

**AUDIT COMMITTEE MEMBERS' SOCIAL IDENTITIES AND
CORPORATE GOVERNANCE ROLES**

by

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ABSTRACT

This dissertation examines whether audit committee members' social identities and related corporate governance roles are associated with the quality of monitoring performed by the audit committee. To guide my dissertation I develop a conceptual model of how audit committee members' social identities ultimately influence the effectiveness of the audit committee. The model proposes that audit committee members' professional experiences outside of the audit committee lead to expertise and the development of a social identity. The social identity provides audit committee members' with internalized beliefs, norms, and expected actions that affect the corporate governance roles these individuals assume, and ultimately affect the quality of monitoring performed by the audit committee.

Within this conceptual framework, I examine whether audit committee members' social identities are associated with the quality of monitoring performed by the audit committee with two related investigations. First, I employ a field interview methodology and interview 26 audit committee members. Based on these interviews I identify four primary audit committee member social identities derived from professional experiences. I find that these social identities appear to influence how audit committee members view their role on the audit committee, perceive that they add value to management and shareholders, how strongly they identify with the company they serve and its management, and ultimately that they influence audit committee members' judgments.

In my second investigation, I employ an archival methodology to examine whether the four social identities identified in my field study are associated with the quality of financial reporting monitoring performed by the audit committee. Specifically, I examine whether the composition of Initial Public Offering audit committees is associated with the likelihood of an

accounting restatement, a material weakness, or whether the company meets or just beats analysts' forecasts. My results suggest that audit committee members' social identities and related corporate governance roles do influence monitoring quality. Furthermore, the results imply that professional experiences typically associated with financial expertise do not provide similar levels of audit committee monitoring effectiveness. Together, my two investigations provide a deeper understanding of determinants of audit committee effectiveness that are not explored in previous research.

CHAPTER 1: INTRODUCTION

Audit committees are critical to the financial reporting process, and an understanding of what makes audit committees effective continues to be an area of significant interest to regulators, practitioners, and academics. In my dissertation, I examine audit committee members' social identities and related corporate governance roles. I seek to understand how these social identities influence the judgments and decisions of audit committee members and ultimately affect the overall quality of monitoring performed by the audit committee.

Social identity is the part of an individual's self-concept (i.e., how one perceives themself) that develops from the social groups to which individuals belong. When individuals identify with their social groups they internalize the group's beliefs, norms, and expected actions. The social groups with whom individuals identify influence the individual's subsequent judgments and decisions (Tajfel 1978; Tajfel and Turner 1985; Turner 1987; Haslam 2001; Bamber and Iyer 2007). Audit committee members have social identities outside of their audit committee member social identity. For example, they may identify as an auditor, CFO, CEO, CPA, or venture capitalist. I predict that the social identities that audit committee members develop from their professional experiences are related to how they view their corporate governance role and ultimately affect how they monitor the financial reporting process.

Audit committee members can serve different corporate governance roles within the organizations they serve. These roles are characterized by various theoretical perspectives, including the following (Cohen, Krishnamoorthy, and Wright 2008):

- **Agency Theory** (Jensen and Meckling 1976): The audit committee is an independent monitor of the agent (i.e., management).

- **Resource Dependence Theory** (Pfeffer and Salancik 1978): The audit committee is a partner with management and assists the company with its strategic objectives (e.g., identifying and securing resources).
- **Institutional Theory** (Powell 1991): Audit committees become similar over time, which can result in a ceremonial and/or symbolic role, neither truly monitoring management nor assisting management in achieving the company's strategic objectives.
- **Managerial Hegemony**: The audit committee is under the control of management and only exists because of regulatory requirements.

I expect that alternative audit committee member social identities relate to different corporate governance roles. For example, I expect a public accounting social identity is more aligned with agency theory because auditors' primary focus is to monitor management, but a CEO social identity is more aligned with resource dependence theory because such individuals routinely face the same strategic challenges as management. Furthermore, I expect that some social identities are consistent with both corporate governance roles. For example, I expect a venture capital social identity to be aligned with both resource dependence and agency theories because these individuals have extensive experience assisting companies with strategic objectives, consistent with resource dependence, as well as extensive experience evaluating financial statements and risks, consistent with agency theory. My dissertation examines the corporate governance roles associated with audit committee member social identities.

Prior research has not explored how social identities can influence audit committee members' effectiveness, nor has it considered the potential joint effects of social identity and corporate governance roles. An important corporate governance synthesis project calls for further research that explores determinants of audit committee effectiveness, develops better measures

of audit committee characteristics, leverages theories from psychology, and uses diverse research methods and approaches (Carcello, Hermanson, and Ye 2011). My dissertation answers this call for research by developing a deeper understanding of audit committee characteristics beyond financial expertise and independence, uses theories from psychology and other fields, and uses diverse research methods.

My multipart dissertation includes the following two investigations. First, I employ a field interview methodology to understand audit committee members' social identities derived from professional experiences, how audit committee members' view their corporate governance role, how they identify with the company they monitor and that company's management, and ultimately how social identity affects audit committee members' judgments and decisions. Second, I employ an archival methodology to examine whether social identities derived from professional experiences outside of the audit committee are associated with the quality of monitoring of financial reporting. Specifically, I examine whether the composition of Initial Public Offering (IPO) audit committees is associated with the likelihood of an accounting restatement, a material weakness, or whether the company meets or just beats analysts' forecasts. Together, these two investigations allow me to develop a deeper understanding of determinants of audit committee effectiveness that are not explored in previous research.

The insights and perspectives I gain from my dissertation allow me to develop a conceptual framework that informs both theory and practice. It informs researchers, regulators, and practitioners about whether and how audit committee members' social identities outside of the audit committee can influence members' perceptions of their corporate governance roles and the overall judgments and decisions made by the audit committee. Ultimately, this research

identifies previously unexplored determinants of and variation in audit committee effectiveness and uncovers future research opportunities aimed at enhancing audit committee effectiveness.

The remainder of my dissertation is organized as follows: Chapter 2 discusses the background of audit committees and related literature. Chapter 3 presents my field investigation. Chapter 4 presents my archival investigation. Finally, I conclude in Chapter 5.

CHAPTER 2: BACKGROUND AND RELATED LITERATURE

Audit Committee Background

In the late 1930s and early 1940s there was a concern that external auditors were not truly independent of management (e.g., McKesson & Robbins, Inc. financial fraud). This led to the New York Stock Exchange (NYSE) in 1939 recommending that auditors be selected by a special committee of non-officer board members, and in 1940 the Securities and Exchange Commission (SEC) recommending that outside members of the board nominate auditors (Birkett 1986).¹ These were the first recommendations that companies establish audit committees. For the next 30 years, while not required, some companies began to establish audit committees. However, during this time the function of the audit committee was not well defined.

Beginning in the 1970's, audit committees began to receive a great deal of attention. In 1972 the SEC formally recommended public companies establish audit committees composed of outside directors to help protect investors who rely on the financial statements. Furthermore, in 1974 the SEC required that issuers identify their audit committee members or state that they do not have an audit committee. During this time the SEC also strongly encouraged or required individual companies to establish audit committees through enforcement actions (Birkett 1986). Soon after the SEC's formal recommendation, the stock exchanges either required or recommended that listed companies establish audit committees.

Initially, the role of the audit committee included overseeing the financial reporting process, selecting the independent auditor, and receiving the external audit results (Vera-Munoz 2005). However, over the past 20 years that role has substantially expanded due to the 1999 Blue

¹ The NYSE specifically stated: "...where practicable, the selection of the auditors by a special committee of the board composed of directors who are not officers of the company appears desirable." (Birkett 1986)

Ribbon Committee's (BRC) *Report and Recommendations on Improving the Effectiveness of Corporate Audit Committees* (BRC 1999) and the Sarbanes-Oxley Act of 2002 (SOX).

In 1998, SEC Chairman Arthur Levitt gave a speech titled the "Numbers Game." In his speech, he voiced concerns about the audit committee process (Levitt 1998). In response to these concerns, the NYSE and the National Association of Securities Dealers (NASD) sponsored the Blue Ribbon Committee which was tasked with making recommendations to strengthen the role of the audit committee (SEC 1998). This panel studied the effectiveness of audit committees in overseeing the financial reporting process and made ten specific recommendations aimed at strengthening that role. The recommendations included: strengthening audit committee independence; setting a minimum audit committee size; enhancing required audit committee member expertise; requiring an audit committee charter; requiring that the audit committee select and evaluate the external auditor; ensuring auditor independence; requiring discussions between the external auditor and the audit committee; requiring an audit committee report; and requiring quarterly review discussions with the external auditor. A number of these recommendations were implemented by the SEC, the exchanges, and the AICPA.

Soon after the BRC report, corporate scandals (e.g., Enron and WorldCom) further impacted the role of the audit committee. In response to these scandals, Congress passed the Sarbanes-Oxley Act of 2002 (SOX). SOX aimed to restore trust in the financial reporting process and included specific audit committee provisions. SOX also included a definition of audit committees: "*A committee (or equivalent body) established by and amongst the board of directors of an issuer for the purpose of overseeing the accounting and financial reporting process of the issuer and audits of the financial statements of the issuer.*" (SOX Section 205)

SOX included a number of provisions that expanded audit committee membership requirements, composition requirements, and the role of the audit committee. For example, SOX enhanced audit committee independence, audit committee communication, and it required companies to disclose audit committee financial expertise. It also designated that the audit committee is responsible for appointing, compensating, and overseeing the external auditor. Furthermore, SOX requires that the audit committee pre-approves all audit and non-audit services and create procedures for handling complaints about accounting practices. Finally, it gave the audit committee the authority to obtain independent counsel or advisors if needed.

A controversial issue related to SOX and audit committees was the definition of financial expertise. In response to SOX, the SEC proposed a definition for financial expertise that was considered by many to be too restrictive (SEC 2003). The SEC's proposed definition for financial expertise was:

- 1) *An understanding of generally accepted accounting principles and financial statements;*
- 2) *Experience applying such generally accepted accounting principles in connection with the accounting for estimates, accruals, and reserves that are generally comparable to the estimates, accruals and reserves, if any, used in the registrant's financial statements;*
- 3) *Experience preparing or auditing financial statements that present accounting issues that are generally comparable to those raised by the registrant's financial statements;*
- 4) *Experience with internal controls and procedures for financial reporting; and*
- 5) *An understanding of audit committee functions (SEC 2003).*

The SEC received more comments related to the above definition than any other topic that was covered in the SEC's proposed rules related to SOX (SEC 2003). Many argued that the definition was too narrow and restrictive. It was argued that companies would have a difficult

time finding audit committee members with these skills (especially smaller companies), that the requirements would reduce board diversity, and that audit committees are responsible for oversight and not the preparation of financial information. Due to this and other feedback the SEC adopted a broader definition of financial expertise:

- *An understanding of generally accepted accounting principles and financial statements;*
- *The ability to assess the general application of such principles in connection with the accounting for estimates, accruals and reserves;*
- *Experience preparing, auditing, analyzing or evaluating financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of issues that can reasonably be expected to be raised by the registrant's financial statements, or experience actively supervising one or more persons engaged in such activities;*
- *An understanding of internal controls and procedures for financial reporting; and
An understanding of audit committee functions (SEC 2003)*

The above final definition was expanded to include individuals who have experience analyzing or evaluating financial statements and those in a supervisory role. For example, the proposed definition included “experience preparing or auditing financial statements” and the final definition was expanded to include “experience preparing, auditing, **analyzing or evaluating** financial statements” (emphasis added). Furthermore, in the final rule the definition was expanded so that experience can be obtained through “experience actively **supervising** one or more persons engaged in such activities” (emphasis added).

Overall, the BRC report and SOX resulted in significant changes to the composition, role, and responsibility of the audit committee. Currently, audit committees must be composed of at

least three independent board members, all members must be financially literate, if a company does not have a financial expert they must disclose why they do not, and companies are required to identify their financial expert. Furthermore, the audit committee's role includes oversight of the financial reporting process including the external auditor, internal audit, and risk management. Examples of specific duties include: appointing, compensating, and overseeing the external auditor; approving any non-audit services; resolving any disagreements between management and the external auditor; and overseeing the internal audit function.

Audit Committee Effectiveness

Due to the significant focus on audit committees over the past 20 years, it is clear that the role of the audit committee is critical to the financial reporting process. Before exploring research related to audit committee effectiveness, it is important to define it. I use the definition proposed by DeZoort, Hermanson, Archambeault, and Reed. (2002):

*“An effective audit committee has **qualified members** with the **authority and resources** to protect stakeholder interests by ensuring reliable financial reporting, internal controls, and risk management through its **diligent oversight efforts.**”(Emphasis added)*

In the definition above, DeZoort et al. (2002) highlight four determinants that contribute to an effective audit committee: composition, authority, resources, and diligence. They argue that the first three are inputs (or the foundation) of audit committee effectiveness and that diligence is the required process component. That is, an audit committee may have the optimal composition, authority, and resources, but it will not be effective unless the audit committee members are diligent. Included within audit committee diligence are incentives, motivation, and perseverance (Keune and Johnstone 2015).

In my dissertation, I am primarily interested in how the composition determinant influences audit committee effectiveness. In this determinant, DeZoort et al. (2002) include audit

committee member expertise, independence, integrity, and objectivity. A significant amount of research examines audit committee effectiveness, and a large portion of this research examines audit committee characteristics that are associated with accounting and auditing outcomes (Carcello et al. 2011). Such research primarily focuses on audit committee member independence (e.g., Abbott et al. 2004; Bédard et al. 2004; Agrawal and Chadha 2005; Bruynseels and Cardinaels 2014), financial expertise (e.g., Abbott et al. 2004; Bédard et al. 2004, Agrawal and Chadha 2005), and a recent study explores audit committee industry expertise (Cohen et al. 2014), reporting that audit committee industry expertise is associated with stronger financial reporting monitoring by the audit committee. Specifically, audit committees with more industry expertise are associated with a lower likelihood of financial restatement, less discretionary accruals, increased audit fees, and a lower ratio of audit to non-audit fees.

Audit Committee Member Independence

Research examining audit committee member independence reports various ways in which independence is associated with financial reporting outcomes. For example, Abbott et al. (2004) find a negative association between restatements and independence. Agrawal and Chadha (2005) find a lower likelihood of restatement when there is an independent director with financial expertise, but do not find independence alone to be predictive. Bédard et al. (2004) results show that a fully independent audit committee is associated with a lower likelihood of aggressive earnings management. Abbott et al. (2003) find that companies who have independent audit committees that meet at least four times a year purchase less non-audit services from their external auditors. Abbott and Parker (2000) show that audit committees who are completely independent and meet at least twice a year are more likely to hire an industry specialist auditor. Carcello and Neal (2003) results suggest that audit committees of companies that receive going-

concern qualifications are less likely to terminate their auditor if they have an independent audit committee. Anderson et al. (2004) find that entirely independent audit committees are associated with a lower cost of debt. Finally, Carcello et al. (2002) show a positive relationship between audit fees and board independence, which they suggest is a sign of demand for higher audit quality.

Collectively, this research suggests that audit committee independence is associated with various positive outcomes: a lower likelihood of financial restatement, less aggressive earnings management, a lower cost of debt, fewer non-audit services provided by external auditors, a greater likelihood that clients hire an industry specialist auditor, a lower likelihood that the auditor is terminated following a going concern, and increased audit quality.

Audit Committee Member Financial Expertise

Research examining audit committee member financial expertise generally finds that expertise is positively associated with financial reporting outcomes. Numerous studies have examined audit committee financial expertise pre- and post-SOX. In the post-SOX environment companies are required to disclose whether their audit committee has a designated financial expert. I begin by discussing research that uses pre-SOX data.

Abbott et al. (2004) find a negative association between restatements and audit committees that include at least one financial expert (CPA, investment banker/VC, CFO, controller, CEO, VP of Finance). Agrawal and Chadha (2005) show a lower likelihood of restatement when there is an independent director with financial expertise (CPA, CFA, or experience in corporate financial management). Bédard et al. (2004) find financial expertise (CPA, CFA, or experience in finance or accounting) is associated with a lower likelihood of aggressive earnings management. Krishnan (2005) reports that financial expertise is negatively

associated with internal control problems (i.e., reportable conditions and material weaknesses). Anderson et al. (2004) find some evidence that audit committee financial expertise (CFOs, investment bankers, investment managers, bankers, financial consultants, auditors and CEOs of financial companies) is associated with a lower cost of debt. DeFond et al. (2005) report positive market responses to the appointment of accounting financial experts to audit committees when there exists strong governance, but the market does not respond to the appointment of non-accounting financial experts.

Collectively, this research reveals that in the pre-SOX environment audit committee financial expertise is associated with positive accounting outcomes. Specifically, it is associated with a lower likelihood of financial restatements, less aggressive earnings management, and less internal control material weaknesses. Furthermore, the market responds positively to the appointment of accounting financial experts and there is some evidence that financial expertise is associated with a lower cost of debt.

A number of studies also examine audit committee financial expertise in a post-SOX environment when companies are required to identify whether they have a financial expert. This post-SOX research also examines the SEC's new definition of financial expertise. For example, Dhaliwal et al. (2010) find that audit committee accounting expertise is positively associated with accruals quality. Furthermore, the most positive impact on accruals quality exists when companies have a combination of audit committee members with both accounting and finance expertise. However, the additional presence of supervisory experts is not associated with any incremental improvement in accruals quality. Hoitash et al. (2009) report that accounting and supervisory experience on the audit committee is associated with a lower likelihood of SOX 404 material weakness disclosures. Krishnan and Visvanathan (2008) show that accounting financial

expertise is positively associated with conservatism, but not non-accounting financial expertise and nonfinancial expertise. Schmidt and Wilkins (2013) examine whether financial expertise is associated with timelier reporting of financial restatements. They find that companies with more accounting financial experts are timelier in reporting these restatements. Furthermore, companies with an audit committee chair who is an accounting financial expert are the timeliest.

A recent study explores audit committee member financial expertise (as defined by the SEC) when combined with the relative status of audit committee members compared to management (Badolato et al. 2014). They report that audit committee financial expertise, when combined with the relative status of audit committee members, constrains earnings management (measured as accounting irregularities). Furthermore, they find that it is supervisory expertise, and not finance or accounting expertise that constrains accounting irregularities when combined with relative status. Inconsistent with the majority of prior research, they do not find that audit committee financial expertise alone constrains earnings management (Badolato et al. 2014).

Overall, similar to pre-SOX research, post-SOX research examining audit committee financial expertise suggests that financial expertise is associated with positive outcomes. Specifically, financial expertise is associated with improved accruals quality, timelier financial restatement reporting, and a reduced likelihood of disclosing a SOX 404 material weakness. Furthermore, it is associated with less earnings management when financial expertise is combined with audit committee member status.

Other Forms of Audit Committee Member Expertise

In addition to financial expertise, recent studies have also explored other types of expertise. For example, Krishnan et al. (2011) examine the influence of legal expertise on financial reporting quality and find a positive association. Furthermore, Cohen et al. (2014)

examine the effect of audit committee industry expertise on financial reporting quality (restatements & discretionary accruals) and oversight of the auditor (audit and non-audit fees). Results show that industry expertise, combined with accounting expertise, can improve audit committee effectiveness from a monitoring perspective.

These previous studies provide valuable insights into audit committee member characteristics that are associated with accounting outcomes. However, due to regulatory changes (e.g., SOX), the financial expertise and independence of audit committee members is becoming more homogenous across audit committees. Even so, there are still varying levels of audit committee effectiveness. For example, an audit committee may have the required expertise and independence in form, but in substance they may not act as effective monitors.

My dissertation investigates other potential factors contributing to audit committee effectiveness that prior research has not examined. Specifically, I explore how audit committee members' social identities and corporate governance roles influence their judgments and decisions and ultimately influence the effectiveness of the overall audit committee.

Social Identity

Social identity is defined as the part of a person's self-concept that develops from the groups in which individuals belong. Groups can include gender, ethnicity, religion, profession, work organization, and many more. Social identity is based on the idea that in many situations a person not only defines them self as an individual, but they also define them self as a group member. Therefore, a person's sense of self includes both their personal identity and the identity that they associate with their internalized group membership (Haslam 2001). The individual's overall behavior is then shaped by this identity.

Social identity theory was first developed by Henri Tajfel and John Turner in their studies of intergroup discrimination (Tajfel & Turner, 1979, 1985). The original foundation of this theory combined three social processes to examine intergroup relations. First, in many situations individuals perceive themselves as part of a social category instead of as a separate individual (social categorization). Second, groups and individuals judge their relative worth by comparing themselves to other groups (social comparison). Third, an individual's identity is affected by the individual's perception of their social situation (social identification) (Haslam et al. 2003). Through the development of social identity theory, a complementary theory evolved called self-categorization theory. While social identity theory focuses on the psychological processes of intergroup relations, self-categorization theory helps explain how people "become, act, think and feel as a psychological group under particular circumstances (Haslam, 2001)." This theory focuses on how individuals shift from seeing themselves as only an individual (personal identity) to also seeing themselves as part of a group (social identity) and how they are influenced by the social categories to which they belong.

There is a great deal of overlap between the ideas and concepts of both social identity theory and self-categorization theory. The ideas of these theories are often combined and referred to collectively as the social identity approach. Taking the ideas presented above together, when an individual is in a certain role they will identify with the social group with which that role is associated (self-categorization). Once they have categorized themselves, their actions will be directed by the actions that are considered appropriate for that group.

There is limited research in accounting incorporating the social identity approach (e.g., Towry 2003; Bamber and Iyer 2007; Reffett et al. 2012; Bauer 2015), and no research has examined the social identities of audit committee members. Bamber and Iyer (2007) leverage

social identity theory to examine the implications of external auditors' identification with their clients and their profession. They find that auditors are more likely to allow managements' preferred accounting treatment when the auditor identifies with the client, and are less likely to do so when they identify with their profession. Similarly, Bauer (2015) examines client and professional identity in auditing, reporting that auditors that more strongly identify with their client (even with a short tenure with that client) are more likely to agree with the client's preferred accounting treatment unless their professional identity is salient.

It is likely that in the audit committee setting there will also be circumstances when, due to social identities, audit committee members identify more with the company they serve and/or its management. For example, an audit committee member who is a CEO may identify more with management than an audit committee member who is an auditor. I seek to use my dissertation to understand the implications of audit committee members identifying with the company they serve and/or management. Furthermore, based on the social identity approach I predict that audit committee members' roles outside of the audit committee shape their behavior on the audit committee. An open empirical question is whether and how different outside social identities influence the behavior of audit committee members. I use my dissertation studies to investigate this question.

Corporate Governance Roles

In addition to examining social identity, I also explore corporate governance roles. While the majority of corporate governance research has focused on agency theory, research has begun to consider different corporate governance theoretical perspectives including resource dependence, institutional theory, and managerial hegemony (e.g., Cohen et al. 2008; Dhaliwal et al. 2010; Hermanson et al. 2012; Clune et al. 2014).

Cohen et al. (2008) encourage researchers to consider four theoretical perspectives on corporate governance: agency, resource dependence, managerial hegemony, and institutional theory. They argue that most of the accounting and auditing literature focus on agency theory. However, there may be circumstances when different theoretical perspective can provide new insights. In the following discussion, I consider each of these theoretical perspectives.

Accounting researchers most commonly employ agency theory (Jensen and Meckling 1976). From an agency theory perspective, the role of the audit committee is to be an independent monitor of the agent (i.e., management) on behalf of the owners (i.e., shareholders). From a resource dependence theory perspective (Pfeffer and Salancik 1978), the audit committee is a partner with management and assists the company with its strategic objectives (e.g., identifying and securing resources). From a managerial hegemony perspective, the audit committee exists only because of regulatory requirements and is under the control of management. From an institutional theory perceptive (Powell 1991), audit committees become more similar over time through institutional isomorphism. Isomorphism can occur due to regulatory pressures, socialization, or during times of uncertainty companies may follow best practices of other companies even if those practices are not necessarily effective (Cohen et al. 2008). There are multiple implications of isomorphism in the audit committee setting. For example, over time audit committees may become similar across companies, even though there is likely not a one-size-fits all audit committee. Furthermore, audit committee composition and activities may be driven by ceremonial or symbolic actions.

Two prior field interview studies that consider audit committees and different corporate governance roles are particularly relevant to my research. Cohen et al. (2010) interview auditors to understand their interactions with the audit committee, board of directors, and internal auditors

in a post-SOX environment. Their results reveal that the corporate governance environment has improved since SOX, and that audit committees are more active, diligent, knowledgeable, and powerful post-SOX. Furthermore, they find that audit committees' corporate governance structure is consistent with a monitoring role (i.e., consistent with agency theory), but there are circumstances where governance is still symbolic (i.e., consistent with institutional theory).

Beasley et al. (2009) interview audit committee members to understand the processes used by the audit committee when fulfilling their duties. They find that audit committee members attempt to provide effective monitoring of financial reporting. However, there are examples where their actions appear to be more ceremonial or symbolic (e.g., they are selected to serve on the board based on personal relationships with management or when their involvement in substantive decision making is minimal).

These two interview studies focus on agency and institutional theory. I further explore the applicability of resource dependence theory in the context of audit committee judgment and decision making. Resource dependence theory suggests that audit committee members may bring the company access to resources or connections that they may not otherwise be able to garner.

A few other studies in accounting also consider different corporate governance roles. Hermanson et al. (2012) interview compensation committee members and Clune et al. (2014) interview nominating committee members. Both studies use interviews to consider the processes used by these committees and consider agency, resource dependence, managerial hegemony, and institutional theory when analyzing the interviews. Both studies find that multiple theoretical perspectives are needed when interpreting the interviews. For example, the nominating committee interviews reveal a tension between committees feeling pressure to pay executives in

a shareholder-friendly manner (agency theory) and the desire to find and retain executive talent that may require more pay (resource dependence theory).

Using an experiment Cohen et al. (2007) examine whether the roles of the board (agency and resource dependence) affect auditors' risk assessments and program planning decisions. They show that auditors do consider the role of the board when making both risk assessment and audit planning decisions. Specifically, control risk judgments are affected when both agency and resource dependence on the board are strong and auditor's increase testing when auditors believe the board is weaker in either agency or resource dependence but decrease testing when they believe the board is strong in both.

Dhaliwal et al. (2010) examine the association between types of financial expertise and financial reporting quality (measured as accruals quality). They use resource dependence theory to argue that some non-accounting expertise on the audit committee can be beneficial. To examine the presence of non-accounting financial experts on the audit committee, they classify financial experts on audit committees as accounting experts (current/prior CPAs, CFOs, VPs of Finance, Controllers, or other major accounting positions), finance experts (investment bankers, financial analysts, or other financial management roles), or supervisory experts (CEOs or Presidents). They then test the association between the mix of accounting and non-accounting expertise on audit committees and accruals quality. Results show the most positive impact on accruals quality occurs when companies have a combination of both accounting and finance experts on the committee. The additional presence of supervisory experts on the AC is not associated with incremental improvement in accruals quality.

In my dissertation I build on this prior literature by incorporating both agency and resource dependence theories into my analysis of audit committees. Specifically, I identify

whether and how the social identities of audit committee members affect the member's corporate governance role, their identification with the company, and their judgments and decisions.

Ultimately, I am examining whether audit committee members' social identities influence audit committee effectiveness.

In the next two sections, I present the results of two investigations. In the first investigation, I interview 26 audit committee members to understand audit committee members' social identities derive from professional experiences, how audit committee members' view their corporate governance role(s), how they identify with the company and management, and ultimately how social identity affects audit committee member judgments and decisions. In the second investigation, I leverage the insights from the first investigation, along with related literature, to develop testable hypotheses of how audit committee members' social identities are associated with the monitoring effectiveness of the audit committee. Specifically, I examine whether the composition of IPO audit committees is associated with the likelihood of an accounting restatement, a material weakness, or whether the company meets or just beats analysts' forecasts. Together, these two investigations allow me to develop a deeper understanding of determinants of audit committee effectiveness.

CHAPTER 3: AUDIT COMMITTEE MEMBER FIELD INTERVIEWS

I. INTRODUCTION

I conduct a field interview investigation to begin my examination of whether and how audit committee members' social identities and related corporate governance roles influence the effectiveness of the overall audit committee. I expect that audit committee member social identities derived from professional roles outside of the audit committee are associated with different corporate governance roles and ultimately affect the judgments and decisions of audit committee members. I also expect that audit committee members' strength of identification with the company and management will vary based on their social identities. This field investigation examines audit committee members' social identities, their identification with the company and management, and ultimately how these influence the judgments and decisions of the audit committee.

To guide my field interviews, I articulate a conceptual model and develop five primary research questions (see Figure 1). This model proposes that audit committee member's professional experiences lead to social identities and expertise that then influence the audit committee member's corporate governance role. Together, the social identities and related corporate governance roles of multiple individual audit committee members then influence the judgments and decisions of the entire audit committee. My research questions derived from this conceptual model seek to reveal the types of social identities that audit committee members possess and whether these identities influence how audit committee members' view their role on the audit committee and influence how they perceive that they add value to management and shareholders. Furthermore, I seek to understand whether social identities influence audit committee members' strength of identification with the company/management/audit committee and whether company characteristics influence how audit committee members perceive they add

value. Finally, I examine whether social identities and related corporate governance roles influence the judgments and decisions of audit committee members.

To examine my research questions, I interview 26 audit committee members. These individuals come from a variety of professional backgrounds and serve many different types of companies. Based on my interviews and pre-interview questions I find that audit committee members have four main social identities: public accounting, executive management, financial management, and investment management. These identities influence how audit committee members view their role on audit committees, perceive they add value, the strength with which they identify with the company and management, and their resulting judgments and decisions.

This field investigation provides deep insights from a relatively small number of actual audit committee members. These audit committee members provide rich information based on their unique institutional perspectives and experiences that cannot be obtained from publicly available information. The results of this study contribute to both literature and practice by enabling a better understanding of the various determinants of audit committee effectiveness. In addition, the information gained from this field investigation, along with related literature, provides a foundation for developing testable hypotheses in the archival part of my dissertation.

