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Board Members With Style: The Effect of Audit Committee Members and Their Personal Styles on Financial Reporting Choices

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Abstract

This article studies whether audit committee members and chairpersons exhibit individual-specific "styles" that affect corporate financial reporting practices. I track 2,941 audit committee members and 683 chairpersons across firms over time, and test whether member (chair)-specific factors explain firms' accounting choices. I find that member and chairperson "style" (captured by fixed effects) is significant in explaining a firm's probability of accounting misstatements and earnings management, and the effects are not explained away by observable member (chairperson) characteristics found by prior literature, or by the effects of CEOs or CFOs.

Keywords

audit committee, individual board member style, financial reporting, upper echelon theory, earnings management

Introduction

The question of what influences a firm's financial reporting practice has been examined extensively in the accounting literature (Dechow, Ge, & Schrand, 2010). Prior studies approach this question by identifying factors at the market level (Leuz, Nanda, & Wysocki, 2003), the firm level (Klein, 2002; Lang, Raedy, & Wilson, 2006), and more recently the individual manager level (Ge, Matsumoto, & Zhang, 2011). However, the papers that study the influence of individuals on corporate financial reporting decisions focus on corporate executives, mostly CEOs and CFOs.[1] This article investigates the impact on corporate financial reporting choices of a different group of individuals: audit committee members. Specifically, this article examines whether financial reporting decisions are affected by differences in individual characteristics among audit committee members that are generated

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from various factors such as personality, ethical beliefs, and personal experiences that are not directly observable.

Audit committees of public firms play the role of ''overseeing the accounting and financial reporting processes of the issuer and audits of the financial statements of the issuer.''[2] Such a role involves ''reviewing and discussing with management, internal and outside auditors the annual audited financial statements . . . and quarterly financial statements'' (Braiotta, 2004). Hence, the financial statements of a firm are the end product of a reporting process which involves *both management and the audit committee*. The audit committee sometimes makes substantial adjustments to the financial statements during this process, by resolving the dispute between outside auditors and management, gathering information from internal auditors, and/or overseeing management's compliance with financial reporting standards and regulation (Caskey, Nagar, & Petacchi, 2010). Prior literature has identified various audit committee characteristics that are associated with financial reporting quality, such as independence (Klein, 2002), expertise (Bédard, Chtourou, & Courteau, 2004), and busyness (Tanyi & Smith, 2014). A common feature of these studies is that they rely on observable characteristics of the audit committee: For example, the expertise of audit committee members is usually captured by their professional qualifications (e.g., Certified Public Accountant [CPA] or Certified Financial Analyst), and independence is measured by whether the member is a current or former employee, is a family member of an executive officer, or receives compensation from the firm other than for being a board member (Klein, 2002). These observable characteristics, while meaningful, may not capture the full picture of how audit committee members can influence their firms' financial reporting. In particular, psychology studies find that an individual's job performance and career outcomes are affected by numerous factors, such as personality traits (e.g., Hurtz & Donovan, 2000), self-perception (Judge, Erez, & Bono, 1998), ethical beliefs (H. Koh & Boo, 2001), and childhood experience (Blustein, Walbridge, Friedlander, & Palladino, 1991), to name but a few. These factors are often not directly observable but are likely to affect the effectiveness of monitoring by audit committee members, and thus in turn influence firms' financial reporting practices. The goal of this study was to examine the overall effect of audit committee members on financial reporting that arise from these unobservable characteristics. Following prior literature, I label these characteristics as ''styles'' of audit committee members (Bertrand & Schoar, 2003).

I choose to study two categories of financial reporting choices that I believe audit committees are most concerned with: The first category is material accounting misstatements. The measure I use to capture the probability of accounting misstatements is the *F*-score from Dechow, Ge, Larson, Sloan, and Investors (2011) (*F_SCORE*). The second category is earnings management, which I measure by absolute discretionary accruals (*ABS_DISACC*), the frequency of meeting or beating analyst forecasts by a small amount (*SMB*) and an earnings smoothness measure (*SMOOTH*): the variance of the residuals for each member firm from regressing the change in earnings on leverage, growth, debt issuance, equity issuance, asset turnover ratio, and size (Ge et al., 2011).

To explore whether audit committee member styles are manifested in financial reporting, I investigate the effect of both members and chairpersons. According to survey and anecdotal evidence, audit committee chairpersons differ from regular members in several ways: First, chairpersons are often the financial experts of their committees.[3] Second, the chair is usually in charge of more formal duties such as setting the agenda of the committee meetings, communicating with the internal and external auditors, and evaluating the performance of regular members (Lipman, 2008). Third, survey evidence suggests that

chairpersons are often more likely to have personal ties with management prior to joining the committee (Beasley, Carcello, Hermanson, & Neal, 2009). Having more expertise and a higher level of responsibility is likely to make it easier for chairs to imprint their own styles on the firm's financial reporting, while being personally connected with the managers could make chairpersons more prone to management's influence and thus less likely to exhibit their own styles (Bruynseels & Cardinaels, 2014). I therefore do not make a directional prediction on whether the personal styles of chairs are more or less conspicuous than members.

I construct panel datasets that track 2,941 audit committee members and 683 chairpersons across different firms over time.[4] Each member (chair) in my sample has served on (chaired) the audit committees of more than one firm, and has held the position of member (chair) for at least 3 years at each firm. I follow the design of Bertrand and Schoar (2003): I first estimate a set of baseline regression models with the financial reporting choice measures as dependent variables and firm indicators, year indicators and a set of time-varying control variables as independent variables. I then add member or chair fixed effects to the baseline models. I examine whether the member or chair fixed effects are jointly significant in explaining the financial reporting choice variables, and compare the R^2 of the baseline model with that of the model with member or chair fixed effects. This design allows me to identify the effects of members or chairs above and beyond persistent firm-specific factors.

Note that this design cannot be applied to the earnings smoothness measures because they are measured using time-series data. I therefore implement a design similar to that in Ge et al. (2011): For each member or chairperson, I test whether the earnings smoothness measures during his or her tenure at the previous firm(s) are positively correlated with that at the subsequent firm(s) he or she worked at. I adjust for firm-specific effects by subtracting earning smoothness measured over the entire time series of the firm from that measured over the member or chairperson's tenure.

The results for both the member and the chairperson samples are consistent with my hypothesis that individual-specific member (chair) styles are associated with firms' financial reporting practices. For the first three dependent variables: *F_SCORE, ABS_DISACC*, and *SMB*, the member (chair) indicator variables are jointly significant, and adding the member (chair) fixed effects increases the adjusted R^2s by 2.3 to 4.9 percentage points. Such magnitudes are comparable with the CEO fixed effects found by Bertrand and Schoar (2003; 2-5 percentage points) and the CFO fixed effects in Ge et al. (2011; 2-3 percentage points). However, I find no evidence that members or chairpersons imprint their styles on earnings smoothness.

To check whether the member (chairperson) fixed effects are captured by unobservable individual characteristics such as disposition, personal attitude, and ethical beliefs or by observable characteristics identified by prior studies, I add observable individual characteristics (age, gender, education, and professional background) to both the baseline model and the fixed effects model. The member (chair) fixed effects are still jointly significant after including the observable characteristics, and the increase to R^2 ranges from 1.9 to 3.8 percentage points. Thus, it appears that the fixed effects are capturing unobservable or observable but not yet identified member (chair) characteristics.[5]

I then conduct a set of sensitivity tests on the member and chairperson fixed effects. First, the results are robust to adding CEO or CFO fixed effects. Second, the frequencies of significant coefficients in the regression models are consistently greater than both the expected frequencies under the null hypotheses and the simulated number of significant fixed effects where the members (chairs) and firms are randomly paired. Thus, my results

are not driven by mechanical biases of the *F*-test. Third, I conduct a set of placebo tests similar to those in Bertrand and Schoar (2003) to further ensure that the member fixed effects are not picking up some unobservable firm characteristics. The results suggest that even when members choose to serve on firms that are similar in their financial reporting, they also imprint their own styles on the firms.[6] Finally, I restrict the sample to be the members (chairs) starting their jobs in or after 2000, thus excluding members (chairs) who have been on the board for a particularly long period of time. The results are overall robust to this requirement, except for *SMB*.

This article makes several contributions: First, it demonstrates the *overall* effect of audit committee members on financial reporting and compliments prior research which mostly focuses on specific features of audit committees. Moreover, a significant portion of the overall effect is not explained by observable characteristics of the members. The findings thus have implication for future studies that aim to examine audit committee characteristics and firm outcomes: While prior studies find that member (chair) characteristics are associated with financial reporting quality (e.g., Klein, 2002), this study shows that these observable characteristics only capture a portion of the total effects of member (chairs) on financial reporting. Thus, it can be a fruitful path for future research to obtain information about and/or find ways to measure the characteristics that are yet unexplored by existing research (e.g., personality traits, disposition, childhood experience, etc.). Second, this article also speaks to the growing literature that studies individual traits of corporate executives. I show that just as personal traits of managers influence firm decisions, the traits of audit committee members are also associated with firm outcomes, in particular financial reporting practices. The broader question of whether these idiosyncratic affect market prices remains an area for future research.

