5-2018

Audit Committee Reputation Incentives

Justin Cole Short
University of Tennessee

To the Graduate Council:

I am submitting herewith a dissertation written by Justin Cole Short entitled "Audit Committee Reputation Incentives." I have examined the final electronic copy of this dissertation for form and content and recommend that it be accepted in partial fulfillment of the requirements for the degree of Doctor of Philosophy, with a major in Business Administration.

Linda A. Myers, Major Professor

We have read this dissertation and recommend its acceptance:

Donald J. Bruce, Lauren M. Cunningham, Terry L. Neal

Accepted for the Council:

Dixie L. Thompson

Vice Provost and Dean of the Graduate School

(Original signatures are on file with official student records.)

Audit Committee Reputation Incentives

A Dissertation Presented for the
Doctor of Philosophy
Degree
The University of Tennessee, Knoxville

Justin Cole Short
May 2018

DEDICATION

This work is dedicated to my wife, Alexandra Gellis. I could not have completed this degree without your unconditional love and encouragement. My future is all the more promising with you in it.

This work is also dedicated to my late grandmother, Ruby A. Ragsdale. She passed away before I completed my doctoral program. The example of perseverance and tenacity that she set for me made my completion of this program possible. Although she is gone, she knew I would complete this endeavor.

ACKNOWLEDGEMENTS

I gratefully acknowledge the support of my dissertation committee: Linda Myers (Chair), Lauren Cunningham, Terry Neal, and Don Bruce. Their advice and expertise was a tremendous resource to me in completing this dissertation. I especially thank Linda and Lauren for their personal mentorship of me during my time in the PhD program. The encouragement and support they provided was invaluable. I also thank Terry for having confidence that I could complete a doctoral program and admitting me as doctoral student. I thank Joe Carcello for taking an interest in me while I served as his graduate teaching assistant as a Master's student. He sparked my interest in research and doctoral studies, and I might not have pursued a Ph.D. if it were not for him. I thank my parents, Lorenzo Short Sr. and Pamela Short. I could not have completed this degree without the constant support that each of you gave me. I also thank my brother, Lorenzo Short, Jr., and my sister, Tanya Washington, for their encouragement during my doctoral studies. I also acknowledge support from my in-laws: Ian Gellis, Maria Gellis, and Danny Gellis. They provided a home away from home for me during my time in Knoxville. I greatly appreciate feedback and helpful suggestions from my fellow doctoral students. Finally, I am grateful for the financial support provided by the University of Tennessee, the Haslam School of Business, the AICPA Foundation, and the KPMG Foundation.

ABSTRACT

The demand for qualified directors to serve in audit committee chair and designated financial expert positions has grown in recent years, increasing the number of these directors that serve on multiple audit committees. Past research has examined the effect of these directors holding multiple audit committee seats on audit committee effectiveness, but no studies to date have examined how these directors allocate their monitoring effort across their multiple audit committee seats. Using a sample of audit committee chairs and financial experts that serve on multiple audit committees from 2004-2014, I examine whether the reputation incentives for these directors are associated with audit committee effectiveness at the firms they serve. Reputation incentives theory suggests that these directors will allocate more monitoring effort to the firms in their portfolio that offer them a greater opportunity to enhance their reputation as a monitor (higher reputation incentives). Consistent with this theory, I find that audit committee effectiveness is higher at firms that offer these directors high reputation incentives as compared to firms that do not. My results suggest that these directors exert varying levels of monitoring effort based on the relative importance of any one audit committee to their portfolio of audit committees. My findings should be of interest to boards, investors, and regulators considering the implications of service on multiple audit committees.

TABLE OF CONTENTS

LIST OF TABLES

I. INTRODUCTION

Economic theory posits that the reputation incentives of players influence their actions (Wilson 1985; Weigelt and Camerer 1988). As it relates to situations involving agency problems, analytical research presents strong support for the theory that reputation incentives can induce the agent to act in the interest of the principal (Fama 1980; Stiglitz and Weiss 1983; Kose and Nachman 1985; Diamond 1989, 1991). Empirical research supports this notion and finds that reputation incentives affect the actions of various agents including auditors (Reynolds and Francis 2000; Larcker and Richardson 2004), analysts (Jackson 2005; Ljungqvist et al. 2007), and underwriters (Carter and Manaster 1990; Carter, Dark, and Singh 1998).

Recent studies examine the effect of the reputation incentives of directors with multiple directorships on firm performance (Masulis and Mobbs 2014) and firm cost of debt capital (Huang et al. 2017). However, there is no research to date examining the effect of the reputation incentives of such directors on financial reporting quality (FRQ).[1] In this study, I examine whether the reputation incentives of two director roles in particular - the audit committee chair and the designated financial expert (collectively, "key audit committee members") affect FRQ. The audit committee is the primary corporate governance mechanism put in place to monitor the accounting and financial reporting processes at public companies (Sarbanes-Oxley Act [SOX] 2002; Beasley et al. 2009). Because audit committee chairs and designated financial experts are the primary individuals driving the committee's efforts to monitor FRQ (DeFond et al. 2005; Carcello et al. 2011a; National Association for Corporate Directors [NACD] 2014; Tanyi and Smith 2015), examining whether the reputation incentives of these directors that serve on

[1] Cao et al. (2012) examine the effect of company reputation on FRQ. While they do not examine the reputation effects of any one agent of the firm, they acknowledge that the effect of company reputation likely manifests itself through the actions of various agents including directors, executives, or auditors.

multiple audit committees affect FRQ is important. Any effect on FRQ is important because FRQ can affect the efficiency of a firm's capital allocation decisions (Biddle et al. 2009), stock liquidity (Daske et al. 2008), cost of capital (Francis et al. 2004), and even audit fees (Abbott et al. 2006; Feldmann et al. 2009).

Reputation incentives theory, in the context of corporate directors, suggests that a director's reputation is the strongest incentive that motivates a director to be an effective monitor because reputation affects a director's marketability and opportunities to gain additional directorships in the future (Fama 1980; Fama and Jensen 1983; Yermack 2004; Srinivasan 2005; Fich and Shivdasani 2007). Because there is a strong incentive to build a reputation as an effective monitor, directors with multiple directorships should exert the most monitoring effort to their directorships offering them the most prestige and the most visibility to build a reputation as an effective monitor (Masulis and Mobbs 2014). Thus, as it relates to key audit committee directors, reputation incentives theory supports the notion that these directors that serve on multiple audit committees will exert more monitoring effort on the audit committees offering them the highest reputation incentives, leading to higher FRQ. This study examines whether there is empirical evidence to support this notion.

Using BoardEx data from 2004-2014, I identify all directors that are audit committee chairs or designated financial experts. I restrict my analysis to the directors that serve on multiple boards in key audit committee roles and, following Masulis and Mobbs (2014), I use firm size relative to the size of other companies that the director serves as a proxy for reputation incentives.[2] I hold the director constant using director fixed effects and estimate analyses at the director-firm-year level, so that FRQ is relative to other boards on which the director serves in

[2] To ensure that the additional board assignment is significant, I do not count firms with less than $1,000,000 in total assets or firms that are a subsidiary of a company that the director serves as an additional board.

the same fiscal year.[3] I use misstatements of annual financial statements, material weaknesses in internal controls over financial reporting quality, performance-adjusted discretionary accruals, and the F-Score as proxies for FRQ. On average, I find that even after controlling for absolute firm size and a host of other firm characteristics, firms that offer key audit committee directors high reputation incentives have significantly higher FRQ, indicating higher audit committee effectiveness. These results are robust to several alternative measures of reputation incentives.

I perform cross-sectional analysis to investigate whether the effect of director reputation incentives on FRQ differs between smaller firms and larger firms. I find that my results are driven by smaller firms. This suggests that director reputation incentives do not matter for FRQ at the largest firms, likely because those firms may have good FRQ regardless of the relative level of reputation incentives offered to key audit committee directors. Director reputation incentives only matter for FRQ at smaller firms that rely more on the input and effort of key audit committee directors.