This paper proceeds as follows: Section II includes a discussion of the conceptual model, literature review, and related research questions; Section III discusses the methodology and sample; Section IV provides results; and finally Section V concludes.

II. CONCEPTUAL MODEL, LITERATURE REVIEW, AND RESEARCH QUESTIONS

I begin by articulating a conceptual model that proposes how professional experiences influence audit committee members' judgments and decisions (see Figure 1). My conceptual model proposes that audit committee members' professional experiences outside of the audit

committee lead to expertise and the development of a social identity. The social identity provides internalized beliefs, norms, and expected actions that affect the corporate governance roles these individuals assume and ultimately the audit committee member's judgments and decisions.

[INSERT FIGURE 1 HERE]

Next, I explain the three stages of my conceptual model and articulate research questions related to each stage. The first stage of my model is the formation and expression of social identities. In this stage, I propose that audit committee members' professional experiences outside of the audit committee lead to expertise and social identities. Both the SEC and academic research consider the important role of audit committee members' professional experiences in the development of expertise. For example, the SEC defines audit committee member financial expertise in the context of members' professional experiences.² Similarly, academic research uses measures of prior professional experiences as proxies for audit committee expertise (e.g., Abbott, Parket, and Peters 2004; Bédard, Chtourou, and Courteau 2004; Cohen, Hoitash, Krishnamoorthy, and Wright 2014). In addition to expertise, this stage of the model proposes that professional experiences aid audit committee members in developing a social identity. Social identity is the part of an individual's self-concept that develops through experiences interacting in a social group, thereby enabling the individual to internalize the group's beliefs, norms, and expected actions (e.g., Tajfel 1978; Tajfel and Turner 1985; Turner 1987; Haslam 2001). In this stage my research questions are:

² The SEC defines financial expertise as "An understanding of generally accepted accounting principles and financial statements; The ability to assess the general application of such principles in connection with the accounting for estimates, accruals and reserves; Experience preparing, auditing, analyzing or evaluating financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of issues that can reasonably be expected to be raised by the registrant's financial statements, or experience actively supervising one or more persons engaged in such activities; An understanding of internal controls and procedures for financial reporting; and an understanding of audit committee functions" (SEC 2003).

RQ1a: What types of experiences, knowledge, and expertise do audit committee members possess?

RQ1b: How are different types of experiences, knowledge, and expertise associated with various social identities?

The second stage of my model is the integration of outside social identities with the corporate governance roles of the audit committee. I first propose that an audit committee member's social identity and expertise influence the member's identification with the company, management, and audit committee. Bamber and Iyer (2007) leverage social identity theory to examine external auditors' identification with their clients and profession, finding that auditors are more likely to allow managements' preferred accounting treatment when the auditor identifies with management, and are less likely to do so when they identify with their profession. Bauer (2015) also examines client and professional identity in an auditing setting using an experiment, reporting that auditors who more strongly identify with their client (even those with a short client tenure) are more likely to agree with the client's preferred accounting treatment, unless their professional identity is salient.

Similar to findings regarding external auditors, I propose that audit committee members' behavior will be influenced by their identification. Specifically, I propose that audit committee members' social identities and expertise will influence their identification with the company, management, and audit committee and this identification will influence corporate governance roles and ultimately the judgments and decisions of the entire audit committee.

Prior research suggests that there exist alternative corporate governance roles for audit committee members, including those consistent with agency theory and resource dependence theory (Cohen et al. 2008). I propose that experience with monitoring financial reporting encourages an audit committee member to perform his or her role consistent with agency theory

(Jensen and Meckling 1976). In contrast, I propose that experience in assisting or advising a company with its strategic objectives (Pfeffer and Salancik 1978) encourages an audit committee member to perform his or her audit committee role consistent with resource dependence theory. Other social identities (or adaptations thereof) may also encourage audit committee members to perform roles consistent with either agency theory and/or resource dependence theory.

I expect that audit committee members' social identities and related corporate governance roles will influence how they view their role on the audit committee. Furthermore, I expect that social identities will influence how members perceive they add the most value to management and shareholders. Related to this stage of my model I pose the following research questions:

RQ2: How do audit committee members' view their role on the audit committee, and perceive that they add the most value? How are these views influenced by their social identities?

RQ3a: Do audit committee members' social identities influence their strength of identification with the company, management, and audit committee?

RQ3b: When and how do audit committee members identify with the company, management, and audit committees of the companies on which they serve, and what are the implications of such identification?

The third and final stage of my model examines the influence on audit committee member judgments and decisions. In this stage I expect that the corporate governance role the audit committee member assumes is also influenced by characteristics of the company they serve. For example, the size of the company or whether the company is public or private. Finally, I ultimately propose that social identities and associated corporate governance roles will influence the audit committee member's judgments and decisions. In this stage of the model, I pose two final research questions:

RQ4: How do characteristics of the companies that audit committee members serve influence how they perceive that they add value to those companies?

RQ5: How do audit committee members' social identities and related corporate governance roles influence their judgments and decisions?

III. METHODOLOGY AND SAMPLE

To examine the conceptual model and associated research questions, I use semi-structured interviews of audit committee members, coupled with information gathered from members' resumes and pre-interview questions. This approach allows me to gain deep insights from practicing audit committee members based upon their deep, professional experiences. These audit committee members provide rich information based on their unique institutional perspectives and experiences that cannot be obtained from publicly available information.

Process of Conducting Interviews and Coding Responses

After audit committee members' agreed to participate in the study, I requested that they complete pre-interview questions and provide me their resume or biography. Appendix A contains the pre-interview questions. I use the pre-interview questions to measure each member's identification with the company, management, and audit committee. In addition, the questions capture information about the companies that these member's serve. I use the resumes and biographies to collect the professional backgrounds of the participants. Once I gathered this information, I interviewed each of the participants individually. I conducted the interviews either in person (N = 5) or over the phone (N = 21). Appendix B contains the interview questions.³

A total of 26 audit committee members participated in this field investigation. I identified participants through University contacts at two major U.S. universities. I recorded all interviews, with the exception of one because that participant requested that I take notes instead. When

³ When developing research questions I obtained feedback on the questions from five senior researchers familiar with the interview approach and audit committee research.

possible, I also conducted the interviews with one or two of my committee members. I scheduled the interviews to last 45 minutes, and the average length was 53 minutes (with a range of 26 to 77 minutes). I sent participants the list of interview questions prior to the interview. When answering the interview questions, I asked participants to think of only one company that they serve on as an audit committee member. I used the online service, TapeACall, to record and professionally transcribe the interviews. I ensured the removal of all individually identifying information, and I had participants review their transcripts. Only a few participants requested minor changes to their transcript.

I coded the interview transcripts using an a priori coding scheme (provided in Appendix C). I developed the coding scheme based on audit committee regulations (e.g., SOX requirements for audit committees) and prior research. After developing the coding scheme I read each transcript and coded the responses provided by each participant.

Descriptive Data

Table 1 provides variable definitions, and Table 2 presents a summary of the sample. The participant's serve companies that cover seven different industries and range in size from less than \$100 million in revenue to over \$5 billion. Table 3 provides descriptive data. The participants have extensive experience on the companies they thought of when answering the interview questions. On average, they have served on the overall board of directors for 7.98 years and have served on the audit committee for 7.29 years. Sixty-five percent of participants are the chair of the audit committee and eight-one percent are designated as a financial expert. On average, the boards on which they serve have 9.04 members and the audit committees have 3.96 members. These audit committees meet on average 4.36 times per year in person and the mean

duration of the meetings is 2.51 hours. Seventy-seven percent of the companies on which participants serve are publicly traded. Finally, all participants in this sample are male.

[INSERT TABLE 1 HERE]

[INSERT TABLE 2 HERE]

[INSERT TABLE 3 HERE]

In the online pre-interview survey, I asked participants why they were selected to serve on the audit committee. Using a scale from 1 (not related to my selection) to 4 (strongly related to my selection) they indicated the extent to which seven different factors were related to their selection: prior accounting experience, prior non-accounting related experience (e.g., CEO), relationship with another board member, relationship with top management, industry expertise, experience on other boards, and because of the board rotation policy. The factors most strongly related to selection are prior accounting experience (average response of 3.27 on 4-point scale), followed by industry expertise (2.80), and experience on other boards (2.69). The least strongly related was a board rotation policy (1.46).

Table 4 provides the professional backgrounds of my participants, and Table 5 provides descriptive data categorized by the four main social identities that I examine (public accounting, executive management, financial management, and investment management). I discuss the participants' backgrounds and the four social identities in the next section.

IV. RESULTS

Tables 6 – 13 present analysis of the coded data. I will frame the discussion of analysis according to the five proposed research questions.

RQ1a: What types of experiences, knowledge, and expertise do audit committee members possess?

RQ1b: How are different types of experiences, knowledge, and expertise associated with various social identities?

To examine RQ1, I collect professional background information about the participants from their resumes and biographies. Table 4, Panel A presents the main professional backgrounds that my analyses reveal. The most common background in my sample is an audit partner (38.46 percent), followed by a Chief Financial Officer (34.62 percent), and then a Chief Executive Officer (30.77 percent). It is important to note that when I coded backgrounds I did not limit participants to only one professional background if they have had multiple experiences. For example, a participant may have been both a CFO and CEO. I recognize both of these professional experiences for this individual.

[INSERT TABLE 4 HERE]

From the nine common professional backgrounds, I identify four main social identities. The first is a Public Accounting social identity, which includes participants with audit partner experience (38.46 percent of the sample). These individuals have experience monitoring financial reporting as an external auditor. The second social identity is Executive Management, which includes participants with Chief Executive Officer or Other Executive experience (also 38.46 percent of the sample). These individuals have experience supervising financial reporting. The third social identity is a Financial Management social identity, which includes participants with Chief Financial Officer or VP of Finance experience (26.92 percent of the sample). These individuals have experience being responsible for financial reporting. The last social identity is Investment Management, which includes those with a background in venture capital, private equity, or private investment (23.08 percent of the sample). These individuals have experience investing in companies, including the analysis of financial statements and risks.

Table 5 reports descriptive statistics by the four social identities. The public accounting social identity has the most audit committee chairs and also the most designated financial experts. However, on average they have served the least amount of time on the board (5.70 years versus 8.35, 9.86, and 11 years for executive management, financial management, and investment management respectively). They have also served the least amount of time on the audit committee (5.60 years versus 8.15, 9.29, and 8.50 years for executive management, financial management, and investment management, respectively).

Considering why audit committee members are selected to serve on the audit committee, the most likely reason for those with a public accounting social identity is unsurprisingly their prior accounting experience (4.00 on a 4-point scale). That is also the most common reason for those with a financial management social identity (3.57 on a 4-point scale). Those with an executive management social identity are selected primarily for their non-accounting experiences (3.60). Finally, those with an investment management social identity indicate they are selected most commonly for their accounting expertise (3.17) and experience on other boards (3.00). This reveals some of the different characteristics that nominating committees are seeking when selecting audit committee members. Next, I turn to examining the influence of these social identities on audit committee members' judgments and decisions.

[INSERT TABLE 5 HERE]

RQ2: How do audit committee members' view their role on the audit committee, and perceive that they add the most value? How are these views influenced by their social identities?

A number of my interview questions probe the manner in which audit committee members' view their role on the audit committee, how they add the most value, and whether these views are influenced by their social identities. Tables 6-9 present these results. My first interview question asks participants how they view their primary role on the audit committee.

Table 6, Panel A presents the roles participants identify. The most common role participants identify is the monitoring of financial reporting (54 percent of participants indicate this role) followed by the monitoring of the external audit (46 percent of participants indicate this role).

[INSERT TABLE 6 HERE]

To understand whether social identities influence the roles audit committee members consider as their primary role, I examine the primary roles identified by social identity. For example, I identify the most common primary roles identified by those with a public accounting social identity. Table 6, Panel B provides this analysis. I find that social identities do influence the primary roles that audit committee members identify. For example, 50 percent of those with a public accounting social identity and 86 percent of those with a financial management social identity indicate the monitoring of the external audit is their primary role. However, only 30 percent of those with an executive management social identity, and no one with an investment management social identity, indicate this role. This is consistent with those that have more direct experience with auditors in their professional careers identifying more with that role on the audit committee than those that do not have direct experience with auditors.

The second interview question asks participants to indicate their top three most important responsibilities on the audit committee. Table 7, Panel A summarizes all of the participants' responses with respect to their most important responsibility, and Panel B provides the most frequent response by social identity. When examining the complete sample, the responsibility participants indicate the most often is the monitoring of financial reporting (38 percent of participants indicate this responsibility). When examining responses by social identity, the monitoring of financial reporting is also the most frequent response across all four of the social identities. When looking at other common responses, most of the social identities also mention

the accuracy of financial statements (all except the public accounting social identity). The public accounting social identity commonly mentions managing the relationship with the auditor (20 percent mention this responsibility as the most important). Similar to above, this is consistent with those who have had more direct experience as an auditor identifying with the importance of managing the auditor relationship in their audit committee role.

[INSERT TABLE 7 HERE]

The third interview question asks participants how they individually add the most value to management and then to stakeholders. There is more variation in responses to this question based on social identity. Table 8, Panel A summarizes what all participants consider to be the value they add to management, and Panel B provides the most frequent responses by social identity. When asked what value the audit committee member adds to management, those with a public accounting social identity focus on their audit partner background (70 percent), financial reporting background (30 percent), and technical background (20 percent). These responses are more consistent with a monitoring or agency corporate governance role. During the interview of one prior audit partner, he discusses his three most important responsibilities on the audit committee as being the value that he adds to management. He states those responsibilities are to help manage the relationship with the auditor, educate the board and management on complex accounting and reporting issues, and finally review financial reports. In his own words:

*"Probably the most important one is to I'd say **be a middle man**, meaning provide a balanced perspective in managing the relationship between management and the auditors. There's some natural tensions that exist between management and auditors of course. What my role is, my most important role is, to **be balanced** in understanding both sides on a particular issue, whatever it may be. That I think would be most important. I take very seriously, this is probably the second most important, is to **educate our board** on complex accounting and reporting issues because they're not accountants. One of my roles is to try to help them understand and give you some examples of that about complex accounting and reporting issues. Third **I still got some audit partner in me**. I review*

documents whether they be Qs or the 10K. I do in essence a full, what I would call, a full partner review just like I did when I was an audit partner from read every single word and nitpick the damn document from both a low level, a 1,000 feet, as well as a high level 30,000. " (Participant 109)

This prior audit partner's response highlights how his prior auditor experiences influence how he views his responsibilities and the value he adds to management. His answer is not the same type of answer provided by those with other social identities. For example, helping manage the relationship with the auditor is not a common response given by any of the other social identities when I ask them about the value they add to management.

[INSERT TABLE 8 HERE]

Those with an executive management social identity more commonly focus their response to this question on their operational and industry experience. This is not a common response to those with a public accounting or investment management social identity. For example, an audit committee member with both an executive management and financial management social identity discusses more of a resource dependence role through his broad business background as to how he provides value to management:

*"My particular background, I was able to manage a lot of things. So finance, legal, HR, IT, corporate planning and development, M & A, public policy, facilities, manufacturing, so a lot of different stuff. Because of that, **I bring a lot of what I'll call business perspective** in addition to being a card-carrying, more narrow CFO" "I can help the CFO and the CEO think about IT, either IT strategy. I help them interview their CIO candidate as they were coming in and transitioning that. Spend time with the CIO about once a quarter, and what, in this case, he's doing, the challenges he has. It's really because of my background that **I can add a broad set of value** to the company management." (Participant 117)*

Those with a financial management social identity focus their responses to the question of adding value to management on providing financial reporting advice (29 percent of those with a financial management social identity) and operating advice to management (29 percent) along with mentoring and evaluating the CFO (also 29 percent). For example, one participant with a

financial management social identity discusses being a sounding board for the CFO as the value he adds to management:

*"I think I do it **by being a good sounding board** for the CFO and in helping in the evaluation of the CFO." (Participant 122)*

Another prior CFO also mentions the following role when asked how he perceives that he individually adds value to management:

*"I think part of what the audit committee's role is to **mentor the CFO** because in some cases the CFO has never been a public company CFO before. I think that's important. **Help them grow and develop** and impart knowledge on them." (Participant 124).*

Finally those with an investment management social identity most commonly highlight their prior experience on other boards and providing financial reporting advice to management as the value they add. For example one participant discusses the multiple boards he serves on:

*"I just would say that I've had a lot of experience on boards and on audit committees, so **I can recognize issues pretty early on**. If there's a weak accounting staff, I can recognize that...." (Participant 114)*

Another participant with an investment management social identity also highlights all of the boards he serves, indicating that he is a professional board member:

*"I'm on something like 13 boards or something like that. I'm probably on a bunch of others, I don't know how many audit committees. That's my job though. It's not like I have another job. My whole job is these boards that we have investments in. We usually have 2 of us on each board. If I say 13, **I might be the lead guy on 6 of the deals and one of my partners maybe is on 6 of them or something as lead. That's all I do. That's my job is to be an investor and to be on those boards**. It seems like a lot. If I had a full time job at a company I wouldn't be able to be on that many boards. That is my full time job, is basically to be director to all these companies that we've invested in." (Participant 114)*

Overall, the responses to the question of how the audit committee member perceives that they add value to management highlights variation across social identities. Those with a public accounting social identity perceive that they add value to management through their auditing and accounting background. Participants with an executive management or financial management

social identity focus their discussion on operational and industry experience, and providing advice/mentoring to management. Finally, those with an investment management social identity add value to management by providing financial reporting advice to management and through their experience on other boards. Overall, based on these interviews audit committee members' view of the value they add to management is related to their social identity.

In addition to asking participants how they perceive that they add value to management, I also ask them how they perceive that they add value to shareholders. Table 9 presents these results. Overall, the most common response by the entire sample is the monitoring of financial reporting (27 percent of all participants mention this). When I look at responses by social identity, I also find that the monitoring of financial reporting is one of the most common responses across all identities. Analyzing responses by social identity, I find that those with a public accounting social identity add value to shareholders by monitoring the control environment (40 percent of those with the public accounting social identity identify this value). Those with an executive management social identity also mention their operational background and ensuring transparency with investors (20 percent mention both of those).

These interview questions highlight the different roles that audit committee members serve and the value they perceive they provide to management and shareholders. By looking at responses by social identity I find that audit committee members' views are influenced by their social identity. With the next research question I examine how audit committee members identify with the company, management, and the audit committee. Furthermore, I examine whether their strength of identification varies based on social identity.

[INSERT TABLE 9 HERE]

RQ3a: Do audit committee members' social identities influence their strength of identification with the company, management, and audit committee?

RQ3b: When and how do audit committee members identify with the company, management, and audit committees of the companies on which they serve, and what are the implications of such identification?

Interview questions 10-13 probe audit committee members' identification with management, board, and other audit committee members. When I asked participants whether they empathize with management, every participant except for one responded that they do empathize with management. Furthermore, every participant that I asked about identifying with the audit committee and board responded that they do, indeed, identify with these two groups.

Due to the lack of variation in these responses I focus on the pre-interview survey to analyze research questions related to identification. In the pre-interview questions, I asked participants questions measuring their strength of identification with the company they serve, management, and the audit committee. To conduct my analysis, I leverage an identification measure from Bamber and Iyer 2007; this measure uses a five point scale with higher scores indicating higher identification (see questions in Appendix A).

[INSERT TABLE 10 HERE]

Table 10 presents the identification scores. When examining the complete sample, participants identify the most with the audit committee (4.07 on a 5-point scale), then the company (3.59), and they identify the least with management (2.91). However, analyzing the data by social identity, I find interesting variation. For example, examining identification with the company those with a financial management social identity identify the most with the company (3.83 on a 5-point scale) and those with a public accounting social identity the least with the company (3.48). The financial management and executive management social identities identify the most with management (3.29 and 3.04 respectively). This is consistent with these individuals that have experience in management identifying with others that are in the same role.

They have been, or are in, management's shoes in their own companies. Again, those with the public accounting social identity identify the least with management (2.72). Finally, when looking at identification with the audit committee the financial management social identity identifies the most with the audit committee (4.29) and the investment management social identity the least (3.80).

Further insights into the influence of identification on audit committee member behavior are found when examining discussion from the interviews. For example, during the interviews audit committee members I asked how identification impacts their behavior. One participant discusses how it leads to frank discussions:

*"I would say it leads to very frank discussions. The feeling of being a peer means if the head of the compensation committee presents a point of view that you may not completely agree with, it makes it much easier for everyone to express their feelings and opinions, and experiences related to whatever issue or case you're presenting. I feel extremely comfortable that **we have very frank discussions that get thoroughly vetted before decisions are made.**" (Participant 110)*

Another participant highlights the importance of identification.

*"You just have to. I think if you didn't identify with them and your context, I don't know how comfortable you'd be in the boardroom. It doesn't mean at all that nobody is challenging, or that there aren't different views. There are always, but you've just got to listen to other people. **That's another way of saying identify. You've got to trust their judgments. You have to have an understanding of where they're coming from. That's what makes a really good board, the butcher, the baker, and the candlestick maker, and they all lived on Main Street. They all did different things, but none of them could exist without the others.**" (Participant 129)*

Another participant discusses how different backgrounds influence audit committee interactions:

*"What I'm trying to explain is **that those different varied backgrounds will impact how I might interact with those other committee members** because of their backgrounds and experience, how you communicate and how you go through certain topics because of how they might process it because of their different backgrounds and different experiences." (Participant 128).*

The above quotes show the importance of identification. However, one participant notes that he has to be careful with his identification with his prior auditor role:

*“I’ve got to be careful because **it might look like I’m always trying to defend the external auditors because that’s what I did.**”* (Participant 128)

Furthermore, another participant also identifies a potential concern of too strongly identifying:

*“**I think if people become too friendly they oftentimes, as you would expect, can maybe be more reluctant to take a hard position against the views of somebody else that’s on the board or against management. I think that’s just natural human nature as opposed to anything else.**”* (Participant 127)

Overall, through examination of the pre-interview and interview questions it is clear that audit committee members do identify with the company, management, and audit committees. However, the strength of identification with each group varies by the social identities of audit committee members. I further probe the implications of social identities on audit committee member behavior in my final research question. However, before I examine that research question I first look at how characteristics of companies that audit committee members serve influence how they add value.

RQ4: How do characteristics of the companies that audit committee members serve influence how they perceive that they add value to those companies?

To examine whether characteristics of the companies that audit committee members serve influence how they perceive that they add value I further examine responses to interview question three. This is the question that asks participants how they add value to management and shareholders. I analyze responses to this question by company size and by whether the company the audit committee member serves is public or private. Tables 11 and 12 present these results. Overall, I find limited variation in perceived value added to management and shareholders by these two company characteristics.

[INSERT TABLE 11 HERE]

[INSERT TABLE 12 HERE]

The main difference in perceived value added to management when comparing responses of private (n=6) to public (n=20) companies is that those who serve private companies feel that they add value through their industry experience (33 percent of those serving private companies mention this). This was not a common answer by those who serve public companies. Rather, those who serve public companies focus on their accounting and financial reporting experience.

When examining perceived value added to shareholders across public versus private companies, there exist some more differences. First, those serving private companies focus their interview discussion on monitoring financial reporting (33 percent), monitoring the control environment (33 percent), and the relationship with the external auditor (33 percent). Second, those who serve public companies also mention monitoring of financial reporting (25 percent), but also discuss the importance of transparency and communication with the investment community (25 percent), monitoring the staffing of the accounting function (15 percent), and avoiding problems (15 percent). Based on these responses, it is clear that those in the sample who serve public companies are aware of the public nature of the company that they serve.

I also examine variation in the perceived value added to management and shareholders by the size of the company. I compare responses between companies that have \$1 billion or more in revenue (n=11) to companies that have \$500 million or less in revenue (n=11). There are some differences when making this comparison. First, I will discuss the value added to management. Those who serve larger companies feel that they add value through their audit partner experience (27 percent) and CPA background (27 percent). On the other hand, those that serve smaller companies also discuss providing financial reporting advice to management and their experience

on other boards (18 percent). Finally, when examining value added to shareholders the most interesting difference is those that serve larger companies also focus on transparency to shareholders (36 percent). Overall, the examination of whether company characteristics influence the audit committees finds only limited variation.

RQ5: How do audit committee members' social identities and related corporate governance roles influence their judgments and decisions?

My last research question examines whether audit committee members' social identities ultimately influence their behavior. I primarily use participants' responses to interview question five and six to probe this research question. Question five asks participants about difficult issues they resolve on the audit committee and what features of their background influence their judgments and decisions. There does exist some variation in what types of difficult issues audit committee members identify based on their social identities (see Table 13). Those with a public accounting social identity are more frequently identify their most difficult issue as an audit related or regulatory/compliance issue. Audit related issues include things like changing auditors, having an auditor that does not maintain independence, or having a bad relationship with the audit partner. Regulatory and compliance issues include things like SEC investigations or PCAOB reviews. The other social identities more frequently identify a personnel issue as the most difficult. For example, issues with CFO turnover, terminating a director of internal audit, or having an executive cheat on their expense reports.

[INSERT TABLE 13 HERE]

When discussing difficult issues, participants also discuss the features of their backgrounds that influence their judgments. They focus this discussion around their most salient professional experiences. For example, those with a public accounting social identity that have

spent their career as an auditor, focus on how their auditing experiences help them respond to difficult issues. For example, a prior audit partner discusses the benefits of his prior auditor experiences when dealing with a regulatory/compliance issue on the audit committee:

*"The things that helped me in this were **I'd been through this with clients before**. I knew somewhat how it should go. I knew the things that we had to be careful of. I was able to help manage the process. I guess that's the kind of things I think about. **I was able to communicate with the management team and actually worked with some of the regulators directly...**" (Participant 105)*

Another audit committee member with a public accounting social identity discusses how his auditing experience helps him in his audit committee role:

"I think it helped me realize what the audit business is like, the challenges that they have, and the limitations they have and how it works, how they get measured and managed, the oversight that they have and things like that. I think it makes me more sensitive to, when they come to me and say, 'I've got to have a fee increase because the PCAOB is asking this,' I get it. Some of those things. It helped me understand their business and business model probably a little bit better than if I hadn't been in public accounting." (Participant 117)

Furthermore, those with an executive management social identity highlight the importance of executive experiences as being critical to their ability to work on their difficult issue. For example, an audit committee member with CEO experience discusses a difficult issue that involves a decision that the CEO of the company he is monitoring is making that he is not comfortable with. When discussing how his background helps him deal with this issue he states:

*"That was one where I think my years of experience in working with a high-powered CEO and COO in one of my companies who had strong opinions and all that, helped, if you will, build a backbone to make sure that the CFO's job and **the audit committee's job is to make sure that you never cross the line, whatever that line is.**" (Participant 117)*

In interview question 6 and through other discussions during the interviews, participants often discuss how their professional experiences influence their audit committee work. For example, one participant discusses the importance of his CEO experience:

“I think because it gives you a better appreciation of what it takes internally to sometimes generate the financial information on a day to day basis that is needed to create correct financial statements. You don't totally get that understanding just being an auditor but having run a mid-size private company, interacting with your financial staff, you know the things that have to happen to make that happen.” (Participant 128)

An audit committee member with a financial management social identity reports the following when discussing how his CFO experience influences his audit committee work:

“I've been on both sides of the table. I bring an operating CFO, or senior financial executive, dealing with the board and the audit committee so I understand what their needs are. Now that I'm on an audit committee, I know what the pressures are in terms of what a CFO has to do, in terms of he and his team getting the numbers ready and making sure it's done on a timely basis, et cetera.” (Participant 126)

An audit committee member with an investment management social identity stated:

“I spend all day every day focused on financial analysis and business leadership. I've been an investor in 40 different companies over the course of my career and I've been involved at a board level in all those companies. It's kind of like my experience is on an everyday basis is pretty direct.” (Participant 127)

Finally, an audit committee member with both an executive and financial management social identity commented:

“Unlike probably most of the people you're talking with, I'm not technically a CPA. I have an undergraduate degree in economics from XXXX and then I went straight to business school. I also took subsequent courses in internal audit, auditing, tax and stuff like that. If I wanted to sit for the CPA exam, which I could have, but I just never did. I tend to take a strategic approach to things and try to deal with the big issues because those are things that will matter.” (Participant 126)

These quotes highlight how the social identities of audit committee members influence their audit committee work. The insights from the interviews suggest that audit committee members' social identities influence their corporate governance roles and ultimately their judgments and decisions. For example, the interview data suggests that audit committee members with a public accounting social identity tend to focus on a monitoring corporate

governance role. This is evident through an emphasis on financial reporting monitoring, and how they perceive that they add value through their monitoring and technical accounting background.

Those with other social identities also focus on a monitoring role but that is in addition to a resource dependence role. For example, those with an executive management and financial management social identity highlight their resource dependence role when asked how they add value to management. Executive management social identities most commonly respond to this question by discussing their operational background and industry expertise. This includes providing operational and accounting/financial reporting advice to management. Audit committee members with a financial management social identity also focus on adding value by providing advice to management (operational and accounting related) and by mentoring the CFO. Audit committee members with an investment management social identity also focus on a resource dependence role in addition to their monitoring role. For example, when discussing the value they add to management they focus on providing accounting/financial reporting advice and their experiences on other boards. Overall, the interviews suggest that the social identities of audit committee members influence their corporate governance roles and ultimately influence judgments and decisions. In the next part of my dissertation I use the insights I gain from these interviews, along with related literature, to develop testable hypotheses. I then use publicly available information to examine these hypotheses.