The remainder of this article is organized as follows: Section ''Financial Reporting Choices and Audit Committee Member Style'' reviews prior literature, and elaborates my choice of the financial reporting variables and the influence of audit committee member styles on these variables. Section ''Sample, Data, and Research Design'' discusses sample selection and research design. Section ''Empirical Results'' presents the results and discusses the implications, and Section ''Conclusion'' concludes.

Financial Reporting Choices and Audit Committee Member Style

Individual Corporate Executive Characteristics and Firm Outcomes

The theoretical foundation for top executives influencing corporate decisions is the ''upper echelon theory'' proposed by Hambrick and Mason (1984). Building on this framework, a growing body of empirical research has found evidence on individual manager traits affecting firm decisions and performance (Bertrand & Schoar, 2003). With respect to accounting choices, studies have documented the effects on financial reporting outcomes of CEO reputation (Francis, Huang, Rajgopal, & Zang, 2008), ''superstar CEOs'' (K. Koh, 2011), management ability (Demerjian, Lewis, Lev, & McVay, 2010), executive overconfidence (Schrand & Zechman, 2012), CEO's facial structure (Jia, Lent, & Zeng, 2014), and executives' ownership of luxury goods and legal infractions (Davidson, Dey, & Smith, 2013). In addition to these observable characteristics, Ge et al. (2011) find that generic, unobservable CFO ''styles'' are associated with financial reporting, and the effects of these ''styles'' are not explained by observable characteristics (e.g., age and gender). Overall, prior evidence

suggests that there is still a significant portion of corporate executives' individual characteristics that cannot be explained by observable measures.

Audit Committee Characteristics and Firm Outcomes

A large body of research documents the effects of audit committee characteristics on firm outcomes. The most commonly documented characteristic is independence, which is found to be negatively correlated with earnings management (Bédard et al., 2004; Klein, 2002) and accounting restatements (Abbott, Parker, & Peters, 2004), and positively correlated with the likelihood of auditors issuing a going-concern opinion (Carcello & Neal, 2000). A second characteristic that is associated with financial reporting outcomes is the committee's activity level (diligence): Higher activity level is associated with less earnings management (Bédard et al., 2004) and fewer occurrences of restatements (Abbott et al., 2004). Another well-examined feature is expertise: It is also found to be effective in mitigating earnings management (Bédard et al., 2004) and reducing the occurrences of restatements (Abbott et al., 2004); in addition, DeFond, Hann, and Hu (2005) find a positive market reaction to adding financial experts to the board of directors. Finally, prior studies have also examined the busyness of audit committee members, and find that financial reporting quality is negatively associated with busyness (Tanyi & Smith, 2014).

As discussed in Section ''Introduction,'' the audit committee characteristics examined by prior literature are mostly observable features. Just as a significant portion of the overall effect of corporate executives cannot be explained by observable features (Ge et al., 2011), it is also likely that the overall effect of audit committee members cannot be explained by the observable characteristics documented by the prior studies. This article thus aims to fill this void by examining the overall effects of audit committee members.

Financial Reporting Choices and Audit Committee Member Style

Audit committee members are the monitors of the financial reporting process and the reviewers of the financial statements of a firm. As a subcommittee to the board of directors, the audit committee cannot ''effectively conduct day-to-day operations'' but rather performs a check on ''corporate financial results and prospects.''[7] Therefore, the financial reporting outcomes of a firm that are most likely to be influenced by the audit committee members are those subject to management discretion (or ''financial reporting choices'' for expositional purpose) rather than those determined by the fundamental earnings process (Dechow et al., 2010).[8]

I examine two categories of financial reporting choices: The first one is the probability of material accounting misstatements. One fundamental role of the audit committee is to ensure financial reporting integrity (Williams, 1977). Thus, I expect audit committee members to pay close attention to the probability of accounting misstatements. Idiosyncratic differences in the committee member's personality, integrity, risk aversion, experience, and time or effort invested may cause one member's way of dealing with potential misstatements to be different from another. I implement the measure developed by Dechow et al. (2011), called the ''F-Score'', to proxy for the likelihood of misstatements of a firm in a given year. The *F*-score is a scaled logistic probability of each firm year based on a model of the determinants of accounting manipulations estimated from a large sample of Accounting and Auditing Enforcement Releases issued by the Securities and Exchange Commission (SEC).[9] Dechow et al. (2011) find this measure to have reasonable out-of-

sample predictive ability of material misstatements. I use the *likelihood* of misstatements rather than the *actual* misstatements for two reasons: First, deliberate fraudulent reporting is difficult to detect, and many audit committee members do not view themselves as being responsible for fraud detection (Beasley et al., 2009). Rather, audit committees focus on reducing the *risk* of misreporting, which is captured by the *F*-score. Second, the number of incidences that a member serves two or more firms that are detected with misstatements is low, owing to the low frequency of detected cases. Yet, that does not mean that there is no variation in the intensity of monitoring conducted by the audit committee to reduce the risk of misreporting across the firms without detected misstatements. Using detected misreporting fails to capture such variation.

The second category of accounting choices I choose to study is earnings management. In his speech ''The Numbers Game,'' former SEC chairman Arthur Levitt identifies ''qualified, committed, independent and tough-minded'' audit committees as an important mechanism to curb earnings management (Levitt, 1998). Prior research finds that committee characteristics, such as size, independence, and expertise, influence earnings management (Abbott et al., 2004; Bédard et al., 2004; Klein, 2002). While the audit committee as a whole plays a role in controlling earnings management, individual member styles may also make a difference—in Mr. Levitt's terms, one member could be more ''qualified, committed and tough-minded'' than another.

I examine a set of proxies that capture different aspects of earnings management. The first proxy is absolute discretionary accruals (*ABS_DISACC*) from the modified Jones (1991) model with an intercept, as suggested by Kothari, Leone, and Wasley (2005) and controlling for performance (Ge et al., 2011; Kim, Park, & Wier, 2012). I use the absolute value rather than signed discretionary accruals because if the main goal of audit committee members is to curb earnings management, the effect of individual member style should be similar for upward or downward earnings management.[10] My second proxy for earnings management is meeting or beating analyst forecasts by a small amount (*SMB*). Specifically, I follow Ge et al. (2011) and compute the percentage of quarters in a given year that a firm meets or beats analyst forecasts by less than or equal to 1 cent.[11,12]

My last proxy captures earnings smoothing, a type of earnings management behavior documented by prior studies.[13] Specifically, I follow Ge et al. (2011) and measure earnings smoothness (*EARN_SMOOTH*) using the variance of the residuals obtained from a regression of the changes in quarterly earnings on a set of control variables, including leverage, sales growth, debt issuance, equity issuance, asset turnover, and size. The earnings data are quarterly, and I take fourth differences to remove the effects of seasonality.

Sample, Data, and Research Design

Sample Construction and Data

I construct an audit committee member (chairperson)-firm-matched panel dataset that tracks members (chairs) across different firms over time. To identify the individual style of a member (chair), I require that the members (chairs) sit on (serve as the chair of) at least two audit committees,[14] with at least 3 years at each committee so as to have enough time to ''imprint'' his or her style.[15] For a firm that has only one member (chair) in my sample, I include all the years of that firm with available data whether that member or chair is serving the firm to increase the power of my tests.