This study contributes to several streams of literature in accounting and corporate governance. First, this study contributes to the audit committee effectiveness literature by documenting an attribute of the audit committee beyond expertise and independence that has an impact on how effective the audit committee is at monitoring FRQ. Second, this study contributes to the director reputation literature. The director reputation literature has documented that the reputation incentives of independent directors with multiple directorships affect firm performance and cost of capital (Masulis and Mobbs 2014; Huang et al. 2017). My study extends this literature and documents a positive relation between the reputation incentives of key audit committee directors that serve on multiple audit committees and another firm outcome - financial

[3] Since I am only examining directors that serve on two or more boards, each director is associated with at least two different firms in each year.

reporting quality. Finally, because my study examines reputation incentives in a setting where key audit committee directors serve on multiple audit committees, I indirectly contribute to the literature on director busyness. Past studies on director busyness measure busyness by adding the total number of directorships held, and implicitly assume that directors allocate their monitoring effort equally across each of their directorships (Fich and Shivdasani 2006; Sharma and Iselin 2012; Masulis and Mobbs 2014; Tanyi and Smith 2015). My results offer a more intricate view into effort allocation and show that directors serving on multiple audit committees distribute their monitoring effort based on the company's relative contribution to their reputation.

This study has implications for practice as well. Over the last decade, proxy advisory firms and investors have expressed concerns about directors becoming too busy from being over-boarded (ISS 2015a; ISS 2015b). These concerns have become particularly relevant to the audit committee, where the bulk of the increase in workload has occurred since the Sarbanes-Oxley Act (Spencer Stuart 2015, 26). This study offers another factor for boards, proxy advisory firms, and investors to consider when evaluating the number of boards that directors serve. Boards at smaller public companies should consider the other firms that any potentially new audit committee directors serve on before they appoint them. While appointing an audit committee director from another larger, more visible firm may seem appealing, it may not result in a more effective audit committee for such firms. Along the same lines, smaller public companies might benefit from setting clear restrictions on *both* the number and the *scale* of outside commitments they will allow existing directors to have while they serve on the board. The relative size of the company compared to the other companies that a director serves can act as a signal to investors and boards about the potential quality of financial reporting monitoring that will be provided.

The remainder of the paper is organized as follows: Section II provides a literature review and develops my hypotheses. Section III discusses my empirical models and sample construction. Section IV presents my main results and the results of additional tests. Finally, Section V concludes.

II. BACKGROUND AND HYPOTHESIS DEVELOPMENT

Reputation Literature Review

Past research uses game theory to show that the reputation of players influences their actions (Wilson 1985; Weigelt and Camerer 1988). In a game where a participant holds inside information about his "type," other participants determine his type by evaluating the participant's reputation, which is based on his past actions. The participant knows this and chooses his actions carefully to maximize his utility. This effect that reputation has on the chosen action of the participant is referred to as the "reputation effect" or "reputation incentives."[5] Analytical research has examined reputation incentives as a mechanism to mitigate agency problems and has found that reputation incentives can strongly motivate the agent to act in the interest of the principal (Fama 1980; Holmstrom 1982; Stiglitz and Weiss 1983; Kose and Nachman 1985; Diamond 1989, 1991; Gomes 2000).

Empirical research also supports the notion that reputation incentives affect the actions of various agents. For example, past empirical work finds that, due to reputational concerns, analysts are less optimistic in their earnings forecasts (Jackson 2005), drop their buy recommendations for stocks more abruptly (Fang and Yasuda 2011), and keep their stock evaluations consistent after they transition to new employers (Clarke et al. 2007). Underwriters and brokerage firms act in a manner indicative of reputation preservation as well (Jo et al. 2007; Ljungqvist et al. 2007).

Auditing research finds that reputation incentives are important for auditors. Damage to the reputation of an audit firm can lead to significant financial downsizing at the audit firm due to loss of clients (Barton 2005; Jensen 2006). Audit firms know this and act accordingly to

[5] Recent work on director reputation refers to this effect as "reputation incentives," so that is how I refer to this effect throughout the paper.

preserve their reputation in the market for audit services. For example, auditors are more conservative in their audit approach for their relatively larger, more important clients and are less pliable in their decision of whether to permit them to use abnormal accruals to manage earnings (Reynolds and Francis 2000; Chung and Kallapur 2003; Larcker and Richardson 2004). There is also experimental work that supports the argument that auditors take steps to defend and protect their reputation (Mayhew 2001).

Most directly relevant to this study is the stream of literature focusing on the reputation incentives of corporate directors. As discussed above, analytical research argues that reputation is one of the strongest motivators for agents, or directors in this case, to act in the interest of the principal (Fama 1980). Consistent with this argument, empirical research finds evidence of reputational penalties for directors at companies experiencing financial fraud and accounting failures (Srinivasan 2005; Fich and Shivdasani 2007; Brochet and Srinivasan 2014). Other studies find negative effects on director reputation when companies cut dividend payments (Kaplan and Reishus 1990), experience poor financial condition (Gilson 1990), go through liquidation (Harford 2003), or report poor performance (Yermack 2004). More recent research examines how directors with multiple directorships allocate monitoring effort, knowing that these reputation penalties can occur for poor monitoring. Masulis and Mobbs (2014) find that independent directors with multiple directorships allocate more monitoring effort to their relatively larger, more important firms, resulting in higher performance and higher likelihood of forced CEO departure following poor performance at these firms. They do this, presumably, because good monitoring at their more important firms will likely make a greater contribution to their reputation as an effective monitor.

While Masulis and Mobbs (2014) provide evidence that the reputation incentives of directors with multiple directorships can affect firm performance, there is no evidence about whether the reputation incentives of directors with multiple directorships affect financial reporting quality. In this study, I fill that gap by specifically examining whether directors that sit on multiple audit committees allocate their monitoring effort unevenly across those audit committees.

Demand for Monitors of Financial Reporting and Multiple Directorships

The passage of the Sarbanes-Oxley Act (SOX) in 2002 brought about numerous regulations aimed at improving corporate governance at publicly traded companies in the U.S. Many of these regulations were focused on making parties that play a key role in the financial reporting process more effective, including the audit committee. After SOX passed, demand for directors with the financial expertise that is required to serve on an audit committee increased significantly (DeFond et al. 2005; Engel et al. 2010). At the same time, the required workload and risk for these directors increased as well. Audit committees meet much more frequently and for longer periods of time since SOX was passed and liability insurance premiums for directors are higher as well (Linck et al. 2008; Beasley et al. 2009). This, coupled with stringent audit committee independence rules that were mandated by SOX, decreased the supply of qualified and eligible directors that could serve on an audit committee (Linck et al. 2008). As a result, many companies were faced with a limited pool of potential candidates from which they could select directors for the audit committee, causing an increase in the number of directors that serve on multiple audit committees (Tanyi and Smith 2015).

Instances of directors serving on multiple boards in general, or director "busyness", has caused concerns from investors, corporate governance activists, and academics that these

directors may be stretching themselves too thin (ISS 2015a; ISS 2015b; Ferris et al. 2003; Fich and Shivdasani 2006). Further, these concerns have become particularly relevant to the audit committee, where the bulk of the increase in workload has occurred since the Sarbanes-Oxley Act (Audit Committee Leader Network [ACLN] 2011; Spencer Stuart 2015, 26). Recent research examines the effect of audit committee director busyness on audit committee effectiveness. Sharma and Iselin (2012) and Tanyi and Smith (2015) both find that audit committee busyness is associated with lower audit committee effectiveness. However, my study differs in that I am not examining busyness. Rather than examining the effect of serving on multiple audit committees (i.e., comparing directors on multiple audit committees to directors on one audit committee), I restrict my sample to directors serving on at least two audit committees and examine how they allocate their monitoring effort across the multiple audit committees they serve, and control for the total number of audit committee directorships.