V. CONCLUSION

In this part of my dissertation, I use a field interview investigation to examine audit committee member social identities and related corporate governance roles. I articulate a conceptual model that proposes that audit committee members' professional experiences lead to social identities and expertise that then influence the audit committee members' corporate

governance role(s). Together, the social identities and related corporate governance roles then influence the judgments and decisions of audit committee members. From this conceptual model I propose five research questions. These questions seek to understand the manner in which audit committee members' view their role on the audit committee, how they add the most value, and whether these views are influenced by their social identities. In addition, I examine audit committee member identification based on social identities, how company characteristics influence the value added by the audit committee, and finally how the social identities of audit committee members' influence audit committee member behavior.

I interview 26 audit committee members from various backgrounds and who serve different types of companies. Based on the interviews and pre-interview questions I find that audit committee members have four main social identities: public accounting, executive management, financial management, and investment management. Furthermore, I find that these social identities influence how audit committee members view their role on audit committees, perceive that they add value, how strongly they identify with the company and management, and finally their judgments and decisions. For example, those with a public accounting social identity focus on monitoring the external/internal audit and financial reporting. They also identify the least with management and the company. Furthermore, there is evidence that their public accounting background influences how they make decisions on the audit committee. On the other hand those with an executive management social identity focus their role on the audit committee more broadly. In addition to monitoring they also focus on providing a resource dependence role to management (e.g., provide operational advice). They also identify more strongly with management and the company. This comparison of a public accounting social identity and an executive management social identity highlights the influence social identities have on audit

committee members' roles, how they perceive that they add value, and the members' identification with the company and management.

While this field investigation provides many deep insights there are a few of limitations. First, the interview methodology requires a smaller sample size. While my sample includes audit committee members that serve different types of companies and have a variety of backgrounds it is not as representative as a larger sample. Second, I only interview audit committee members who are willing to be interviewed. This may bias my sample towards more active audit committee members (i.e., those who are not as engaged in corporate governance will likely not agree to be interviewed). Finally, my sample only includes male audit committee members. I did not intentionally exclude females from my sample but the only contacts for this study were male.

This field investigation provides deep insights from a relatively small number of actual audit committee members. These audit committee members provide rich information based on their unique institutional perspectives and experiences that cannot be obtained from publicly available information. The results of this study contribute to both literature and practice by providing a better understanding of determinants of audit committee effectiveness. In addition, the information gained from this field investigation, along with related literature, provides a foundation for me to develop testable hypotheses in the second investigation in my dissertation.

CHAPTER 4: EVIDENCE FROM INITIAL PUBLIC OFFERINGS

I. INTRODUCTION

The role of the audit committee has expanded substantially over the past 20 years (Blue Ribbon Committee 1999; U.S. House of Representatives 2002), and regulators continue to scrutinize this element of the corporate governance mosaic (Cohen, Krishnamoorthy, and Wright 2004; SEC 2015). Audit committees are critical to the financial reporting process and an understanding of what makes audit committees effective, versus ineffective, continues to be of great interest to financial statement users, regulators, practitioners, and academics (e.g., Bédard and Gendron 2010; Carcello, Hermanson, and Ye 2011; Keune and Johnstone 2015). In this study, I develop a conceptual model that proposes audit committee members' professional experiences lead to the development of a social identity that includes internalized beliefs, norms, and expected actions that in turn affect the corporate governance role these individuals assume, and ultimately affect the quality of monitoring performed by the overall audit committee.

Social identity is the part of an individual's self-concept (i.e., how one perceives one's self) that develops from the individual's experiences interacting in social groups. An individual internalizes the beliefs, norms, and expected actions from the social groups that he/she belongs, which then influences subsequent judgments and decisions (Tajfel 1978; Tajfel and Turner 1985; Turner 1987; Haslam 2001; Bamber and Iyer 2007). Audit committee members possess a social identity uniquely relevant to that role, but I anticipate that this identity is shaped by the other social identities that develop through professional experiences outside of audit committee roles (e.g., identifying as a CPA, CEO, CFO, and/or venture capitalist).

Audit committee members can serve different corporate governance roles within the organizations they serve. These roles are characterized by various theoretical perspectives

including agency and resource dependence theories (e.g., Jensen and Meckling 1976; Pfeffer and Salancik 1978; Cohen, Krishnamoorthy, and Wright 2008). Agency theory treats the audit committee as an independent monitor of management, while resource dependence theory treats the audit committee as a partner with management that assists the company with strategic objectives (e.g., identifying and securing resources). I propose that audit committee members with different social identities perform different corporate governance roles. For example, I propose that a public accounting social identity is more aligned with an agency role because an auditor's primary focus is to monitor management. However, I propose that an executive management social identity is more aligned with a resource dependence role because these individuals routinely face the same strategic challenges as management. Furthermore, I propose that some social identities are consistent with the corporate governance roles under both perspectives. For example, I propose that a venture capital social identity is aligned with both resource dependence and agency theory perspectives. Individuals with such identities have experience assisting companies with strategic objectives, consistent with resource dependence, as well as experience evaluating financial statements and risks, consistent with agency theory.

I examine the association between audit committee member social identities and the quality of the audit committee's monitoring of the financial reporting process for companies that have recently completed an initial public offering (IPO). The process of becoming a public company is an important stage in a company's life cycle that involves significant change and uncertainty. This is also a time when the company may not have a well-established accounting and finance department. Both monitoring and the development and execution of strategic objectives are essential during this time; therefore, both agency and resource dependency theories suggest the audit committee performs a critical role during this stage.

Leveraging insights from social identity theory, I expect that the internalized beliefs, norms, and expected actions that audit committee members develop from the social groups to which they belong will influence the corporate governance roles they assume. I also leverage insights from in-depth interviews of audit committee members from the first investigation in my dissertation to develop holistic, testable hypotheses about associations between audit committee member social identities and the effectiveness of financial reporting monitoring.

My sample includes companies that went public for the first time between 2005 and 2009. I use the Kenney and Patton (2013) Firm Database of Emerging Growth Initial Public Offerings, which includes all first time IPOs on American stock exchanges filed with the SEC. For each company, I hand collect data for the year the company goes public and the subsequent five years. Using this data, I proxy for audit committee member social identities based upon these individuals' recent non-audit committee professional experiences, including those in public accounting, executive management (e.g., CEO), financial management (e.g., CFO or VP of Finance), and investment management (e.g., venture capital or private equity).⁴ I expect that these identities influence the governance roles that individual audit committee members perform within the audit committee. I measure the relative effectiveness of the audit committee's financial reporting monitoring using three dependent variables: whether the company has (1) a financial restatement, (2) a material weakness, and (3) earnings management behavior as indicated by meeting or just beating analysts' forecasts.

My restatement sample includes 293 unique companies and 1,389 company-years. Of the 293 IPO companies, 83 (or 28.3 percent) have a restatement within the subsequent five years,

⁴ I measure each identity as a continuous variable (i.e., the proportion of the audit committee with the related social identity) and as an indicator variable (i.e., whether the social identity is present or not on the audit committee).

representing restatements in 152 company-years.⁵ My material weakness sample includes 281 unique companies and 1,133 company years. There are 61 (or 21.7 percent) unique companies that have a material weakness within the subsequent five years and 99 company-years. Finally, my meet or beat analyst forecast sample includes 280 unique companies and 1,282 company-years. There are 93 (33.2 percent) unique companies that just meet or beat analysts' forecasts and 117 company-years.

The results reveal that social identities are associated with the effectiveness of financial reporting monitoring. Specifically, I find that audit committees that have proportionally more members with a financial management social identity are associated with a higher likelihood of financial restatement in the post-IPO period. Audit committees with more members with an investment management social identity are associated with a decreased likelihood of financial restatement. Audit committees that have proportionally more members with an executive management social identity are associated with a lower likelihood of material weaknesses and meeting or just beating analysts' forecasts. Finally, audit committees with proportionally more members with a public accounting social identity are associated with a lower likelihood of material weaknesses.

This study yields theoretical inferences that provide important insight for financial statement users, regulators, practitioners, and academics. First, it provides evidence suggesting that social identities that derive from recent professional experiences influence the quality of financial reporting monitoring. The popular press suggests that a relatively high level of restatements among IPO companies reflects a lack of resources in the accounting and finance departments of companies in the early stage of their life cycle (e.g., *Wall Street Journal* 2012).

⁵ As an example, a company that went public in 2006 might have a restatement that covers 2007 and 2008. That restatement would cover two company-years.

My results illustrate the critical role of divergent professional experiences of those charged with governance with respect to determinants of financial reporting quality and reliability. This highlights the critical importance of audit committee composition in the context of financial reporting monitoring. Audit committee members possess a variety of social identities. As such, it is important to understand how different audit committee member social identities influence the effectiveness of the audit committee in monitoring the financial reporting process (Hillman, Nicholson, and Shropshire 2008). Inferences from this study imply that nominating committees should carefully contemplate the ‘social identity matrix’ of the current and successive audit committee when selecting potential new audit committee members (Clune, Hermanson, Tompkins, and Ye 2014).

Second, my study proposes a new way to think about audit committee expertise. While prior research measures audit committee member financial expertise using information about professional experiences, this research does not use a consistent definition of financial expertise (e.g., Anderson, Mansi, and Reeb 2004; Abbott, Parker, and Peters 2004; Bédard, Chtourou, and Courteau 2004; Agrawal and Chadha 2005; Hoitash, Hoitash, and Bedard 2009; Dhaliwal, Naiker, and Navissi 2010; Cohen, Hoitash, and Wright 2014). For example, some studies use broad definitions of expertise that include CPA, CFO, venture capitalists, investment banking, controllers, VP of Finance, and CEOs (e.g., Abbott et al. 2004). Other studies separate expertise into categories by classifying accounting (CPA, CFO, VP of Finance, controllers, or other major accounting position), finance (investment bankers, financial analysts, or other financial management role), and supervisory expertise (CEO or President) (e.g., Dhaliwal et al. 2010). I contribute to this research by more closely examining specific backgrounds that are generally considered indicative of financial expertise.

My results suggest that different social identities and corresponding alternative internalized governance roles that derive from prior experiences yield variation in financial reporting monitoring quality. Specifically, my results suggest that audit committee monitoring is *more* effective when the audit committee has more members with an investment management or executive management identity. Furthermore, there is some evidence that it is *more* effective when the audit committee has more members with a public accounting social identity and some evidence that it is *less* effective when the audit committee has more members with a financial management identity. Combining these alternative social identities into one financial expertise measure, as is done in prior research, introduces measurement error. This increases the difficulty of detecting empirical associations that exist between observable indicators of financial expertise and financial reporting monitoring, and, in turn, inhibits the ability to draw reliable inferences.

This paper proceeds as follows: Section II includes a discussion of the conceptual model, literature review, and hypotheses. Section III describes the sample and method. Section IV reports results and Section V concludes.

II. CONCEPTUAL MODEL, LITERATURE REVIEW, AND HYPOTHESES

A Conceptual Model of Audit Committee Financial Reporting Monitoring

I begin by articulating a conceptual model of audit committee financial reporting monitoring (see Figure 2). The model proposes that audit committee members' professional experiences lead to expertise and the development of a social identity. The social identity provides internalized beliefs, norms, and expected actions that affect the corporate governance roles these individuals assume, thereby affecting financial reporting monitoring.

[INSERT FIGURE 2 HERE]

Audit committee members have professional experiences outside of their audit committee roles, and these experiences yield expertise and alternative perspectives that complement, enhance, or possibly compete with the audit committee members' perceived corporate governance role (e.g., DeZoort 1998). Both the SEC and academic research consider the important role of audit committee members' professional experiences in the development of expertise. For example, the SEC defines audit committee member financial expertise in the context of the members' professional experiences.⁶ Similarly, academic research uses measures of prior professional experiences as proxies for audit committee expertise (e.g., Abbott et al. 2004; Bédard et al. 2004; Cohen et al. 2014).

The conceptual model in Figure 2, proposes that professional experiences provide relevant knowledge and expertise that aids audit committee members in developing a social identity. Social identity is the part of an individual's self-concept that develops through experiences interacting in a social group, thereby enabling him or her to internalize the group's beliefs, norms, and expected actions (e.g., Tajfel 1978; Tajfel and Turner 1985; Turner 1987; Haslam 2001). I expect these social identities are consistent with the corporate governance role the audit committee member assumes.

Prior research suggests that there are alternative corporate governance roles audit committee members assume, including those consistent with agency theory and resource dependence theory (Cohen et al. 2008). I propose that experience in monitoring financial reporting encourages an audit committee member to perform his or her role consistent with an

⁶ The SEC defines financial expertise as “An understanding of generally accepted accounting principles and financial statements; The ability to assess the general application of such principles in connection with the accounting for estimates, accruals and reserves; Experience preparing, auditing, analyzing or evaluating financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of issues that can reasonably be expected to be raised by the registrant's financial statements, or experience actively supervising one or more persons engaged in such activities; An understanding of internal controls and procedures for financial reporting; and an understanding of audit committee functions” (SEC 2003).

agency theory perspective (Jensen and Meckling 1976). In contrast, I propose that experience in assisting or advising a company with its strategic objectives (Pfeffer and Salancik 1978) encourages an audit committee member to perform his or her role consistent with a resource dependence theory perspective. Other social identities (or adaptations thereof) may also encourage audit committee members to perform roles consistent with one or both perspectives.

Ultimately, I propose that the respective social identity and associated corporate governance role will affect the quality of financial reporting monitoring. The model also acknowledges the importance of other important determinants of financial reporting monitoring identified by prior research (e.g., DeZoort, Hermanson, Archambeault, and Reed 2002): independence, authority, resources, and diligence. In the following sections, I articulate more completely each of the phases in the proposed conceptual model of audit committee financial reporting monitoring and develop associated research hypotheses.

Audit Committee Member Characteristics

A significant body of research examines the antecedents and consequences of audit committee effectiveness (e.g., Carcello et al. 2011a). Antecedents that this research (and regulatory guidance) explores include audit committee independence (e.g., Abbott et al. 2004; Bédard et al. 2004; Agrawal and Chadha 2005; Bruynseels and Cardinaels 2014), legal or industry expertise (Krishnan, Wen, and Zhao 2011; Cohen et al. 2014), and financial expertise (e.g., SEC 2003; Abbott et al. 2004; Bédard et al. 2004, Agrawal and Chadha 2005; Dhaliwal et al. 2010). In terms of consequences, research finds audit committee financial expertise is associated with a lower likelihood of restatement (Abbott et al. 2004), less aggressive earnings management (Bédard et al. 2004; Badolato, Donelson, and Ege 2014), improved accruals quality

(Dhaliwal et al. 2010), more timely financial restatement reporting (Schmidt and Wilkins 2013), and a lower likelihood of SOX 404 material weaknesses (Hoitash et al. 2009).

Collectively, this research demonstrates that audit committee members' prior experiences and resulting characteristics are critical determinants of audit committee effectiveness. While many studies examine audit committee characteristics, there remains a call for further research that explores determinants of audit committee effectiveness, develops better measures of audit committee characteristics, and leverages theories from psychology (Carcello et al. 2011a). I answer this call by developing a conceptual model of audit committee financial reporting monitoring that incorporates a precise consideration of current and prior audit committee experiences and that leverages social identity theory.

The Theory of Social Identity

Social identity is the part of a person's self-concept that develops from the interactive groups to which the individual belongs. Interactive groups can include gender, ethnicity, religion, profession, work organization, among others. Social identity is based on the idea that a person defines his or her 'self' not only as an individual, but also as a part of a group. Therefore, a person's sense of self includes both a personal identity and an identity associated with internalized group membership(s) (Haslam 2001). These identities then powerfully shape the individual's overall behavior.

Emerging research in accounting incorporates social identity theory (e.g., Towry 2003; Bamber and Iyer 2007; Reffett, Brewster, and Ballou 2012; Bauer 2015). In an auditing setting, Bamber and Iyer (2007) examine the implications of external auditors' identification with their clients and their profession through the lens of social identity theory. They find that auditors are more likely to allow management's preferred accounting treatment when the auditor identifies

with management, and are less likely to do so when they identify with their profession. Bauer (2015) also examines client and professional identity in an auditing setting using an experiment and finds that auditors who more strongly identify with their client are more likely to agree with the client's preferred accounting treatment, unless their professional identity is salient.

While prior literature has examined the social identity of auditors, it has not examined the social identities of audit committee members. In the audit committee setting there are likely circumstances when, due to prior professional experiences and associated social identities, audit committee members identify relatively more with an agency or resource dependence role. Furthermore, these experiences and associated social identities may result in these members identifying relatively more with either the shareholders of the company they serve or its management. I seek to understand the implications of audit committee members' differential identification. Drawing on social identity theory, I propose that audit committee members' roles outside of the audit committee shape their behavior on the audit committee and examine whether different outside social identities influence the effectiveness of financial reporting monitoring.

Corporate Governance Roles

While the majority of corporate governance research uses agency theory to anticipate role-consistent behavior, recent research explores alternative theoretical perspectives including resource dependence, institutional theory, and managerial hegemony (e.g., Cohen et al. 2008; Dhaliwal et al. 2010; Hermanson, Topkins, Veliyath, and Ye 2012; Clune et al. 2014). Cohen et al. (2008) encourage researchers to consider each of these alternative theoretical perspectives in corporate governance research, arguing that doing so may enhance theoretical insights.

From an agency theory perspective, the role of the audit committee is to be an independent monitor of the agent (i.e., management) on behalf of the owners (i.e., shareholders).

Under this perspective, ensuring high-quality financial reporting is a critically important role of the audit committee (Cohen et al. 2008). Resource dependence theory (Pfeffer and Salancik 1978) treats the audit committee as a partner of management that assists the company with its strategic objectives (e.g., identifying and securing resources). Ensuring high quality financial reporting is less important under this perspective than under the agency theory perspective. However, prior research has argued that there can be benefits of audit committee members assuming a resource dependence role. Consistent with this perspective, Dhaliwal et al. (2010) examine the association between types of audit committee expertise and financial reporting quality and find that non-accounting expertise can be beneficial. Furthermore, Cohen et al. (2008) identify audit committee member industry expertise as one primary board attribute under resource dependence and Cohen et al. (2014) find audit committee industry expertise improves the monitoring of financial reporting.

Managerial hegemony theory asserts that the audit committee is under the control of management and exists only because management seeks to superficially comply with regulatory requirements, not truly using the audit committee to assist in substantive governance (Kosnik 1987). Institutional theory (DiMaggio and Powell 1983) anticipates that audit committees become more similar over time through institutional isomorphism (i.e., the convergence of behavior due to regulatory pressures, socialization, or uncertainty), whereby audit committees follow similar practices of other organizations even if those practices are ineffective or inapplicable to their own organization (i.e., ceremonially or symbolically) (Cohen et al. 2008).

Prior descriptive research in non-IPO settings reveals the potential applicability of a broad range of theoretical perspectives in anticipating audit committee governance roles. For example, Cohen, Krishnamoorthy, and Wright (2010) find that in a post-SOX environment, audit

committees' corporate governance roles are consistent with both agency theory and institutional theory. Beasley, Carcello, Hermanson, and Neal (2009) find that audit committee members attempt to provide effective financial reporting monitoring, but their actions are ceremonial or symbolic in some instances (e.g., when an audit committee member had been selected to serve on the board based on personal relationships with management).

In the IPO setting, I propose that agency and resource dependence theories are most applicable because these organizations are especially vulnerable given that they are emerging through a critical lifecycle stage characterized by significant change and uncertainty. Furthermore, these companies often do not have the same level of resources in their accounting and finance departments compared to more mature companies (WSJ 2012). Thus, IPO companies have significant needs with respect to both strategic objectives (i.e., resource dependence theory perspective) and monitoring (i.e., agency theory perspective).

Hypotheses

Based on the conceptual model of audit committee financial reporting monitoring and insights from interviews of audit committee members, I develop testable hypotheses related to social identities and corporate governance roles. Specifically, I examine audit committee member experience in public accounting, executive management (e.g., CEO), financial management (e.g., CFO), and investment management (e.g., venture capital).

Public Accounting Social Identity

Audit committee members with a public accounting social identity have extensive experience monitoring financial reporting. This is consistent with agency theory and the adoption of a corporate governance role focused primarily on monitoring. In one of my audit committee

member interviews, a former audit partner explained the value he adds to management and shareholders as follows:

“...the oversight of the financial reporting processes and the financials themselves and the related controls to be sure that all of that is solid. It's in place. It's solid. It's operating as it should.”

Another former partner articulated his corporate governance role as follows:

“I view my job, or primary role, is both financial oversight and to challenge the entire accounting and reporting of the company, the way it goes about reporting to the public. From a shareholder perspective...having sound financials and no restatements is really important to the marketplace.”

A third former partner articulated why he was recruited to serve on the audit committee:

“They wanted somebody that really was a technical financial reporting, and accounting, and knew the auditing business, because at this stage ‘Bob’ and I are really the only members of the audit committee that have that deep background, if you will. The other current audit committee member's a president of a private equity company, he's been involved with this company, originally helped take them public back in the early '90s, so he's a great businessman, MBA, has bought and sold many companies, but isn't a, I'll call it, a technical accountant. I think what they're really looking for in me, is I'm that one that sees as new pronouncements come out or changes come out, that I'll be aware of those types of things. Then given as I was in the accounting and auditing business, overseeing the auditor relationship, they're looking for somebody that really knows that. I think that's probably the two things, then, that they're really looking for me personally to be a strong participant on the committee.”

Following these insights and the theory developed in my conceptual model, I propose the following hypothesis:

H1: Audit committees with proportionally more members who have public accounting social identities will be associated with more effective financial reporting monitoring.

Executive Management Social Identity

Audit committee members with an executive management social identity have extensive experience in making operational and strategic decisions. Furthermore, these individuals will empathize and identify with the operating and financial pressures management faces.

Accordingly, I expect such audit committee members will view their corporate governance role as one in which aiding management in identifying and securing resources is more important than monitoring management (Hillman et al. 2008). Interview excerpts illustrate the governance role associated with an executive management social identity. For example, I asked an audit committee member, who is currently a CEO, about the experiences that he views as important contributors to audit committee effectiveness, and he noted:

“Being a C-level executive for a number of years gives me insights into strategic planning dimensions of senior management.”

Another former CEO mentioned:

“I’ve been the CEO of a public company, led it through IPO and became public, and I think it is valuable to have that experience so that you can get to a balanced view on things rather than just a financial view...Having sat in the CEO’s shoes is helpful to do that.”

A third former CEO/CFO commented on a broad array of prior experiences that he views as helpful in his corporate governance role on the audit committee:

“My particular background, I was able to manage a lot of things. So finance, legal, HR, IT, corporate planning and development, M and A, public policy, facilities, manufacturing, so a lot of different stuff. Because of that, I bring a lot of what I’ll call business perspective in addition to being a card-carrying, more narrow CFO.”

While the above insights suggest that audit committee members with an executive management social identity will be more likely to identify with management and focus on securing resources these individuals have been identified by the SEC to provide financial expertise on the audit committee. Furthermore, Hoitash et al. 2009 find that executives are associated with stronger internal control quality. As such, I propose the following non-directional hypothesis:

H2: Audit committees with proportionally more members who have executive management social identities will be associated with the effectiveness of financial reporting monitoring.

Financial Management Social Identity

I expect that those with current or prior experiences in a financial management role will have a relatively complex set of influences that affect their social identities on audit committees. On one hand, CFOs likely empathize and identify with management and the importance of identifying and securing resources, which may result in less effective monitoring of financial reporting. However, these individuals also have been responsible for understanding GAAP-based financial reporting requirements, which provides them with expertise to monitor the financial reporting process differently than a CEO (e.g., Abbott et al. 2004, Agrawal and Chadha 2005, Bédard et al. 2004). Financial management professionals also are likely keenly aware of the antecedents and consequences of poor financial reporting quality (e.g., financial restatements).

Interview excerpts illustrate the complex and sometimes conflicted governance role those with a financial management social identity assume. For example, one current CFO noted:

“I think part of what the audit committee's role is to mentor the CFO because in some cases the CFO has never been a public company CFO before.”

Similarly, another CFO articulated his role as follows:

“I think I do it by being a good sounding board for the CFO.”

Illustrating more allegiance to executive management, a former CFO responded as follows:

“On all my audit committees I've received feedback that because I've been a CFO and interacted in that capacity with audit committees, that I have a good understanding of the pressures that management is under.”

Yet, the same CFO articulated another manner in which he adds value to stakeholders:

“...because I've supervised the production of financial statements and interaction with auditors and understand areas where there is some leeway in accounting....I think I

understand the buttons that can be pushed, the areas where there's subjectivity in judgment involved and to properly make sure that the financial statements properly reflect what's going on and have integrity."

Another former CFO shared the following perspective, which also illustrates the many conflicting roles that CFO responsibilities entail, and how those responsibilities help shape an audit committee member's social identity as a result:

"...in no way am I saying that people have more narrow and even deeper financial experience, have any more or less value. But in my particular case, the fact that I have been a CFO and had to manage Wall Street and work with Wall Street and shareholders, and the public accountants, and all the complexities of business as well as I literally was VP of HR for a while, and CIO for a while, and these other roles. I know what those functions entail. I know what some of their risks are. I know what the challenges and opportunities are and I can help the CFO in the allocation of resource simultaneous equation; that's one of the harder parts of the job by being able to help him in this case understand them a bit better."

These interview responses highlight CFOs that identify with the CFO role and the pressures these professionals face, which may lead to *less* effective monitoring. However, the interviews also highlight CFOs' expertise in ensuring the financial statements are fairly stated, which suggests *more* effective monitoring. Given these competing possibilities, I propose the following non-directional hypothesis:

H3: Audit committees with proportionally more members who have financial management social identities will be associated with the effectiveness of financial reporting monitoring.

Investment Management Social Identity

I expect that audit committee members with venture capital, private equity, and investment banking experiences have developed an investment management social identity. Such individuals have experience guiding companies as they go public, which is consistent with a resource dependence theory perspective. Related to this experience, they also spend a significant amount of time examining and analyzing financial statements and evaluating risks. This may

make them better monitors (i.e., consistent with an agency corporate governance role).

Therefore, like audit committee members with a financial management social identity, those with investment management experience may feel somewhat conflicted in terms of their appropriate corporate governance role. For example, I interviewed an audit committee member who has spent over 25 years in private equity. When asked what experiences he considers important to audit committee effectiveness, he responded:

*“In my case, **I’m a professional investor**. I’ve spent my entire career investing in companies so reviewing financial statements and understanding what financial statements say is kind of my core expertise. **It’s less about the technology of the financial statements and the requirements**. In my case **I personally don’t get a lot of energy from being an expert on those things**. Mine is more as a practical investor, reading the financial statements and ensuring that they fairly and accurately portray the operating results of business.”*

When asked how he believes he adds value to shareholders, he responded as follows:

*“I think investors and investment bankers bring a perspective on reading financial statements with that eye, which I think is helpful to shareholders **because if you read financial statements for a living being able to interpret them and ensure that they fairly represent the operating results of business, that we can bring that perspective.**”*

Another audit committee member with investing experience responded as follows:

*“I think my experience of 15 years as an investor using the audited financial statements and understanding how the investors use financial statements and what way they use financial statements (...is important). I think helps inform me **not only the accuracy, which should be 100% and 99.9%, but the level of detail and significance.**”*

These quotes highlight the tension that likely exists for audit committee members with investment management experience who may feel somewhat conflicted in terms of their corporate governance role. Some of the quotes highlight investors with extensive experience reviewing and interpreting financial statements, which suggests the ability to monitor financial reporting *more* effectively. However, in the first quote the investor highlights a relatively

minimal focus on financial reporting rules and requirements, which suggests *less* effective monitoring ability. Given these competing possibilities, I propose the following non-directional hypothesis:

H4: Audit committees with proportionally more members who have investment management social identities will be associated with the effectiveness of financial reporting monitoring.

III. SAMPLE AND METHOD

Sample Description

My sample includes companies that went public for the first time between 2005 and 2009. I use the companies in the Kenney and Patton (2013) Firm Database of Emerging Growth Initial Public Offerings, which includes all IPOs on American stock exchanges filed with the SEC. The database excludes mutual funds, real estate investment trusts (REITs), asset acquisition or blank check companies, foreign F-1 filers, spin-offs, and firms that are not true emerging growth firms. For the purposes of this database, emerging growth firms are considered to be firms that are newly established or not based on older firms that are spun off or a subsidiary operation.

Table 14 provides sample derivation for the restatement sample, Table 15 for the material weakness sample, and Table 16 for the meet or beat sample. From Kenney and Patton (2013) database, I identify 374 IPOs issued between 2005 and 2009. I remove financial service companies ($n = 49$), companies without proxy statements containing governance data ($n = 2$), companies not in Audit Analytics ($n = 3$), companies not in Compustat ($n = 8$), unit offerings ($n = 2$), and companies with data missing to calculate control variables ($n = 16$ restatement sample; 28 material weakness sample; 29 meet or beat sample). After removing these observations, my final restatement (material weakness; meet or beat) sample includes 293 (281; 280) unique IPOs,

representing 1,389 (1,133; 1,282) company-years.⁷ Of the 293 IPO companies in my restatement sample, 83 unique companies (or 28.3 percent) have at least one restatement within five years of the IPO, representing restatements in 152 company-years. Of the 281 IPO companies in my material weakness sample, 61 unique IPOs (or 21.7 percent) have at least one material weakness within five years, representing 99 company years. Finally, of the 280 IPO companies in my meet or beat sample, 93 unique companies (or 33.2 percent) meet or beat analyst forecasts at least once within five years, representing 117 company-years.

[INSERT TABLE 14 HERE]

[INSERT TABLE 15 HERE]

[INSERT TABLE 16 HERE]

Independent Variables

In this study, I examine the association between audit committee members' social identities and the effectiveness of financial reporting monitoring performed by the audit committee using logistic regression models. My operational proxy for social identities is the recent professional experiences of audit committee members. Prior studies that use the professional backgrounds of audit committee members when examining financial expertise tend to use a broad definition of expertise that includes all types of financial experience including CPA, investment banker, venture capitalist, CFO, controller, CEO, and others (e.g., Abbott et al. 2004). Other studies use narrower definitions of expertise (e.g., Krishnan and Visvanathan 2008; Dhaliwal et al. 2010), but still combine multiple types of prior experiences into their measures.