The requirement that all members (chairs) in my sample have been at multiple firms deserves some discussion. It is plausible that members sit on audit committees of firms that have similar characteristics. The member or chairperson fixed effects thus could capture the effects of these firm characteristics rather than member or chair-specific style. Therefore, it is especially important to control for firm effects. Following the design of Bertrand and Schoar (2003), I include firm fixed effects and year fixed effects in my regression models.[16] Figure 1, Panel A shows an example of how this design works for Robert Agate, audit committee chairman of Timberland Co. (TC) from 1993 to 2004 and Allied Waste Industries Inc. (AW) from 2000 to 2008. I control for fixed effects of TC and AW, as well as year fixed effects and time-varying control variables from 1993 to 2004. The fixed effect of Mr. Agate thus reflects how TC's accounting choices during the period of 1993 to 2004 differ from its average accounting choices, and how AW's accounting choices from 2000 to 2008 differ from the firm average (after also teasing out the effect of time-varying firm characteristics and year-specific factors). Note that in Panel A of Figure 1, Mr. Dennis Hendrix and Ms. Irene Esteves also served as audit committee chairpersons of TC and AW, respectively; however, neither Mr. Hendrix nor Ms. Esteves has worked as a chairperson for another firm and not included in my sample. Theoretically, I would still be able to disentangle the fixed effect of Ms. Esteves from the fixed effect of AW because Ms. Esteves's tenure does not exactly overlap with the entire time series of AW. The caveat of including Ms. Esteves, however, is that she is observed only at AW from 1993 to 1999. The effect of any time-varying-omitted firm characteristics of AW during this period would be mistakenly identified as Ms. Esteves's effect. In other words, requiring that all members (chairs) sit on at least two committees guarantees that omitted correlated variables would only bias the results if they are both time varying and correlated across firms.[17]

Data on audit committee members are taken from BoardEx. BoardEx contains information on board members in the United States that includes a director's name, age, gender, role on the board, specific committees he or she serves on, and the start and end dates of his or her tenure.[18] From BoardEx, I identify 5,079 distinct firms with 23,418 distinct audit committee members and 4,847 distinct firms with 6,572 distinct chairpersons in the United States. From this original sample, I exclude members or chairpersons whose tenures are less than 3 years, and firm-member or chairperson pairs that have missing Compustat data required for the control variables and all the dependent variables. This step excludes 5,208 distinct members at 676 distinct firms and 744 firms with identifiable chairs and 1,152 distinct chairs. Finally, I exclude members or chairpersons who only have available data for one firm. The final sample contains 3,010 firms with 2,941 members and 1,340 firms with 683 chairpersons. For the tests using absolute discretionary accruals as the dependent variable, I further exclude financial firms.[19]

Descriptive Statistics

Table 2 provides descriptive statistics of my sample. Compared with firms in Compustat from 1987 to 2010,[20] the firms in my sample are larger (median total assets of US$471,620 and US$595,620 for the members sample and the chairpersons sample, respectively, vs. US$97,700 for the Compustat firms) and more profitable (median ROA of 0.04 for the members sample and 0.05 for the chairpersons sample vs. 0.02 for the Compustat firms).[21] The last four rows of each panel in Table 2 provide information on board characteristics. Typically a board in my sample has 7 (first quartile) to 10 (third quartile) members, and a

Panel A: Illustration of *F*-tests.

	93	94	95	96	97	98	99	00	01	02	03	04	05	06	07	08
Timberland (TC)	Robert M. Agate												Dennis R. Hendrix			
Allied Waste (AW)	Ms. Irene Esteves							Robert M. Agate								

Panel B: Illustration of placebo tests.[a]

	93	94	95	96	97	98	99	00	01	02	03	04	05	06	07	08
	Chairman: Robert M. Agate															
Real	Timberland Co. (TC)															
Real								Allied Waste Ind. Inc. (AW)								
Placebo					Allied Waste Ind. (AW)											

Figure 1. Sample construction.

[a]Steps of placebo tests.

Step 1: Regress financial reporting choice variables on the control variables (Table 1), industry dummies and year dummies.

Step 2: Take the average residuals of the regression during each member or chairperson's tenure ("real residuals").

Step 3: Take the average residuals of the regression 3 years before the member or chairperson actually joined the firm ("placebo residuals").

Step 4: Regress the "placebo residuals" of the subsequent firm(s) on the "real residuals" of the previous firm(s).

Table 1. Variable Definitions.

Variable	Definition
Financial reporting choice variables	
ABS_DISACC	Absolute value of residuals from the following pooled regression based on two-digit SIC code: $$\frac{TA_{i,t}}{ASSET_{i,t-1}} = \alpha_0 + \alpha_1 \frac{1}{ASSET_{t-1}} + \alpha_2 \frac{\Delta SALES_{i,t} - \Delta AR_{i,t}}{ASSET_{i,t-1}} + \alpha_3 \frac{PPE_{i,t}}{ASSET_{i,t-1}} + \alpha_4 \frac{NI_{i,t}}{ASSET_{i,t-1}} + \epsilon_{i,t},$$ where for firm *i* year *t*, $TA_{i,t}$ is total accruals, which equals net income minus cash flow from operations; $ASSET_{i,t-1}$ is lagged total assets; $\Delta SALES_{i,t}$ is the change in sales; $\Delta AR_{i,t}$ is the change in accounts receivables; and $PPE_{i,t}$ is net property, plant, and equipment. *NI* is the net income.
F_SCORE	The scaled predicted probability from plugging time-variant firm characteristics into the following logit model, which uses estimated coefficients from Dechow, Ge, Larson, Sloan, and Investors (2011): *Manipulation*$_t$ = –8.252 + 0.665 × *RSST accruals* + 2.457 × *Change in receivables* + 1.393 × *Change in inventory* + 2.011 × *%Soft assets* + 0.159 × *Change in cash sales* – 1.029×*Change in ROA* + 0.983 × *Actual issuance* – 0.150 × *Abnormal change in employees* + 0.419 × *Existence of operating leases*. In the above model, *RSST accruals* are accruals defined by Richardson, Sloan, Soliman, and Tuna. (2005): the change in noncash net operating assets; *Change in receivables* is Δ accounts receivables/average total assets; *Change in inventory* is Δ inventory/average total assets; *% of Soft assets* is (total assets – PPE-cash and cash equivalents) / total assets; *Change in cash sales* is percentage change in cash sales, where cash sales is *sales – Δ accounts receivables; Change in ROA* is [*earnings*$_t$ / *average total assets*$_t$] – [*earnings*$_{t-1}$ / *average total assets*$_{t-1}$]; *Actual issuance* is an indicator variable which is 1 if the firm has issued new debt or equity during the time period; *Abnormal change in employees* is the percentage change in the number of employees minus the percentage change in assets; *Existence of operating leases* is an indicator variable coded 1 if future operating lease obligations are greater than 0. *F_SCORE* is the predicted probability from the above model, scaled by the unconditional probability of having accounting manipulations. A *F_SCORE* of 1 indicates that the firm has the same probability of manipulation as the unconditional expectation. A *F_SCORE* less (more) than 1 indicates a lower (higher) probability of manipulation than the unconditional expectation.
SMOOTH	The variance of the residuals for each member (chairperson)-firm from regressing the change in net income (current quarter net income taking fourth differences and scaled by total assets) on the following variables: leverage (total liabilities divided by total assets), growth (the percentage change in sales), debt issuance (percentage change in long-term debt), equity issuance (the percentage change in common shares outstanding), asset turnover ratio (sales divided by total assets), and size (natural log of sales). *SMOOTH* is measured as the variance during a member (chairperson)'s tenure minus the variance of the firm during the sample period (thus removing the firm effect), then multiplied by –1,000 for easiness of interpretation.
SMB	The percentage of quarters the firm meets or beats analyst forecasts by 1 cent per share or less (US$0.00 ≤ EPS – Meanest ≤ US$0.01) each year during the audit committee member or chair's tenure, where Meanest is the last consensus forecast for the quarter.

(continued)

Table 1. (continued)

Variable	Definition
Control variables	
ROA	Return on assets ratio, defined as EBITDA over lagged total assets.
SIZE	Log of total assets.
BTM	Book to market ratio, defined as book value of equity over market value of equity.
LEVERAGE	Leverage ratio, defined as long-term debt plus debt in current liabilities over long-term debt plus debt in current liabilities plus the book value of common equity.
GROWTH	Sales growth, defined as the percentage change in total sales.
CFF	Cash flow from financing activities deflated by total assets.
LOG_BUSSEG	The natural log of the number of business segments.
FOREIGN_DUMMY	An indicator variable that equals 1 if the firm has foreign operations and 0 otherwise.
BIG_N	An indicator variable that equals 1 if the firm's auditor is one of the Big 4/5/6 audit firms (Big 6 auditors include Arthur Andersen, Coopers and Lybrand, Deloitte Touche Tohmatsu, Ernst and Young, KPMG and PricewaterhouseCoopers).
AUDIT_TENURE	The number of years an auditor is retained by the firm. In the case of change in the audit firm's name as a result of audit firm mergers, the incumbent auditor–client relationship remains unchanged.
AUDIT_EXPERTISE	An indicator variable that equals 1 if the firm's auditor ranks highest in its share of its clients' total assets in the two-digit SIC industry group and 0 otherwise.
FEMALE	An indicator variable that equals 1 if the audit committee member (chairperson) is female and 0 otherwise.
MBA	An indicator variable that equals 1 if the audit committee member (chairperson) has a MBA degree and 0 otherwise.
CPA	An indicator variable that equals 1 if the audit committee member (chairperson) is a CPA and 0 otherwise.
AGE	The age of the audit committee member (chairperson).

Note. EBITDA = Earnings Before Interest, Tax and Depreciation (Amortization).

Table 2. Descriptive statistics.

