired by other companies, filed for bankruptcy protection, or were not public companies during the entire 12-month period before earnings releases were issued.

For further comparisons, researchers chose at random 200 U.S. companies reporting positive net income in both quarters and 200 U.S. companies reporting net losses in both quarters of the study period. After winnowing the companies using the aforementioned criteria, data were collected on 150 companies reporting two profitable quarters and 116 companies reporting losing quarters.[6] Data from Research Insight include net income, and two measures that offer insight into a company's desirability to investors: the number of shares traded by quarter, and each company's third-quarter 2003 market capitalization, a measure of the number of shares issued by a company multiplied by its stock price.

The units of analysis are each press release. Researchers obtained press releases from corporate Web sites, from Nexis, and from SEC filings collected by 10kWizard, an Internet-based service that offers advanced searching capabilities of corporate filings with the SEC. Researchers copied the headline of each press release and the body of each press release into word-processing files. To focus on the portion of the press release with information specific for that quarter, researchers eliminated the boilerplate typically at the bottom of releases, including information about a conference call with stock analysts and the description of the company's business. Also eliminated from analysis were the accompanying financial tables

[6] The SEC does not require companies to issue press releases to correspond with quarterly or annual earnings reports. The discarded companies were not subjected to statistical tests, but researchers noted that companies that made money during both quarters were more likely to issue press releases than companies that lost money. At least dozen companies did not issue press releases during the money-losing quarter but issued press releases when they made money, which could be a function of social desirability or a practical reality, such as not having personnel to write a release.

typically included below the text of press releases, although financial tables were included in the analysis when they were weaved into the text of the quarterly earnings releases.

Researchers counted the number of words in each press release (from the end of the headline to the start of the boilerplate.) The word count started at the first sub-headline item for companies that used multiple sub-headlines to highlight key topics discussed in greater detail in the press releases. Using those criteria, researchers also counted the words until the first mention of GAAP net income or per-share GAAP earnings, and the number of words until the first mention of a corporate officer or comments from that officer.

Researches also noted what they determined to be substantial differences between quarters in the headlines and the body of press releases for each company. A substantial difference in headlines, for example, would be "Crompton Reports Second Quarter Results" in a money-losing quarter and "Crompton's Third Quarter Earnings Significantly Exceed Prior Year" in the subsequent, money-making quarter.[7] Companies that mentioned a loss in the second-quarter headline and profit in the third-quarter headline were not coded as "significantly different," because net income was highlighted in both headlines. A substantial difference in the body of press releases, for example, would be a company's top mention of a six-month net income above a quarterly loss in the second quarter, but the top mention of a quarterly profit above nine-month earnings in the subsequent third quarter.

To account for differences in the number of words in press releases[8] and to account for the 35 press releases by companies that failed to report GAAP net income in a money-losing quarter but included it in a profitable quarter, a score for each press release was

[7] This is an actual example of "significantly different" headlines by a company reporting a second-quarter loss and third-quarter profit. But because the company mentioned its GAAP net income 10 words into both press releases, the text of this company's releases were not coded as "significantly different."
[8] The shortest press release was 70 words; the longest, 5,653 words. The median press release was 886 words; the mean was 725 words.

calculated to reflect how early the net income was mentioned in each press release. The formula for the "prominence score:" 1 minus the number of words until net income is mentioned, divided by total number of words in the press release. Press releases with prominent mention of net income therefore received higher scores; press releases with no mention of GAAP net income were given a .001 score.

Findings

Public companies have a considerable amount of latitude in what financial information they put in the text of earnings press releases, and in where and how they report financial information in those releases. And many of those companies use that latitude to highlight good news and put less emphasis on bad news.

H1 states that companies that lose money in a quarter tend to wait longer in their earnings releases to provide net income (or per-share earnings) than companies that make money in a quarter. A variety of statistical tests support this hypothesis, but simple word counts seem sufficient to show that companies wait longer in an earnings release to reveal a loss than to mention a profit. Table 1 shows descriptive statistics for all press releases based on whether the press release was issued by a company that made money or lost money. The mean profitable company mentions GAAP net income in the 68th word of press release; a money-losing company waits until the 112th word to mention net income in a press release. This difference was significant, $t(1,279) = -5.36$, $p<.001$.