⁷ The maximum initial company-year sample size is larger. For example, in my restatement sample the maximum initial company-year sample size is 1,758 company-years (293 IPO companies x 6 years). Six years includes the year the company went public and the subsequent five years. However, some of these companies terminate or are acquired by another company, which reduces my initial company-year sample size.

For example, Krishnan and Visvanathan (2008) examine accounting financial experts (CPA, auditor, principal or CFO, controller, chief accounting officer), non-accounting financial experts (CEO or president), and non-financial experts (all others). My theory suggests that some of the social identities and associated corporate governance roles differ based upon these types of prior experiences. Thus, I contend that a very precise measure that reflects particular types of recent financial experiences may prove useful in explaining the association between audit committee composition in terms of social identity and financial reporting monitoring.

I measure an audit committee member's social identity based upon the recent, salient professional backgrounds of these individuals; these include the roles they have served in the most recent five years. I hand collect audit committee background information from SEC Proxy Statement filings (Form Def14a) for the year the company went public and the following five fiscal years. In total, my sample includes 4,408 audit committee biographies and 1,300 unique audit committee members. I read each audit committee member biography and code each audit committee member's background as including experiences in public accounting, in executive management, in financial management, and/or in investment management. The backgrounds I consider consistent with each of these social identities are as follows:

<i>PROP_PUB_ACCT</i> <i>PUB_ACCT</i>	<i>PROP_EXEC_MGT</i> <i>EXEC_MGT</i>	<i>PROP_FIN_MGT</i> <i>FIN_MGT</i>	<i>PROP_INVEST_MGT</i> <i>INVEST_MGT</i>
<ul style="list-style-type: none"> • Audit partner • Public accounting 	<ul style="list-style-type: none"> • CEO • President • Other Executive 	<ul style="list-style-type: none"> • CFO • VP of Finance 	<ul style="list-style-type: none"> • Private Equity • Venture Capital • Investment Banking

For each company-year observation I calculate the proportion of the audit committee that has each social identity and whether each social identity is present or not (indicator variable).⁸

For example, if an audit committee for the company-year has one or more members with financial management experiences I code that company-year audit committee as having a financial management social identity present, i.e., $FIN_MGT = 1$. If that audit committee has one of the three audit committee members with financial management experience, then the proportion of the audit committee with a financial management social identity is coded as $PROP_FIN_MGT = 0.33$. Audit committee members can be coded as having more than one social identity if they have more than one recent relevant professional experience during the past five years. For example, if an audit committee member has recent executive management and financial management experience I code that audit committee member as having both an executive management and financial management social identity.

Below, I have included an example of how I coded the proportion and indicator measures of social identity for Ruth's Chris Steak House's 2009 company-year.

Ruth's Chris Steak House (Company-year 2009)

	Public Accounting	Executive Management	Financial Management	Investment Management
Mr. Hudson	0	1	0	0
Ms. Cooper	0	1	0	0
Mr. Merritt	0	1	1	0
TOTAL	0	3	1	0
	<i>PROP_PUB_ACCT</i>	<i>PROP_EXEC_MGT</i>	<i>PROP_FIN_MGT</i>	<i>PROP_INVEST_MGT</i>
	0.00	1.00	0.33	0.00
	<i>PUB_ACCT</i>	<i>EXEC_MGT</i>	<i>FIN_MGT</i>	<i>INVEST_MGT</i>
	0	1	1	0

⁸ In my calculations I use the audit committee members who signed the audit committee report for the related year. For example, for company-year 2009 I use the audit committee members who signed the 2009 audit committee report.

In this example, the audit committee did not have any members with recent public accounting or investment management experiences. However, all three members had recent executive management experience and one member also had recent financial management experience. That results in the presence (i.e., indicator measure) of public accounting and investment management social identities to be zero (i.e., $PUB_ACCT = 0$; $INVEST_MGT = 0$), and the indicators for executive management and financial management to be one (i.e., $EXEC_MGT = 1$; $FIN_MGT = 1$). Regarding the proportion measure, the proportion of the audit committee with public accounting and investment management social identities are both zero (i.e., $PROP_PUB_ACCT = 0.00$; $PROP_INVEST_MGT = 0.00$), and the proportion of the audit committee with executive management and financial management social identities is 1.00 and 0.33 respectively (i.e., $PROP_EXEC_MGT = 1.00$; $PROP_FIN_MGT = 0.33$). Appendix D provides further discussion of this example.

Dependent Variable: Restatement Model

My conceptual dependent variable of interest is the effectiveness of financial reporting monitoring by the audit committee. My first operational proxy for audit committee monitoring effectiveness is whether or not the company has a financial restatement period during each company-year within five years of the IPO.⁹ Examining financial restatements as a proxy for monitoring effectiveness is consistent with prior research (e.g., Abbott et al. 2004; Cohen et al. 2014). I collect restatement data from Audit Analytics, which defines restatements as a revision of previously filed financial statements as a result of a clerical error, GAAP failure, or fraud. Changes in accounting principles, retrospective adoptions of new accounting principles, and changes in the reporting entity after mergers are manually excluded from the database. I also

⁹ I consider a company-year to have a restatement if that company-year's financial statements are restated. I do not consider when the restatement was announced.

manually exclude clerical restatements and fraud. Table 14 (panels C-E) contain a summary of the sample.

Control Variables: Restatement Model

I also control for audit committee, board of director, and auditor characteristics, along with relevant financial control variables (e.g., Abbott et al. 2004; Carcello, Neal, Palmrose, and Scholz 2011; Cohen et al. 2014). In terms of the audit committee, I control for audit committee size (*AC_SIZE_LN*) as a proxy for resources allocated to the audit committee and audit committee independence (*AC_IND*). I anticipate these variables will be negatively associated with *RESTATEMENT*. I control for the number of audit committee meetings (*AC_MEETINGS_LN*) but do not make a direction prediction as it could proxy for audit committee diligence or indicate more financial reporting complexity which increases the likelihood of financial restatement (Sharma and Iselin 2012). I also control for the audit committee members' average age (*ACM_AGE_LN*), which I anticipate as a proxy for expertise, but I do not make a directional prediction with respect to its association with *RESTATEMENT*.

In terms of board characteristics, I control for size (*BOARD_SIZE_LN*) to proxy for coordination issues (Carcello et al. 2011b), CEO/Chairman duality (*CEO_CHAIR*), and for the relative number of employees (i.e., non-independent members) serving on the board (*PROP_BOARD_EMP*); I anticipate that each of these variables will be positively associated with *RESTATEMENT*. I include a control for the number of board meetings (*BOARD_MEETINGS_LN*) and similar to the number of audit committee meetings I do not make a directional prediction of its association with *RESTATEMENT*.

With respect to auditor characteristics, I control for whether the company is audited by a Big 4 auditor (*BIG4*), anticipating a negative association between this variable and

RESTATEMENT. I also control for the relative lack of auditor independence (*AUDITOR_IND*) using the proportion of client audit fees divided by the total audit fees earned by the audit firm, and for whether the company had an auditor change (*AUDITOR_CHANGE*) during the fiscal year (reflecting start-up difficulties in terms of less client-specific knowledge); I anticipate that these variables will be positively associated with *RESTATEMENT*.

In terms of financial control variables, I use the market value of equity (*MVE_LN*) and the age of the company (*CO_AGE_LN*) as proxies for size and maturity respectively; I anticipate a negative association between each of these variables and *RESTATEMENT*. I control for whether the company has had a loss in either of the two prior fiscal years (*LOSS*), relative debt-to-assets (*LEVERAGE*), year-over-year industry adjusted sales growth in the top quintile (*GROWTH*), restructuring activities (*RESTRUCTURE*), and involved in any acquisitions (*ACQUISITION*); I anticipate that each of these variables will be positively associated with *RESTATEMENT*.

I also include year fixed effects and industry fixed effects in my restatement model. Industry fixed effects are based on the industry classifications in Panel F of Table 14. In addition, I cluster standard errors by company. Table 17 includes variable definitions.

[INSERT TABLE 17 HERE]

Dependent Variable: Material Weakness Model

My second operational proxy for audit committee monitoring effectiveness is whether or not the company has a material weakness period during each company-year within five years of the IPO. Material weaknesses have been used in prior research as a proxy for corporate governance and monitoring effectiveness (e.g., Hoitash et al. 2009). I collect SOX 404(b) audit

opinions and SOX 302 management reports from Audit Analytics. Table 15 (panels C-E) contain a summary of the sample.

Control Variables: Material Weakness Model

I control for audit committee, board of director, auditor, and company characteristics that impact the effectiveness of internal controls (Ashbaugh-Skaife, Collins, and Kinney 2007; Hoitash et al. 2009). To control for audit committee and board characteristics I include audit committee size (*AC_SIZE_LN*), board of director size (*BOARD_SIZE_LN*), the number of audit committee meetings (*AC_MEETINGS_LN*), the number of board of director meetings (*BOARD_MEETINGS_LN*), and board independence (*PROP_BOARD_EMP*). I expect larger audit committees and board of directors to proxy for more resources and reduce the likelihood of a material weakness. I do not make a directional prediction for the number of audit committee and board of director meetings as more meetings can indicate more diligence or indicate more complexity, which increases the risk of material weaknesses (Sharma and Iselin 2012). I expect less independent board of directors to be positively associated with material weakness due to decreased incentives to monitor.

To control for auditor characteristics I include whether the company is audited by a Big 4 auditor (*BIG4*), a Mid-Tier auditor (*MID_TIER*), and whether they have had a new auditor during the fiscal year (*AUDITOR_CHANGE*). I expect a positive association between each of these variables and the disclosure of material weaknesses (e.g., Ashbaugh-Skaife et al. 2007; Hoitash et al. 2009).

Finally, I include a number of controls for company characteristics. I expect that more mature companies will be less likely to have material weaknesses (*CO_AGE_LN*). Furthermore, I expect complexity and recent changes to be positively associated with material weaknesses:

companies that have been involved in an acquisition (*ACQUISITION*,) had a restructuring (*RESTRUCTURE*), experienced recent extreme growth (*GROWTH*), have more segments (*SEGMENTS*), and have foreign operations (*FOREIGN*). I expect companies that have experienced a recent loss (*LOSS*) to have fewer resources to spend on internal controls, which increases the likelihood of a material weakness. To capture control risk, I control for litigious industries (*LITIGATION*). Finally, I control for company size (*MVE_LN*) as I expect smaller companies to be more likely to disclose material weaknesses. I also include year fixed effects and cluster standard errors by company.

Dependent Variable: Meet or Beat Analyst Forecast Model

My third and final operational proxy for audit committee monitoring effectiveness is whether or not the company meets or just beats analysts' forecasts. Meeting or just beating analyst forecasts has been used in prior literature as a measure of earnings quality and audit committee monitoring effectiveness (e.g., Cheng and Warfield 2005; Keune and Johnstone 2012). To calculate this variable I collect analyst forecast data from I/B/E/S (Summary History File). I measure my meet or beat variable (*MB01*) as an indicator variable equal to 1 if the company just meets or beats the last analysts' median consensus forecast before the earnings report by 1 cent, and 0 if they do not. Similar to my other two dependent variables I capture this variable for each company-year within five years of the IPO. Table 16 (panels C-E) contain a summary of the sample.

Control Variables: Meet or Beat Analyst Forecast Model

I also control for audit committee, analyst, and company characteristics (e.g., Cheng and Warfield 2005; Keune and Johnstone 2012). I expect larger (*AC_SIZE_LN*) and more independent audit committees (*AC_IND*) to be more diligent and negatively associated with the

likelihood of the company meeting or just beating analysts' forecasts (*MB01*). I also include controls for analyst forecast characteristics. I expect more pressure for companies to meet forecasts if they are more heavily followed by analysts (*NUM_EST*) or if the analyst forecasts are less dispersed (*SD*). It has also been found to be easier to meet or beat analysts' forecasts if there has been downward guidance. As such, I expect a positive association between analysts revising their forecast down (*ANALYST_DOWN*) and *MB01*.

I also include a number of company characteristic controls. I expect more mature companies (*CO_AGE_LN*) to be more likely to meet or beat analyst forecasts. There are incentives for companies to not have negative earnings surprises and be more likely to at least meet earnings forecast to limit negative publicity. These incentives increase for companies in litigious industries (*LITIGATION*) and companies with more implicit claims (*IMPLICIT_CLAIM*). Prior research has found that companies with higher net operating assets (*NOA*) in the prior year are less likely to meet or beat analysts' forecasts. Furthermore, I expect that the number of outstanding shares is positively associated with *MB01* as these companies have smaller earnings per share and will be more likely to meet or beat (Barton and Simko 2002; Cheng and Warfield 2005). Finally, I also control for company size (*MVE_LN*), growth (*BOOK_TO_MARKET*), include year fixed effects, and cluster standard errors by company.¹⁰

IV. RESULTS

Descriptive Statistics

Table 18 reports descriptive statistics for the restatement model, Table 19 for the material weakness model, and Table 20 for the meet or beat model. The mean *proportion* of the audit

¹⁰ Cheng and Warfield 2005 find that equity incentives in the form of options are associated with the likelihood of a company meeting or just beating analysts' forecasts. In the IPO setting options are used often in Biotech and Internet companies but not as common in other industries (CAP Flash 2015). I do control for industry effects but am not able to control for equity incentives without significant hand collection.

committee with a public accounting, executive management, financial management, and investment management social identity in my restatement (material weakness; meet or beat) sample is 2.5 (2.3; 2.6) percent, 55.7 (56.4; 55.7) percent, 19.3 (19.6; 19.0) percent, and 29.1 (26.8; 29.2) percent respectively. Furthermore, the *existence* of at least one member on the audit committee with a public accounting, executive management, financial management, and investment management social identity is 8.0 (7.1; 8.2) percent, 90.4 (90.8; 90.8) percent, 49.4 (49.6; 49.0) percent, and 61.9 (58.6; 62.8) percent, respectively. Finally, in the restatement sample 10.9 percent of the company-years have a restatement, in the material weakness sample 8.7 percent of the company-years have a material weakness, and in the meet or beat sample 9.1 percent of the company-years meet or just beat analysts' forecasts.

[INSERT TABLE 18 HERE]

[INSERT TABLE 19 HERE]

[INSERT TABLE 20 HERE]

Table 21 compares company-years with and without a restatement (*RESTATEMENT*). Results show that companies with restatements have a marginally higher proportion of audit committee members with financial management experience (*PROP_FIN_MGT*; $p = 0.10$), a smaller proportion of audit committee members with investment management experience (*PROP_INVEST_MGT*; $p = 0.00$), more audit committee meetings (*AC_MEETINGS*; $p = 0.00$), larger boards (*BOARD_SIZE*; $p = 0.03$), are less likely to have a Big 4 auditor (*BIG4*; $p = 0.00$), are more likely to have been involved in an acquisition (*ACQUISITION*; $p = 0.00$) or restructuring (*RESTRUCTURE*; $p = 0.00$), and are more highly leveraged (*LEVERAGE*; $p = 0.00$).

[INSERT TABLE 21 HERE]

Table 22 compares company-years with and without a material weakness (*MW*). Results show that companies with material weaknesses have a marginally lower proportion of audit committee members with executive management experience (*PROP_EXEC_MGT*; $p = 0.10$), smaller audit committees (*AC_SIZE*; $p = 0.05$), smaller boards (*BOARD_SIZE*; $p = 0.03$), less independent boards (*PROP_BOARD_EMP*; $p = 0.00$), more board meetings (*BOARD_MEETINGS*; $p = 0.04$), less likely to have a Big 4 auditor (*BIG4*; $p = 0.00$), more likely to use a Mid-Tier auditor (*MID_TIER*; $p = 0.00$), more likely to have had experienced an auditor change (*AUDITOR_CHANGE*; $p = 0.00$), are a younger company (*CO_AGE*; $p = 0.00$), are more likely to have been involved in a restructuring (*RESTRUCTURE*; $p = 0.08$), more likely to have had a loss (*LOSS*; $p = 0.04$), and less likely to be in a litigious industry (*LITIGATION*; $p=0.01$).

[INSERT TABLE 22 HERE]

Table 23 compares company-years with and without meeting or beating analyst forecasts (*MBOI*). Results show that companies that meet or beat analyst forecasts have less independent audit committees (*AC_IND*; $p = 0.07$), more analysts that lower their forecasts (*ANALYST_DOWN*; $p = 0.03$), and are older companies (*CO_AGE*; $p = 0.01$). I also examine the size of the earnings surprise in my sample. I calculate earnings surprise as the difference between actual earnings and the last analysts' median consensus forecast before the earnings report.

[INSERT TABLE 23 HERE]

Table 24 presents the size of the earnings surprises in my sample and compares it to the earnings surprise size of more mature companies. Specifically, I compare my sample to the sample from Cheng and Warfield 2005. I find that I have fewer companies meeting or beating analysts' forecasts by 1 cent (9.1 percent from my IPO sample compared to 41.9 percent of the

Cheng and Warfield 2005 sample). Furthermore, I have a larger portion of my sample that is more than five cents from the forecast (67.4 percent of my sample compared to 20.6 percent of the Cheng and Warfield 2005 sample). These differences highlight the difficulty analysts of younger, less mature, companies have in forecasting earnings and the difficulty these younger, less mature, companies have in meeting these forecasts.

[INSERT TABLE 24 HERE]

Table 25 reports correlations for the restatement sample. Results show that *RESTATEMENT* is negatively and significantly ($p < 0.05$) associated with *PROP_INVEST_MGT* and *BIG4*. The following variables are positively and significantly ($p < 0.05$) associated with *RESTATEMENT*: *BOARD_SIZE_LN*, *ACQUISITION*, *RESTURCTURE*, and *LEVERAGE*.¹¹

Table 26 reports correlations for the material weakness sample. Results show that *MW* is negatively and significantly ($p < 0.05$) associated with *AC_SIZE_LN*, *BOARD_SIZE_LN*, *BIG4*, *CO_AGE_LN*, *MVE_LN*, and *LITIGATION*. The following variables are positively and significantly ($p < 0.05$) associated with *MW*: *PROP_BOARD_EMP*, *BOARD_MEETINGS_LN*, *MID_TIER*, *AUDITOR_CHANGE*, and *LOSS*. Table 27 reports correlations for the meet or beat sample. Results show that *MB01* is negatively and significantly ($p < 0.05$) associated with *ANALYST_DOWN* and positively and significantly ($p < 0.05$) associated with *CO_AGE*.

[INSERT TABLE 25 HERE]

[INSERT TABLE 26 HERE]

[INSERT TABLE 27 HERE]

Hypothesis Tests

¹¹ To assess multicollinearity, I calculate variance inflation factors (VIF) that are computed using an ordinary least squares regression that includes my same model variables. I find that all of VIFs are within acceptable limits for all 3 models (Kutner, Nachstein, Neter, and Li 2004).

Table 28, 29, and 30 present hypothesis-testing results for the restatement, material weakness, and meet or beat samples respectively. In each table, column (1) presents results when audit committee member social identities are measured as the proportion of the audit committee and column (2) presents results measured as the presence of the social identities (indicator variable equal to one if at least one audit committee member has the related social identity).

[INSERT TABLE 28 HERE]

H1 predicts that audit committees with members who have public accounting social identities will be associated with more effective financial reporting monitoring; the results only partially support this hypothesis. Regarding the restatement model both the proportion of public accounting social identities (*PROP_PUB_ACCT*; $p = 0.435$) and the presence of at least one public accounting social identity (*PUB_ACCT*; $p=0.402$) are not associated with the quality of financial reporting monitoring when operationalized with restatements. The association between the proportion of public accounting social identities and the likelihood of material weaknesses is marginally significant (*PROP_PUB_ACCT*; $p=0.097$) but the presence of at least one public accounting social identity is not significant (*PUB_ACCT*; $p=0.145$). Finally, in the meet or beat model both the proportion and presence of public accounting social identities are not significant ($p=0.294$ and $p=0.403$ respectively). It is important to note that while I find little significance for this hypothesis, there are very few public accounting social identities in my sample. As mentioned previously, only seven to eight percent of my samples have a member with recent public accounting experience.

[INSERT TABLE 29 HERE]

H2 predicts that an executive management social identity is associated with the monitoring of the financial reporting process. Results also do not support this hypothesis in the

restatement model. Both the proportion of executives (*PROP_EXEC_MGT*; $p=0.535$) and presence of an executive (*EXEC_MGT*; $p=0.578$) are not associated with the effectiveness of monitoring of the financial reporting process as measured by the likelihood of a restatement in the five-year post-IPO period. However, results do support this hypothesis in the material weakness and meet or beat sample. Both the proportion of executives (*PROP_EXEC_MGT*; $p=0.028$) and the presence of an executive (*EXEC_MGT*; $p=0.007$) are associated with more effective monitoring indicating a decreased likelihood of a material weakness. Furthermore, the proportion of executives is marginally significant (*PROP_EXEC_MGT*; $p=0.078$) in decreasing the likelihood of companies meeting or just beating analyst forecasts. However, the presence variable is not significant in the meet or beat sample (*EXEC_MGT*; $p=0.350$).

[INSERT TABLE 30 HERE]

H3 predicts that a financial management social identity is associated with the effectiveness of monitoring, but does not make a directional prediction. I find that the proportion of financial executives is positively associated with the likelihood of restatement (*PROP_FIN_MGT*; $p = 0.024$). This result is economically significant, as the likelihood of restatement increases from 7.88 percent to 9.71 percent (a 23.2 percent increase) when the proportion of audit committee members with a financial executive management social identity increases by one standard deviation over the sample mean, holding all other variables at their sample means. Furthermore, the presence of at least one finance executive is also positively associated with the likelihood of restatement (*FIN_MGT*; $p = 0.008$), which represents an economically significant 66.94 percent increase in restatement likelihood when there is at least one financial executive social identity on the audit committee compared to none (restatement likelihood is 6.17 percent with no financial executive social identities and 10.30 percent with at

least one).¹² These results are consistent with finance executives being associated with less effective financial reporting monitoring when measured using restatements. While the coefficients are in the same direction as the restatement model I do not find that finance executives are associated with the effectiveness of financial reporting monitoring when measured using material weaknesses or meeting or beating analysts' forecasts.

Finally, H4 predicts that the investment management social identity is associated with the effectiveness of monitoring. The results reveal that the proportion of investment experience is negatively associated with the likelihood of restatement (*PROP_INVEST_MGT*; $p = 0.007$). This result is also economically significant. The likelihood of restatement decreases from 7.87 percent to 5.85 percent (a 25.7 percent decrease) when the proportion of audit committee members with an investment social identity increases by one standard deviation over the sample mean, holding all other variables at their sample means. Furthermore, the presence of at least one audit committee member with investment experience is also negatively associated with the likelihood of restatement (*INVEST_MGT*; $p = 0.031$). These results are consistent with the investment social identity being associated with more effective financial reporting monitoring when examining restatements. However, I do not find significance when examining material weaknesses or meeting or beating analyst forecasts.

Results for control variables are generally consistent with expectations.¹³ However, results for two control variables provide interesting new insights in the restatement model. First, I find that audit committee members' age is negatively associated with the likelihood of a post-

¹² If I add 2004 data to my sample the coefficient on this variable is in the same direction but no longer significant. I have chosen to not include 2004 in my sample as it is the first year of SOX implementation. Furthermore, when I compare descriptive data by year there are significant differences in descriptive data between 2004 and the rest of my sample (e.g., *CEO_CHAIR*, *AUDITOR_IND*, and *AUDITOR_CHANGE*).

¹³ Exceptions include that *MVE_LN* is unexpectedly positive and significantly associated with *RESTATEMENT* ($p = 0.030$), *BIG4* and *LITIGATION* are unexpectedly negative and significantly associated with *MW* ($p=0.007$ and $p=0.058$ respectively), and *ANALYST_DOWN* is unexpectedly negative and significantly associated with *MB01* ($p = 0.061$).

IPO restatement (ACM_AGE_LN ; $p = 0.032$), suggesting that more-extensive prior experiences are important to enabling audit committee members' to effectively monitor financial reporting. Second, in contrast to prior research in the context of financial monitoring of relatively more-established companies, I find that CEO duality (i.e., CEO who is also the Chairman of the Board) is negatively associated with the likelihood of a post-IPO restatement (CEO_CHAIR ; $p = 0.032$). This may derive from the dual importance of both resource dependence and monitoring during the post-IPO period as the company struggles with the strategic execution of its business plan.

V. CONCLUSION

In this study, I articulate a conceptual model that proposes that audit committee members' professional experiences provide expertise and lead to the development of a social identity that includes internalized beliefs, norms, and expected actions that affect the corporate governance roles these individuals assume, and ultimately affect the quality of monitoring performed by the overall audit committee. Using IPOs between 2005 and 2009, I examine the association between four audit committee member social identities and the quality of financial reporting monitoring. Specifically, I examine social identities developed through experiences in public accounting, executive management, financial management, and investment management.

I find that a financial management social identity is associated with *less* effective financial reporting monitoring when measured as the likelihood of financial restatement, an investment management social identity is associated with *more* effective monitoring when measured as the likelihood of financial restatement, an executive management social identity is associated with *more* effective monitoring when measured as the likelihood of a material weakness and meeting or beating analysts' forecasts, and some evidence that a public accounting social identity is associated with *more* effective monitoring when measured as the likelihood of a

material weakness. Furthermore, I also find that the age of audit committee members and CEO/Chairman of the Board duality are both associated with *more* effective monitoring when measured as financial restatements.

Results of this study provide new insights to users, regulators, practitioners, and to academic literature. First, they provide evidence consistent with social identities impacting the quality of monitoring performed by the audit committee. My results highlight the critical role of audit committee composition, and its relative corporate governance role focus in relation to the monitoring of financial reporting. As audit committee members have a variety of potential social identities, it is important for nominating committees to carefully consider implications of different social identities when selecting potential new audit committee members (Clune, Hermanson, Tompkins, and Ye 2014).

Second, the results provide evidence regarding the importance of using a finer measure of financial expertise when measuring audit committee characteristics. Prior research has used multiple definitions of financial expertise and tends to combine a number of different backgrounds into single measures. My results show that different experiences that are typically considered to be related to financial expertise are not all associated with similar levels of monitoring effectiveness (Bédard and Gendron 2010).

Third, my results suggest boundaries to prior corporate governance research findings. For example, I find that CEO/Chairman of the board duality is negatively associated with restatement likelihood in the IPO setting. This finding highlights the importance of considering company characteristics in corporate governance research.

As with all research there are limitations to my study. First, I acknowledge that I cannot completely disentangle audit committee member's social identity from expertise. Second, my

sample is from one specific setting (the IPO setting). While this is an important setting to explore, my results may not generalize to other settings and future research can examine this. Third, I only examine resource dependence and agency roles and do not consider managerial hegemony or institutional theory.

My results also suggest other areas for future research. In my setting I find that recent CFO or VP of Finance experience is associated with less effective monitoring, which is not consistent with prior literature. There are two reasons why this finding may not be consistent. First, prior research has primarily combined this role with other roles (e.g., CPA, investment banker, controller, treasurer, etc.). A combined measure hides the more nuanced role each of these backgrounds has on the monitoring performed by the audit committee. Or this role is offset by the presence of other audit committee member backgrounds. Second, the IPO stage for a company is a unique point in a company's life. It is a period of time that a company is facing significant change and uncertainty. This may be a setting where previous findings do not generalize.

CHAPTER 5: CONCLUSION

In my dissertation, I explore audit committee members' social identities and related corporate governance roles. My research goal is to understand how these social identities influence the judgments and decisions of audit committee members and ultimately how they affect the quality of monitoring performed by the overall audit committee. To do this I perform two related investigations.

In my first investigation, I employ a field interview methodology. I use semi-structured interviews of 26 audit committee members to understand audit committee members' social identities derived from their professional backgrounds, understand how they view their role on the audit committee, how they identify with the company and management, and ultimately how social identities affect audit committee members' judgments and decisions. Based on this investigation I find four main social identities that audit committee members hold: public accounting, executive management, financial management, and investment management. Furthermore, I find these four social identities influence how audit committee members view their role on the audit committee, how they identify with the company and management, and ultimately that they influence their judgments and decisions.

In my second investigation I leverage the insights I gain from my field investigation, and related literature, to develop testable hypotheses of how I predict audit committee member social identities are associated with the monitoring of financial reporting by the audit committee. Using publicly available data from the IPO setting I examine whether the composition of IPO audit committees is associated with the likelihood of an accounting restatement, a material weakness, or whether the company meets or just beats analysts' forecasts. I find that a financial management social identity is associated with *less* effective financial reporting monitoring when

measured as the likelihood of financial restatement, an investment management social identity is associated with *more* effective monitoring when measured as the likelihood of financial restatement, an executive management social identity is associated with *more* effective monitoring when measured as the likelihood of a material weakness or meeting or beating analysts' forecasts, and some evidence that a public accounting social identity is associated with *more* effective monitoring when measured as the likelihood of a material weakness.

The results of my two investigations allow me to develop two related conceptual frameworks that inform both theory and practice. My first conceptual framework from my field interview investigation begins with audit committee members' professional experiences outside of the audit committee leading to expertise and the development of a social identity. The audit committee members' expertise, social identities, and related identification with the company/management/audit committee affect the corporate governance roles these individuals assume and ultimately the audit committee members' judgments and decisions. Furthermore, in this framework I acknowledge the influence of company characteristics on audit committee members' corporate governance roles.