Audit Committee Effectiveness Literature Review

The audit committee is the primary governance mechanism put in place to monitor the accounting and financial reporting processes at public companies (Blue Ribbon Committee [BRC] 1999; Sarbanes-Oxley Act [SOX] 2002; Gendron and Bedard 2006; Beasley et al. 2009). There is a large body of research examining the role of the audit committee in monitoring the financial reporting process. Many of these studies focus on characteristics of the individuals serving on the audit committee.

Various studies have focused on the independence of the audit committee. Klein (2002) documents a negative association between audit committees being comprised of a majority of independent directors and abnormal accruals. Abbot et al. (2004) find that the presence of a fully independent audit committee is negatively associated with restatements. Carcello et al. (2011b)

examine independence from a different aspect and find that audit committee independence, as defined in earlier studies, does not decrease the likelihood of restatements when the CEO of the firm is involved in director selection. Similarly, Bruynseels et al. (2014) and Cassell et al. (2017) examine independence differently than earlier studies. Bruynseels et al. (2014) document that firms at which the audit committee members have social ties to the CEO purchase fewer audit services and engage more in earnings management. Cassell et al. (2017) measure audit committee independence using the proportion of the committee that is co-opted (appointment of audit committee members after the current CEO) and find a positive relation between audit committee co-option and misstatements as well as between audit committee co-option and absolute discretionary accruals.[6]

Numerous studies have also examined the effect of the expertise of members of the audit committee. A few of the studies mentioned previously that examine audit committee independence also examine audit committee financial expertise and find that audit committee financial expertise is positively associated with audit committee effectiveness (Abbot et al. 2004; Carcello et al. 2011b). Agrawal and Chadha (2005) document that the presence of an independent financial expert on the audit committee is negatively associated with restatements. Krishnan and Visvanathan (2008) distinguish between different types of financial expertise and find that accounting financial expertise is positively associated with accounting conservatism, while the more general financial expertise defined by the SEC in SOX is not significantly

[6] Other studies examine the effect of audit committee independence on auditor contracting and auditor reporting outcomes rather than directly examining financial reporting quality. For example, Abbot et al. (2003) examines the effect of audit committee independence on audit fees. Also, Carcello and Neal (2000) examine how audit committee independence affects the probability the auditor will issue a going concern report for a financially distressed firm, and Carcello and Neal (2003) examine how audit committee independence affects the likelihood the auditor will be dismissed after a first time going concern report for the audit client.

associated with conservatism. Dhaliwal et al. (2010) find that audit committees with both non-accounting financial expertise and accounting financial expertise are most effective at constraining accruals management as compared to audit committees with only one type of financial expertise. Lisic et al. (2016) find that audit committee financial expertise is negatively associated with instances of internal control weaknesses, but that this affect no longer exists when the CEO is extremely powerful. Similarly, Badolato et al. (2014) find that the positive effect of audit committee financial expertise on earnings quality is significantly weaker when audit committee members have lower relative status compared to management. Other types of audit committee expertise that have been found to improve audit committee effectiveness are industry specific expertise (Cohen et al. 2010), legal expertise (Krishnan et al. 2011), and auditing expertise, as measured by experience as an audit partner (Naiker and Sharma 2009).[7]

Most relevant to my study is the recent research examining the effect of audit committee director busyness on audit committee effectiveness. Sharma and Iselin (2012) and Tanyi and Smith (2015) both document a negative association between audit committee busyness and audit committee effectiveness. As stated previously, my study differs in that I am not examining the effect of serving on multiple audit committees. My sample only contains directors that serve on at least two audit committees and I examine how they allocate their monitoring effort across the multiple audit committees that they serve.

Development of Hypotheses

Past work on director reputation documents that directors have a strong incentive to develop a reputation as an effective monitor so that they can obtain more board seats in the future (Yermack 2004). Directors face reputational penalties in the director labor market when severe

[7] Other studies that examine the effect of additional attributes of the audit committee on financial reporting quality include Xie et al. (2003), Krishnan (2005), Vafeas (2005), Archambeault et al. (2008), and Campbell et al. (2015).

monitoring failures occur (Gilson 1990; Harford 2003; Fich and Shivdasani 2007), and this is particularly true when financial reporting failures occur (Srinivasan 2005; Brochet and Srinivasan 2014). Thus, directors that hold multiple directorships must strategically allocate their monitoring effort across their directorships to maximize their reputation. Fama and Jensen (1983) argue that larger firms provide greater visibility, prestige, and reputation value to the directors at those firms, thereby increasing the reputation incentive for directors to be effective monitors at those firms. If potential to build reputation and visibility is greater at larger firms, then directors on multiple boards should exert more monitoring effort at the relatively larger firms in their portfolio of board seats (Masulis and Mobbs 2014).

I argue that in the case of directors that serve on multiple audit committees, directors will allocate more of their monitoring effort to the audit committees at the relatively larger, more important firms in their portfolio because these firms offer the director higher reputation incentives. My hypothesis, stated in the alternative, is:

> *H1: Directors that serve on multiple audit committees exert more monitoring effort on the audit committees at firms that offer relatively higher reputation incentives in their portfolio of audit committee seats, as evidenced by higher FRQ.*

III. SAMPLE SELECTION AND METHODOLOGY

Sample Selection and Data

I focus on audit committee chairs and designated financial experts because these individuals drive the financial reporting monitoring activities of the audit committee (DeFond et al. 2005; Beasley et al. 2009; Carcello et al. 2011a; National Association for Corporate Directors [NACD] 2014; Tanyi and Smith 2015). The audit committee chair sets the agenda in preparation for committee meetings, coordinates communication between the auditor and management, and keeps the remainder of the board informed on the audit committee's work (KPMG 2015; Audit Committee Leadership Network [ACLN] 2017). The designated financial expert is also a key member on the audit committee. The importance of the financial expert is evidenced by the SOX mandate that companies disclose whether they have a designated financial expert on the audit committee and, if not, to explain why. Also, as discussed previously, there is a sizeable body of research that supports the notion that the presence of a financial expert on the audit committee is an important factor in determining audit committee effectiveness (Agrawal and Chadha 2005; Abbot et al. 2004; Krishnan and Visvanathan 2008; Dhaliwal et al. 2010; Carcello et al. 2011b). Audit committee chairs and financial experts are the directors held most accountable for monitoring FRQ, so their reputation will be most negatively affected if there is a financial reporting failure. Thus, I restrict my analysis to these directors because the reputation incentives for them are most salient.[8]

[8] To provide anecdotal context to the academic literature, I spoke with an experienced audit committee member of several public companies. The audit committee member revealed that the most accountable members of the audit committee are the chair and the designated financial expert. Audit committee chairs receive extra compensation for being the chair, which is indicative of a higher level of accountability. Furthermore, in serious financial reporting failures, the chair has been singled out and named individually in litigation (LaCroix 2014).

To form my sample, I identify all director-firm-years that represent an audit committee chair (AC CHAIR) or designated financial expert (FINEXP) covered by Compustat, Audit Analytics, and BoardEx for fiscal years 2004 through 2014 with all necessary data.[9] I drop regulated firms (following Reichelt and Wang 2010) and create a director-firm-year level datatset of all observations where the director is either the designated financial expert or the audit committee chair for at least two firms in my sample. This results in 3,140 firm-years in the misstatement sample, 2,747 firm-years in the F-Score sample, 2,129 firm-years in the material weaknesses sample, and 2,779 firm-years in the accruals sample. My sample selection process is described further in Table 1.