	Member sample			Chair sample		
	M	Median	*SD*	*M*	Median	*SD*
Dependent variables						
ABS_DISACC	0.07	0.04	0.07	0.06	0.04	0.07
F_SCORE	1.03	0.92	0.61	1.05	0.93	0.64
SMOOTH	2.17	0.00	18.64	2.00	0.00	17.83
SMB	0.10	0.00	0.19	0.10	0.00	0.19
Control variables						
ROA	0.03	0.04	0.22	0.03	0.05	0.16
SIZE	6.65	6.61	1.92	6.65	6.58	1.89
BTM	0.54	0.46	0.41	0.53	0.44	0.41
LEVERAGE	0.33	0.31	0.28	0.33	0.31	0.28
GROWTH	0.15	0.09	0.32	0.16	0.10	0.33
CFF	0.02	0.00	0.14	0.02	-0.01	0.14
LOG_BUSSEG	1.96	1.61	1.36	2.25	2.40	1.34
FOREIGN_DUM	0.63	1.00	0.48	0.66	1.00	0.47
BIG_N	0.91	1.00	0.28	0.93	1.00	0.26
AUD_TENURE	10.99	8.00	8.64	10.94	8.00	8.48
AUDIT_EXPERTISE	0.27	0.00	0.45	0.28	0.00	0.45
Firm characteristics						
Total assets	2601.76	471.62	6126.96	3042.87	595.62	6789.15
Market value	2146.99	466.63	5040.35	2749.32	621.30	6583.29
Board characteristics						
Board size	8.78	8.00	2.69	8.94	9.00	2.64
Audit committee size	3.95	4.00	1.10	3.93	4.00	1.13
Member (chair) characteristics						
AGE	60.48	60.00	7.78	60.53	60.00	6.34
FEMALE	0.10	0.00	0.30	0.07	0.00	0.25
MBA	0.34	0.00	0.48	0.33	0.00	0.47
CPA	0.12	0.00	0.32	0.24	0.00	0.43
Tenure	12.54	11.00	2.56	13.81	13.00	7.25

Note. Member (chair) sample refers to firms that meet the data requirements for audit committee members and chairs described in Section "Sample Construction and Data." Board size refers to number of board members. Audit committee size refers to number of audit committee members. Tenure refers to the number of years a person works as the audit committee member (chair) in a given firm. *BoardEx* only has board characteristics data from 2000 to 2008. Hence, the descriptive statistics reported in this table for these characteristics are computed using data from 2000 to 2008. All the other variables are defined in Table 1.

typical committee has 3 (first quartile) to 4 (third quartile) people (for the members sample). The median length of the tenure of a member (chairperson) is 11 (13) years.

Research Design

For each financial reporting choice variable except *SMOOTH*, I first run a baseline regression with firm dummies, year dummies, and time-varying firm characteristics as the independent variables:

$$DEPENDENT\_VARS_{it} = \beta_0 + FIRM\_CONTROLS_{i,t} + FIRM_i + YEAR_t + \epsilon_{it}, \qquad (1)$$

where *DEPENDENT_VARS* are *F_SCORE, ABS_DISACC*, and *SMB*. Then, I add audit committee member or chairperson fixed effects to the baseline model:

$$DEPENDENT\_VARS_{it} = \beta_0 + FIRM\_CONTROLS_{i,t} + \boldsymbol{MEMBER/CHAIR_j} + FIRM_i + YEAR_t + \epsilon_{it.} \quad (2)$$

For each regression, I perform an *F*-test for the joint significance of the member or chairperson dummy variables. Joint significance of the member or chair fixed effects would indicate that individual-specific style of audit committee members or chairpersons has an influence on firms' financial reporting choices. I also compare the increase in adjusted R^2 from Model 1 to Model 2 to examine the explanatory power of member or chairperson fixed effects.

I control for a set of time-varying firm characteristics (*FIRM_CONTROLS*): firm size (*SIZE*) and return on assets (*ROA*; Dechow et al., 2010); book to market ratio (*BTM*) and sales growth (*GROWTH*; Dechow & Dichev, 2002; Lee, Li, & Yue, 2006), debt to equity ratio (*LEVERAGE*), and cash flow from financing activities (*CFF*; Dichev & Skinner, 2002; Teoh, 1998); the log of the total number of business segments (*LOG_BUSSEG*); an indicator variable for having foreign operations (*FOREIGN_DUMMY*; Hoitash, Hoitash, & Bedard, 2009) whether the firm is audited by a Big N auditor (*BIG_N*), and the auditor's tenure and expertise (*AUDIT_TENURE* and *AUDIT_EXPERTISE*; Gul, Fung, & Jaggi, 2009).[22]

To test whether the fixed effects are driven by observable characteristics that are already identified by prior studies, I add four characteristics to both Equations 1 and 2: *FEMALE* (an indicator variable that equals 1 if the member or chair is female), *MBA* (an indicator variable that equals 1 if the member or chair has a MBA degree), *CPA* (an indicator variable that equals 1 if the member or chair is a CPA), and *AGE* (the age of the member or chair in the given year; Ge et al., 2011). I choose these four characteristics for the following reasons: First, prior research provides evidence that gender is associated with risk aversion (women are more risk averse than men) and overconfidence (men exhibit higher level of overconfidence than women; for example, Eckel & Grossman, 2008; Prince, 1993). Both traits could lead female members to be more conservative as monitors, and thus potentially reducing managers' opportunistic financial reporting behavior (Abbott, Parker, & Presley, 2012). However, prior studies also find that the difference in the risk appetite between men and women may not be generalizable to corporate executives, as women who are able to break the glass ceiling are considerably different from the general population (Adams & Funk, 2012). Therefore, it is also possible that female members (chairs) are more tolerant toward aggressive financial reporting practices (Adams & Funk, 2012; Adams & Ragunathan, 2015). In addition to gender, age and educational background are characteristics that have been shown to be associated with risk aversion. Specifically, age is found to be positively correlated with risk aversion (e.g., Morin & Suarez, 1983), while the evidence on educational background is mixed: Having a MBA degree can suggest the choice of a relatively conservative career path and thus higher risk aversion (Graham, Harvey, & Puri, 2013), yet Chevalier and Ellison (1999) find that mutual fund managers with MBA degrees take higher systematic risk. Finally, an audit committee member's financial expertise can directly affect her ability to spot opportunistic financial reporting behavior (Abbott et al., 2004; Bédard et al., 2004). I therefore examine whether the member (chairperson) is a CPA. I then conduct an *F*-test for the joint significance of the member (chairperson) fixed

effects with these observable characteristics included. If the fixed effects are driven by the observable characteristics, including them in the regression models will render the fixed effects insignificant.

The traditional fixed effects design cannot be implemented on the earnings smoothness measure because computing it requires time-series data. Thus, for each member or chairperson-firm-matched pair, I only have one observation, and for each member or chairperson, I only have five observations at the maximum, as the maximum number of audit committees a member sits on is 5 in my sample. To test the individual-specific effects of members or chairpersons, I follow the design of Ge et al. (2011). Specifically, for each member (chair), I arrange the firms that he or she has worked at in chronological order by his or her starting date. Then, I regress the earnings smoothness measure of each subsequent firm the member (chair) worked at on that of the previous firm. If a member (chair) imprints his or her own style to the firms he or she worked at, the earnings smoothness measures should be positively correlated among these firms. To adjust for persistent firm factors, I subtract earnings smoothness computed over the entire time series of the firm from that computed over the member or chairperson's tenure. In other words, the earnings smoothness measure (*SMOOTH*) is a firm-adjusted, member or chair-firm-specific variable.

To give an example, in Figure 1 Panel A, Mr. Agate first worked as the audit committee chairman of TC, and then at AW. I thus test whether the earnings smoothness measure of TC is positively correlated with that at AW during Mr. Agate's tenure. I first calculate *SMOOTH* for TC from 1993 to 2004 ($SMOOTH^{TC}$) and for AW from 2000 to 2008 ($SMOOTH^{AW}$). Then, I subtract from the earnings smoothness measure calculated from 1993 to 2008 for both firms (*Adjusted* $SMOOTH^{TC}$ and *Adjusted* $SMOOTH^{AW}$). Finally, I regress the adjusted smoothness measure of AW on that of TC and predict a positive coefficient.

In cases where a member (chair) worked at more than two firms, a similar design is applied. In the above example, suppose Mr. Agate served as the audit committee chairman at a third company, Trio Inc. (Trio) in 2009. Then, the regression models would be (a) regressing the adjusted smoothness measure of AW on that of TC, (b) regressing the adjusted smoothness measure of Trio on that of AW, and (c) regressing the adjusted smoothness measure of Trio on that of TC.