My second conceptual framework, from my archival investigation, is closely related to the first model. This second framework also begins with audit committee members' professional experiences outside of the audit committee leading to expertise and the development of a social identity. The social identity and expertise influence the corporate governance roles these individuals assume and ultimately audit committee members' judgments and decisions. This model also acknowledges the importance of other determinants of financial reporting monitoring identified by prior research (e.g., independence, authority, resources, and diligence).

These two conceptual frameworks complement and extend each other but do have a couple of differences. For example, in my first model I include audit committee members' identification with the company, management, and audit committee. I am able to investigate identification in the interview setting but am unable to do so with the publicly available data used in my second investigation. In my second model I also include other factors that influence financial reporting monitoring. These factors have been well researched in prior literature and are necessary controls in my archival analyses but are not critical to examine in my interviews.

These two related frameworks inform researchers, regulators, and practitioners about whether and how an audit committee member's social identities outside of the audit committee influence audit committee member's perceptions of their corporate governance role and the overall judgments and decisions made by audit committee members. Ultimately, this research identifies previously unexplored determinants of audit committee effectiveness and provides motivation for future research.

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FIGURE 1: Field Investigation - Conceptual Model and Research Questions

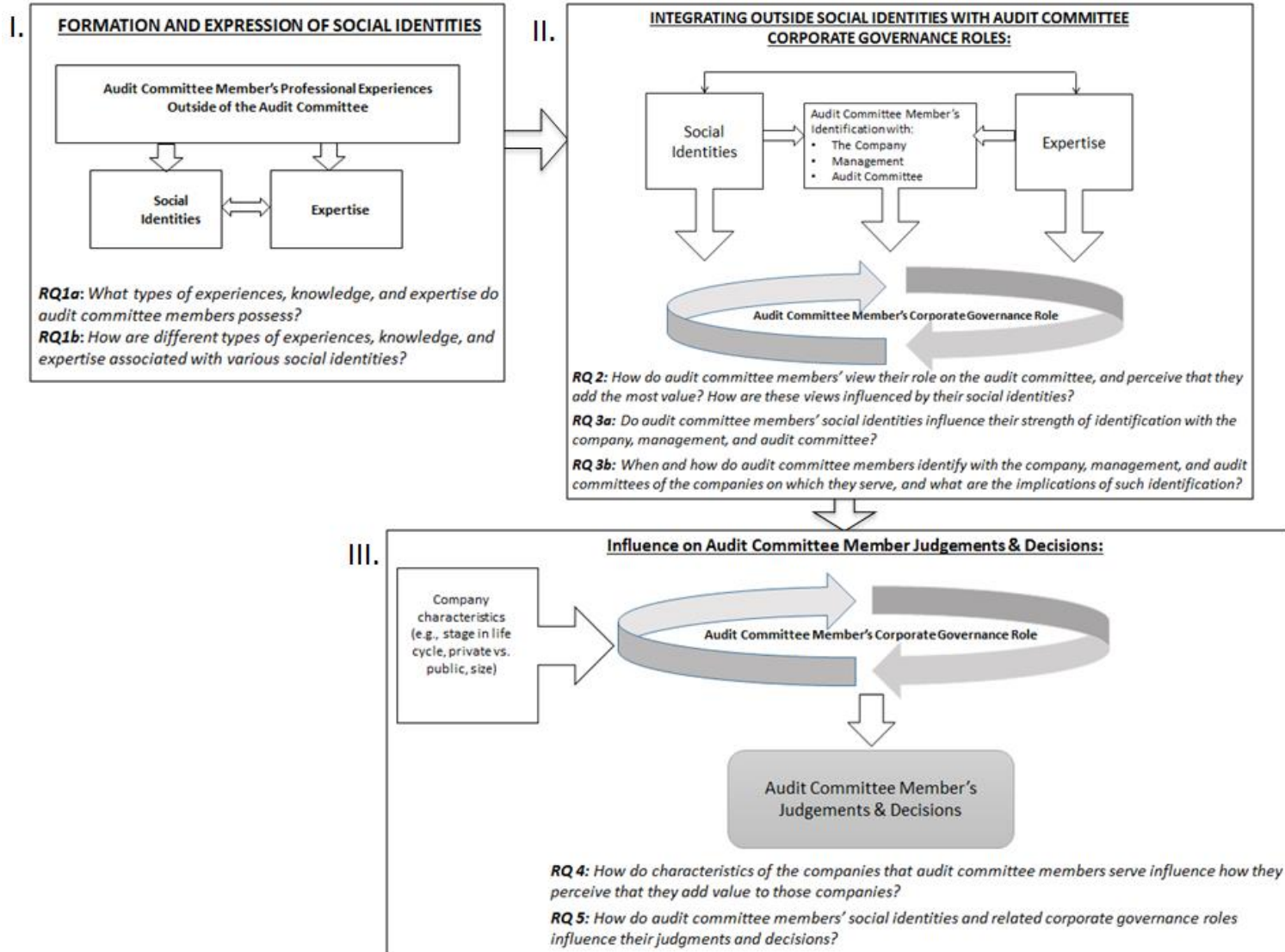


FIGURE 2: Archival Investigation - Conceptual Model of Audit Committee Financial Reporting Monitoring

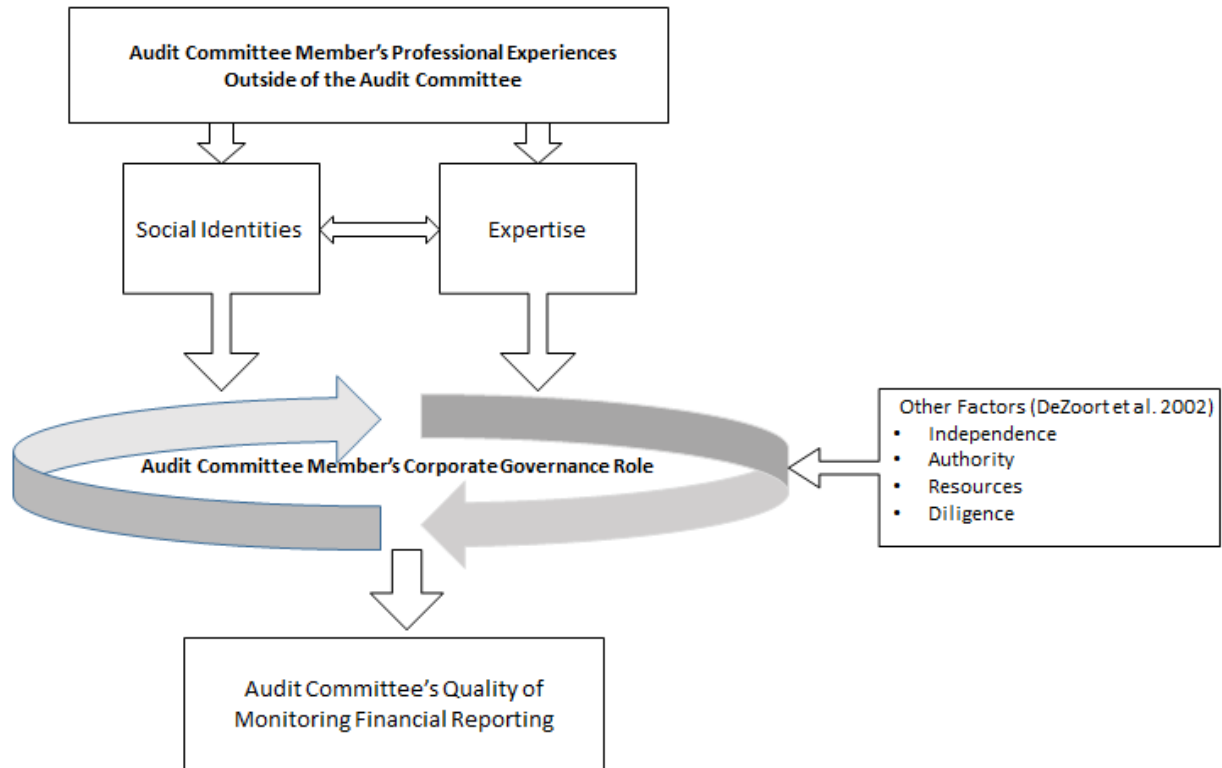


TABLE 1
Variable Definitions

Variable Name	Description
<i>Interview Length</i>	Length of interview (in minutes).
<i>YRS_Served_BRD</i>	Number of years the interviewee has served as a member of the company's board of directors.
<i>YRS_Served_AC</i>	Number of years the interviewee has served as a member of the company's audit committee.
<i>AC_CHAIR</i>	Indicator variable equal to 1 if interviewee is the audit committee chair, 0 otherwise.
<i>DES_FIN_EXPERT</i>	Indicator variable equal to 1 if interviewee is a designated financial expert, 0 otherwise.
<i>#_AC_MEMBERS</i>	Number of audit committee members serving the company.
<i>#_BOARD_MEMBERS</i>	Number of board members serving the company.
<i>#_IND_BOARD_MEMBERS</i>	Number of independent board members serving the company.
<i>#_AC_Mtgs_In_Person</i>	Number of in-person audit committee meetings per year.
<i>Duration_ACMTG_In_Person</i>	Average duration of in-person audit committee meetings (in hours).
<i>PUBLIC_CO</i>	Indicator variable equal to 1 if the company the interviewee serves is a public company, 0 otherwise.
<i>Other_Board_Committees</i>	Indicator variable equal to 1 if the interviewee serves on other board committees in addition to the audit committee, 0 otherwise.
<i>Gender</i>	Indicator variable equal to 1 if the interviewee is male, 0 otherwise.
<i>SELECT_for_prior_acct</i>	The interviewee's indication of being selected to serve on the audit committee because of their prior accounting related professional experience on a scale of 1 (not related to selection) to 4 (strongly related to selection).
<i>SELECT_for_non-acct</i>	The interviewee's indication of being selected to serve on the audit committee because of their prior non-accounting related professional experience (e.g., CEO) on a scale of 1 (not related to selection) to 4 (strongly related to selection).

<i>SELECT_for_Brd_relation</i>	The interviewee's indication of being selected to serve on the audit committee because of their relationship with another board member on a scale of 1 (not related to selection) to 4 (strongly related to selection).
<i>SELECT_for_TopMgt_relation</i>	The interviewee's indication of being selected to serve on the audit committee because of their relationship with top management on a scale of 1 (not related to selection) to 4 (strongly related to selection).
<i>SELECT_for_Ind_Expertise</i>	The interviewee's indication of being selected to serve on the audit committee because of their industry expertise on a scale of 1 (not related to selection) to 4 (strongly related to selection).
<i>SELECT_for_exp_on_other_brds</i>	The interviewee's indication of being selected to serve on the audit committee because of their experience serving on other boards on a scale of 1 (not related to selection) to 4 (strongly related to selection).
<i>SELECT_for_rotate_policy</i>	The interviewee's indication of being selected to serve on the audit committee because of the board rotation policy on a scale of 1 (not related to selection) to 4 (strongly related to selection).

TABLE 2
Interview Sample

Panel A: Sample Frequency by Industry

<i>Industry</i>	<i>Number</i>	<i>Percentage</i>
Energy	5	19.23%
Financial Services	4	15.38%
Government/Not-for-profit	2	7.69%
Healthcare/Pharmacy	3	11.54%
Manufacturing	6	23.08%
Insurance	5	19.23%
Online Services	1	3.85%
TOTAL	26	100.00%

Panel B: Sample Frequency by Company Size

<i>Company Revenue</i>	<i>Number</i>	<i>Percentage</i>
Less than \$100 million	5	19.23%
\$100 million to \$500 million	6	23.08%
\$500 million to \$1 billion	3	11.54%
\$1 billion to \$5 billion	7	26.92%
Greater than \$5 billion	5	19.23%
TOTAL	26	100.00%

TABLE 3
Descriptive Statistics

Variable	<i>Mean</i>	<i>Min</i>	<i>25th Percentile</i>	<i>Median</i>	<i>75th Percentile</i>	<i>Max</i>	<i>SD</i>
<i>Interview Length</i>	53.00	26.00	45.00	50.50	59.00	77.00	13.43
<i>YRS_Served_BRD</i>	7.98	2.00	4.00	8.00	11.00	15.00	4.32
<i>YRS_Served_AC</i>	7.29	2.00	3.50	7.00	10.00	15.00	4.11
<i>AC_CHAIR</i>	0.65	0.00	0.00	1.00	1.00	1.00	0.49
<i>DES_FIN_EXPERT</i>	0.81	0.00	1.00	1.00	1.00	1.00	0.40
<i>#_AC_MEMBERS</i>	3.96	3.00	3.00	4.00	5.00	7.00	1.10
<i>#_BOARD_MEMBERS</i>	9.04	5.00	8.00	9.00	10.00	16.00	2.24
<i>#_IND_BOARD_MEMBERS</i>	7.40	2.00	5.00	7.00	9.00	16.00	2.93
<i>#_AC_Mtgs_In_Person</i>	4.36	1.00	4.00	4.00	5.00	8.00	1.52
<i>Duration_ACMTG_In_Person</i>	2.51	1.00	2.00	2.13	3.00	5.00	0.96
<i>PUBLIC_CO</i>	0.77	0.00	1.00	1.00	1.00	1.00	0.43
<i>Other_Board_Committees</i>	0.68	0.00	0.00	1.00	1.00	1.00	0.48
<i>Gender</i>	1.00	1.00	1.00	1.00	1.00	1.00	0.00
<i>SELECT_for_prior_acct</i>	3.27	1.00	3.00	4.00	4.00	4.00	1.12
<i>SELECT_for_non-acct</i>	2.58	1.00	1.00	3.00	4.00	4.00	1.27
<i>SELECT_for_Brd_relation</i>	2.04	1.00	1.00	2.00	3.00	4.00	1.14
<i>SELECT_for_TopMgt_relation</i>	2.00	1.00	1.00	2.00	3.00	4.00	1.10
<i>SELECT_for_Ind_Expertise</i>	2.80	1.00	2.00	3.00	4.00	4.00	1.08
<i>SELECT_for_exp_on_other_brds</i>	2.69	1.00	1.00	3.00	4.00	4.00	1.23
<i>SELECT_for_rotate_policy</i>	1.46	1.00	1.00	1.00	1.50	4.00	0.88

NOTES:

- All variables are defined in Table 1.

TABLE 4
Social Identities

Panel A: Sample Frequency by Professional Background

<i>Professional Background</i>	<i>Number of Interviewees with the Background^a</i>	<i>Percentage of Sample that has the Background</i>
Audit Partner	10	38.46%
Chief Financial Officer	9	34.62%
Vice President of Finance	2	7.69%
Chief Executive Officer	8	30.77%
Other Executive	5	19.23%
Venture Capital	2	7.69%
Private Equity	4	15.38%
Private Investment	3	11.54%
Academic	1	3.85%

Panel B: Sample Frequency by Social Identity

<i>Social Identity</i>	<i>Number of Interviewees with the Social Identity^a</i>	<i>Percentage of Sample that has the Social Identity</i>
Public Accounting (Audit Partner)	10	38.46%
Executive Management (CEO, Other Executive)	10	38.46%
Financial Management (CFO, VP of Finance)	7	26.92%
Investment Management (VC, PE, Private Investment)	6	23.08%

^a Participants can be recorded for more than one professional background and social identity if they have had multiple professional roles.

TABLE 5
Descriptive Statistics - By Social Identity

Variable	Public Accounting (n=10)							Executive Management (n=10)							Financial Management (n=7)							Investment Management (n=6)						
	25th			75th				25th			75th				25th			75th				25th			75th			
	Mean	Min	Perc.	Med.	Perc.	Max	SD	Mean	Min	Perc.	Med.	Perc.	Max	SD	Mean	Min	Perc.	Med.	Perc.	Max	SD	Mean	Min	Perc.	Med.	Perc.	Max	SD
<i>AC_CHAIR</i>	0.80	0.00	1.00	1.00	1.00	1.00	0.42	0.60	0.00	0.00	1.00	1.00	1.00	0.52	0.57	0.00	0.00	1.00	1.00	1.00	0.53	0.50	0.00	0.00	0.50	1.00	1.00	0.55
<i>DES_FIN_EXPERT</i>	0.90	0.00	1.00	1.00	1.00	1.00	0.32	0.80	0.00	1.00	1.00	1.00	1.00	0.42	0.86	0.00	1.00	1.00	1.00	1.00	0.38	0.83	0.00	1.00	1.00	1.00	1.00	0.41
<i>YRS_Served_BRD</i>	5.70	3.00	3.00	5.00	6.00	15.00	3.62	8.35	2.00	3.50	8.00	14.00	15.00	5.02	9.86	3.00	8.00	10.00	14.00	15.00	3.98	11.00	6.00	10.00	10.00	15.00	15.00	3.46
<i>YRS_Served_AC</i>	5.60	3.00	3.00	4.50	6.00	15.00	3.66	8.15	2.00	3.50	8.00	12.00	15.00	4.81	9.29	3.00	8.00	9.00	12.00	15.00	3.73	8.50	2.00	6.00	9.00	10.00	15.00	4.37
<i>#_AC_MEMBERS</i>	3.70	3.00	3.00	3.00	5.00	6.00	1.16	4.60	3.00	4.00	4.50	5.00	7.00	1.07	3.83	3.00	3.00	4.00	4.00	5.00	0.75	4.17	3.00	4.00	4.00	5.00	5.00	0.75
<i>#_BOARD_MEMBERS</i>	9.70	7.00	8.00	9.00	10.00	16.00	2.50	9.60	5.00	9.00	10.00	11.00	12.00	2.01	9.33	6.00	8.00	9.50	11.00	12.00	2.34	8.33	6.00	6.00	7.50	11.00	12.00	2.58
<i>#_IND_BOARD_MEMBERS</i>	7.70	2.00	5.00	8.50	9.00	16.00	3.80	8.30	4.00	7.00	9.00	10.00	11.00	2.11	7.83	5.00	5.00	8.00	10.00	11.00	2.56	6.67	3.00	5.00	6.00	9.00	11.00	2.88
<i>Other_Board_Committees</i>	0.60	0.00	0.00	1.00	1.00	1.00	0.52	0.60	0.00	0.00	1.00	1.00	1.00	0.52	0.67	0.00	0.00	1.00	1.00	1.00	0.52	1.00	1.00	1.00	1.00	1.00	1.00	0.00
<i>PUBLIC_CO</i>	0.70	0.00	0.00	1.00	1.00	1.00	0.48	0.70	0.00	0.00	0.00	1.00	1.00	0.48	0.86	0.00	1.00	1.00	1.00	1.00	0.38	0.83	0.00	1.00	1.00	1.00	1.00	0.41
<i>SELECT_for_prior_acct</i>	4.00	4.00	4.00	4.00	4.00	4.00	0.00	2.60	1.00	1.00	3.00	4.00	4.00	1.26	3.57	3.00	3.00	4.00	4.00	4.00	0.53	3.17	1.00	3.00	3.50	4.00	4.00	1.17
<i>SELECT_for_non-acct</i>	1.60	1.00	1.00	1.00	2.00	4.00	1.07	3.60	3.00	3.00	4.00	4.00	4.00	0.52	2.29	1.00	1.00	3.00	3.00	4.00	1.25	2.67	1.00	3.00	3.00	3.00	3.00	0.82
<i>SELECT_for_Brd_relation</i>	2.40	1.00	1.00	3.00	3.00	4.00	1.07	1.89	1.00	1.00	1.00	3.00	4.00	1.17	2.33	1.00	1.00	2.50	3.00	4.00	1.21	2.20	1.00	1.00	2.00	3.00	4.00	1.30
<i>SELECT_for_TopMgt_relation</i>	2.30	1.00	1.00	3.00	3.00	4.00	1.16	1.75	1.00	1.00	1.00	2.50	4.00	1.16	2.00	1.00	1.00	2.00	2.00	4.00	1.22	2.60	2.00	2.00	2.00	3.00	4.00	0.89
<i>SELECT_for_Ind_Expertise</i>	2.90	1.00	2.00	3.00	4.00	4.00	1.20	2.89	1.00	3.00	3.00	4.00	4.00	1.17	2.00	1.00	1.00	2.00	3.00	3.00	1.10	1.80	1.00	1.00	1.00	3.00	3.00	1.10
<i>SELECT_for_exp_on_other_brds</i>	1.70	1.00	1.00	1.50	2.00	3.00	0.82	3.30	1.00	3.00	3.50	4.00	4.00	0.95	2.71	1.00	1.00	3.00	4.00	4.00	1.38	3.00	1.00	1.00	4.00	4.00	4.00	1.55
<i>SELECT_for_rotate_policy</i>	1.20	1.00	1.00	1.00	1.00	3.00	0.63	1.63	1.00	1.00	1.00	2.50	3.00	0.92	1.40	1.00	1.00	1.00	1.00	3.00	0.89	1.60	1.00	1.00	1.00	1.00	4.00	1.34

NOTES:

- All variables are defined in Table 1.

TABLE 6
Audit Committee Member's Indication of their Primary Role on the Audit Committee

PANEL A: ENTIRE SAMPLE

Primary Role	Number of Interviewees that Indicate this Role	Percentage of Interviewees that Indicate this Role
Monitor financial reporting including preparation, integrity, and timeliness.	14	0.54
Monitor the external audit including managing the relationship with the auditor.	12	0.46
Manage the audit committee including leading the AC, engaging members, fulfilling the executive charter, planning meetings, and setting tone.	10	0.38
Monitor internal audit.	9	0.35
Monitor risks.	5	0.19
Monitor the staffing of the accounting function (e.g., competent CFO, controller).	3	0.12
Legal/Compliance/Regulations	2	0.08
Monitor the control environment.	2	0.08
Provide industry related expertise.	2	0.08

PANEL B: BY SOCIAL IDENTITY

Public Accounting (n=10)

Primary Role	Number of Interviewees that Indicate this Role	Percentage of Interviewees that Indicate this Role
Manage the audit committee including leading the AC, engaging members, fulfilling the executive charter, planning meetings, and setting tone.	5	0.50
Monitor the external audit including managing the relationship with the auditor.	5	0.50
Monitor internal audit.	3	0.30
Monitor financial reporting including preparation, integrity, and timeliness.	3	0.30
Legal/Compliance/Regulations	2	0.20

Executive Management (n=10)

Primary Role	Number of Interviewees that Indicate this Role	Percentage of Interviewees that Indicate this Role
Manage the audit committee including leading the AC, engaging members, fulfilling the executive charter, planning meetings, and setting tone.	5	0.50
Monitor financial reporting including preparation, integrity, and timeliness.	4	0.40

(table 6 continued)

Monitor the external audit including managing the relationship with the auditor.	3	0.30
Monitor internal audit.	3	0.30
Monitor risks.	2	0.20

Financial Management (n=7)

Primary Role	Number of Interviewees that Indicate this Role	Percentage of Interviewees that Indicate this Role
Monitor financial reporting including preparation, integrity, and timeliness.	6	0.86
Monitor the external audit including managing the relationship with the auditor.	6	0.86
Monitor internal audit.	3	0.43
Monitor risks.	1	0.14
Monitor the staffing of the accounting function (e.g., competent CFO, controller).	1	0.14
Legal/Compliance/Regulations	1	0.14
Manage the audit committee including leading the AC, engaging members, fulfilling the executive charter, planning meetings, and setting tone.	1	0.14
Be a competent, capable, and available audit committee member.	1	0.14

Investment Management (n=6)

Primary Role	Number of Interviewees that Indicate this Role	Percentage of Interviewees that Indicate this Role
Monitor financial reporting including preparation, integrity, and timeliness.	4	0.67
Monitor the staffing of the accounting function (e.g., competent CFO, controller).	2	0.33
Legal/Compliance/Regulations	2	0.33
Provide industry related expertise.	2	0.33

TABLE 7
Audit Committee Member's Indication of their Most Important Responsibility on the Audit Committee

PANEL A: ENTIRE SAMPLE

Most Important Responsibility	Number of Interviewees that Indicate this Responsibility	Percentage of Interviewees that Indicate this Responsibility
Monitor financial reporting including integrity of and understanding how aggressive management is in regards to financial reporting.	10	0.38
Financial statements are accurate.	5	0.19
Manage the audit committee including setting the agenda and building the charter.	4	0.15
Manage the relationship with the auditor	3	0.12
Monitor the external audit and auditors.	2	0.08
Monitor the control environment.	1	0.04
Monitor internal audit.	1	0.04

PANEL B: BY SOCIAL IDENTITY

Public Accounting (n=10)

Most Important Responsibility	Number of Interviewees that Indicate this Responsibility	Percentage of Interviewees that Indicate this Responsibility
Monitor financial reporting including integrity of and understanding how aggressive management is in regards to financial reporting.	3	0.30
Manage the relationship with the auditor.	2	0.20
Manage the audit committee including setting the agenda and building the charter.	2	0.20

Executive Management (n=10)

Most Important Responsibility	Number of Interviewees that Indicate this Responsibility	Percentage of Interviewees that Indicate this Responsibility
Monitor financial reporting including integrity of and understanding how aggressive management is in regards to financial reporting.	5	0.50
Financial statements are accurate.	2	0.20

(table 7 continued)

Financial Management (n=7)

Most Important Responsibility	Number of Interviewees that Indicate this Responsibility	Percentage of Interviewees that Indicate this Responsibility
Monitor financial reporting including integrity of and understanding how aggressive management is in regards to financial reporting.	3	0.43
Financial statements are accurate.	2	0.29

Investment Management (n=6)

Most Important Responsibility	Number of Interviewees that Indicate this Responsibility	Percentage of Interviewees that Indicate this Responsibility
Monitor financial reporting including integrity of and understanding how aggressive management is in regards to financial reporting.	3	0.50
Financial statements are accurate.	3	0.50

TABLE 8
Audit Committee Member's Indication of how they Perceive that they Individually add Value to Management

PANEL A: ENTIRE SAMPLE

Add Value to Management	Number of Interviewees that Indicate this Value	Percentage of Interviewees that Indicate this Value
Audit partner experience including regulatory experience, managing the relationship with the auditor, and comfortable working with external auditors.	8	0.31
Provide accounting/financial reporting advice to management.	5	0.19
Technical background (e.g., IT background, industry association experience, IPO experience, compliance experience)	4	0.15
My CPA background including technical financial reporting/accounting background.	3	0.12
My industry experience	3	0.12
My experience on other boards.	3	0.12
Independent set of experienced eyes, challenge processes, fresh approach, and another perspective.	3	0.12
Monitor financial reporting including integrity of.	2	0.08
Monitor operational decisions.	2	0.08
My operational background	2	0.08
My accounting knowledge.	2	0.08
Monitor the staffing of the accounting function (e.g., competent CFO, controller, etc.).	2	0.08
Provide operational advice.	2	0.08
Mentor and evaluate the CFO.	2	0.08
My CFO background.	2	0.08
Monitor the control environment.	1	0.04
My experience on other audit committees.	1	0.04
Make sure management is getting the right information	1	0.04
Explain things to management.	1	0.04
Get more value out of the audit functions.	1	0.04
Share best practices.	1	0.04
Having a collaborative process with management, outsiders, and the audit committee.	1	0.04
Ensure effective communication with the investment community.	1	0.04

(table 8 continued)

Ability to focus on accounting issues	1	0.04
Educate management about financial reporting.	1	0.04
Having a complete picture of the company (know how the company works) and how that fits into the financial reports	1	0.04
His focus on risk avoidance.	1	0.04
Depth of knowledge from background.	1	0.04
Understand the pressures that management faces.	1	0.04

PANEL B: BY SOCIAL IDENTITY*Public Accounting (n=10)*

Add Value to Management	Number of Interviewees that Indicate this Value	Percentage of Interviewees that Indicate this Value
Audit partner experience including regulatory experience, managing the relationship with the auditor, and comfortable working with external auditors.	7	0.70
My CPA background including technical financial reporting/accounting background.	3	0.30
Monitor financial reporting including integrity of.	2	0.20
Technical background (e.g., IT background, industry association experience, IPO experience, compliance experience)	2	0.20

Executive Management (n=10)

Add Value to Management	Number of Interviewees that Indicate this Value	Percentage of Interviewees that Indicate this Value
My operational background	2	0.20
My industry experience	2	0.20
Provide accounting/financial reporting advice to management.	2	0.20
Provide operational advice.	2	0.20

Financial Management (n=7)

Add Value to Management	Number of Interviewees that Indicate this Value	Percentage of Interviewees that Indicate this Value
Provide accounting/financial reporting advice to management.	2	0.29
Provide operational advice.	2	0.29

(table 8 continued)

Mentor and evaluate the CFO.	2	0.29
My CFO background.	2	0.29

Investment Management (n=6)

Add Value to Management	Number of Interviewees that Indicate this Value	Percentage of Interviewees that Indicate this Value
Provide accounting/financial reporting advice to management.	4	0.67
My experience on other boards.	2	0.33

TABLE 9
Audit Committee Member's Indication of how they Perceive that they Individually add Value to Shareholders

PANEL A: ENTIRE SAMPLE

Add Value to Shareholders	Number of Interviewees that Indicate this Value	Percentage of Interviewees that Indicate this Value
Monitor financial reporting including integrity of.	7	0.27
Ensure transparency and effective communication with the investment community.	5	0.19
Monitor the control environment.	4	0.15
Avoiding problems including reducing downside risk and not having restatements.	4	0.15
Independent oversight.	4	0.15
My industry experience	3	0.12
Monitor the staffing of the accounting function (e.g., competent CFO, controller, etc.).	3	0.12
Ensure accurate financial reporting	3	0.12
Relationship with external auditor (e.g., have a relationship with the audit partner, ensure the right relationship in place).	3	0.12
Monitor operational decisions.	2	0.08
My CPA background	2	0.08
My operational background	2	0.08
My experience on other boards.	2	0.08
Monitor external audit and auditors.	2	0.08
Monitor risks.	2	0.08
Technical background/help (e.g., IT background, IPO experience).	2	0.08
Compliance	2	0.08
Make sure management is doing it right; company is operating in a fiscally responsible manner	2	0.08
My experience on other audit committees.	1	0.04
Accounting knowledge	1	0.04
Ensure timely financial reporting	1	0.04
Monitor internal audit.	1	0.04
Setting tone.	1	0.04
Monitor management.	1	0.04
Provide operational advice.	1	0.04
CFO background.	1	0.04
Being sensitive to shareholder returns.	1	0.04

(table 9 continued)

Someone looking out for your best interests	1	0.04
Having a relationship with the CFO	1	0.04
Understand accounting rules.	1	0.04
Having been a shareholder.	1	0.04

PANEL B: BY SOCIAL IDENTITY*Public Accounting (n=10)*

Add Value to Shareholders	Number of Interviewees that Indicate this Value	Percentage of Interviewees that Indicate this Value
Monitor financial reporting including integrity of.	4	0.40
Monitor the control environment.	4	0.40

Executive Management (n=10)

Add Value to Shareholders	Number of Interviewees that Indicate this Value	Percentage of Interviewees that Indicate this Value
Monitor financial reporting including integrity of.	2	0.20
My operational background	2	0.20
Ensure transparency and effective communication with the investment community.	2	0.20

Financial Management (n=7)

Add Value to Shareholders	Number of Interviewees that Indicate this Value	Percentage of Interviewees that Indicate this Value
Monitor financial reporting including integrity of.	2	0.29
Make sure management is doing it right; company is operating in a fiscally responsible manner.	2	0.29

Investment Management (n=6)

Add Value to Shareholders	Number of Interviewees that Indicate this Value	Percentage of Interviewees that Indicate this Value
Monitor financial reporting including integrity of.	2	0.33

TABLE 10
Identification with Company, Management, and the Audit Committee

Identification with the Company^a

	<i>Mean</i>	<i>n</i>	<i>Min</i>	<i>Max</i>	<i>SD</i>
Complete Sample	3.59	26	2.40	5.00	0.61
Public Accounting	3.48	10	2.40	4.40	0.65
Executive Management	3.68	10	3.00	5.00	0.69
Financial Management	3.83	7	3.00	4.60	0.50
Investment Management	3.67	6	2.80	4.60	0.59

Identification with Management^a

	<i>Mean</i>	<i>n</i>	<i>Min</i>	<i>Max</i>	<i>SD</i>
Complete Sample	2.91	26	1.80	4.60	0.70
Public Accounting	2.72	10	1.80	4.00	0.71
Executive Management	3.04	10	2.20	4.60	0.76
Financial Management	3.29	7	2.20	4.00	0.62
Investment Management	2.80	6	1.80	3.60	0.70

Identification with the Audit Committee^a

	<i>Mean</i>	<i>n</i>	<i>Min</i>	<i>Max</i>	<i>SD</i>
Complete Sample	4.07	26	2.40	5.00	0.58
Public Accounting	4.00	10	3.40	5.00	0.46
Executive Management	4.10	10	2.40	5.00	0.73
Financial Management	4.29	7	3.80	4.80	0.34
Investment Management	3.80	6	3.00	4.60	0.52

^a Scores are on a five-point scale. Higher scores indicate higher identification.