Methodology

I follow prior research and proxy for low financial reporting quality using misstatements (Palmrose et al. 2004; Desai et al. 2006; Dechow et al. 2010; Cao et al. 2012), high F-Scores (Dechow et al. 2011; Wang et al. 2015; Bradley et al. 2017), higher levels of the absolute value of discretionary accruals (Myers et al. 2003; Dechow et al. 2010; Cao et al. 2012), and material weaknesses in internal control (Dechow et al. 2010; Costello and Wittenberg-Moerman 2011; Garrett et al. 2014). I test *H1* by estimating the following equations:

[9] In most cases, the designated financial expert is the same individual that serves as the audit committee chair. However, there are instances where the two roles are held by two different directors. If the two roles are held by different directors and *both* directors serve on multiple audit committees, then there will be repeated firm-year observations for that firm. This occurs for only a very small portion of my sample (95 duplicate firm-years). Dropping these observations does not change my results and inferences.

$$
\begin{aligned}
MISSTATE_{dit}\ or\ & \\
HIGH\_FSCORE_{dit} &= \alpha_0 + \alpha_1 HIGH\_REP_{dit} + \alpha_2 SIZE_{dit} + \alpha_3 MTB_{dit} + \alpha_4 ROA_{dit} \\
&+ \alpha_5 LOSS_{dit} + \alpha_6 LEV_{dit} + \alpha_7 AR\_INV_{dit} + \alpha_8 BIG4_{dit} \\
&+ \alpha_9 AUD\_IMPORT_{dit} + \alpha_{10} IND\_SPECIALIST_{dit} + \alpha_{11} BUS\_SEG_{dit} \\
&+ \alpha_{12} RESTRUCTURE_{dit} + \alpha_{13} M\&A_{dit} + \alpha_{14} FOREIGN_{dit} \\
&+ \alpha_{15} BD\_INDEP_{dit} + \alpha_{16} BD\_SIZE_{dit} + \alpha_{17} AC\_SIZE_{dit} \\
&+ \alpha_{18} NUM\_AC_{dit} + \alpha_{19} DIR\_TENURE_{dit} + \alpha_j YEARFE + \alpha_k INDFE \\
&+ \alpha_L DIRFE + \varepsilon_{dit} \qquad (1)
\end{aligned}
$$

$$
\begin{aligned}
MWEAK_{dit} &= \beta_0 + \beta_1 HIGH\_REP_{dit} + \beta_2 SIZE_{dit} + \beta_3 MTB_{dit} + \beta_4 ROA_{dit} + \beta_5 LOSS_{dit} \\
&+ \beta_6 LEV_{dit} + \beta_7 AR\_INV_{dit} + \beta_8 BIG4_{dit} + \alpha_9 AUD\_IMPORT_{dit} \\
&+ \beta_{10} IND\_SPECIALIST_{dit} + \beta_{11} BUS\_SEG_{dit} \\
&+ \beta_{12} RESTRUCTURE_{dit} + \beta_{13} M\&A_{dit} + \beta_{14} FOREIGN_{dit} \\
&+ \beta_{15} BD\_INDEP_{dit} + \beta_{16} BD\_SIZE_{dit} + \beta_{17} AC\_SIZE_{dit} \\
&+ \beta_{18} NUM\_AC_{dit} + \alpha_{19} DIR\_TENURE_{dit} + \beta_{20} AGE_{dit} \\
&+ \beta_{21} SALES\_GROWTH_{dit} + \beta_j YEARFE + \beta_k INDFE \\
&+ \beta_L DIRFE + e_{dit} \qquad (2)
\end{aligned}
$$

$$
\begin{aligned}
ABSDA_{dit} &= \chi_0 + \chi_1 HIGH\_REP_{dit} + \chi_2 SIZE_{dit} + \chi_3 MTB_{dit} + \chi_4 ROA_{dit} \\
&+ \chi_5 LOSS_{dit} + \chi_6 LEV_{dit} + \chi_7 AR\_INV_{dit} + \chi_8 BIG4_{dit} \\
&+ \chi_9 AUD\_IMPORT_{dit} + \chi_{10} IND\_SPECIALIST_{dit} + \chi_{11} BUS\_SEG_{dit} \\
&+ \chi_{12} RESTRUCTURE_{dit} + \chi_{13} M\&A_{dit} + \chi_{14} FOREIGN_{dit} \\
&+ \chi_{15} BD\_INDEP_{dit} + \chi_{16} BD\_SIZE_{dit} + \chi_{17} AC\_SIZE_{dit} \\
&+ \chi_{18} NUM\_AC_{dit} + \alpha_{19} DIR\_TENURE_{dit} + \chi_{20} VOL\_CF\_OP_{dit} \\
&+ \chi_{21} LAG\_ABSDA_{dit} + \chi_j YEARFE + \chi_k INDFE + \chi_L DIRFE + \varpi_{dit} \qquad (3)
\end{aligned}
$$

where the dependent variable in Equation (1) is either *MISSTATE* (an indicator variable equal to one if any of the core accounts in the year *t* annual financial statements of firm *i* were misstated, as identified in a future restatement from Audit Analytics' Non-Reliance database, and zero otherwise) or *HIGH_FSCORE*, (an indicator variable equal to one if the F-Score for firm *i* in year *t*, as calculated in Dechow et al. (2011), is higher than 1.85).[10] The dependent variable in

[10]To classify core and non-core misstatements, I follow Pittman and Zhao (2017) and classify a core accounting misstatement as one where the "res_acc_res_fkey_list" field in Audit Analytics includes any of the following: 1, 3, 4, 6, 7, 12, 14, 20, 21 23, 29, or 42. Pittman and Zhao (2017) follow Palmrose and Scholz (2004) and Cassell, Dreher, and Myers (2013) in capturing core accounting issues as those related to revenue, cost of sales, operating expenses, etc. The F-Score is the calculated probability of a firm misstating the financial statements so egregiously that the firm receives an Accounting and Auditing Enforcement Release (AAER) from the SEC. It measures the likelihood of fraudulent financial reporting. This measure allows me to observe firms that likely have serious financial reporting irregularities, regardless of whether or not the SEC identifies the firm and issues an AAER to the firm. To calculate the F-score, the predicted probability is derived as $e^{PV} / (1 + e^{PV})$ divided by the unconditional probability of an AAER (0.0037), where PV is the predicted value from model 1 in Dechow et al. (2011): Predicted

Equation (2) is *MWEAK* (an indicator variable equal to one if the auditor for firm *i* reported a material weakness in internal control in year *t*, identified using Audit Analytics' SOX 404 database, and zero otherwise). The dependent variable in Equation (3) is *ABSDA* (the absolute value of discretionary accruals for firm *i* in year *t*, estimated using the performance-adjusted modified Jones model (Jones 1991; Dechow et al. 1995) following Kothari et al. (2005).[11] The variable of interest is *HIGH_REP*, an indicator variable equal to one if firm *i* is the largest, or within 10% of the largest, directorship that the director *d* holds (as measured by market capitalization of the firm), and zero otherwise.[12] *HIGH_REP* is a proxy for high reputation incentives *relative* to the other firms served by the same director *d*. Thus, to ensure that the coefficient on *HIGH_REP* is relative to the other firms served by the same director *d*, I include director fixed effects in my model. I estimate the *MISSTATE, HIGH_FSCORE,* and *MWEAK* models as linear probability models and estimate the *ABSDA* model using ordinary least squares

Value = -7.893 + 0.790*rsst_acc + 2.518*ch_rec + 1.191*ch_inv + 1.979*soft_assets + 0.171*ch_cs - 0.932*ch_roa + 1.029*issue. All terms are as defined in Dechow et al. (2011). Dechow et al. (2011) classify firms with an F-Score greater than 1.85 as a firm with "substantial risk" or "high risk" of receiving an AAER from the SEC.