Empirical Results

Main Results

Table 3 presents the results of the effects on firm accounting choices of audit committee members and chairpersons. Panel A of Table 3 presents the *F*-test results of audit committee member (chair) fixed effects on *F_SCORE, ABS_DISACC*, and *SMB*. For each dependent variable, the first row (column 5) reports the adjusted R^2 of the baseline model (Equation 1), and the second row reports the *F* value (column 2) of audit committee member (chair) fixed effects, the adjusted R^2 with member dummies added (column 5), and the increase in adjusted R^2 from Equations 2 to 1 (column 6). The results in Panel A of Table 3 demonstrate that the audit committee member (chair) fixed effects are jointly significant for all the three dependent variables: *F_SCORE, ABS_DISACC*, and *SMB*. Adding audit committee member (chair) fixed effects to the baseline model increases adjusted R^2 by 2.4 (2.3), 2.6 (2.7), and 4.9 (3.1) percentage points for *F_SCORE, ABS_DISACC*, and

Table 3. Audit Committee Member and Chair Effects on Financial Reporting Practices.

Panel A: Accounting Misstatements and Earnings Management.

(1)	(2) *F* value on fixed effects	(3) *p* value	(4) Number of constraints	(5) Adjusted R^2	(6) Increase in R^2	(7) Number of observations
Members						
F_SCORE				.5341		19,351
	1.68	<.0001	1,618	.5584	**.0243**	19,351
ABS_DISACC				.4912		18,868
	1.56	<.0001	1,568	.5167	**.0255**	18,868
SMB				.2495		25,596
	1.72	<.0001	2,195	.2980	**.0485**	25,596
Chairpersons						
F_SCORE				.5689		7,646
	2.32	<.0001	343	.5923	**.0234**	7,646
ABS_DISACC				.4526		7,388
	2.05	<.0001	327	.4798	**.0272**	7,388
SMB				.2691		11,419
	1.93	<.0001	484	.3001	**.0310**	11,419

Panel B: Earnings Smoothness.

(1) Dependent variable	(2) Independent variable	(3) Predicted sign	(4) Coefficient estimate	(5) *t*-statistics	(6) R^2	(7) Number of observations
SMOOTH (Member)	*Lag_SMOOTH (Member)*	+	0.0130	0.62	.0002	4,323
SMOOTH (Chair)	*Lag_SMOOTH (Chair)*	+	0.0143	0.33	.0002	854

Note. This table reports audit committee member and chair effects on financial reporting practices. The sample is the member(chair)-firm-matched panel data described in Section "Sample Construction and Data." Panel A reports regression results of *F_SCORE, ABS_DISACC*, and *SMB*. The regression specifications are provided in Equations 1 and 2. For each dependent variable (in column 1), the first row reports the adjusted R^2 without member (chair) fixed effects; the second row reports the *F* values on the joint significance of member (chair) fixed effects (column 2), the *p* values (column 3), the number of constraints in the *F* values (column 4), the adjusted R^2, including member (chair) fixed effects (column 5) and the increase in adjusted R^2 from adding member (chair) effects (column 6). Panel B reports regression results for the earnings smoothness measure (*SMOOTH*). For each member (chair), I regress the earnings smoothness measure over his or her tenure at the first firm on that at the subsequent firm(s). The coefficient is reported in column 4. The standard errors are clustered by member (chair). All variables are defined in Table 1.

SMB, respectively. The magnitude is comparable with adding CEO fixed effects in Bertrand and Schoar (2003) and adding CFO fixed effects in Ge et al. (2011).[23]

Panel B contains results for earnings smoothness. If individual committee members and/or chairpersons bring their own style to their firms' earnings smoothing, the earnings smoothness measure of the previous firm that the member worked at should be positively correlated with that of the subsequent firm(s). In other words, the coefficient on earnings smoothness of the previous firm(s) (*Lag_SMOOTH*) should be positive and significant. The results in Panel B of Table 4 do not support this prediction. The coefficient is significant for neither audit committee members nor chairpersons. Thus, I find no evidence that audit committee members or chairpersons imprint their styles on earnings smoothness.

Table 4. Audit Committee Member and Chair Effects on Financial Reporting Practices: Replacing Fixed Effects With Observable Individual Member and Chair Characteristics.

Panel A: Audit Committee Members' Gender, Age, Education, and Professional Qualification Effects on Financial Reporting Practices.

(1)	(2) *FEMALE* coefficient (*t*-statistics)	(3) *MBA* coefficient (*t*-statistics)	(4) *CPA* coefficient (*t*-statistics)	(5) *AGE* coefficient (*t*-statistics)	(6) Number of observations
F_SCORE	0.0038	0.0014	–0.0388	–0.0009	6,325
	(0.13)	(0.07)	(–1.27)	(–0.66)	6,325
ABS_DISACC	0.0045	–0.0012	0.0001	–0.0002	6,227
	(1.16)	(–0.47)	(0.02)	(–0.99)	6,227
SMB	–0.0051	–0.0123**	–0.0090	–0.0001	11,796
	(–0.66)	(–2.48)	(–1.20)	(–0.24)	11,796

Panel B: *F* test on the Joint Effects of Audit Committee Members' Gender, Age, Education, and Professional Qualification.

(1)	(2) *F* value on member characteristics	(3) *p* value	(4) Number of constraints	(5) Adjusted R^2	(6) Increase in R^2	(7) Number of observations
F_SCORE				.5949		6,325
	0.53	.7119	4	.5948	**–.0001**	6,325
ABS_DISACC				.4107		6,227
	0.85	.4958	4	.4106	**–.0001**	6,227
SMB				.2467		11,796
	1.99	.0927	4	.2470	**.0003**	11,796

Panel C: Audit Committee Chairs' Gender, Age, Education, and Professional Qualification Effects on Financial Reporting Practices.

(1)	(2) *FEMALE* coefficient (*t*-statistics)	(3) *MBA* coefficient (*t*-statistics)	(4) *CPA* coefficient (*t*-statistics)	(5) *AGE* coefficient (*t*-statistics)	(6) Number of observations
F_SCORE	0.0258	–0.0169	–0.0654***	0.0016	6,416
	(0.68)	(–0.74)	(–2.84)	(1.05)	6,416
ABS_DISACC	0.0118**	–0.0047	–0.0028	0.0003*	6,311
	(2.43)	(–1.60)	(–0.92)	(1.70)	6,311
SMB	–0.0039	–0.0071	0.0014	–0.0006	11,419
	(–0.36)	(–1.14)	(0.21)	(–1.34)	11,419

Panel D: *F* test on the Joint Effects of Audit Committee Chairs' Gender, Age, Education, and Professional Qualification.

(1)	(2) *F* value on chair characteristics	(3) *p* value	(4) Number of constraints	(5) Adjusted R^2	(6) Increase in R^2	(7) Number of observations
F_SCORE				.6184		6,416
	2.58	.0354	4	.6188	**.0004**	6,416
ABS_DISACC				.4093		6,311
	2.69	.0297	4	.4100	**.0007**	6,311
SMB				.2726		11,419
	0.68	.6072	4	.2725	**–.0001**	11,419

(*continued*)

Note. This table reports the effects of audit committee members' and chairs' observable characteristics (gender, age, education, and professional qualifications) on their firms' financial reporting practices, when audit committee (chairperson) fixed effects are excluded. The regression model is similar to that specified in Equation 2, only that the member (chair) dummies are not included. Panel A (Panel C) presents the coefficients of gender (*FEMALE*), age (*AGE*), education (*MBA*), and professional qualification (*CPA*) on the financial reporting practice variables (*F_SCORE, ABS_DISACC*, and *SMB*) for audit committee members (chairpersons). Panel B (Panel D) presents the results for *F*-tests on the joint significance of *FEMALE, AGE, MBA*, and *CPA* of the audit committee members (chairpersons) on the financial reporting practice variables. For each financial reporting choice variable (column 1), the first row reports the adjusted R^2 without the member (chairperson) characteristics (column 5). The second row reports the results when including the member (chairperson) characteristics. Specifically, column 2 reports the *F* value of the joint effects of *FEMALE, AGE, MBA*, and *CPA*; column 3 reports the *p* value of the *F*-statistics; column 5 reports the adjusted R^2 when including the member (chair) characteristics; column 6 reports the increase in adjusted R^2 (difference between the second and the first row in column 5). All variables are defined in Table 1.

Controlling for Observable Audit Committee Member (Chairperson) Characteristics

The tests in Table 3 do not include observable member (chairperson) characteristics. Therefore, it is possible that the member (chairperson) fixed effects are capturing observable member (chairperson) characteristics such as gender, age, education, and professional backgrounds (Abbott et al., 2004; Bédard et al., 2004; Klein, 2002). To test whether the fixed effects are capturing time-invariant characteristics of audit committee members (chairpersons), I conduct two empirical tests. Note that I do not conduct any sensitivity test for earnings smoothness as I find no evidence of audit committee member (chair) style being imprinted on earnings smoothness.