TABLE 11
Value Added to Management and Shareholders by Public vs. Private

PANEL A: VALUE ADDED TO MANAGEMENT

Public Companies (n=20)

Add Value to Management	Number of Interviewees that Indicate this Value	Percentage of Interviewees that Indicate this Value
Audit partner experience including regulatory experience, managing the relationship with the auditor, and comfortable working with external auditors.	5	0.25
Provide accounting/financial reporting advice to management.	4	0.20
My CPA background including technical financial reporting/accounting background.	3	0.15

Private Companies (n=6)

Add Value to Management	Number of Interviewees that Indicate this Value	Percentage of Interviewees that Indicate this Value
Audit partner experience including regulatory experience, managing the relationship with the auditor, and comfortable working with external auditors.	3	0.50
My industry experience	2	0.33
Technical background (e.g., IT background, industry association experience, IPO experience, compliance experience)	2	0.33

PANEL B: VALUE ADDED TO SHAREHOLDERS

Public Companies (n=20)

Add Value to Shareholders	Number of Interviewees that Indicate this Value	Percentage of Interviewees that Indicate this Value
Monitor financial reporting including integrity of.	5	0.25
Ensure transparency and effective communication with the investment community.	5	0.25
Monitor the staffing of the accounting function (e.g., competent CFO, controller, etc.).	3	0.15
Ensure accurate financial reporting	3	0.15
Avoiding problems including reducing downside risk and not having restatements.	3	0.15

(table 11 continued)

Private Companies (n=6)

Add Value to Shareholders	Number of Interviewees that Indicate this Value	Percentage of Interviewees that Indicate this Value
Monitor financial reporting including integrity of.	2	0.33
Monitor the control environment.	2	0.33
Relationship with external auditor (e.g., have a relationship with the audit partner, ensure the right relationship in place).	2	0.33

TABLE 12
Value Added to Management and Shareholders by Company Size

PANEL A: VALUE ADDED TO MANAGEMENT

Companies with \$1B or More in Revenue (n=11)

Add Value to Management	Number of Interviewees that Indicate this Value	Percentage of Interviewees that Indicate this Value
My CPA background including technical financial reporting/accounting background.	3	0.27
Audit partner experience including regulatory experience, managing the relationship with the auditor, and comfortable working with external auditors.	3	0.27

Companies with \$500M or Less in Revenue (n=11)

Add Value to Management	Number of Interviewees that Indicate this Value	Percentage of Interviewees that Indicate this Value
Audit partner experience including regulatory experience, managing the relationship with the auditor, and comfortable working with external auditors.	5	0.45
Provide accounting/financial reporting advice to management.	3	0.27
My experience on other boards.	2	0.18

PANEL B: VALUE ADDED TO SHAREHOLDERS

Companies with \$1B or More in Revenue (n=11)

Add Value to Shareholders	Number of Interviewees that Indicate this Value	Percentage of Interviewees that Indicate this Value
Monitor financial reporting including integrity of.	4	0.36
Ensure transparency and effective communication with the investment community.	4	0.36
Monitor the control environment.	2	0.18

(table 12 continued)

Companies with \$500M or Less in Revenue (n=11)

Add Value to Shareholders	Number of Interviewees that Indicate this Value	Percentage of Interviewees that Indicate this Value
Monitor financial reporting including integrity of.	3	0.27
Relationship with external auditor (e.g., have a relationship with the audit partner, ensure the right relationship in place).	3	0.27
Avoiding problems including reducing downside risk and not having restatements.	3	0.27

TABLE 13
Audit Committee Member's Indication of Difficult Issues

PANEL A: ENTIRE SAMPLE

Difficult Issues	Number of Interviewees that Identify this Issue	Percentage of Interviewees that Identify this Issue
Personnel Issue.	6	0.23
Audit related issue (e.g., disagreement between management and the auditor).	4	0.15
Regulatory/compliance issue (e.g., SEC investigation, PCAOB reviews)	4	0.15
Recognition issue.	3	0.12
Complex accounting issues	3	0.12
Operational issue.	3	0.12
Disclosure issue.	2	0.08
Developing a joint venture or acquisition	2	0.08
Restatement.	2	0.08
Taxes	1	0.04
Executive compensation.	1	0.04

PANEL B: BY SOCIAL IDENTITY

Public Accounting (n=10)

Difficult Issues	Number of Interviewees that Identify this Issue	Percentage of Interviewees that Identify this Issue
Audit related issue (e.g., disagreement between management and the auditor).	2	0.20
Regulatory/compliance issue (e.g., SEC investigation, PCAOB reviews)	2	0.20

Executive Management (n=10)

Difficult Issues	Number of Interviewees that Identify this Issue	Percentage of Interviewees that Identify this Issue
Recognition issue.	3	0.30
Personnel Issue.	3	0.30

(table 13 continued)

Financial Management (n=7)

Difficult Issues	Number of Interviewees that Identify this Issue	Percentage of Interviewees that Identify this Issue
Personnel Issue.	3	0.43
Regulatory/compliance issue (e.g., SEC investigation, PCAOB reviews)	2	0.29

Investment Management (n=6)

Difficult Issues	Number of Interviewees that Identify this Issue	Percentage of Interviewees that Identify this Issue
Personnel Issue.	3	0.50
Audit related issue (e.g., disagreement between management and the auditor).	2	0.33

TABLE 14
Restatements
Sample Composition

Panel A: Sample Selection (Companies)

Number of IPO Companies (2005-2009)	374
<i>Less:</i> Financial service companies (SIC 6000-6999)	49
<i>Less:</i> Companies without proxy statements available	2
<i>Less:</i> Companies not in Audit Analytics	3
<i>Less:</i> Companies not in Compustat	9
<i>Less:</i> Unit offerings	2
<i>Less:</i> Companies with data missing to calculate control variables	16
Total IPO Companies in Sample	<u>293</u>

Panel B: Sample Selection (Company-Years)

Initial Company-year observations	1,556
<i>Less:</i> Company-years with missing data to calculate control variables	167
Final Sample (restatement and non-restatement company-years)	<u>1,389</u>

Panel C: Restatements by IPO Year

Year Company Completed IPO	# of IPOs	# of IPO Companies with a Restatement Period within 5 years	% of IPO Companies with a Restatement Period within 5 years
2005	97	23	23.7%
2006	93	27	29.0%
2007	79	24	30.4%
2008	9	4	44.4%
2009	15	5	33.3%
TOTAL	<u>293</u>	<u>83</u>	<u>28.3%</u>

Panel D: Company-Year Restatements by IPO Year

Year Company Completed IPO	# of IPOs	Company-Years	Total # of Restatement Periods within 5 years	% of Restatement Periods within 5 years
2005	97	478	33	6.9%
2006	93	447	56	12.5%
2007	79	353	45	12.7%
2008	9	45	10	22.2%
2009	15	66	8	12.1%
TOTAL	293	1,389	152	10.9%

Panel E: Company-year Restatement by Year

Year	Company- Years in Sample	Total # of Restatements During the Year	% of Restatements During the Year
2005	83	7	8.4%
2006	184	23	12.5%
2007	246	27	11.4%
2008	231	21	9.1%
2009	230	21	9.1%
2010	209	25	12.0%
2011	129	17	13.2%
2012	59	8	13.6%
2013	18	3	16.7%
TOTAL	1,389	152	10.9%

Panel F: Sample Frequency by Industry (Defined by SIC Code)

<i>Industry Description</i>	Restatement		No Restatement		Total	
	<i>Number</i>	<i>Percentage</i>	<i>Number</i>	<i>Percentage</i>	<i>Number</i>	<i>Percentage</i>
Food (2000-2111)	1	0.66%	17	1.37%	18	1.30%
Textiles & Printing/Publishing (2200-2799)	3	1.97%	48	3.88%	51	3.67%
Chemicals (2800-2824, 2840-2899)	1	0.66%	31	2.51%	32	2.30%
Pharmaceuticals (2830-2836)	14	9.21%	185	14.96%	199	14.33%
Construction & Extractive (1011-1799, 2900-2999)	6	3.95%	75	6.06%	81	5.83%
Durable Manufactures (3000-3999, excluding 3570-3579, 3661-3679, 3711-3873)	13	8.55%	66	5.34%	79	5.69%
Communications (3661-3669, 4812-4899)	7	4.61%	83	6.71%	90	6.48%
Transportation (3711-3799, 4000-4789)	9	5.92%	58	4.69%	67	4.82%
Instruments (3812-3873)	13	8.55%	129	10.43%	142	10.22%
Utilities (4900-4999)	4	2.63%	10	0.81%	14	1.01%
Retail (5000-5999)	15	9.87%	91	7.36%	106	7.63%
Services (6000-8999, excluding 7370-7379)	36	23.68%	180	14.55%	216	15.55%
Computers (3570-3579, 3670-3679, 7370-7379)	30	19.74%	264	21.34%	294	21.17%
TOTAL	152	100.00%	1,237	100.00%	1,389	100.00%

TABLE 15
Material Weaknesses
Sample Composition

Panel A: Sample Selection (Companies)

Number of IPO Companies (2005-2009)	374
<i>Less:</i> Financial service companies (SIC 6000-6999)	49
<i>Less:</i> Companies without proxy statements available	2
<i>Less:</i> Companies not in Audit Analytics	3
<i>Less:</i> Companies not in Compustat	9
<i>Less:</i> Unit offerings	2
<i>Less:</i> Companies with data missing to calculate control variables	28
Total IPO Companies in Sample	<u>281</u>

Panel B: Sample Selection (Company-Years)

Initial Company-year observations	1,556
<i>Less:</i> Company-years with missing data	423
Final Sample (restatement and non-restatement company-years)	<u>1,133</u>

Panel C: Material Weaknesses by IPO Year

Year Company Completed IPO	# of IPOs	# of IPO Companies with a Material Weakness Period within 5 years	% of IPO Companies with a Material Weakness Period within 5 years
2005	94	17	18.1%
2006	88	17	19.3%
2007	75	20	26.7%
2008	9	3	33.3%
2009	15	4	26.7%
TOTAL	<u>281</u>	<u>61</u>	<u>21.7%</u>

Panel D: Company-Year Material Weaknesses by IPO Year

Year Company Completed IPO	# of IPOs	Company-Years	Total # of Material Weakness Periods within 5 years	% of Material Weakness Periods within 5 years
2005	94	383	25	6.5%
2006	88	364	23	6.3%
2007	75	291	41	14.1%
2008	9	40	3	7.5%
2009	15	55	7	12.7%
TOTAL	281	1,133	99	8.7%

Panel E: Company-year Material Weakness by Year

Year	Company- Years in Sample	Total # of Material Weaknesses During the Year	% of Material Weaknesses During the Year
2005	11	8	72.7%
2006	80	10	12.5%
2007	185	20	10.8%
2008	223	12	5.4%
2009	218	14	6.4%
2010	209	12	5.7%
2011	130	10	7.7%
2012	59	12	20.3%
2013	18	1	5.6%
TOTAL	1,133	99	8.7%

Panel F: Sample Frequency by Industry (Defined by SIC Code)

<i>Industry Description</i>	Material Weakness		No Material Weakness		Total	
	<i>Number</i>	<i>Percentage</i>	<i>Number</i>	<i>Percentage</i>	<i>Number</i>	<i>Percentage</i>
Food (2000-2111)	1	1.01%	14	1.35%	15	1.32%
Textiles & Printing/Publishing (2200-2799)	0	0.00%	43	4.16%	43	3.80%
Chemicals (2800-2824, 2840-2899)	4	4.04%	23	2.22%	27	2.38%
Pharmaceuticals (2830-2836)	5	5.05%	152	14.70%	157	13.86%
Construction & Extractive (1011-1799, 2900-2999)	2	2.02%	64	6.19%	66	5.83%
Durable Manufactures (3000-3999, excluding 3570-3579, 3661-3679, 3711-3873)	9	9.09%	55	5.32%	64	5.65%
Communications (3661-3669, 4812-4899)	7	7.07%	65	6.29%	72	6.35%
Transportation (3711-3799, 4000-4789)	2	2.02%	56	5.42%	58	5.12%
Instruments (3812-3873)	16	16.16%	95	9.19%	111	9.80%
Utilities (4900-4999)	2	2.02%	11	1.06%	13	1.15%
Retail (5000-5999)	5	5.05%	82	7.93%	87	7.68%
Services (6000-8999, excluding 7370-7379)	25	25.25%	156	15.09%	181	15.98%
Computers (3570-3579, 3670-3679, 7370-7379)	21	21.21%	218	21.08%	239	21.09%
TOTAL	99	100.00%	1,034	100.00%	1,133	100.00%

TABLE 16
Meet or Beat
Sample Composition

Panel A: Sample Selection (Companies)

Number of IPO Companies (2005-2009)	374
<i>Less:</i> Financial service companies (SIC 6000-6999)	49
<i>Less:</i> Companies without proxy statements available	2
<i>Less:</i> Companies not in Audit Analytics	3
<i>Less:</i> Companies not in Compustat	9
<i>Less:</i> Unit offerings	2
<i>Less:</i> Companies with data missing to calculate control variables	29
Total IPO Companies in Sample	<u>280</u>

Panel B: Sample Selection (Company-Years)

Initial Company-year observations	1,556
<i>Less:</i> Company-years with missing data	274
Final Sample (restatement and non-restatement company-years)	<u>1,282</u>

Panel C: Meet or Beat by IPO Year

Year Company Completed IPO	# of IPOs	# of IPO Companies that Meet or Beat within 5 years	% of IPO Companies that Meet or Beat within 5 years
2005	95	31	32.6%
2006	89	26	29.2%
2007	74	24	32.4%
2008	8	5	62.5%
2009	14	7	50.0%
TOTAL	<u>280</u>	<u>93</u>	<u>33.2%</u>

Panel D: Company-Year Meet or Beat by IPO Year

Year Company Completed IPO	# of IPOs	Company-Years	Total # of Meet or Beat Periods within 5 years	% of Meet or Beat Periods within 5 years
2005	95	435	35	8.0%
2006	89	411	37	9.0%
2007	74	319	31	9.7%
2008	8	44	6	13.6%
2009	14	73	8	11.0%
TOTAL	280	1,282	117	9.1%

Panel E: Company-year Meet or Beat by Year

Year	Company-Years in Sample	Total # of Meet or Beat Companies During the Year	% of Meet or Beat Companies During the Year
2005	74	5	6.8%
2006	169	12	7.1%
2007	228	20	8.8%
2008	216	21	9.7%
2009	209	22	10.5%
2010	186	18	9.7%
2011	119	10	8.4%
2012	55	6	10.9%
2013	17	2	11.8%
2014	9	1	11.1%
TOTAL	1,282	117	9.1%

Panel F: Sample Frequency by Industry (Defined by SIC Code)

<i>Industry Description</i>	Meet or Beat		No Meet or Beat		Total	
	<i>Number</i>	<i>Percentage</i>	<i>Number</i>	<i>Percentage</i>	<i>Number</i>	<i>Percentage</i>
Food (2000-2111)	1	0.85%	15	1.29%	16	1.25%
Textiles & Printing/Publishing (2200-2799)	7	5.98%	34	2.92%	41	3.20%
Chemicals (2800-2824, 2840-2899)	1	0.85%	31	2.66%	32	2.50%
Pharmaceuticals (2830-2836)	8	6.84%	177	15.19%	185	14.43%
Construction & Extractive (1011-1799, 2900-2999)	7	5.98%	71	6.09%	78	6.08%
Durable Manufactures (3000-3999, excluding 3570-3579, 3661-3679, 3711-3873)	5	4.27%	60	5.15%	65	5.07%
Communications (3661-3669, 4812-4899)	5	4.27%	64	5.49%	69	5.38%
Transportation (3711-3799, 4000-4789)	5	4.27%	62	5.32%	67	5.23%
Instruments (3812-3873)	6	5.13%	119	10.21%	125	9.75%
Utilities (4900-4999)	2	1.71%	13	1.12%	15	1.17%
Retail (5000-5999)	12	10.26%	91	7.81%	103	8.03%
Services (6000-8999, excluding 7370-7379)	20	17.09%	179	15.36%	199	15.52%
Computers (3570-3579, 3670-3679, 7370-7379)	38	32.48%	249	21.37%	287	22.39%
TOTAL	117	100.00%	1,165	100.00%	1,282	100.00%

TABLE 17
Variable Definitions

Variable Name	Description [Source of Data]
<i>Independent Variables of Interest</i>	
PROP_EXEC_MGT EXEC_MGT	Audit committee members who have been a CEO, President, or Other Executive within the past five years measured as proportion/indicator [Proxy Statements].
PROP_FIN_MGT FIN_MGT	Audit committee members who have been a CFO or VP of Finance within the past five years measured as proportion/indicator [Proxy Statements].
PROP_INVEST_MGT INVEST_MGT	Audit committee members who have been in Venture Capital, Private Equity, Investment Banking, or Other Investing within the past five years measured as proportion/indicator [Proxy Statements].
PROP_PUB_ACCT PUB_ACCT	Audit committee members who have been in public accounting within the past five years measured as proportion/indicator [Proxy Statements].
<i>Dependent Variables</i>	
RESTATEMENT	Indicator variable equal to 1 if company had a restatement during the company-year, 0 otherwise [Audit Analytics].
MW	Indicator variable equal to 1 if company had a Section 404 or Section 302 material weakness during the company-year, 0 otherwise [Audit Analytics].
MB01	Indicator variable equal to 1 if company meet or beat by .01 the last analysts' median consensus forecast before earnings report, 0 otherwise [I/B/E/S Summary History File].
<i>Control Variables - Restatement Model</i>	
Audit Committee Controls	
ACM_AGE_LN	Average age of the audit committee members (natural log) [Proxy Statement].
AC_SIZE_LN	Number of audit committee members (natural log) [Proxy Statement].
AC_IND	Indicator variable equal to 1 if the audit committee is fully independent, 0 otherwise [Proxy Statement].
AC_MEETINGS_LN	Number of audit committee meetings during the year (natural log) [Proxy Statement].
Board of Director Controls	
BOARD_SIZE_LN	Number of board members (natural log) [Proxy Statement].

CEO_CHAIR	Indicator variable equal to 1 if CEO is also Chairman of the Board of directors, 0 otherwise [Proxy Statement].
PROP_BOARD_EMP	Proportion of employees who serve on the board [Proxy Statement].
BOARD_MEETINGS_LN	Number of board meetings during the fiscal year (natural log) [Proxy Statement].
Auditor Controls	
BIG4	Indicator variable equal to 1 if company is audited by a Big 4 auditor, 0 otherwise [Audit Analytics].
AUDITOR_IND	Proportion of client audit fees divided by total fees received [Audit Analytics].
AUDITOR_CHANGE	Indicator variable equal to 1 if company changed its auditor during the fiscal year, 0 otherwise [Audit Analytics].
Company Characteristics	
MVE_LN	Market value of equity (natural log) [Compustat CSHO*PRCC_F].
LOSS	Indicator variable if the company has a net loss in either of the two previous fiscal years, 0 otherwise [Compustat NI].
CO_AGE_LN	Age of company calculated based on when the company was founded (natural log) [Kenney & Patton 2013].
LEVERAGE	Ratio of total liabilities to total assets [Compustat (DLC + DLTT)/AT].
GROWTH	Indicator variable equal to 1 if the year over year industry Adjusted sales growth falls into the top quintile, 0 otherwise [Compustat SALES].
RESTRUCTURE	Indicator variable equal to 1 if the company had a restructuring during the fiscal year, 0 otherwise [Compustat RCA, RCD, RCEPS, RCP].
ACQUISITION	Indicator variable equal to 1 if the company was involved in an acquisition during the fiscal year, 0 otherwise [SDC Platinum].

Control Variables - Material Weakness Model

Audit Committee Controls

AC_SIZE_LN	Number of audit committee members (natural log) [Proxy Statement].
AC_MEETINGS_LN	Number of audit committee meetings during the year (natural log) [Proxy Statement].

Board of Director Controls

BOARD_SIZE_LN	Number of board members (natural log) [Proxy Statement].
PROP_BOARD_EMP	Proportion of employees who serve on the board [Proxy Statement].

BOARD_MEETINGS_LN	Number of board meetings during the fiscal year (natural log) [Proxy Statement].
Auditor Controls	
BIG4	Indicator variable equal to 1 if company is audited by a Big 4 auditor, 0 otherwise [Audit Analytics].
MID_TIER	Indicator variable equal to 1 if company is audited by a Mid-Tier auditor (Grant Thornton or BDO Seidman), 0 otherwise [Audit Analytics].
AUDITOR_CHANGE	Indicator variable equal to 1 if company changed its auditor during the fiscal year, 0 otherwise [Audit Analytics].
Company Characteristics	
CO_AGE_LN	Age of company calculated based on when the company was founded (natural log) [Kenney & Patton 2013].
ACQUISITION	Indicator variable equal to 1 if the company was involved in an acquisition during the fiscal year, 0 otherwise [SDC Platinum].
RESTRUCTURE	Indicator variable equal to 1 if the company had a restructuring during the fiscal year, 0 otherwise [Compustat RCA, RCD, RCEPS, RCP].
LOSS	Indicator variable if the company has a net loss in either of the two previous fiscal years, 0 otherwise [Compustat NI].
MVE_LN	Market value of equity (natural log) [Compustat CSHO*PRCC_F].
GROWTH	Indicator variable equal to 1 if the year over year industry adjusted sales growth falls into the top quintile, 0 otherwise [Compustat SALES].
SEGMENTS	Sum of reported business and geographic segments [Compustat Segments File].
FOREIGN	Indicator variable equal to 1 if the company has non-zero foreign currency translation, and 0 otherwise [Compustat]
LITIGATION	Indicator variable equal to 1 if a company is in a litigious industry (SIC codes 2833 to 2836, 3570-3577, 3600-3674, 5200-5961, and 7370), and 0 otherwise.
<i>Control Variables - Meet or Beat Model</i>	
Audit Committee Controls	
AC_SIZE_LN	Number of audit committee members (natural log) [Proxy Statement].
AC_IND	Indicator variable equal to 1 if the audit committee is fully independent, 0 otherwise [Proxy Statement].
Analyst Controls	

ANALYST_DOWN	The number of downward revisions since the last forecast calculation [I/B/E/S].
NUM_EST	Number of analysts whose forecasts are included in the consensus forecast used to calculate <i>MB01</i> [I/B/E/S Summary History File].
SD	Standard deviation scaled by the mean of the consensus forecast used to calculate <i>MB01</i> [I/B/E/S Summary History File].
Company Characteristics	
CO_AGE_LN	Age of company calculated based on when the company was founded (natural log) [Kenney & Patton 2013].
MVE_LN	Market value of equity (natural log) [Compustat CSHO*PRCC_F].
BOOK_TO_MARKET	Book-to-market ratio at the end of the current year [Compustat].
NOA	Net operating assets at the end of the prior year scaled by prior year sales [Compustat].
SHARES	Number of common shares outstanding at the end of the current fiscal year [Compustat].
IMPLICIT_CLAIM	1 minus the ratio of gross PPE to total assets at the end of the current year [Compustat].
LITIGATION	Indicator variable equal to 1 if a company is in a litigious industry (SIC codes 2833 to 2836, 3570-3577, 3600-3674, 5200-5961, and 7370), and 0 otherwise.

TABLE 18
Restatements - Descriptive Statistics

Variable	<i>Mean</i>	<i>Min</i>	<i>25th Percentile</i>	<i>Median</i>	<i>75th Percentile</i>	<i>Max</i>	<i>SD</i>
<i>RESTATEMENT</i>	0.109	0.000	0.000	0.000	0.000	1.000	0.312
<i>PROP_PUB_ACCT</i>	0.025	0.000	0.000	0.000	0.000	0.333	0.086
<i>PROP_EXEC_MGT</i>	0.557	0.000	0.333	0.667	0.667	1.000	0.299
<i>PROP_FIN_MGT</i>	0.193	0.000	0.000	0.000	0.333	1.000	0.220
<i>PROP_INVEST_MGT</i>	0.291	0.000	0.000	0.333	0.333	1.000	0.281
<i>PUB_ACCT</i>	0.080	0.000	0.000	0.000	0.000	1.000	0.271
<i>EXEC_MGT</i>	0.904	0.000	1.000	1.000	1.000	1.000	0.294
<i>FIN_MGT</i>	0.494	0.000	0.000	0.000	1.000	1.000	0.500
<i>INVEST_MGT</i>	0.619	0.000	0.000	1.000	1.000	1.000	0.486
<i>ACM_AGE</i>	58.19	37.50	54.33	58.00	62.00	77.67	5.67
<i>AC_SIZE</i>	3.138	1.000	3.000	3.000	3.000	6.000	0.473
<i>AC_IND</i>	0.964	0.000	1.000	1.000	1.000	1.000	0.186
<i>AC_MEETINGS</i>	6.981	0.000	5.000	6.000	8.000	38.000	3.185
<i>BOARD_SIZE</i>	7.614	3.000	7.000	7.000	9.000	13.000	1.499
<i>CEO_CHAIR</i>	0.451	0.000	0.000	0.000	1.000	1.000	0.498
<i>PROP_BOARD_EMP</i>	0.188	0.000	0.125	0.143	0.250	0.750	0.093
<i>BOARD_MEETINGS</i>	8.448	0.000	6.000	8.000	10.000	33.000	3.960
<i>BIG4</i>	0.816	0.000	1.000	1.000	1.000	1.000	0.387
<i>AUDITOR_IND</i>	0.010	0.000	0.000	0.000	0.001	1.000	0.055
<i>AUDITOR_CHANGE</i>	0.040	0.000	0.000	0.000	0.000	1.000	0.197
<i>CO_AGE</i>	17.26	0.00	8.00	11.00	18.00	116.00	18.11
<i>ACQUISITION</i>	0.275	0.000	0.000	0.000	1.000	1.000	0.447
<i>RESTRUCTURE</i>	0.178	0.000	0.000	0.000	0.000	1.000	0.383
<i>LOSS</i>	0.555	0.000	0.000	1.000	1.000	1.000	0.497
<i>LEVERAGE</i>	0.237	0.000	0.000	0.047	0.300	19.385	0.807
<i>MVE</i>	778.71	0.11	140.48	353.66	742.27	20990.53	1450.89
<i>GROWTH</i>	0.289	0.000	0.000	0.000	1.000	1.000	0.453

NOTES:

- All variables are defined in Table 17.
- Descriptive statistics are based on actual values, not natural log values.