[11] Using all firms in Compustat with available data, I estimate the absolute value of discretionary accruals (*ABSDA*) cross-sectionally by year and two-digit SIC industry following Kothari et al. (2005). Thus, I estimate the performance-adjusted modified Jones model (Jones 1991; Dechow et al. 1995) by including lagged return on assets, and retaining only those industry-years with a minimum of 10 observations. The model is as follows: $TA_{it} = \gamma_1(1/A_{it-1}) + \gamma_2((\Delta S_{it} - \Delta AR_{it})/A_{it-1}) + \gamma_3(PPE_{it}/A_{it-1}) + \gamma_4(ROA_{it-1}) + \zeta_{it}$. To maximize data retention, I calculate total accruals (*TA*) using the cash flow method (i.e., income before extraordinary items minus operating cash flows from continuing operations (Hribar and Collins 2002), and if the data necessary to calculate the cash flow method are missing, I set *TA* equal to total accruals following the balance sheet method in Kothari et al. (2005) (i.e., change in non-cash current assets minus the change in current liabilities excluding the current portion of long-term debt, minus depreciation and amortization, scaled by lagged total assets). This substitution method is based on Wilson (2009). *A* is equal to total assets; *ΔS* is equal to the change in total sales revenue from the prior year; *ΔAR* is equal to the change in accounts receivable from prior year; *PPE* is equal to property, plant, and equipment; and *ROA* is equal to net income divided by lagged total assets. *ABSDA* is equal to the absolute value of the residual (ζ).

[12] I use 10% because Masulis and Mobbs (2014) use this threshold. However, in later sensitivity tests, I examine whether my results are sensitive to using different thresholds. See Appendix B for a detailed example of how my measure is constructed.

regression, with robust standard errors clustered by firm.[13] The variables are defined in detail in Appendix A.

Control Variables

For the *MISSTATE* model in Equation (1), I control for variables that have been found to affect the likelihood of a misstatement. Because larger firms are less likely to misstate financial statements, and my variable of interest is constructed based on *relative* size of the firm, I control for the *absolute* size (*SIZE*) of the firm. Because more complex firms are more likely to misstate financial statements, I also control for complexity (*RESTRUCTURE*, *FOREIGN*, *M&A*, *BUS_SEG*) of the firm (Cao et al. 2012; DeHaan et al. 2013). I control for the financial condition of the firm (*LOSS, LEV, ROA*) because financially weak firms are more likely to misstate financial statements (Cao et al. 2012; DeHaan et al. 2013). I control for expected growth (*MTB*) because it is positively associated with misstatements (Cao et al. 2012; DeHaan et al. 2013), and for the proportion of assets in receivables and inventory (*AR_INV*) because misstatements are more likely when this proportion is higher (Cao et al. 2012). I control for characteristics of the auditor (*BIG4, AUD_IMPORT, IND_SCPECIALIST*) because auditors are an important determinant of FRQ (Reynolds and Francis 2000; Reichelt and Wang 2010). I control for governance characteristics related to the likelihood of misstatements (*AC_SIZE*, *BD_INDEP, BD_SIZE*) (Cao et al. 2012). I also include the number of audit committees that the director serves on (*NUM_AC*) and director tenure (*DIR_TENURE*) in my model because both have been found to be related to FRQ (Sharma and Iselin 2012; Tanyi and Smith 2015). I include year fixed

[13] Even though *MISSTATE, HIGH_FSCORE,* and *MWEAK* are dichotomous variables, I use linear probability models, as opposed to a non-linear model, because the latter would drop observations where there is no variation in the dependent variable within one of my fixed effect categories (i.e., industry and year). Moreover, Wooldridge (2010) supports the use of linear probability models when estimating the average partial effects of explanatory variables on a binary outcome variable, which is my main objective in Equations (1) and (2).

effects to control for trends in misstatement rates over time (*YEARFE*) and industry fixed effects because firms in some industries could be more likely to misstate (INDFE). I use this same equation for the *HIGH_FSCORE* model, since it is a measure of the likelihood of fraudulent financial misreporting. The measure is similar in nature to my misstatement measure, but is different in that it captures the likelihood of financial statement irregularities so egregious that the firm receives an AAER from the SEC.

In Equation (2), I control for the variables from Equation (1) but add the following control variables that predict material weaknesses in Doyle et al. (2007): company age (*AGE*) and sales growth (*SALES_GROWTH*).

I include the same set of control variables from Equation (1) in Equation (3) because discretionary accruals is another measure of FRQ so any relations could be similar. I also control for factors commonly included in discretionary accruals models. Specifically, I also control for volatility of cash flows from operations (*VOL_CF_OP*) and lagged discretionary accruals (*LAG_ABSDA*) (Reichelt and Wang 2010).

IV. RESULTS

Descriptive Statistics and Univariate Tests

Panel A and Panel B of Table 2 report descriptive statistics for my sample. Panel A reports statistics at a director-firm-year level. My variable of interest, *HIGH_REP*, has a reported mean of 0.48, so about half of the companies in my sample offer the director relatively high reputation incentives compared to the other companies that the director serves. Panel B reports descriptive statistics at a director-year level. The mean of the number of audit committees that an individual director serves (*NUM_AC*) is 2.37. By construction of my sample, all directors serve on the audit committee of at least two different companies. The 75th percentile of *NUM_AC* is 3.00, indicating that there is a considerable number of directors that serve on three audit committees. Each director has at least one high reputation incentive company (*NUM_HIGH_REP*) and at least one non-high reputation incentive company (*NUM_NOT_HIGH_REP*) at which they sit on the audit committee. The 75th percentile of *NUM_HIGH_REP* and *NUM_NOT_HIGH_REP* is 1.00 and 2.00, respectively. This indicates that most of the time, directors have only one firm that offers them high reputation incentives, and if the director happens to serve on more than two audit committees, then they usually have one high reputation incentive firm and multiple non-high reputation incentive firms.

Panel A and Panel B of Table 3 report descriptive statistics on the financial reporting quality measures in my various samples for firms that are high reputation incentive firms (*HIGH_REP* = 1) and firms that are not high reputation incentive firms (*HIGH_REP* = 0). The first column in Panel A reports that the likelihood of a misstatement, *MISSTATE*, is not significantly different for high reputation incentive firms (6 percent) compared to firms that are not high reputation incentive firms (6 percent). The means of the two partitions for *MISSTATE* is

consistent with past research examining misstatements (Cao et al. 2012). The second column in Panel A reports that the probability that the F-Score is greater than 1.85, *HIGH_FSCORE*, is significantly lower for high reputation incentive firms (8 percent) compared to firms that are not high reputation incentive firms (9 percent). The means of *HIGH_FSCORE* for the two sample partitions are consistent with Dechow et al. (2011).[14] The first column of Panel B shows that the likelihood of material weakness, *MWEAK*, is significantly lower for high reputation incentive firms (4 percent) compared to firms that are not high reputation incentive firms (6 percent). The means of the two partitions for *MWEAK* are consistent with past research examining material weaknesses (Garrett et al. 2014). The second column of Panel B reports the results for discretionary accruals, *ABSDA*, and shows that *ABSDA* is significantly lower for high reputation incentive firms (0.05) compared to firms that are not high reputation incentive firms (0.06). The means are generally consistent with Kothari et al. (2005). In summary, *H1* is supported, on a univariate basis, using three of my four measures of audit committee effectiveness in monitoring FRQ.

Each column in Panel A and Panel B of Table 3 shows univariate tests for the control variables. Univariate tests consistently show that high reputation incentive firms (*HIGH_REP* = 1) are quite different from firms that that are not considered high reputation incentive firms (*HIGH_REP* = 0). As expected, size is significantly different between the two groups. High reputation incentive firms are significantly larger than low reputation incentive firms, which illustrates the importance of controlling for absolute size in my multivariate analysis in the next section. Additionally, high reputation incentive firms are more complex, have better

[14] Dechow et al. (2011, 63) details that 10 percent of the 132,967 non-AAER firms in their sample and 32.6 percent of the 494 AAER firms in their sample have a F-Score greater than 1.85. This translates into a 10 percent {[(.10*132,967) +(.326*494)] /(132,967+494)} rate of the population of firms in general having a F-Score greater than 1.85.

performance, have better governance, and are more likely to have large and specialized auditors. The differences in the characteristics between the two groups further highlight the importance of controlling for each characteristic in my multivariate analyses.