First, I replace the fixed effects with the following observable member (chairperson) characteristics as discussed in Section ''Research Design'': *FEMALE, MBA, CPA*, and *AGE*, and test whether these observable characteristics are correlated with financial reporting practices and whether they are jointly significant. Table 4 presents the results. Using the member (chair) sample, Panel A (Panel C) reports the coefficients of *FEMALE, MBA, CPA*, and *AGE* on *F_SCORE, ABS_DISACC*, and *SMB*, and Panel B (Panel D) reports the joint significance of these individual characteristics. For the member sample, the only coefficient that is statistically significant is *MBA* on *SMB* (*t*-statistic = –2.48), and the four variables are only jointly significant for *SMB* (Panel B). The results are stronger for the chairperson sample: The audit committee chairperson being a CPA is negatively correlated with the propensity to misreport, and *AGE* and *FEMALE* are positively associated with the level of absolute discretionary accruals. In addition, the four characteristics are jointly significant for *F_SCORE* (*p* value = .0354) and *ABS_DISACC* (*p* value = .0297) but not significant for *SMB* (*p* value = .6072). Overall, it seems that the observable characteristics of audit committee chairpersons have a stronger association with financial reporting practices compared with those of ordinary members.

To test whether the explanatory power of fixed effects is driven by observable individual characteristics, I add the observable characteristics (*FEMALE, MBA, CPA*, and *AGE*) to the model specified in Equation 2. I then test the joint significance of the member (chairperson) fixed effects using the same *F*-test discussed in Section ''Research Design.'' As there can be multiple audit committee members in each firm, for the audit committee member sample, I randomly select one member from each firm.[24]

Table 5 shows the results. Even when including the observable member (chairperson) characteristics, the fixed effects are still jointly significant for both the member (Panel A) and the chairperson sample (Panel B), and including member (chairperson) fixed effects

Table 5. Audit Committee Member and Chair Effects on Financial Reporting Practices: Controlling for Observable Member and Chair Characteristics.

Panel A: Audit Committee Member Effects: Controlling for Observable Member Characteristics.

(1)	(2) *F* value on member fixed effects	(3) *p* value	(4) Number of constraints	(5) Adjusted R^2	(6) Increase in R^2	(7) Number of observations
F_SCORE				.5948		6,325
	1.34	<.0001	827	.6171	**.0223**	6,325
ABS_DISACC				.4136		6,227
	1.19	.0005	821	.4322	**.0186**	6,227
SMB				.2498		11,796
	1.3	<.0001	1,518	.2839	**.0341**	11,796

Panel B: Audit Committee Chairperson Effects: Controlling for Observable Chairperson Characteristics.

(1)	(2) *F* value on chair fixed effects	(3) *p* value	(4) Number of constraints	(5) Adjusted R^2	(6) Increase in R^2	(7) Number of observations
F_SCORE				.6188		6,416
	2.32	<.0001	312	.6438	**.0250**	6,416
ABS_DISACC				.41		6,311
	2.29	<.0001	311	.4483	**.0383**	6,311
SMB				.2749		11,419
	1.72	<.0001	486	.2978	**.0229**	11,419

Note. This table reports audit committee member (Panel A) and chair (Panel B) fixed effects on financial reporting practices when controlling for the member's (chair's) gender, age, education, and professional qualification. For each dependent variable (in column 1), the first row reports the adjusted R^2 without audit committee member or chair fixed effects; the second row reports the *F* values on the joint significance of audit committee member or chair fixed effects (column 2), the *p* values (column 3), the number of constraints in the *F* values (column 4), the adjusted R^2, including audit committee member or chair fixed effects (column5) and the increase in adjusted R^2 from adding audit committee member or chair fixed effects (column 6). All variables are defined in Table 1.

increases the R^2 by 1.86 to 3.83 percentage points. Thus, the results in Table 7 suggest that even when observable individual characteristics may be significantly associated with financial reporting practices in some cases, there are still unobservable or not yet identified observable characteristics of audit committee members (chairs) that are correlated with a firm's financial reporting choices.

The test results in Tables 3 through 5 are remarkably similar for audit committee members and chairpersons. This may be surprising at the first sight, as audit committee chairpersons are in the leading position of the committee. However, there are reasons why the conspicuousness of the individual styles may not differ between members and chairs. Besides the survey evidence that audit committee chairs are more likely to have personal ties with managers and are thus more likely to be influenced by them as noted in ''Introduction,'' the dynamics of the audit committee could make regular members equally important as the chairpersons. Both anecdotal and empirical evidence suggests that board members work as a team that shares the leadership role among its members (Forbes & Milliken, 1999; Nadler, 2004; Vandewaerde, Voordeckers, Lambrechts, & Bammens,

2011). The same can be said for audit committees. The audit committee chair holds no real formal authority over his or her fellow members, and is considered the first among equals (Pick, 2009). Also, inputs from all members in the committee are necessary for the committee's oversight process (Morrow & Pastor, 2007). Therefore, it is reasonable that individual members of the audit committee can imprint their styles on financial reporting as much as the chairpersons.

Sensitivity Tests

Controlling for CEO and CFO fixed effects. The results in Table 3 have one caveat. Although audit committee members, especially the chairpersons, are independent of the firms, it is still possible for management to influence their decisions (Beasley, 1996; Vicknair, Hickman, & Carnes, 1993). To investigate whether the member (chair) fixed effects are in fact capturing the effects of firm management, I perform two additional tests: First, I control for CEO fixed effects as prior studies find that CEO reputation, ability, and personality are associated with financial reporting choices (Demerjian et al., 2010; Francis et al., 2008; K. Koh, 2011; Schrand & Zechman, 2012); second, I control for CFO fixed effects as Ge et al. (2011) find that CFOs imprint their own styles on the financial reporting of their firms.

Data on CEO (CFO) information are obtained from Execucomp. Requiring firms to have CEO (CFO) information in Execucomp reduces the member sample to 1,247 (557) firms and 1,219 (397) members, and the chair sample to 981 (326) firms and 821 (205) chairs. For each dependent variable except the earnings smoothness measures, I first estimate a benchmark regression similar to Equation 1 with CEO (CFO) fixed effects included. Then, I add audit committee member (chair) fixed effects ($MEMBER$ / $CHAIR_j$) to the benchmark model. Note that I do not require CEOs (CFOs) to have worked at no less than two firms because such a restriction would make my sample too small to have any power. Table 6 presents the results on members when CEO (Panel A) or CFO (Panel B) fixed effects are included. The results on chairs are similar and omitted for brevity.[25] Adding CEO (CFO) fixed effects does not adversely affect the significance of member fixed effects. The increase in adjusted R^2 when CEO fixed effects are included is comparable with the main test for *F_SCORE* and *ABS_DISACC*, while smaller for *SMB*. When CFO fixed effects are included, however, the magnitude of the increase in adjusted R^2 is not as large as in the main tests. Specifically, adding member fixed effects to the benchmark model with CFO fixed effects only increases adjusted R^2 by 1.4, 1.1, and 1.3 percentage points for *F_SCORE, ABS_DISACC*, and *SMB*, respectively. As Ge et al. (2011) find that CFOs are able to imprint their personal styles on the financial reporting choices of their firms, it is not surprising that some explanatory power of the audit committee member fixed effects are taken away by the inclusion of CFO fixed effects. Overall, the individual member styles remain significant in the presence of CEO (CFO) styles, and the results in my main tests do not seem to be driven by the effect of management.

Robustness of F-tests. One drawback of the *F*-test is that the significance of the *F*-statistics could be driven by only a small number of significant indicator variables. To test whether this is the case, I count the number of significant member indicator variables in each fixed effect regression, and compare it with what would be expected under the null. Specifically, there are 1,943, 1,880, and 2,589 member indicator variables in the regressions of

Table 6. Audit Committee Member Effects on Financial Reporting Practices: Controlling for CEO and CFO Effects.

Panel A: Controlling for CEO Fixed Effects.

	F value on fixed effects		Number of constraints		Adjusted R^2	Increase in R^2	Number of observations
(1)	(2) CEO	(3) Member	(6) CEO	(7) Member	(8)	(9)	(10)
F_SCORE	13.15	—	883		.7206		4,784
	7.48	**6.35**	422	758	.7419	**.0213**	4,784
ABS_DISACC	5.32	—	800		.4760		4,590
	3.43	**3.79**	392	716	.5121	**.0361**	4,590
SMB	3.44	—	1,210		.2875		8,283
	2.04	**2.12**	646	1,174	.3252	**.0377**	8,283

Panel B: Controlling for CFO Fixed Effects.