Table 1

Number of words until first mention of net income, regardless of quarter

Variable	N	Mean words until first mention of GAAP net income	Standard deviation	Standard error
In quarters with positive net income	675	68.25	111.18	4.28
In quarters with negative net income	606	112.50	179.54	7.29

Companies that lost money in second quarter and made money in the third quarter are included once on both sides of the equation, suggesting that some of these companies change the placement of net income in press releases based on whether they made or lost money. The differences are offered in greater detail in Table 2, which shows the mean number of words until the first mention of net income, based on the quarter and whether the company earned or lost money that quarter. The analysis shows that companies that consistently made money also were consistent in where they first mentioned net income in the text of their earnings press releases. These companies usually highlighted their profits by the first 50 words of their releases, which is more than twice "as fast" as companies that lost money regardless of quarter. Also consistent were companies that lost money in both quarters. The nine-word difference between the quarters perhaps can be explained by differences in press releases that include annual financial data along with quarterly data, or of coding error. Whatever the explanations, the differences are not statistically significant.

Companies that lost money in the second quarter took longer to mention net income than in their third-quarter earnings releases, when the reported profits. In short, companies that lost money in the second quarter of 2003 took 31 percent fewer words before mentioning their third-quarter profit.

Table 2

Number of words until first mention of net income, by quarter and profit/loss

Companies recording:	Number of companies in analysis*		Mean number of words until first mention of GAAP net income	
	Q2	Q3	Q2	Q3
Profits in both quarters	150	150	50.3	49.4
Losses in both quarters	114	116	116.0	107.1
Second quarter loss; third quarter profit	355	375	121.5	83.1
All companies	619	641	103.3	79.6

* Some companies did not file press releases in both quarters.

Table 3 shows analysis of variances in mean words until net income is mentioned between companies, by quarter, based on their performance across the two-quarter period. In all but one instance, companies that made money in a quarter were statistically more likely to mention net income higher in press releases than companies that lost money, regardless of quarter. The lone exception is the third-quarter comparison between companies that lost money in both quarters and companies that had a second-quarter loss and third-quarter profit. The hypothesis would suggest a significant difference, but a Tukey score between these groups in the third quarter is not statistically significant. An ANOVA of the "prominence score," to account for press releases that did not include GAAP net income, showed a wider difference, but again, not statistically significant, with a Tukey score of 0.14 at $p<0.09$.

Table 3

Analysis of variance between quarters and financial results

Comparisons of companies by profit/loss and by quarter			Mean Difference		Standard error	Sig. level
Second Quarter	Both profit	Both losses	-65.73	*	21.75	0.01
		Q2 loss; Q3 profit	-71.19	*	17.07	0.00
	Both losses	Both profit	65.73	*	21.75	0.01
		Q2 loss; Q3 profit	-5.46		18.82	0.95
	Q2 loss; Q3 profit	Both profit	71.19	*	17.07	0.00
		Both losses	5.46		18.82	0.95
Third Quarter	Both profit	Both losses	-57.73	*	14.54	0.00
		Q2 loss; Q3 profit	-33.76	*	11.36	0.01
	Both losses	Both profit	57.73	*	14.54	0.00
		Q2 loss; Q3 profit	23.97		12.49	0.13
	Q2 loss; Q3 profit	Both profit	33.76	*	11.36	0.01
		Both losses	-23.97		12.49	0.13

* The mean difference is significant at the .05 level.

H2 states that companies that lose money in a quarter tend to "wait" longer in their earnings releases to offer a comment from a corporate officer than companies that make money in a quarter. As Table 4 indicates, this hypothesis was not supported at a statistically significant level in a comparison between press releases reporting net profits and press releases reporting net losses. While companies that made money in both quarters include the name of a corporate official a mean 15 words higher in a press release than companies that lost money, companies varied widely in where they first mentioned the chief executive, chairman, chief financial officer, or other corporate official. This was not significant, $t(1,133) = 0.529$, $p < 0.597$.