The Effect of Reputation Incentives on Audit Committee Effectiveness (*H1*)

I report the results from estimating Equation (1) in Panel A of Table 4. Column 1 reports the multivariate regression results for the association between high reputation incentives for the director and misstatements. *HIGH_REP* is not statistically significant ($p > 0.10$), suggesting that directors on multiple audit committees do not provide differential levels of monitoring to each of their directorships, which is inconsistent with *H1*. Column 2 in Panel A of Table 4 reports the multivariate regression results for the association between high reputation incentives for the director and the probability of having a F-Score greater than 1.85. *HIGH_REP* is negative and significant ($p < 0.10$), suggesting that directors on multiple audit committees provide more monitoring effort over financial reporting on the audit committees at firms offering them higher reputation incentives, which is consistent with *H1*.

I report the results from estimating Equation (2) in Panel B of Table 4. Panel B of Table 4 reports the multivariate regression results for the association between high reputation incentives for the director and the likelihood of a material weaknesses in internal control over financial reporting. *HIGH_REP* is negative and significant ($p < 0.10$), suggesting that directors on multiple audit committees provide more monitoring effort over financial reporting on the audit committees offering them higher reputation incentives, which is consistent with *H1*.

I report the results from estimating Equation (3) in Panel C of Table 4. Panel C of Table 4 reports the multivariate regression results for the association between high reputation incentives for the director and the absolute value of discretionary accruals. *HIGH_REP* is negative and

significant ($p < 0.10$), suggesting that AC Chairs on multiple audit committees provide more monitoring effort over financial reporting on the audit committees at firms offering them higher reputation incentives, which is consistent with *H1*.

Based on these results, *H1* is supported using three of my four measures of audit committee effectiveness, even after controlling for a host of firm characteristics, year fixed effects, industry fixed effects, and director fixed effects.

Additional Analysis

Busyness Level Analysis

While my sample only contains directors that serve on multiple audit committees, there is still variation in the number of audit committees that the directors serve. Table 5 shows that 452 director-years out of the 1,493 unique director-years in my sample are associated with directors serving on three or more audit committees. So, roughly one third of the directors in my sample serve on three or more audit committees, meaning that those directors have a higher level of busyness than directors that only serve on two audit committees. The level of busyness that an individual director has may affect the extent to which that director needs to strategically allocate monitoring effort across audit committees. The effect of *HIGH_REP* may be driven by directors serving on more audit committees (three or more) as opposed to less audit committees (only two). To examine whether this is the case, I perform cross-sectional analysis to investigate whether the effect of reputation incentives differs between directors that serve two audit committees and directors that serve three or more audit committees.

Table 6 presents the results of this additional test. I create an indicator variable (*THREE_OR_MORE)* that is equal to one if the director serves on 3 or more audit committees, and zero otherwise. I re-estimate the analyses from Table 4, and I interact *HIGH_REP* with

THREE_OR_MORE. A negative and significant coefficient on the interaction term would mean that the effect of *HIGH_REP* is stronger when the director serves on three or more audit committees as compared to when the director serves on two audit committees. Panels A-C of Table 6 show that the coefficient on *HIGH_REP*THREE_OR_MORE* is statistically insignificant in all models. This indicates that there is no statistically significant difference between the effect of *HIGH_REP* when the director serves on two audit committees and the effect of *HIGH_REP* when the director serves on three or more audit committees. Thus, the effect does not appear to be driven by the directors serving on three or more audit committees.

Early Tenure Analysis

While I control for the tenure of directors at the firms they serve (*DIR_TENURE*), the effect of *HIGH_REP* may differ depending on the director's tenure. Past work has documented a negative relation between audit committee director effectiveness and audit committee director tenure (Sharma and Iselin 2012). The effect of *HIGH_REP* may be strongest when the director is still in the early stages of tenure at a firm because the director may be more independent of management and the director still has yet to develop a reputation at that firm for being an effective monitor. To examine whether this is the case, I perform cross-sectional analysis to investigate whether the effect of reputation incentives differs between directors in the early stages of tenure and directors in later years of tenure at their respective firms.

I create an indicator variable (*EARLY_TENURE)* that is equal to one if the director is in year one or year two of their tenure at a given firm, and zero otherwise. Table 7 presents the reported means for *EARLY_TENURE* in each of my samples. I re-estimate the analyses from Table 4, and I interact *HIGH_REP* with *EARLY_TENURE.* A negative and significant coefficient on the interaction term would mean that the effect is stronger when the director is in the early

stages of tenure at a firm. Panels A-C of Table 8 show that the coefficient on *HIGH_REP*EARLY_TENURE* is statistically insignificant in all models. This indicates that there is no statistically significant difference between the effect of *HIGH_REP* when the director is in the early stages of tenure and the effect of *HIGH_REP* when the director is not in the early stages of tenure. Thus, the effect does not appear to be driven by directors in the early stages of their tenure at the firm.

Threshold in Measurement of High Reputation Incentives

I follow Masulis and Mobbs (2014) and use a 10% threshold for difference in firm size to determine whether reputation incentives are high or not. It could be argued, however, that 10% is an arbitrary threshold to use. As a robustness check, I re-estimate Equations (1) through (3) and I use different thresholds for my measurement of *HIGH_REP* to examine whether my results are sensitive to the threshold used. I use both 20% and 50% thresholds to measure *HIGH_REP* in this analysis. For each threshold, I continue to require that each director has at least one high reputation incentive observation and at least one not-high reputation incentive observation in each year. This results in my sample size dropping as the threshold increases. Panel A of Table 9 shows that the coefficient on *HIGH_REP* remains insignificant ($p>0.10$) for the misstatement model when I use 20% as a threshold to measure *HIGH_REP* in Column 1 and when I use 50% as a threshold to measure *HIGH_REP* in Column 2. Thus, I do not find evidence that directors allocate effort to the point that their less important directorships are more likely to misstate. Panel B of Table 9 shows that the coefficient on *HIGH_REP* remains negative and significant ($p<0.10$) for the F-Score model when I use 20% and 50% thresholds to measure *HIGH_REP* in Columns 1 and 2, respectively. Panel C of Table 9 shows that the coefficient on *HIGH_REP* remains negative and significant ($p<0.10$) for the material weakness model when I use 20% and

50% thresholds to measure *HIGH_REP* in Columns 1 and 2, respectively. Panel D of Table 9 shows that the coefficient on *HIGH_REP* remains negative and significant ($p<0.10$) for the accruals model when I use 20% and 50% thresholds to measure *HIGH_REP* in Columns 1 and 2, respectively. Thus, my inferences are not sensitive to the threshold used to measure *HIGH_REP*.

Big R Analysis

I re-estimate Equation (1) using another measure of misstatements as my dependent variable, *BIG_R*. Following Tan and Young (2015), I define *BIG_R* as an indicator variable equal to one if the firm misstated financial statements in year *t* and the subsequent restatement was disclosed in an 8-K under item 4.02. "Big R" misstatements are more material in nature and magnitude and are clearer signals of poor financial reporting than the other "little r" misstatements that Audit Analytics captures (Tan and Young 2015). *BIG_R* is an appropriate measure worth examining because investors and boards should care more about these types of misstatements.

Table 10 presents the multivariate analysis using *BIG_R* as the dependent variable. Columns 1, 2, and 3 use a 10%, 20%, and 50% relative size threshold to measure *HIGH_REP,* respectively. The coefficient on *HIGH_REP* in Columns 1 – 3 are all statistically insignificant ($p>0.10$). I, again, do not find evidence that directors unevenly allocate effort across their audit committees to the point that their less important firms are more likely to misstate, even when focusing on more material and problematic misstatements.