TABLE 19
Material Weaknesses - Descriptive Statistics

Variable	<i>Mean</i>	<i>Min</i>	<i>25th Percentile</i>	<i>Median</i>	<i>75th Percentile</i>	<i>Max</i>	<i>SD</i>
<i>MW</i>	0.087	0.000	0.000	0.000	0.000	1.000	0.283
<i>PROP_PUB_ACCT</i>	0.023	0.000	0.000	0.000	0.000	0.333	0.082
<i>PROP_EXEC_MGT</i>	0.564	0.000	0.333	0.667	0.750	1.000	0.300
<i>PROP_FIN_MGT</i>	0.196	0.000	0.000	0.000	0.333	1.000	0.225
<i>PROP_INVEST_MGT</i>	0.268	0.000	0.000	0.333	0.333	1.000	0.274
<i>PUB_ACCT</i>	0.071	0.000	0.000	0.000	0.000	1.000	0.258
<i>EXEC_MGT</i>	0.908	0.000	1.000	1.000	1.000	1.000	0.289
<i>FIN_MGT</i>	0.496	0.000	0.000	0.000	1.000	1.000	0.500
<i>INVEST_MGT</i>	0.586	0.000	0.000	1.000	1.000	1.000	0.493
<i>AC_SIZE</i>	3.152	1.000	3.000	3.000	3.000	6.000	0.492
<i>AC_MEETINGS</i>	7.244	0.000	5.000	7.000	9.000	38.000	3.028
<i>BOARD_SIZE</i>	7.657	3.000	7.000	8.000	9.000	13.000	1.521
<i>PROP_BOARD_EMP</i>	0.185	0.000	0.125	0.143	0.222	0.750	0.091
<i>BOARD_MEETINGS</i>	8.500	2.000	6.000	8.000	10.000	33.000	3.912
<i>BIG4</i>	0.820	0.000	1.000	1.000	1.000	1.000	0.384
<i>MID_TIER</i>	0.106	0.000	0.000	0.000	0.000	1.000	0.308
<i>AUDITOR_CHANGE</i>	0.042	0.000	0.000	0.000	0.000	1.000	0.202
<i>CO_AGE</i>	17.889	0.000	9.000	11.000	19.000	116.000	18.396
<i>ACQUISITION</i>	0.294	0.000	0.000	0.000	1.000	1.000	0.456
<i>RESTRUCTURE</i>	0.205	0.000	0.000	0.000	0.000	1.000	0.404
<i>LOSS</i>	0.539	0.000	0.000	1.000	1.000	1.000	0.499
<i>MVE</i>	823.83	0.111	135.44	352.37	770.85	20990.53	1560.26
<i>GROWTH</i>	0.267	0.000	0.000	0.000	1.000	1.000	0.442
<i>SEGMENTS</i>	3.858	0.000	2.000	3.000	5.000	24.000	3.032
<i>FOREIGN</i>	0.305	0.000	0.000	0.000	1.000	1.000	0.461
<i>LITIGATION</i>	0.304	0.000	0.000	0.000	1.000	1.000	0.460

NOTES:

- All variables are defined in Table 17.
- Descriptive statistics are based on actual values, not natural log values.

TABLE 20
Meet or Beat - Descriptive Statistics

Variable	<i>Mean</i>	<i>Min</i>	<i>25th Percentile</i>	<i>Median</i>	<i>75th Percentile</i>	<i>Max</i>	<i>SD</i>
<i>MB01</i>	0.091	0.000	0.000	0.000	0.000	1.000	0.288
<i>PROP_PUB_ACCT</i>	0.026	0.000	0.000	0.000	0.000	0.333	0.087
<i>PROP_EXEC_MGT</i>	0.557	0.000	0.333	0.667	0.667	1.000	0.300
<i>PROP_FIN_MGT</i>	0.190	0.000	0.000	0.000	0.333	1.000	0.219
<i>PROP_INVEST_MGT</i>	0.292	0.000	0.000	0.333	0.333	1.000	0.276
<i>PUB_ACCT</i>	0.082	0.000	0.000	0.000	0.000	1.000	0.274
<i>EXEC_MGT</i>	0.908	0.000	1.000	1.000	1.000	1.000	0.289
<i>FIN_MGT</i>	0.490	0.000	0.000	0.000	1.000	1.000	0.500
<i>INVEST_MGT</i>	0.628	0.000	0.000	1.000	1.000	1.000	0.484
<i>AC_SIZE</i>	3.147	2.000	3.000	3.000	3.000	6.000	0.448
<i>AC_IND</i>	0.968	0.000	1.000	1.000	1.000	1.000	0.176
<i>ANALYST_DOWN</i>	0.351	0.000	0.000	0.000	1.000	1.000	0.477
<i>NUM_EST</i>	6.509	1.000	3.000	5.000	8.000	45.000	4.885
<i>SD</i>	0.223	0.000	0.022	0.059	0.167	16.000	0.865
<i>CO_AGE</i>	17.260	0.000	8.000	11.000	18.000	116.000	17.645
<i>MVE_LN</i>	788.40	4.77	161.51	374.11	758.66	20991.53	1463.10
<i>BOOK_TO_MARKET</i>	0.430	-24.647	0.187	0.324	0.565	14.949	1.048
<i>NOA</i>	0.140	176.262	0.104	0.336	0.794	28.076	7.480
<i>SHARES</i>	42.928	2.959	20.730	28.899	47.883	476.800	44.586
<i>IMPLICIT_CLAIM</i>	0.629	-1.886	0.471	0.784	0.899	0.999	0.390
<i>LITIGATION</i>	0.441	0.000	0.000	0.000	1.000	1.000	0.497

NOTES:

- All variables are defined in Table 17.
- Descriptive statistics are based on actual values, not natural log values.

TABLE 21
Restatements - Descriptive Statistics
Comparison of Restatement vs. Non-Restatement Observations

Variable	No Restatement (n=1,237)							Restatement (n=152)							Stat.	p-value
	Mean	Min	25th Perc.	Median	75th Perc.	Max	SD	Mean	Min	25th Perc.	Median	75th Perc.	Max	SD		
<i>PROP_PUB_ACCT</i>	0.025	0.000	0.000	0.000	0.000	0.333	0.086	0.027	0.000	0.000	0.000	0.000	0.333	0.086	-0.253	0.801
<i>PROP_EXEC_MGT</i>	0.555	0.000	0.333	0.667	0.667	1.000	0.297	0.574	0.000	0.333	0.667	0.667	1.000	0.309	-0.740	0.460
<i>PROP_FIN_MGT</i>	0.189	0.000	0.000	0.000	0.333	1.000	0.219	0.220	0.000	0.000	0.250	0.333	1.000	0.231	-1.640	0.101
<i>PROP_INVEST_MGT</i>	0.298	0.000	0.000	0.333	0.500	1.000	0.284	0.229	0.000	0.000	0.250	0.333	1.000	0.245	2.908	0.004
<i>PUB_ACCT</i>	0.078	0.000	0.000	0.000	0.000	1.000	0.269	0.092	0.000	0.000	0.000	0.000	1.000	0.290	0.345	0.557
<i>EXEC_MGT</i>	0.905	0.000	1.000	1.000	1.000	1.000	0.294	0.901	0.000	1.000	1.000	1.000	1.000	0.299	0.017	0.896
<i>FIN_MGT</i>	0.487	0.000	0.000	0.000	1.000	1.000	0.500	0.553	0.000	0.000	1.000	1.000	1.000	0.499	2.357	0.125
<i>INVEST_MGT</i>	0.629	0.000	0.000	1.000	1.000	1.000	0.483	0.539	0.000	0.000	1.000	1.000	1.000	0.500	4.595	0.032
<i>ACM_AGE</i>	58.218	42.000	54.333	58.000	62.000	77.667	5.651	57.939	37.500	54.167	58.500	62.500	70.000	5.809	0.573	0.567
<i>AC_SIZE</i>	3.136	1.000	3.000	3.000	3.000	6.000	0.465	3.151	1.000	3.000	3.000	3.000	5.000	0.537	-0.381	0.703
<i>AC_IND</i>	0.965	0.000	1.000	1.000	1.000	1.000	0.183	0.954	0.000	1.000	1.000	1.000	1.000	0.210	0.497	0.481
<i>AC_MEETINGS</i>	6.895	0.000	5.000	6.000	8.000	23.000	2.957	7.678	0.000	5.000	7.000	9.000	38.000	4.593	-2.867	0.004
<i>BOARD_SIZE</i>	7.584	3.000	7.000	7.000	9.000	13.000	1.489	7.862	3.000	7.000	8.000	9.000	12.000	1.557	-2.163	0.031
<i>CEO_CHAIR</i>	0.454	0.000	0.000	0.000	1.000	1.000	0.498	0.428	0.000	0.000	0.000	1.000	1.000	0.496	0.366	0.545
<i>PROP_BOARD_EMP</i>	0.186	0.000	0.125	0.143	0.222	0.667	0.089	0.199	0.000	0.125	0.167	0.250	0.750	0.116	-1.565	0.118
<i>BOARD_MEETINGS</i>	8.407	1.000	6.000	8.000	10.000	33.000	3.958	8.776	0.000	6.000	8.000	10.000	27.000	3.977	-1.084	0.279
<i>BIG4</i>	0.827	0.000	1.000	1.000	1.000	1.000	0.378	0.730	0.000	0.000	1.000	1.000	1.000	0.445	8.452	0.004
<i>AUDITOR_IND</i>	0.010	0.000	0.000	0.000	0.001	1.000	0.054	0.015	0.000	0.000	0.000	0.002	0.543	0.063	-1.036	0.300
<i>AUDITOR_CHANGE</i>	0.038	0.000	0.000	0.000	0.000	1.000	0.191	0.059	0.000	0.000	0.000	0.000	1.000	0.237	1.575	0.210
<i>CO_AGE</i>	17.036	0.000	8.000	11.000	18.000	116.000	17.665	19.046	0.000	8.500	12.000	18.000	111.000	21.352	-1.292	0.197
<i>ACQUISITION</i>	0.260	0.000	0.000	0.000	1.000	1.000	0.439	0.395	0.000	0.000	0.000	1.000	1.000	0.490	12.269	0.000
<i>RESTRUCTURE</i>	0.167	0.000	0.000	0.000	0.000	1.000	0.373	0.263	0.000	0.000	0.000	1.000	1.000	0.442	8.501	0.004
<i>LOSS</i>	0.551	0.000	0.000	1.000	1.000	1.000	0.498	0.592	0.000	0.000	1.000	1.000	1.000	0.493	0.948	0.330
<i>LEVERAGE</i>	0.211	0.000	0.000	0.045	0.290	13.037	0.579	0.444	0.000	0.002	0.076	0.467	19.385	1.789	-3.363	0.001
<i>MVE</i>	765.23	2.32	139.70	353.66	721.92	20990.5	1451.87	888.37	0.11	151.49	351.19	884.41	10234.3	1443.01	-0.987	0.324
<i>GROWTH</i>	0.292	0.000	0.000	0.000	1.000	1.000	0.455	0.263	0.000	0.000	0.000	1.000	1.000	0.442	0.542	0.462

NOTES:

- All variables are defined in Table 17.
- Descriptive statistics are based on actual values, not natural log values.
- The continuous variable statistics are t-statistics from means tests. The indicator variable statistics are Chi-Squared statistics. All p-values are two-tailed.

TABLE 22
Material Weaknesses - Descriptive Statistics
Comparison of Material Weakness vs. Non-Material Weakness Observations

Variable	No Material Weakness (n=1,034)							Material Weakness (n=99)							Stat.	p-value
	Mean	Min	25th Perc.	Median	75th Perc.	Max	SD	Mean	Min	25th Perc.	Median	75th Perc.	Max	SD		
<i>PROP_PUB_ACCT</i>	0.023	0.000	0.000	0.000	0.000	0.333	0.084	0.015	0.000	0.000	0.000	0.000	0.333	0.067	0.958	0.339
<i>PROP_EXEC_MGT</i>	0.569	0.000	0.333	0.667	0.750	1.000	0.296	0.517	0.000	0.333	0.500	0.667	1.000	0.332	1.654	0.098
<i>PROP_FIN_MGT</i>	0.198	0.000	0.000	0.000	0.333	1.000	0.227	0.184	0.000	0.000	0.250	0.333	1.000	0.206	0.561	0.575
<i>PROP_INVEST_MGT</i>	0.268	0.000	0.000	0.333	0.333	1.000	0.276	0.271	0.000	0.000	0.333	0.333	1.000	0.243	-0.115	0.909
<i>PUB_ACCT</i>	0.074	0.000	0.000	0.000	0.000	1.000	0.261	0.051	0.000	0.000	0.000	0.000	1.000	0.220	0.720	0.396
<i>EXEC_MGT</i>	0.915	0.000	1.000	1.000	1.000	1.000	0.279	0.838	0.000	1.000	1.000	1.000	1.000	0.370	6.344	0.012
<i>FIN_MGT</i>	0.495	0.000	0.000	0.000	1.000	1.000	0.500	0.505	0.000	0.000	1.000	1.000	1.000	0.503	0.035	0.851
<i>INVEST_MGT</i>	0.580	0.000	0.000	1.000	1.000	1.000	0.494	0.646	0.000	0.000	1.000	1.000	1.000	0.481	1.632	0.201
<i>AC_SIZE</i>	3.161	1.000	3.000	3.000	3.000	6.000	0.475	3.061	1.000	3.000	3.000	3.000	6.000	0.636	1.934	0.053
<i>AC_MEETINGS</i>	7.205	1.000	5.000	7.000	9.000	38.000	2.894	7.646	0.000	5.000	7.000	9.000	23.000	4.176	-1.386	0.166
<i>BOARD_SIZE</i>	7.688	4.000	7.000	8.000	9.000	13.000	1.498	7.333	3.000	6.000	7.000	9.000	11.000	1.714	2.219	0.027
<i>PROP_BOARD_EMP</i>	0.182	0.000	0.125	0.143	0.222	0.600	0.086	0.217	0.000	0.125	0.167	0.250	0.750	0.131	-3.635	0.000
<i>BOARD_MEETINGS</i>	8.427	2.000	6.000	8.000	10.000	33.000	3.889	9.263	4.000	6.000	8.000	11.000	23.000	4.087	-2.032	0.042
<i>BIG4</i>	0.838	0.000	1.000	1.000	1.000	1.000	0.369	0.636	0.000	0.000	1.000	1.000	1.000	0.483	24.764	0.000
<i>MID_TIER</i>	0.098	0.000	0.000	0.000	0.000	1.000	0.297	0.192	0.000	0.000	0.000	0.000	1.000	0.396	8.474	0.004
<i>AUDITOR_CHANGE</i>	0.036	0.000	0.000	0.000	0.000	1.000	0.186	0.111	0.000	0.000	0.000	0.000	1.000	0.316	12.636	0.000
<i>CO_AGE</i>	18.378	0.000	9.000	12.000	19.000	116.000	19.011	12.778	2.000	8.000	11.000	15.000	61.000	8.377	2.903	0.004
<i>ACQUISITION</i>	0.289	0.000	0.000	0.000	1.000	1.000	0.454	0.343	0.000	0.000	0.000	1.000	1.000	0.477	1.282	0.258
<i>RESTRUCTURE</i>	0.198	0.000	0.000	0.000	0.000	1.000	0.399	0.273	0.000	0.000	0.000	1.000	1.000	0.448	3.077	0.079
<i>LOSS</i>	0.530	0.000	0.000	1.000	1.000	1.000	0.499	0.636	0.000	0.000	1.000	1.000	1.000	0.483	4.116	0.042
<i>MVE</i>	846.95	2.32	138.18	368.20	775.56	20990.5	1608.06	582.42	0.11	95.25	242.06	607.19	5522.18	893.41	1.613	0.107
<i>GROWTH</i>	0.266	0.000	0.000	0.000	1.000	1.000	0.442	0.273	0.000	0.000	0.000	1.000	1.000	0.448	0.021	0.884
<i>SEGMENTS</i>	3.848	0.000	2.000	3.000	5.000	24.000	2.949	3.960	1.000	1.000	3.000	5.000	19.000	3.809	-0.349	0.727
<i>FOREIGN</i>	0.308	0.000	0.000	0.000	1.000	1.000	0.462	0.283	0.000	0.000	0.000	1.000	1.000	0.453	0.260	0.610
<i>LITIGATION</i>	0.315	0.000	0.000	0.000	1.000	1.000	0.465	0.182	0.000	0.000	0.000	0.000	1.000	0.388	7.611	0.006

NOTES:

- All variables are defined in Table 17.
- Descriptive statistics are based on actual values, not natural log values.
- The continuous variable statistics are t-statistics from means tests. The indicator variable statistics are Chi-Squared statistics. All p-values are two-tailed.

TABLE 23
Meet or Beat - Descriptive Statistics
Comparison of Meet or Beat vs. Non-Meet or Beat Observations

Variable	No Meet or Beat (n=1,165)							Meet or Beat (n=117)							Stat.	p-value
	Mean	Min	25th Perc.	Median	75th Perc.	Max	SD	Mean	Min	25th Perc.	Median	75th Perc.	Max	SD		
<i>PROP_PUB_ACCT</i>	0.026	0.000	0.000	0.000	0.000	0.333	0.088	0.021	0.000	0.000	0.000	0.000	0.333	0.080	0.586	0.558
<i>PROP_EXEC_MGT</i>	0.560	0.000	0.333	0.667	0.750	1.000	0.299	0.530	0.000	0.333	0.500	0.667	1.000	0.303	1.029	0.304
<i>PROP_FIN_MGT</i>	0.189	0.000	0.000	0.000	0.333	1.000	0.218	0.206	0.000	0.000	0.250	0.333	1.000	0.234	-0.797	0.426
<i>PROP_INVEST_MGT</i>	0.295	0.000	0.000	0.333	0.333	1.000	0.278	0.263	0.000	0.000	0.333	0.333	1.000	0.257	1.206	0.228
<i>PUB_ACCT</i>	0.083	0.000	0.000	0.000	0.000	1.000	0.276	0.068	0.000	0.000	0.000	0.000	1.000	0.253	0.313	0.576
<i>EXEC_MGT</i>	0.910	0.000	1.000	1.000	1.000	1.000	0.286	0.889	0.000	1.000	1.000	1.000	1.000	0.316	0.560	0.454
<i>FIN_MGT</i>	0.488	0.000	0.000	0.000	1.000	1.000	0.500	0.504	0.000	0.000	1.000	1.000	1.000	0.502	0.107	0.744
<i>INVEST_MGT</i>	0.632	0.000	0.000	1.000	1.000	1.000	0.483	0.590	0.000	0.000	1.000	1.000	1.000	0.494	0.803	0.370
<i>AC_SIZE</i>	3.149	2.000	3.000	3.000	3.000	6.000	0.446	3.128	2.000	3.000	3.000	3.000	6.000	0.465	0.487	0.627
<i>AC_IND</i>	0.971	0.000	1.000	1.000	1.000	1.000	0.168	0.940	0.000	1.000	1.000	1.000	1.000	0.238	3.225	0.073
<i>ANALYST_DOWN</i>	0.361	0.000	0.000	0.000	1.000	1.000	0.480	0.256	0.000	0.000	0.000	1.000	1.000	0.439	5.058	0.025
<i>NUM_EST</i>	6.491	1.000	3.000	5.000	8.000	45.000	4.933	6.684	1.000	3.000	6.000	9.000	25.000	4.396	-0.407	0.684
<i>SD</i>	0.234	0.000	0.023	0.063	0.176	16.000	0.904	0.111	0.000	0.017	0.034	0.109	1.333	0.220	1.471	0.142
<i>CO_AGE</i>	16.877	0.000	8.000	11.000	18.000	116.000	17.342	21.068	1.000	9.000	13.000	25.000	115.000	20.102	-2.454	0.014
<i>MVE_LN</i>	791.67	4.773	155.75	369.03	737.28	20991.53	1493.24	755.89	19.88	254.04	446.39	860.27	10115.33	1124.18	0.252	0.801
<i>BOOK_TO_MARKET</i>	0.427	-24.647	0.188	0.325	0.565	14.949	1.088	0.457	-0.469	0.178	0.319	0.547	2.866	0.505	-0.298	0.766
<i>NOA</i>	0.110	-176.26	0.104	0.335	0.795	28.076	7.808	0.441	-14.658	0.103	0.343	0.737	10.570	2.446	-0.456	0.679
<i>SHARES</i>	42.718	2.959	20.614	28.461	47.263	476.800	45.575	45.021	7.274	21.958	36.128	56.906	221.566	33.243	-0.533	0.595
<i>IMPLICIT_CLAIM</i>	0.625	-1.89	0.472	0.782	0.898	0.999	0.396	0.659	-0.221	0.470	0.796	0.906	0.991	0.328	-0.895	0.371
<i>LITIGATION</i>	0.435	0.000	0.000	0.000	1.000	1.000	0.496	0.496	0.000	0.000	0.000	1.000	1.000	0.502	1.581	0.209

NOTES:

- All variables are defined in Table 17.
- Descriptive statistics are based on actual values, not natural log values.
- The continuous variable statistics are t-statistics from means tests. The indicator variable statistics are Chi-Squared statistics. All p-values are two-tailed.

TABLE 24
Earnings Surprise

<u>Earnings Surprise ^a</u>	<u>n</u>	<u>% of my Sample</u>	<u>% of Cheng & Warfield 2005 Sample</u>
-0.05 or Less	388	30.27%	8.18%
-0.04	30	2.34%	1.65%
-0.03	29	2.26%	2.19%
-0.02	30	2.34%	4.05%
-0.01	51	3.98%	8.81%
0.00	57	4.45%	24.58%
0.01	60	4.68%	17.34%
0.02	64	4.99%	10.42%
0.03	47	3.67%	6.30%
0.04	50	3.90%	4.09%
0.05 or Greater	<u>476</u>	37.13%	12.39%
TOTAL	<u><u>1,282</u></u>		

^a Earnings surprise is the per share difference between actual earnings and the last median consensus forecast before earnings are reported.

TABLE 25
Restatements - Correlations

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23
1 <i>RES_ACCT</i>	1																						
2 <i>PROP_PUB_ACCT</i>	0.01	1																					
3 <i>PROP_EXEC_MGT</i>	0.02	-0.14	1																				
4 <i>PROP_FIN_MGT</i>	0.04	-0.11	0.14	1																			
5 <i>PROP_INVEST_MGT</i>	-0.08	-0.08	-0.24	-0.16	1																		
6 <i>ACM_AGE_LN</i>	-0.02	0.04	-0.03	-0.19	-0.34	1																	
7 <i>AC_SIZE_LN</i>	0.00	0.03	0.02	-0.05	0.03	0.01	1																
8 <i>AC_IND</i>	-0.02	0.03	0.01	0.02	-0.07	0.10	-0.02	1															
9 <i>AC_MEETINGS_LN</i>	0.05	0.03	0.04	0.06	-0.02	0.00	0.11	0.21	1														
10 <i>BOARD_SIZE_LN</i>	0.06	0.04	-0.07	0.00	0.03	0.02	0.29	0.08	0.11	1													
11 <i>CEO_CHAIR</i>	-0.02	0.01	0.02	0.09	0.00	0.04	0.03	-0.03	0.03	-0.04	1												
12 <i>PROP_BOARD_EMP</i>	0.04	0.00	0.04	0.00	-0.05	0.00	-0.21	-0.03	-0.04	-0.34	0.16	1											
13 <i>BOARD_MEETINGS_LN</i>	0.03	0.01	0.04	0.07	0.01	-0.07	0.05	0.07	0.27	0.02	-0.05	0.01	1										
14 <i>BIG4</i>	-0.08	-0.07	-0.05	0.15	0.08	-0.05	0.01	0.07	0.13	0.20	-0.07	-0.14	0.04	1									
15 <i>AUDITOR_IND</i>	0.03	0.07	0.00	0.01	0.07	-0.03	-0.02	-0.01	-0.14	-0.15	0.08	0.12	-0.08	-0.37	1								
16 <i>AUDITOR_CHANGE</i>	0.03	0.02	0.02	-0.03	-0.01	-0.02	-0.03	-0.06	0.00	-0.03	-0.02	0.10	0.00	-0.12	0.07	1							
17 <i>CO_AGE_LN</i>	0.02	0.00	0.05	-0.06	-0.21	0.29	0.08	0.04	0.00	0.01	0.06	-0.07	-0.11	0.05	-0.11	-0.03	1						
18 <i>ACQUISITION</i>	0.09	0.03	-0.01	0.00	-0.06	0.05	0.04	0.07	0.07	0.05	0.13	-0.03	-0.02	0.02	-0.04	0.05	0.03	1					
19 <i>RESTRUCTURE</i>	0.08	0.01	-0.01	0.05	-0.09	0.09	-0.02	0.04	0.09	0.04	-0.01	-0.08	0.03	0.07	-0.07	0.04	0.11	0.04	1				
20 <i>LOSS</i>	0.03	0.01	0.00	0.09	0.07	-0.17	-0.14	0.03	0.02	-0.02	-0.13	0.03	0.14	-0.07	-0.02	0.02	-0.22	-0.16	0.07	1			
21 <i>LEVERAGE</i>	0.07	-0.02	0.00	-0.08	-0.04	0.15	-0.04	-0.08	-0.06	0.01	0.05	0.01	0.01	-0.04	0.03	0.05	0.12	0.00	0.11	0.00	1		
22 <i>MVE_LN</i>	0.03	-0.06	0.00	0.08	-0.01	0.00	0.24	0.01	0.17	0.23	0.04	-0.13	-0.04	0.26	-0.16	-0.10	0.07	0.20	-0.08	-0.38	-0.08	1	
23 <i>GROWTH</i>	-0.02	-0.01	-0.01	0.06	0.06	-0.12	0.00	-0.02	-0.04	-0.12	-0.02	0.07	-0.05	0.01	0.05	0.06	-0.13	0.05	-0.10	-0.05	-0.08	0.17	1

bold = p<.05 (two tailed)

TABLE 26
Material Weaknesses - Correlations

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	
1 <i>MW</i>	1																						
2 <i>PROP_PUB_ACCT</i>	-0.03	1																					
3 <i>PROP_EXEC_MGT</i>	-0.05	-0.15	1																				
4 <i>PROP_FIN_MGT</i>	-0.02	-0.11	0.16	1																			
5 <i>PROP_INVEST_MGT</i>	0.00	-0.10	-0.24	-0.15	1																		
6 <i>AC_SIZE_LN</i>	-0.09	0.01	0.01	-0.05	0.03	1																	
7 <i>AC_MEETINGS_LN</i>	-0.01	0.00	0.01	0.06	0.06	0.09	1																
8 <i>BOARD_SIZE_LN</i>	-0.08	0.05	-0.07	0.00	0.03	0.30	0.09	1															
9 <i>PROP_BOARD_EMP</i>	0.11	0.00	0.07	0.01	-0.08	-0.24	-0.04	-0.37	1														
10 <i>BOARD_MEETINGS_LN</i>	0.06	-0.01	0.05	0.06	0.01	0.07	0.21	0.01	0.01	1													
11 <i>BIG4</i>	-0.15	-0.06	-0.06	0.14	0.09	0.02	0.17	0.21	-0.13	0.02	1												
12 <i>MID_TIER</i>	0.09	-0.02	0.02	-0.12	-0.06	0.04	0.00	-0.06	0.04	0.03	-0.73	1											
13 <i>AUDITOR_CHANGE</i>	0.11	0.01	0.00	-0.02	0.00	-0.05	-0.02	-0.04	0.12	-0.01	-0.11	0.04	1										
14 <i>CO_AGE_LN</i>	-0.08	0.03	0.04	-0.08	-0.18	0.10	-0.05	0.03	-0.06	-0.12	0.05	0.00	-0.04	1									
15 <i>ACQUISITION</i>	0.03	0.03	-0.01	0.00	-0.03	0.03	0.06	0.05	-0.01	-0.03	0.03	-0.02	0.03	0.02	1								
16 <i>RESTRUCTURE</i>	0.05	0.03	-0.03	0.04	-0.06	-0.02	0.05	0.03	-0.07	0.04	0.07	-0.05	0.03	0.09	0.02	1							
17 <i>LOSS</i>	0.06	0.00	0.01	0.10	0.04	-0.16	0.03	-0.02	0.04	0.12	-0.10	0.08	0.05	-0.20	-0.18	0.10	1						
18 <i>MVE_LN</i>	-0.08	-0.06	-0.01	0.08	0.00	0.26	0.21	0.25	-0.16	-0.04	0.27	-0.10	-0.11	0.08	0.20	-0.10	-0.41	1					
19 <i>GROWTH</i>	0.00	0.02	-0.03	0.07	0.04	0.01	0.01	-0.09	0.07	-0.05	-0.01	0.01	0.07	-0.12	0.06	-0.10	-0.08	0.16	1				
20 <i>SEGMENTS</i>	0.01	0.08	-0.07	0.05	-0.09	0.02	0.15	0.02	0.08	-0.02	0.02	0.01	-0.01	0.04	0.12	0.19	-0.09	0.21	0.00	1			
21 <i>FOREIGN</i>	-0.02	0.05	0.07	0.03	-0.03	-0.05	0.17	-0.02	0.13	0.00	0.04	-0.05	-0.01	-0.07	0.04	0.08	-0.01	0.15	0.03	0.39	1		
22 <i>LITIGATION</i>	-0.08	0.00	-0.03	0.05	-0.01	0.01	0.01	-0.03	0.06	0.01	0.06	-0.03	-0.03	-0.05	-0.14	-0.02	0.19	-0.15	-0.04	-0.05	-0.2	1	

bold = p<.05 (two tailed)