	F value on fixed effects		Number of constraints		Adjusted R^2	Increase in R^2	Number of observations
(1)	(2) CFO	(3) Member	(6) CFO	(7) Member	(8)	(9)	(10)
F_SCORE	9.69	**—**	245		.7619		834
	8.36	**7.78**	116	169	.7759	**.0140**	834
ABS_DISACC	5.31	**—**	229		.6039		778
	5.63	**3.75**	91	154	.6145	**.0106**	778
SMB	1.82	**—**	537		.2405		2,253
	1.14	**1.29**	206	385	.2532	**.0127**	2,253

Note. This table reports audit committee member effects on financial reporting choice variables when controlling for CEO or CFO fixed effects. Panel A reports the results when controlling for CEO fixed effects, and Panel B reports the results when controlling for CFO fixed effects. I first regress financial reporting choice variables (column 1) on the control variables in Equation 1 and CEO or CFO dummies, then I add audit committee member dummies to the regression model. For each financial reporting choice variable, the first row reports the *F* values of the joint significance of CEO or CFO fixed effects (column 2), the *p* values of the *F* tests (column 4), the number of constraints in the *F* tests (column 6), the adjusted R^2 without audit committee member fixed effect (column 8), and the number of observations (column 10). The second row reports the results with audit committee member fixed effects added. Specifically, column 3 reports the *F* value on audit committee member fixed effects, column 5 reports the *p* value, column 7 shows the number of constraints used in the *F* tests, column 8 reports the adjusted R^2, and the increase in R^2 by adding audit committee member fixed effects is shown in column 9.

F_SCORE, ABS_DISACC, and *SMB*, respectively. Thus, under the null hypothesis, the numbers of fixed effects significant at the 10% level, 5% level, and 1% level are 194, 97, and 19 for *F_SCORE*, 188, 94, and 19 for *ABS_DISACC*, and 259, 130, and 26 for *SMB*, respectively. The results (presented in Figure A1 of the Online Supplemental Appendix) show that the actual frequencies of significant members are consistently much higher than what would be expected under the null in all three financial reporting variables. These results suggest that the joint significance of the member fixed effects is not driven by only a small number of member indicators.

To further test the robustness of the *F*-test, I simulate the distribution of the number of significant member fixed effects by randomly assigning each member to a firm at which he

or she did not work. I then run the same regressions shown in Equation 2 using the shuffled data and compute the number of significant fixed effects. I repeat this randomization 200 times and generate a simulated distribution of the number of significant fixed effects, as reported in Figure A2 of the Online Supplemental Appendix. The maximum numbers of fixed effects significant at the 5% level from the simulated distributions are 103, 104, and 170 for *F_SCORE, ABS_DISACC*, and *SMB*, respectively, none of which exceeds the actual frequencies shown in Figure A2.[26] Thus, my results do not appear to be driven by mechanical biases of the *F*-test.

Placebo tests. To further address the concern that audit committee members choose similar firms to work for, and that my results are driven by these unobservable common firm characteristics, I conduct ''placebo tests'' similar to those shown in Bertrand and Schoar (2003) and Ge et al. (2011). Figure 1, Panel B illustrates the test design. Take Mr. Agate as an example. For all dependent variables except the earnings smoothness measures, I first run the following regression:

$$DEPENDENT\_VARS_{it} = \beta_0 + FIRM\_CONTROLS_{i,t} + INDUSTRY_k + YEAR_t + \epsilon_{it}, \quad (3)$$

where *INDUSTRY* denotes industry indicator variables based on two-digit Standard Industrial Classification (SIC) codes. Then for each member (Mr. Agate in this example), I take the average of the residuals during his tenure at each firm. The average residual captures the variation of the financial reporting choice variables unexplained by the control variables. If Mr. Agate's style has an effect on the dependent variables, it should be captured in this average residual, and the residuals of TC and AW should be positively correlated due to the effect of Mr. Agate. Thus, I regress the average residuals of the members' subsequent firm(s) on those of the previous firm(s) and predict a positive coefficient. I then take the average residual of the member's subsequent firm (in this example AW) not during his tenure but 3 years prior to the year he actually joined the firm. I call this residual the ''placebo residual.'' The ''placebo residual'' of AW should not be positively correlated with the real residual of TC, unless some unobserved similarity between the two firms drove Mr. Agate's decision to become audit committee member for both firms. Hence, regressing the ''placebo residuals'' of the subsequent firm(s) on the real residuals of the previous firms should result in no positive and significant coefficients.[27]

Table 7, Panel A shows the placebo test results. Columns 2 to 4 show the regression results using real data, and columns 5 to 7 show the results using placebo data. For *F_SCORE*, the coefficients are positive and significant using both the real data and the placebo data. However, the magnitude of the coefficient for *F_SCORE* using the real data is 1.83 times of the coefficient using the placebo data (0.088 for the real data and 0.048 for the placebo data). For *ABS_DISACC*, neither the coefficient using the real data nor that using the placebo data is statistically significant.[28] For *SMB*, both coefficients are positive and significant, and the magnitudes are similar. Overall, the placebo test results suggest that there is a matching process between audit committee members and firms: The likelihood of misreporting and meeting and beating analyst forecasts by a small amount is correlated across the firms that share the same member even before he or she joins the firms. However, the evidence also suggests that the member does imprint his or her own style onto the firm, especially for *F_SCORE*, as the magnitude of the coefficient using real data is much larger than that of the placebo data. Note that the two scenarios are not mutually exclusive: An audit committee member who is especially concerned about the likelihood of

Table 7. Placebo Test and Audit Committee Member Effects on Financial Reporting Practices Post 2000.

Panel A: Placebo Test of Audit Committee Member Effects on Financial Reporting Practices.

	Real data			Placebo data		
(1)	(2) Coefficient	(3) *t*-statistics	(4) R^2	(5) Coefficient	(6) *t*-statistics	(7) R^2
Probability of misstatements						
F_SCORE	0.0879***	3.25	.01	0.0480**	2.40	.00
Earnings management						
ABS_DISACC	0.0224	0.87	.00	–0.0194	–0.91	.00
SMB	0.0349**	2.08	.00	0.0437***	3.17	.01

*$p < .1$. **$p < .05$. ***$p < .01$.

Panel B: Audit Committee Member Effects on Financial Reporting Practices Post 2000.

(1)	(2) *F* value on member fixed effects	(3) *p* value	(4) Number of constraints	(5) Adjusted R^2	(6) Increase in R^2	(7) Number of observations
F_SCORE				.7095		4,322
	1.25	.0100	217	.7109	**.0014**	4,322
ABS_DISACC				.5424		4,230
	1.28	.0048	217	.5526	**.0102**	4,230
SMB				.3068		6,407
	1.06	.2200	386	.3100	**.0032**	6,407

Note. This table reports the placebo test results (Panel A) and audit committee member effects on financial reporting practices (Panel B). See Figure 1 for the steps of the placebo test conducted for members who have worked for two firms. Similar steps are taken for members who have worked for more than three firms. In the sample, the maximum number of firms a director has worked at is 5. If a member's tenure at one firm overlaps with that at another firm, the average residual of the firm at which the member has started earlier is treated as the dependent variable. In each placebo regression, the independent variable is the average residual over the 3 years before the member joined the firm; the dependent variable is the average residual over the member person's actual tenure. Standard errors are clustered by member. The sample of the results reported in Panel B is the audit committee member-firm-matched panel with audit committee members who have started their positions in or after 2000. For each dependent variable (in column 1), the first row reports the adjusted R^2 without audit committee member fixed effects; the second row reports the *F* values on the joint significance of audit committee member fixed effects (column 2), the *p* values (column 3), the number of constraints in the *F* values (column 4), the adjusted R^2 including audit committee member fixed effects (column5) and the increase in adjusted R^2 from adding audit committee member fixed effects (column 6). The standard errors are clustered by member. All variables are defined in Table 1.

misreporting is not only likely to choose a firm with low *F_SCORE* ex ante but also put in more effort to curb the manager's propensity to engage in misreporting.

Including only members or chairpersons who started in or after 2000. BoardEx contains data on audit committee members from 2000 to 2008, yet the starting dates of the members are not restricted to post 2000. In other words, some audit committee members (chairs) of my main sample are those who started before 2000, and remain as members (chairs) in or after 2000. To address the concern that my sample is biased toward the members (chairs) who have held their jobs for a long period, I replicate the tests in Table 3 using a

subsample restricted to the members who started their jobs in or after 2000. In addition, this subsample allows me to control for board and audit committee characteristics, which mitigates the concern that the board or audit committee structure drives my results.

Table 7, Panel B reports the joint significance of member fixed effects in the regressions specified in Equation 2, with the following variables included as additional controls: board size, audit committee size, percentage of independent directors, and an indicator variable for audit committees with members all independent from the firm. Panel B of Table 7 shows that the member fixed effects are still jointly significant for *F_SCORE* and *ABS_DISACC* but not for *SMB*. The magnitudes of the increase in R^2 are smaller than those in the main test: They range from 0.14 to 1.02 percentage points, compared with the 2.43- to 4.85-percentage-point increase in Table 3. In sum, the joint significance of member fixed effects does not appear to be driven by members with long tenure, and is not explained away by including board and audit committee characteristics.

Conclusion

This article examines whether individual-specific ''styles'' of audit committee members and chairs have an impact on firms' financial reporting practices. Focusing on two categories of financial reporting choice variables—the probability of accounting misstatements and earnings management—I find evidence that audit committee members (chairs) exhibit individual-specific styles in influencing the financial reporting choices. The overall effect of members (chairs) is not explained by observable characteristics (gender, age, educational and professional backgrounds) found by prior literature (Abbott et al., 2004; Bédard et al., 2004; Klein, 2002).