F-Score Continuous Measure Analysis

While Dechow et al. (2011) define firms with an F-Score greater than 1.85 as having "substantial risk" of receiving an AAER from the SEC, the F-Score itself is a continuous measure of the probability of receiving an AAER from the SEC because of financial reporting

irregularities. I re-estimate Equation (1) using the continuous measure of the F-Score (*FSCORE*), rather than the indicator variable from my previous analyses (*HIGH_FSCORE*), to investigate whether my results are robust to the continuous measure of the F-Score.

Table 11 presents the multivariate analysis using *FSCORE* as the dependent variable. Columns 1, 2, and 3 use a 10%, 20%, and 50% relative size threshold to measure *HIGH_REP,* respectively. The coefficient on *HIGH_REP* in Columns 1-3 are all negative and significant ($p<0.10$), consistent with my analysis using the indicator variable. My results are robust to the continuous measure of the F-Score.

Firm Fixed Effects

In Table 12*,* I re-estimate Equations (1)–(3), but I use firm fixed effects rather than industry fixed effects. On the one hand, using firm fixed effects controls for potentially omitted time-invariant characteristics of each firm that may determine FRQ. Firm fixed effects allows for a stronger inference that my variable of interest is a determinant of FRQ, and is not just associated with some unobserved inherent firm characteristic that is a determinant of FRQ. On the other hand, firm fixed effects can also fail to detect a relation that exists between the explanatory variable of interest and the dependent variable when the explanatory variable does not vary much within firms, as is the case in my sample (Adams and Ferreira 2008).

In each Panel of Table 12, Columns 1, 2, and 3 use a 10%, 20%, and 50% relative size threshold to measure *HIGH_REP,* respectively. Panel A presents the misstatement analysis. The results are consistent with the analysis using industry fixed effects. The coefficient on *HIGH_REP* in Columns 1, 2, and 3 are all statistically insignificant. Panel B presents the F-Score analysis. The results are generally consistent with my analysis using industry fixed effects. While the coefficient on *HIGH_REP* in Column 2 is statistically insignificant ($p>0.10$), it is approaching significance

and the coefficient is negative. Further, the coefficient on *HIGH_REP* in Columns 1 and 3 are both negative and significant ($p<0.10$). Panel C presents my material weakness analysis. The results are inconsistent with my analysis using industry fixed effects. The coefficient on *HIGH_REP* in Columns 1, 2, and 3 are all statistically insignificant ($p>0.10$), while they were all negative and significant using industry fixed effects. Panel D presents the accruals analysis. The results are consistent with the analysis using industry fixed effects. The coefficient on *HIGH_REP* in Columns 1, 2, and 3 are all negative and significant ($p<0.10$). Three of my four measures give me consistent results whether I use firm fixed effects or industry fixed effects. The only measure that gives me inconsistent results is material weaknesses, and this is likely because of how rarely material weaknesses occur. *MWEAK* is the dependent variable with the least amount of variation. The fact that I find statistically significant and consistent results on two of my measures using firm fixed effects provides reasonable evidence that the results from my previous analysis are not simply correlated with unobserved time-invariant firm characteristics that determine FRQ.

Continuous Measure of Reputation Incentives

In my main tests, I use an indicator variable based on relative firm size to measure reputation incentives. I classify firms as either offering a director high reputation incentives or *not* offering the director high reputation incentives. While this measure clearly distinguishes between the two groups of firms, there is still variation within groups that my measure does not capture. I perform additional analysis to examine whether my results are consistent using a continuous measure of reputation incentives. I create a variable, *DIST_FROM_MEDIAN*, that is calculated as the difference between the *SIZE* variable of firm *i* and the median of the *SIZE* variable of all the firms that director *d* serves in year *t.* While *HIGH_REP* measures *whether* a firm is significantly larger than the other firms that a director serves, *DIST_FROM_MEDIAN*

measures the *magnitude* of how much larger or smaller a firm is than the other firms that a director serves. *DIST_FROM_MEDIAN* preserves the variation in the measure of reputation incentives.

I re-estimate Equations (1)–(3) using *DIST_FROM_MEDIAN* as the independent variable in Table 13. Consistent with my main analysis using *HIGH_REP*, the coefficient on *DIST_FROM_MEDIAN* is negative and significant in Columns 2-4. The coefficient on *DIST_FROM_MEDIAN* is statistically insignificant in the misstatement model, which is also consistent with my main analysis. Thus, my results are robust to a continuous measure of director reputation incentives.

Size Distribution Analysis

I follow past studies and control for absolute firm size in each of my analyses because firm size is a key determinant of FRQ (Cao et al. 2012; DeHaan et al. 2013; Doyle et al. 2007). However, the effect of director reputation incentives that I document in my analyses may differ depending on the firm's absolute size. On one hand, the largest firms have inherently higher FRQ because of significantly more robust systems of controls, more expert personnel, and stronger governance. Thus, the effect of *HIGH_REP* on FRQ may not be as strong for the largest firms because those firms may have good FRQ regardless of the relative level of reputation incentives the firm offers to key audit committee directors. One may expect the result of *HIGH_REP* to be strongest for smaller firms that likely rely more on the input and effort of key audit committee directors. On the other hand, the effect of *HIGH_REP* could be driven by larger firms. To the extent that my absolute size variable (*SIZE*) does not adequately control for the effect of absolute firm size, *HIGH_REP* could simply be capturing an absolute size effect. The larger the firm, the more likely the firm is going to be classified as a high reputation incentive

firm for the director. Panel A of Table 14 illustrates this point and shows that the reported mean of *HIGH_REP* differs in the two distributions of firm size. The reported mean for *HIGH_REP* in the top half of the distribution (0.66) is much higher than the reported mean in the bottom half of the distribution of firm size (0.30). This highlights the importance of my cross-sectional analysis to investigate whether the effect of *HIGH_REP* differs between smaller firms and larger firms.

To perform my analysis, I split my sample at the median of firm size and create a subsample of larger firms with size above the median and a subsample of smaller firms with size below or equal to the median. I re-estimate the main analyses from Table 4 on the two subsamples. For each sample's analysis, I again require each director to have at least one high reputation incentive firm and at least one non-high reputation incentive firm. This requirement reduces my sample size, but is critical to the interpretation of my coefficient of interest. Panel A of Table 15 presents my analysis on firms in the top half of the distribution of firm size. The coefficient on *HIGH_REP* is statistically insignificant in all columns. Panel B of Table 15 presents my analysis on firms in the bottom half of the distribution of firm size. The coefficient on *HIGH_REP* is negative and significant in three of my four models, including the misstatement model. The fact that *HIGH_REP* is now negative and significant in the misstatement analyses suggests that the effect of reputation incentives is particularly strong for the smallest firms. Thus, the effect appears to be driven by smaller firms, and not larger firms. These results alleviate the concern that *HIGH_REP* is capturing an absolute firm size effect. Additionally, the results suggest that the reputation incentives of directors only matter for FRQ at smaller firms that likely depend more on director effort and monitoring.