Table 5 shows that companies reporting profits in both quarters were the most consistent in where they placed the first mention of a corporate executive. But differences in means based on profits or losses were not statistically significant. This perhaps can be explained by the consistent writing techniques employed by some companies in their press releases. Some companies begin all their releases with the name of the top official making an announcement. Other companies, regardless of profit or loss, place the management's comments at the end of the body of the press release. This second approach is similar to what is required in quarterly statements filed with the Securities and Exchange Commission, which has a set place (item two of part one) for the management's discussion of analysis of financial condition and results.

Table 4

First mention of corporate official, regardless of quarter

Variable	N	Mean words until first mention of corporate official	Standard deviation	Standard error
In quarters with positive net income	612	285	586.1	23.69
In quarters with negative net income	523	300	259.4	11.34

Table 5

Number of words until first mention of corporate official, by quarter and profit/loss

	Number of companies in analysis*		Mean number of words until first mention of corporate official	
Companies recording:	Q2	Q3	Q2	Q3
Profits in both quarters	136	136	233.5	231.0
Losses in both quarters	94	94	295.6	341.9
Second quarter loss; third quarter profit	336	340	290.3	287.3
All companies	566	570	277.6	282.9

* Some companies did not file press releases in both quarters, or did not include management comment.

H3 states that companies that lose money in a quarter are less likely to state their net loss in a headline than companies that make money. This hypothesis was supported. Companies earning a quarterly profit trumpeted that fact in nearly half (48 percent) of their press releases, but 10 percent of press releases issued after a money-losing quarter mentioned a net loss. Money-losing companies either tend to use the semantically neutral term "report" in their headlines, or to highlight revenue or a pro forma measure such as EBITDA (earnings before interest, taxes, depreciation, and amortization.)

As Table 6 shows, companies that lost money were consistently unlikely to mention net income in a headline (4 percent in both quarters), while companies with positive earnings in both quarters were consistently likely to mention net income about half the time (52 percent and 55 percent in the third and fourth quarters, respectively.) Much more inconsistent were companies that lost money in the second quarter but turned a third-quarter profit. While 12 percent (45 of 375) mentioned net loss in the headline for a money-losing quarter, it jumped to 43 percent (161 of 375) in the quarter when they made money. Chi square tests show significance in both the second quarter, $X^2(2, N=641) = 123.9, p > 0.001$) and in the third quarter, $X^2(2, N= 641) = 78.04, p>0.001$), among the headlines. This further suggests that companies are more likely to highlight good news and suppress bad news.

Table 6

Percentage of press releases mentioning net income in headline

Companies recording:	Q2	Q3
Profits in both quarters	52%	55%
Losses in both quarters	4%	4%
Second quarter loss; third quarter profit	13%	43%

Conclusion

As predicted by literature and observation, companies that lose money are generally less likely to convey that fact as prominently in an earnings press release than companies that make money. This tends to be true in both the headline of the press release and in the text of the press release prepared especially for that quarter. As the literature revealed, companies make their decisions based upon their desire to appear like a socially desirable corporation that makes money instead of loses it.

What is not mentioned in the literature, but deserves further scrutiny, is the relative futility of moving financial data in a press release to marginalize a loss. Unlike other types of press releases that require the public to take a company at its word and offer no additional evidence, most earnings releases include GAAP financial tables at the bottom of the release – and all companies must file GAAP financial tables with the Securities and Exchange Commission. Simply put, a company can never do more than try to hide a loss in plain sight by using semantic fig leafs within press releases.[9]

Ultimately, in the collective efforts by companies to seem socially desirable by minimizing news of poor results, the effect can backfire. The sheer number of earnings that adopt rhetorical techniques to play down losses makes it difficult to hide the losses. Since most press releases that use the word "earnings" or "profits" in a headline are written by a profitable company and most press releases merely "report financial results" are written by companies that lose money, the differences can be spotted by financial journalists and savvy investors who deal with multiple press releases on a regular basis. Further research could study the attitudes that investors and financial journalists have toward companies that make significant changes in earnings releases based on net incomes. Additional research into the ethical practices of both investor relations practitioners and other corporate officials could evaluate disparate attitudes between the groups.

[9] This assumes, of course, that a company's financial report is accurate. Examining the earnings releases of Enron, WorldCom, and other companies that lied about profits is beyond the scope of this study.

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