TABLE 27
Meet or Beat - Correlations

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17
1 <i>MB01</i>	1																
2 <i>PROP_PUB_ACCT</i>	-0.02	1															
3 <i>PROP_EXEC_MGT</i>	-0.03	-0.15	1														
4 <i>PROP_FIN_MGT</i>	0.02	-0.12	0.13	1													
5 <i>PROP_INVEST_MGT</i>	-0.03	-0.08	-0.18	-0.14	1												
6 <i>AC_SIZE_LN</i>	-0.02	0.02	0.10	-0.08	-0.01	1											
7 <i>AC_IND</i>	-0.05	0.03	0.03	0.01	-0.08	-0.03	1										
8 <i>ANALYST_DOWN</i>	-0.06	-0.04	0.05	0.05	-0.02	0.05	0.09	1									
9 <i>NUM_EST</i>	0.01	-0.06	0.00	0.05	0.00	0.09	0.10	0.22	1								
10 <i>SD</i>	-0.04	0.03	0.03	0.02	-0.04	0.02	0.01	0.06	-0.06	1							
11 <i>CO_AGE</i>	0.09	0.00	0.05	-0.08	-0.20	0.07	0.03	-0.04	0.03	-0.04	1						
12 <i>MVE_LN</i>	0.04	-0.06	0.02	0.06	-0.01	0.17	0.01	0.10	0.52	-0.03	0.06	1					
13 <i>BOOK_TO_MARKET</i>	0.01	0.04	-0.01	0.05	-0.06	-0.07	0.01	0.09	-0.07	0.01	0.01	-0.35	1				
14 <i>NOA</i>	0.00	0.01	-0.02	-0.03	-0.01	0.05	-0.05	0.03	0.04	-0.06	0.02	0.11	0.284	1			
15 <i>SHARES</i>	0.01	-0.02	-0.06	0.13	-0.10	0.18	0.04	0.10	0.24	0.03	0.06	0.47	-0.029	0.14	1		
16 <i>IMPLICIT_CLAIM</i>	0.02	0.05	-0.06	0.12	0.02	-0.06	-0.04	-0.16	0.00	-0.05	-0.15	-0.04	-0.13	-0.30	-0.16	1	
17 <i>LITIGATION</i>	0.04	-0.01	0.00	0.03	0.00	-0.02	0.04	-0.08	0.05	-0.02	-0.07	-0.13	-0.10	-0.29	-0.08	0.28	1

bold = p<.05 (two tailed)

TABLE 28
Restatements
Logistic Regression - Likelihood of Restatement

Variables	Pred. Sign	(1) <i>Proportion of Audit Committee</i>			(2) <i>Presence on Audit Committee</i>		
		Coeff.	z-stat.	p	Coeff.	z-stat.	p
<i>PROP_PUB_ACCT</i>	-	(H1) -0.179	-0.16	0.435	--	--	--
<i>PROP_EXEC_MGT</i>	+/-	(H2) -0.201	-0.62	0.535	--	--	--
<i>PROP_FIN_MGT</i>	+/-	(H3) 1.038	2.26	0.024 **	--	--	--
<i>PROP_INVEST_MGT</i>	+/-	(H4) -1.137	-2.71	0.007 **	--	--	--
<i>PUB_ACCT</i>	-	(H1) --	--	--	0.083	0.25	0.402
<i>EXEC_MGT</i>	+/-	(H2) --	--	--	-0.180	-0.56	0.578
<i>FIN_MGT</i>	+/-	(H3) --	--	--	0.558	2.67	0.008 **
<i>INVEST_MGT</i>	+/-	(H4) --	--	--	-0.436	-2.15	0.031 **
<i>ACM_AGE_LN</i>	+/-	-2.412	-2.15	0.032 **	-2.127	-1.94	0.052 *
<i>AC_SIZE_LN</i>	-	-0.516	-0.80	0.212	-0.446	-0.68	0.250
<i>AC_IND</i>	-	-0.418	-0.85	0.198	-0.413	-0.84	0.200
<i>AC_MEETINGS_LN</i>	+/-	0.480	1.82	0.069 *	0.450	1.70	0.089 *
<i>BOARD_SIZE_LN</i>	+	1.532	2.89	0.002 **	1.526	2.88	0.002 **
<i>CEO_CHAIR</i>	+	-0.441	-2.15	0.032 **	-0.449	-2.20	0.028 **
<i>PROP_BOARD_EMP</i>	+	2.819	2.64	0.004 **	2.901	2.73	0.003 **
<i>BOARD_MEETINGS_LN</i>	+/-	0.323	1.25	0.210	0.318	1.24	0.216
<i>BIG4</i>	-	-0.904	-3.58	0.000 ***	-0.940	-3.74	0.000 ***
<i>AUDITOR_IND</i>	+	1.869	1.23	0.110	1.366	0.88	0.188
<i>AUDITOR_CHANGE</i>	+	0.086	0.21	0.418	0.117	0.28	0.389
<i>CO_AGE_LN</i>	-	0.020	0.13	0.899	0.056	0.36	0.721
<i>ACQUISITION</i>	+	0.582	2.85	0.002 **	0.576	2.83	0.003 **
<i>RESTRUCTURE</i>	+	0.840	3.53	0.000 ***	0.853	3.60	0.000 ***
<i>LOSS</i>	+	0.350	1.59	0.056 *	0.332	1.51	0.066 *
<i>LEVERAGE</i>	+	0.815	2.46	0.007 **	0.808	2.44	0.008 **
<i>MVE_LN</i>	-	0.204	2.17	0.030 **	0.191	2.03	0.042 **
<i>GROWTH</i>	+	-0.265	-1.20	0.229	-0.249	-1.13	0.257
Observations			1,389			1,389	
Fiscal year dummies			YES			YES	
Industry dummies			YES			YES	
Pseudo R-squared			11.86%			11.62%	

Notes:

- All p-values are two-tailed, except for variables with directional predictions. P-values denoted as follows: *** p < 0.01, **p < 0.05, *p < 0.10
- Industry dummies are coded based on industries defined in Panel F of Table 14.
- Standard errors are clustered by firm.
- All variables are defined in Table 17.

TABLE 29
Material Weaknesses
Logistic Regression - Likelihood of Material Weakness

Variables	Pred. Sign	(1) <i>Proportion of Audit Committee</i>			(2) <i>Presence on Audit Committee</i>		
		Coeff.	z-stat.	p	Coeff.	z-stat.	p
<i>PROP_PUB_ACCT</i>	-	(H1) -2.819	-1.30	0.097 *	--	--	--
<i>PROP_EXEC_MGT</i>	+/-	(H2) -1.289	-2.20	0.028 **	--	--	--
<i>PROP_FIN_MGT</i>	+/-	(H3) 0.204	0.31	0.759	--	--	--
<i>PROP_INVEST_MGT</i>	+/-	(H4) -0.130	-0.26	0.794	--	--	--
<i>PUB_ACCT</i>	-	(H1) --	--	--	-0.737	-1.06	0.145
<i>EXEC_MGT</i>	+/-	(H2) --	--	--	-1.143	-2.69	0.007 **
<i>FIN_MGT</i>	+/-	(H3) --	--	--	0.334	1.11	0.267
<i>INVEST_MGT</i>	+/-	(H4) --	--	--	0.273	0.84	0.399
<i>AC_SIZE_LN</i>	-	-1.033	-1.13	0.130	-0.944	-1.00	0.159
<i>AC_MEETINGS_LN</i>	+/-	0.556	1.36	0.174	0.560	1.38	0.168
<i>BOARD_SIZE_LN</i>	-	-0.107	-0.12	0.453	-0.185	-0.20	0.420
<i>PROP_BOARD_EMP</i>	+	2.598	1.82	0.035 **	2.182	1.50	0.067 *
<i>BOARD_MEETINGS_LN</i>	+/-	0.671	2.05	0.041 **	0.640	1.90	0.057 *
<i>BIG4</i>	+	-1.304	-2.71	0.007 **	-1.263	-2.61	0.009 **
<i>MID_TIER</i>	+	-0.295	-0.51	0.613	-0.210	-0.36	0.717
<i>AUDITOR_CHANGE</i>	+	0.889	2.27	0.012 **	0.914	2.35	0.010 **
<i>CO_AGE_LN</i>	-	-0.243	-1.32	0.093 *	-0.206	-1.12	0.132
<i>ACQUISITION</i>	+	0.151	0.56	0.288	0.170	0.63	0.264
<i>RESTRUCTURE</i>	+	0.695	2.20	0.014 **	0.666	2.13	0.017 **
<i>LOSS</i>	+	0.102	0.32	0.374	0.084	0.26	0.396
<i>MVE_LN</i>	-	-0.089	-0.76	0.225	-0.112	-0.93	0.175
<i>GROWTH</i>	+	-0.167	-0.53	0.599	-0.209	-0.66	0.508
<i>SEGMENTS</i>	+	-0.004	-0.06	0.952	0.003	0.04	0.967
<i>FOREIGN</i>	+	-0.228	-0.55	0.581	-0.276	-0.67	0.502
<i>LITIGATION</i>	+	-0.817	-1.90	0.058 *	-0.869	-2.00	0.046 **
Observations			1,133			1,133	
Fiscal year dummies			YES			YES	
Pseudo R-squared			18.18%			18.60%	

Notes:

- All p-values are two-tailed, except for variables with directional predictions. P-values denoted as follows: *** p < 0.01, **p < 0.05, *p < 0.10
- Standard errors are clustered by firm.
- All variables are defined in Table 17.

TABLE 30
Meet or Beat
Logistic Regression - Likelihood of Meeting or Beating

Variables	Pred. Sign	(1) <i>Proportion of Audit Committee</i>			(2) <i>Presence on Audit Committee</i>		
		Coeff.	z-stat.	p	Coeff.	z-stat.	p
<i>PROP_PUB_ACCT</i>	-	(H1) -0.643	-0.54	0.294	--	--	--
<i>PROP_EXEC_MGT</i>	+/-	(H2) -0.630	-1.76	0.078 *	--	--	--
<i>PROP_FIN_MGT</i>	+/-	(H3) 0.456	1.04	0.297	--	--	--
<i>PROP_INVEST_MGT</i>	+/-	(H4) -0.447	-1.23	0.219	--	--	--
<i>PUB_ACCT</i>	-	(H1) --	--	--	-0.091	-0.25	0.403
<i>EXEC_MGT</i>	+/-	(H2) --	--	--	-0.291	-0.93	0.350
<i>FIN_MGT</i>	+/-	(H3) --	--	--	0.144	0.68	0.495
<i>INVEST_MGT</i>	+/-	(H4) --	--	--	-0.114	-0.56	0.576
<i>AC_SIZE_LN</i>	-	-0.839	-1.06	0.144	-0.959	-1.25	0.107
<i>AC_IND</i>	-	-1.229	-2.45	0.007 **	-1.242	-2.50	0.006 **
<i>ANALYST_DOWN</i>	+	-0.455	-1.87	0.061 *	-0.459	-1.88	0.060 *
<i>NUM_EST</i>	+	-0.034	-1.52	0.130	-0.034	-1.46	0.145
<i>SD</i>	-	-0.725	-1.37	0.085 *	-0.743	-1.38	0.085 *
<i>CO_AGE</i>	+	0.399	2.76	0.003 **	0.408	2.85	0.002 **
<i>MVE_LN</i>	+/-	0.174	1.48	0.139	0.163	1.35	0.178
<i>BOOK_TO_MARKET</i>	-	0.168	0.65	0.518	0.154	0.57	0.567
<i>NOA</i>	-	-0.072	-0.92	0.178	-0.065	-0.85	0.198
<i>SHARES</i>	+	0.000	0.15	0.442	0.001	0.34	0.367
<i>IMPLICIT_CLAIM</i>	+	0.353	0.95	0.172	0.350	0.90	0.185
<i>LITIGATION</i>	+	0.560	1.20	0.115	0.586	1.31	0.095 *
Observations			1,282			1,282	
Fiscal year dummies			YES			YES	
Pseudo R-squared			7.52%			7.13%	

Notes:

- All p-values are two-tailed, except for variables with directional predictions. P-values denoted as follows: *** p < 0.01, **p < 0.05, *p < 0.10
- Standard errors are clustered by firm.
- All variables are defined in Table 17.

APPENDIX A: PRE-INTERVIEW QUESTIONS

Participants were asked to answer the following pre-interview questions prior to the interview.

[This is in Qualtrics.]

INSTRUCTIONS

When answering these questions please only consider your work as an audit committee member of one company (i.e., if you serve as an audit committee member for more than one company, select one company and answer these questions for that one company). This is the same company we will ask you to think about when we ask you questions during the interview. The company you choose can be a public, private, or not-for profit company.

Overall Company Identification [This heading is not in Qualtrics]

1. When someone praises this company, it feels like a personal compliment.

1-----2-----3-----4-----5
 Strongly Disagree Strongly Agree

2. When I talk about this company, I usually say “We” rather than “They.”

1-----2-----3-----4-----5
 Strongly Disagree Strongly Agree

3. I am very interested in what others think about this company.

1-----2-----3-----4-----5
 Strongly Disagree Strongly Agree

4. This company’s successes are my successes.

1-----2-----3-----4-----5
 Strongly Disagree Strongly Agree

5. When someone criticizes this company, it feels like a personal insult.

1-----2-----3-----4-----5
 Strongly Disagree Strongly Agree

Audit Committee Identification [This heading is not in Qualtrics]

1. When someone criticizes this audit committee, it feels like a personal insult.

1-----2-----3-----4-----5
 Strongly Disagree Strongly Agree

2. When I talk about this audit committee, I usually say “We” rather than “They.”

1-----2-----3-----4-----5

- | | | | |
|--|---------------------------|--|-------------------|
| | Strongly
Disagree | | Strongly
Agree |
| 3. I am very interested in what others think about this audit committee. | 1-----2-----3-----4-----5 | | |
| | Strongly
Disagree | | Strongly
Agree |
| 4. This audit committee's successes are my successes. | 1-----2-----3-----4-----5 | | |
| | Strongly
Disagree | | Strongly
Agree |
| 5. When someone praises this audit committee, it feels like a personal compliment. | 1-----2-----3-----4-----5 | | |
| | Strongly
Disagree | | Strongly
Agree |

Top Management Identification [This heading is not in Qualtrics]

- | | | | |
|--|---------------------------|--|-------------------|
| | Strongly
Disagree | | Strongly
Agree |
| 1. When someone praises a member of top management, it feels like a personal compliment. | 1-----2-----3-----4-----5 | | |
| | Strongly
Disagree | | Strongly
Agree |
| 2. When I talk about members of top management, I usually say "We" rather than "They." | 1-----2-----3-----4-----5 | | |
| | Strongly
Disagree | | Strongly
Agree |
| 3. I am very interested in what others think about top management of this company audit committee. | 1-----2-----3-----4-----5 | | |
| | Strongly
Disagree | | Strongly
Agree |
| 4. The top management members' successes are my successes. | 1-----2-----3-----4-----5 | | |
| | Strongly
Disagree | | Strongly
Agree |
| 5. When someone criticizes a member of top management, it feels like a personal insult. | 1-----2-----3-----4-----5 | | |
| | Strongly
Disagree | | Strongly
Agree |

Background Questions

1. How many years have you served as a board member of this company?
2. How many years have you served as an audit committee member of this company?
3. How many times during the year does the audit committee usually meet.....

	How many times during the year?	What is the duration of these meetings (in hours)?
in person?		
via conference call?		
some other technology-enabled medium (e.g., Skype)?		

4. Why were you selected to serve on this audit committee?

	Not related to my selection	Slightly related to my selection	Related to my selection	Strongly related to my selection
My prior accounting related professional experience (e.g. CPA, audit partner).	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
My prior non-accounting related professional experience (e.g., CEO).	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
My relationship with another board member.	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
My relationship with top management.	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
My industry expertise.	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
My experiences serving on other boards.	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Board committee rotation policy.	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Other: Please describe	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

Other: Please describe	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
------------------------	-----------------------	-----------------------	-----------------------	-----------------------

The following series of questions concerns data about the company, board of directors, and the audit committee. For public companies, the researchers will collect this data from publicly available information. For private companies, the researchers will collect this data via the current survey. Please indicate whether this company is public or private.

If they indicate PRIVATE these questions will be asked:

1. How many individuals serve on the board of directors?
2. How many board members are independent?
3. How many individuals serve on the audit committee?
4. What are the backgrounds of the other individuals serving on the audit committee (e.g., CFO at another company, retired audit partner, etc.)?
5. Are you the chair of this audit committee? If so, for how many years have you been the chair?
6. Are you the designated financial expert on this audit committee? If so, for how many years have you been the designated financial expert on this audit committee?
7. In addition to the audit committee, do you also serve on other board committees for this particular company?

b) If Yes: Please list each committee besides the audit committee that you serve for this particular company and whether you are the chair of each committee listed:

Name of the Committee	Are you the chair of this committee?	
	Yes	No
	<input type="radio"/>	<input type="radio"/>
	<input type="radio"/>	<input type="radio"/>
	<input type="radio"/>	<input type="radio"/>
	<input type="radio"/>	<input type="radio"/>
	<input type="radio"/>	<input type="radio"/>

8. Indicate the number of audit committee members who have turned over in the past 3 years.
9. What is the approximate size of this company in terms of Total Revenue at year end?
 - Less than \$100 million
 - \$100 million → \$500 million
 - \$500 million → \$1 billion
 - \$1 billion → 5 billion
 - Greater than \$5 billion
10. Indicate the primary industry in which the company operates.

When we conduct the interview, we prefer to audio record the session so that we have a complete and accurate record of your responses. Do you give us permission to audio record your remarks when we conduct the interview?

Thank you for answering these questions. To help us prepare for your interview please send a copy of your resume to Kara Obermire (kobermire@bus.wisc.edu). Once we receive your resume, we will send you a copy of our interview questions so that you will have a sense of the direction that are questions will take when we meet.

APPENDIX B: INTERVIEW QUESTIONS

Role of the audit committee/audit committee effectiveness

1. Explain how you view your primary role on this audit committee.
2. What are your top three or so most important responsibilities on this audit committee? If you had to rank these in order of importance, what would be the order and why?
3. As an audit committee member, how do you perceive that you individually add the most value to the:
 - a) management of this company?
 - b) Shareholders (or stakeholders) of this company?
4. What experiences outside of your audit committee service do you consider to be important for you to be effective on this audit committee?
5. What was the most difficult issue that this audit committee resolved in the recent past?
 - a) What made your judgments and decisions effective in this instance (e.g., features of your background that influenced how you handled related challenges)?
 - b) What made your judgments and decisions less effective in this instance?

Experiences outside of the audit committee

6. How specifically has your role as a _____ [this will be updated based on your specific background] influenced your work on the audit committee?
7. Does the company and the board of directors consider director status (e.g., how well connected the board member is, how many other boards the member serves, whether the director is associated with admired firms, social club memberships, elite education, etc.) of potential new audit committee members when nominating new members?
8. Can an audit committee member's relative status compared to managements' status (e.g., audit committee member has a higher or lower status than management) influence the effectiveness of the audit committee? By status, we mean a person's relative professional, social, educational standing, or power.
9. How can an audit committee member's status make an audit committee member more effective?

Understanding of management and other board members

10. Do you empathize with the challenges faced by management? If so, please give specific examples.
11. Do you perceive that you identify well with the other audit committee members of this company (i.e., understand them or their situation on the board)? In what ways do you identify with them? In what ways do you not identify with them?
12. Do you perceive that you identify well with the other board members of this company (i.e., understand them or their situation on the board)? In what ways do you identify with them? In what ways do you not identify with them?
13. Provide examples about how that identification has impacted your behavior in your audit committee role.
14. What other factors may enhance or diminish your ability to be an effective audit committee member?

APPENDIX C: CODING SCHEME

View of Primary Role	Coding
Monitor financial reporting including preparation, integrity, and timeliness.	(1=mentioned; 0=not mentioned)
Monitor the external audit including managing the relationship with the auditor.	(1=mentioned; 0=not mentioned)
Manage the audit committee including leading the AC, engaging members, fulfilling the executive charter, planning meetings, and setting tone.	(1=mentioned; 0=not mentioned)
Monitor internal audit.	(1=mentioned; 0=not mentioned)
Monitor risks.	(1=mentioned; 0=not mentioned)
Monitor the staffing of the accounting function (e.g., competent CFO, controller).	(1=mentioned; 0=not mentioned)
Legal/Compliance/Regulations	(1=mentioned; 0=not mentioned)
Monitor the control environment.	(1=mentioned; 0=not mentioned)
Provide industry related expertise.	(1=mentioned; 0=not mentioned)

Most Important Responsibility

Monitor financial reporting including integrity of and understanding how aggressive management is in regards to financial reporting.	(1=mentioned; 0=not mentioned)
Financial statements are accurate.	(1=mentioned; 0=not mentioned)
Manage the audit committee including setting the agenda and building the charter.	(1=mentioned; 0=not mentioned)
Manage the relationship with the auditor	(1=mentioned; 0=not mentioned)
Monitor the external audit and auditors.	(1=mentioned; 0=not mentioned)
Monitor the control environment.	(1=mentioned; 0=not mentioned)
Monitor internal audit.	(1=mentioned; 0=not mentioned)

Individually Add Value to Management

Audit partner experience including regulatory experience, managing the relationship with the auditor, and comfortable working with external auditors.	(1=mentioned; 0=not mentioned)
Provide accounting/financial reporting advice to management.	(1=mentioned; 0=not mentioned)
Technical background (e.g., IT background, industry association experience, IPO experience, compliance experience)	(1=mentioned; 0=not mentioned)

My CPA background including technical financial reporting/accounting background.	(1=mentioned; 0=not mentioned)
My industry experience	(1=mentioned; 0=not mentioned)
My experience on other boards.	(1=mentioned; 0=not mentioned)
Independent set of experienced eyes, challenge processes, fresh approach, and another perspective.	(1=mentioned; 0=not mentioned)
Monitor financial reporting including integrity of.	(1=mentioned; 0=not mentioned)
Monitor operational decisions.	(1=mentioned; 0=not mentioned)
My operational background	(1=mentioned; 0=not mentioned)
My accounting knowledge.	(1=mentioned; 0=not mentioned)
Monitor the staffing of the accounting function (e.g., competent CFO, controller, etc.).	(1=mentioned; 0=not mentioned)
Provide operational advice.	(1=mentioned; 0=not mentioned)
Mentor and evaluate the CFO.	(1=mentioned; 0=not mentioned)
My CFO background.	(1=mentioned; 0=not mentioned)
Monitor the control environment.	(1=mentioned; 0=not mentioned)
My experience on other audit committees.	(1=mentioned; 0=not mentioned)
Make sure management is getting the right information	(1=mentioned; 0=not mentioned)
Explain things to management.	(1=mentioned; 0=not mentioned)
Get more value out of the audit functions.	(1=mentioned; 0=not mentioned)
Share best practices.	(1=mentioned; 0=not mentioned)
Having a collaborative process with management, outsiders, and the audit committee.	(1=mentioned; 0=not mentioned)
Ensure effective communication with the investment community.	(1=mentioned; 0=not mentioned)
Ability to focus on accounting issues	(1=mentioned; 0=not mentioned)
Educate management about financial reporting.	(1=mentioned; 0=not mentioned)
Having a complete picture of the company (know how the company works) and how that fits into the financial reports	(1=mentioned; 0=not mentioned)
His focus on risk avoidance.	(1=mentioned; 0=not mentioned)
Depth of knowledge from background.	(1=mentioned; 0=not mentioned)
Understand the pressures that management faces.	(1=mentioned; 0=not mentioned)

Individually Add Value to Shareholders

Monitor financial reporting including integrity of.	(1=mentioned; 0=not mentioned)
Ensure transparency and effective communication with the investment community.	(1=mentioned; 0=not mentioned)
Monitor the control environment.	(1=mentioned; 0=not mentioned)

Avoiding problems including reducing downside risk and not having restatements.	(1=mentioned; 0=not mentioned)
Independent oversight.	(1=mentioned; 0=not mentioned)
My industry experience	(1=mentioned; 0=not mentioned)
Monitor the staffing of the accounting function (e.g., competent CFO, controller, etc.).	(1=mentioned; 0=not mentioned)
Ensure accurate financial reporting	(1=mentioned; 0=not mentioned)
Relationship with external auditor (e.g., have a relationship with the audit partner, ensure the right relationship in place).	(1=mentioned; 0=not mentioned)
Monitor operational decisions.	(1=mentioned; 0=not mentioned)
My CPA background	(1=mentioned; 0=not mentioned)
My operational background	(1=mentioned; 0=not mentioned)
My experience on other boards.	(1=mentioned; 0=not mentioned)
Monitor external audit and auditors.	(1=mentioned; 0=not mentioned)
Monitor risks.	(1=mentioned; 0=not mentioned)
Technical background/help (e.g., IT background, IPO experience).	(1=mentioned; 0=not mentioned)
Compliance	(1=mentioned; 0=not mentioned)
Make sure management is doing it right; company is operating in a fiscally responsible manner	(1=mentioned; 0=not mentioned)
My experience on other audit committees.	(1=mentioned; 0=not mentioned)
Accounting knowledge	(1=mentioned; 0=not mentioned)
Ensure timely financial reporting	(1=mentioned; 0=not mentioned)
Monitor internal audit.	(1=mentioned; 0=not mentioned)
Setting tone.	(1=mentioned; 0=not mentioned)
Monitor management.	(1=mentioned; 0=not mentioned)
Provide operational advice.	(1=mentioned; 0=not mentioned)
CFO background.	(1=mentioned; 0=not mentioned)
Being sensitive to shareholder returns.	(1=mentioned; 0=not mentioned)
Someone looking out for your best interests	(1=mentioned; 0=not mentioned)
Having a relationship with the CFO	(1=mentioned; 0=not mentioned)
Understand accounting rules.	(1=mentioned; 0=not mentioned)
Having been a shareholder.	(1=mentioned; 0=not mentioned)

Difficult Issue

Personnel Issue.	(1=mentioned; 0=not mentioned)
Audit related issue (e.g., disagreement between management and the auditor).	(1=mentioned; 0=not mentioned)

Regulatory/compliance issue (e.g., SEC investigation, PCAOB reviews)	(1=mentioned; 0=not mentioned)
Recognition issue.	(1=mentioned; 0=not mentioned)
Complex accounting issues	(1=mentioned; 0=not mentioned)
Operational issue.	(1=mentioned; 0=not mentioned)
Disclosure issue.	(1=mentioned; 0=not mentioned)
Developing a joint venture or acquisition	(1=mentioned; 0=not mentioned)
Restatement.	(1=mentioned; 0=not mentioned)
Taxes.	(1=mentioned; 0=not mentioned)
Executive compensation.	(1=mentioned; 0=not mentioned)

APPENDIX D: SOCIAL IDENTITY CODING EXAMPLE

For each company-year in my sample I collected the biographies of each audit committee member from the Proxy Statements filed with the SEC (form Def14a). I coded the social identities of each audit committee member. I used those classifications to calculate whether each social identity was present or not (indicator variable) on the audit committee during the company-year, and the proportion of the audit committee (continuous variable) that had each social identity during the company-year. Below is an example of how I coded social identities for one company-year.

Example: Ruth's Chris Steak House Inc. (Company-year 2009)

The biographies below are for the three audit committee members serving Ruth's Chris Steak House in 2009. I coded social identities based on their professional experiences within the past 5 years (2004-2009).

*Mr. Hudson, age 64, was elected to our Board of Directors in June 2005. Mr. Hudson served as Chairman of the Board of Beverages & More, Inc., an affiliate of Madison Dearborn, from November 1998 to February 2007. From October 1997 to February 2007, Mr. Hudson served as **President and Chief Executive Officer** of Beverages & More, Inc. Mr. Hudson has leadership experience in food companies and is very knowledgeable of human resource management.*

*Ms. Cooper, age 59, has served as a member of our Board of Directors since December 2003. Ms. Cooper served as **Senior Vice President** of Quaker, Tropicana and Gatorade Sales for PepsiCo, Inc. from November 2003 to August 2009. From February 2001 to October 2003, Ms. Cooper served as President of Kellogg Company's Natural and Frozen Foods Division. From February 2000 to February 2001, Ms. Cooper was Senior Vice President and General Manager of Foodservice for Kellogg Company. From June 1988 to November 2000, Ms. Cooper was employed in various positions with Coca-Cola USA, including as Vice President, Customer Marketing. Ms. Cooper has extensive experience in sales, marketing and franchising in the food industry and has insight into vendor relationships.*

*Mr. Merritt, age 58, has served as a member of our Board of Directors since October 2009. Mr. Merritt currently serves as Chairman of the Board of Directors for Cosi, Inc., a NASDAQ listed restaurant company. From March 2007 to September 2008, Mr. Merritt served as Cosi, Inc.'s Interim **Chief Executive Officer and President**, while continuing to serve as a director. In 2005, Mr. Merritt retired from Outback Steakhouse, Inc., where he served as **Senior Vice President of Finance, Chief Financial Officer**, Treasurer and Secretary since February 1991, and served as Vice President and Chief Financial Officer from January 1990 to February 1991. Mr. Merritt also served as a director for Outback Steakhouse, Inc. and each of its subsidiaries and affiliates from 1992 to 2005. From 1988 to 1989, he served as Executive Vice President of Administration and Chief Financial Officer of JB's Restaurants, Inc., a restaurant operator. From 1985 to 1988, he was Vice President of Finance for JB's Restaurants. From 1981 to 1985, Mr. Merritt was employed by Vie de France Corporation, a restaurant and specialty baking company, as Vice President of Finance and Accounting and Chief Financial Officer. Mr. Merritt has knowledge and experience in accounting as well as restaurant finances, and extensive leadership experience with public restaurant companies.*

Based on the biographies above I coded Mr. Hudson as having an executive management social identity, Ms. Cooper as having an executive management social identity, and Mr. Merritt as having an executive management and financial management social identity. I have included below how I calculated the proportion and indicator variables for this company-year observation:

Ruth's Chris Steak House (Company-year 2009)

	Public Accounting	Executive Management	Finance Executive Management	Investment Management
Mr. Hudson	0	1	0	0
Ms. Cooper	0	1	0	0
Mr. Merritt	0	1	1	0
TOTAL	0	3	1	0

<i>PROP_PUB_ACCT</i>	<i>PROP_EXEC_MGT</i>	<i>PROP_FIN_MGT</i>	<i>PROP_INVEST_MGT</i>
0.00	1.00	0.33	0.00

<i>PUB_ACCT</i>	<i>EXEC_MGT</i>	<i>FIN_MGT</i>	<i>INVEST_MGT</i>
0	1	1	0