The findings are robust to a series of sensitivity tests: I first control for CEO (CFO) fixed effects to address the concern that audit committee member fixed effects are capturing the influence of management. I then count the number of significant member (chair) fixed effects to make sure that the significance of the *F*-statistics is not merely driven by a small number of member (chair) indicator variables. I also conduct ''placebo tests'' to mitigate the possibility that unobservable similarities across firms that have the same audit committee member (chair) drive my test results. Finally, I perform the tests with a subsample of members (chairs) who started their jobs post 2000, and control for board and audit committee characteristics.

My findings extend the literature on audit committee characteristics and financial reporting by documenting the overall effect of audit committee members (chairpersons). The fact that this overall member (chair) effect cannot be fully explained by observable characteristics identified by the existing literature has implication for future research. Specifically, research on individual corporate executives has already started to find ways to measure characteristics that are not directly observable, such as overconfidence (e.g., Malmendier & Tate, 2005) and personality traits (Gay, Ke, Qiu, & Qu, 2017; Gow, Kaplan, Larcker, & Zakolyukina, 2016). The findings of this article suggest that such effort is also worthwhile for research on audit committee members. However, the question of whether such idiosyncratic effects on reporting choices can be diversified away by investors also remains an open area for further research.

Author' Note

All data are available from the public sources described in the article.

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Notes

1. See, for example, Bamber, Jiang, and Wang (2010), Demerjian, Lewis, Lev, and McVay (2010), Dyreng, Hanlon, and Maydew (2010), K. Koh (2011), and Matsunaga and Yeung (2008).
2. Sarbanes–Oxley Act, Section 2(a) (3), 2002.
3. See, for example, ''Rurban Financial Corp. Announces Appointment of Director'' (*Global Newswire*, September 1, 2010) and ''Addvalue Appoints Michael Butler, the Former President and Chief Operating Officer of Inmarsat, as an Additional Independent Director'' (*PRNewswire*, August 31, 2010).
4. The dataset for audit committee members contains 3,010 distinct firms, and the dataset for audit committee chairpersons contains 1,340 firms. See Section ''Sample Construction and Data'' for details.
5. As I find no evidence of audit committee member (chairperson) fixed effects on earnings smoothness, I do not conduct further sensitivity tests on earnings smoothness.
6. See Section ''Placebo tests'' for details on the design and results of the placebo tests.
7. The Business Roundtable (1978), The Role and Composition of the Board of Directors of the Large Publicly Owned Corporations, pp. 10-13.
8. Recent anecdotal evidence suggests that audit committees are paying more attention to the risk management of investments of firms. To the extent that a firm's investment pattern is part of a firm's underlying earnings process that affects its financial reporting outcomes, audit committee member styles might be manifested in the fundamental earnings process. However, such an increased attention has only arisen since the last crisis, and there is still disagreement among audit committee members whether a firm's investment risk management is the responsibility of the audit committee (Johnson, 2011).
9. All variables are defined in detail in Table 1.
10. Of course, one could argue that some members may be more comfortable with management managing earnings upward or downward, in which case signed discretionary accruals would better capture member style. I also examined signed discretionary accruals, and the results (not reported) are robust.
11. The results are robust to defining *SMB* as meeting or beating analyst forecasts by less than 2 or 3 cents.
12. It is possible that a firm meets or beats analyst forecasts by issuing earnings guidance and managing analyst expectations (Matsumoto, 2002). It is also often the audit committee's job to review and discuss with management a firm's earnings guidance information (Karamanou & Vafeas, 2005). I therefore recognize the possibility that *SMB* reflects committee member's style when overseeing earnings guidance as much as earnings management. One could potentially disentangle the two mechanisms by studying the impact of member fixed effects on management forecasts. This is, however, beyond the scope of this article.

13. See, for example, Graham, Harvey, and Rajgopal (2005); Lang, Raedy, and Wilson (2006); Leuz, Nanda, and Wysocki (2003); Myers, Myers, and Skinner (2007).
14. In the entire BoardEx sample, most members or chairpersons serve on one to two committees, as many public firms require that their audit committee members serve on no more than three audit committees simultaneously. The mean/median number of committees a member (chair) serves on is 1.7/1 (2.2/1). In terms of percentage, 17.4% of members and 14.2% of chairpersons have been at two or more firms.
15. It is quite common for a member or chairperson to stay on a committee for more than 3 years: In the entire BoardEx sample, 85.4% of audit committee members and 89.2% of audit committee chairpersons have held their position for more than 3 years.
16. Similar design is also implemented by Bamber et al. (2010), Dyreng et al. (2010), and Ge, Matsumoto, and Zhang (2011).
17. I acknowledge that my sample consisted of audit committee members and chairpersons who have worked at multiple firms. The number of different audit committees a person sits on is often used as a proxy for the person's reputation, and a more reputable chairperson should have stronger influence on the firm. Therefore, I cannot guarantee that my results are generalizable to chairpersons who only sit on one audit committee.
18. Note that BoardEx only contains detailed information on firms' boards from 2000 to 2008. However, for each director, the start dates are available and not truncated at Year 2000. Hence, my member or chairperson-matched panel dates back to 1987, the year of which data on all my control variables are available. To address the concern that my sample is biased toward members or chairpersons who have held their positions for a long period of time, I replicate my main tests with a subsample restricted to chairpersons who have started their jobs in or after 2000. See Section ''Including only members or chairpersons who started in or after 2000'' for a discussion of the results. For some directors, the start/end dates are precise to the exact date, whereas for others only the start/end months and years are available. Thus, if a director has started his or her position less than half a year before the nearest fiscal year end, I set his or her starting year to the next fiscal year. If he or she has started the position more than half a year from the nearest fiscal year end, then I consider him or her starting in that fiscal year.
19. Defined as Standard Industrial Classification (SIC) codes 6000 to 6999.
20. Descriptive statistics for the Compustat firms are not tabulated.
21. The reason why BoardEx typically contains information on large, reputable firms is that its original purpose was fund raising via social networks of the board members. In addition, audit committee members with good reputation are more likely to sit on boards of large firms and on multiple boards (Fich & Shivdasani, 2007). Thus, the requirement that the members or chairpersons in my sample hold their positions in at least two firms would also bias my sample toward larger firms. To the extent that it is more difficult for individuals to imprint their own styles on large firms than on small firms, this bias would be against me finding significant results.
22. All variables are defined in Table 1. I do not control for board and audit committee characteristics for my main tests because BoardEx only has detailed data from 2000 to 2008. Controlling for audit committee characteristics would thus require that all members in my sample have been in at least two firms during the period of 2000 to 2008. To the extent that audit committee and board characteristics are sticky over time, controlling for firm fixed effects would mitigate the concern that audit committee characteristics rather than individual member styles are driving my results. That said, I do control for observable individual audit committee member (chair) characteristics, and the results are presented in Section ''Controlling for Observable Audit Committee Member (Chairperson) Characteristics.'' In addition, I replicate the *F*-tests with a subsample that requires all committee members (chairpersons) start their positions in or after 2000. See Section ''Including only members or chairpersons who started in or after 2000'' for a discussion of the results.

23. Adding CFO fixed effects increases adjusted R^2 by 2 to 3 percentage points in Ge et al. (2011), and adding CEO fixed effects increases adjusted R^2 by 2 to 5 percentage points in Bertrand and Schoar (2003).
24. An alternative approach is to take the average value of the audit committee member characteristics. However, taking the average value would capture the characteristics of the *audit committee*, rather than those of the individual members. Furthermore, as not all audit committee members of each firm are included in the sample (the sample requires that the audit committee members serve at least two firms), even the average value of the characteristics does not capture the full picture of the audit committee. To mitigate the concern that the results in Tables 4 and 5 for audit committee members are driven only by the members who are randomly selected, I run the same tests as in Tables 4 and 5 by randomly selecting from the audit committee members who were not chosen in the first random assignment. The results (untabulated) are robust.
25. The results of the robustness tests on the chairperson sample are all similar to those on the member sample. Therefore, the remainder of this article only tabulates the robustness check results for the member sample.
26. None of the simulated numbers of fixed effects significant at the 10% and 1% levels (not tabulated) exceed the actual frequencies either.
27. In cases where a member has worked at more than two firms, the regression is run with each subsequent firm's placebo residuals as the independent variables and each previous firm's real residuals as the dependent variables. This design is similar to that implemented in the main tests for earnings smoothness (Panel B of Table 3).
28. This finding is similar to Ge et al. (2011): Using discretionary accruals, they find that the coefficient is not statistically significant for either the real data or the placebo data.

Supplemental Material

Supplementary material is available online for this article.

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