I also estimate Equations (1)–(3) separately on each tercile. I perform tercile analysis for the sake of having a "mid-sized" firm classification. Panel B of Table 14 presents the reported

means for *HIGH_REP* in the top, middle, and bottom terciles of the distribution of firm size. For each tercile's analysis, I again require each director to have at least one high reputation incentive firm and at least one non-high reputation incentive firm. Panel A of Table 16 presents the results for the regressions using the top tercile of firms. The coefficient on *HIGH_REP* is statistically insignificant in all models, suggesting that director reputation incentives appear to not matter for FRQ at the very largest firms. Panel B of Table 16 presents the results for the regressions using the middle tercile of firms. The coefficient on *HIGH_REP* is statistically insignificant in all models, suggesting that director reputation incentives do not matter for FRQ at mid-sized firms either. Panel C of Table 16 presents the results for the regressions using the bottom tercile of firms. The coefficient on *HIGH_REP* is negative and significant in three of my four models, including the misstatement model. The fact that *HIGH_REP* is negative and significant in the misstatement analyses in Panel B of Table 15 and in Panel C of Table 16 suggests that the effect of reputation incentives is particularly strong for smaller firms. The only dependent variable that does not have a negative and significant coefficient for the smallest firms in Table 15 and Table 16 is *HIGH_FSCORE.* This may be because the F-Score is a measure of the likelihood of fraud. While my other measures can capture both errors and fraud committed by management in generating the financial statements, the F-Score is meant to solely capture egregious manipulation and misconduct. The uniqueness of the F-Score measure compared to my other measures may be the reason that the effect of *HIGH_REP* does not differ with firm size. Still, taken together, my results provide evidence that director reputation incentives matter more for FRQ at smaller firms, while they appear to not matter for FRQ at larger firms.

The Addition of Audit Committee Seats by Directors

A stream of recent literature has documented the negative effects of a director holding multiple directorships (Fich and Shivdasani 2006; Sharma and Iselin 2012; Tanyi and Smith 2015). Given that multiple directorships are associated with negative firm outcomes, directors are risking their reputations by accepting additional directorships. In the case of audit committee directors, poor financial reporting can result in directors losing their directorships and failing to gain directorships in the future because of damaged reputation (Srinivasan 2005). Audit committee directors are also more likely to be named in lawsuits after negative corporate outcomes (Brochet and Srinivasan 2014). So, the question of why audit committee directors are willing to accept additional audit committee seats is a compelling one. In this paper, I predict that directors on multiple audit committees should strategically allocate more of their monitoring effort to their audit committees at larger firms to maximize their reputation. Consistent with the reasoning behind this prediction, I also predict that directors are more willing to add another audit committee to their responsibilities when the audit committee is at a firm that is significantly larger than any firm they have served previously as an audit committee member. Such an addition to their responsibilities would contribute more to their reputation than the addition of an audit committee seat at smaller firm.[15]

Table 17 presents descriptive statistics on the addition of new audit committee seats by directors. Panel A reports descriptive statistics for all director-years associated with a FINEXP or an AC CHAIR. Five percent of all director-years are years in which a director added a new audit

[15] To provide some anecdotal support for the reasoning behind this assumption, I spoke with an experienced audit committee chair with experience serving on multiple audit committees. The audit committee member indicated that audit committee directors tend to add audit committee seats at larger, more reputable companies as their number of audit committees increases and their career as a director progresses. The director indicated that this likely occurs because directors consider the reputational risk of joining a board and whether the potential benefit to their reputation outweighs that risk.

committee seat to their responsibilities (*ADD1*). Most of those additions are instances where the director is adding an audit committee seat at a firm that is either similar in size or significantly larger than any firm they have served previously (*ADD_SIMILAR_OR_LARGER*). Additionally, most of the additions are instances where the director is adding their second audit committee seat (*BECOME_2*) as opposed to adding a third or fourth seat (*BECOME_3ORMORE*). I separate the descriptive statistics by the number of audit committee seats that the director ends up with in Panel B and Panel C. Panel B presents descriptive statistics for additions where directors are adding their second audit committee and Panel C presents descriptive statistics for additions where directors end up with three or more audit committee seats (adding third, fourth, etc.). Panel B reports that, for directors adding their second audit committee, there is significant variation in whether the directors add an audit committee seat at a firm that is a similar size or significantly larger than the firm they currently serve (*ADD_SIMILAR_OR_LARGER*). Only 45 percent of additions that represent the addition of a second audit committee seat are instances in which the director is adding an audit committee seat at a firm that is a similar size or significantly larger than the firm they currently serve. Panel C, however, reports that, for directors ending up with three or more audit committee seats (adding third, fourth, etc.), almost all the directors add an audit committee seat at a firm that is a similar size or significantly larger than any firm they currently serve (*ADD_SIMILAR_OR_LARGER*). Only eight percent of additions in Panel C are instances in which the director is adding an audit committee seat at a firm that is significantly smaller than any firm the director currently serves (*ADD_SMALLER*). The stark differences in the descriptive statistics for additions in Panel B and Panel C suggests that directors are generally only willing to add an audit committee seat at a smaller firm than their current firm if it will be their second audit committee seat. Going from serving one audit

committee to serving two is something that directors may view as enhancing their reputation in and of itself, regardless of the size of the new firm. When adding a third or fourth audit committee seat, however, directors appear to discriminate based on firm size (i.e. they are only willing to potentially overburden themselves if adding firms that are larger than any firm they currently serve).

V. CONCLUSION

Reputation incentives theory suggests that reputation provides strong incentives for independent directors to be effective monitors. As it relates to the audit committee, key directors such as the audit committee chair and the designated financial experts should have very strong reputation incentives to effectively monitor the financial reporting process. Given the increased interest in audit committee members serving on multiple audit committees, it is important to understand how key members of the audit committee that serve on multiple audit committees prioritize their competing responsibilities.

In this study, I examine whether key audit committee members that serve on multiple audit committees allocate their monitoring effort unequally across their various audit committees. I find that even after controlling for absolute firm size and a host of other firm characteristics, firms that offer these directors a greater opportunity to enhance their reputation as a monitor (higher reputation incentives) have significantly higher FRQ, indicating higher audit committee effectiveness. I also find that my results are driven by smaller companies that likely rely more on the input and effort of key audit committee directors. My results are robust to various measures of high reputation incentives.

In summary, I provide empirical evidence of the association between the reputation incentives of key audit committee members and audit committee effectiveness. My findings suggest that audit committee chairs and designated financial experts that serve on multiple audit committees tend to be more effective monitors on audit committees at companies that offer them the most potential to build a reputation as an effective monitor. The findings contribute to the audit committee effectiveness literature by documenting another attribute of the audit committee that impacts audit committee effectiveness. The findings also contribute to the literature on

director reputation incentives by showing that director reputation incentives not only affect firm performance, but affect FRQ as well. Further, I indirectly contribute to the director busyness literature by offering a more intricate view into director effort allocation. While past busyness studies focus on the number of directorships that a director holds, I show that directors that hold multiple directorships strategically distribute their monitoring effort based on the company's relative contribution to their reputation.

My findings should be of interest to boards, investors, and regulators considering the implications of key audit committee members that serve on multiple audit committees. In particular, boards at smaller public companies should consider the other firms that any potentially new audit committee directors serve on before they appoint them. While appointing an audit committee director from another larger, more visible firm may seem appealing, it may not result in a more effective audit committee for such firms. Along the same lines, smaller public companies might benefit from setting clear restrictions on *both* the number and the *scale* of outside commitments they will allow existing directors to have while they serve on the board. The relative size of the company compared to the other companies that a director serves can act as a signal to investors and boards about the potential quality of financial reporting monitoring that will be provided.

REFERENCES

Abbott, L.J., S. Parker, G. F. Peters, and K. Raghunandan. 2003. The association between audit committee characteristics and audit fees. Auditing: A Journal of Practice & Theory 22 (2): 17-32.

Abbott, L. J., S. Parker, and G. F. Peters. 2004. Audit committee characteristics and restatements. *Auditing: A Journal of Theory and Practice* 23 (1): 69-87.

Abbott, L. J., S. Parker, and G. F. Peters. 2006. Earnings management, litigation risk, and asymmetric audit fee responses. *Auditing: A Journal of Theory and Practice* 25 (1): 85-98.

Adams, R.B. and D. Ferreira. 2008. Do directors perform for pay? *Journal of Accounting and Economics* 46 (1): 154-171.

Agrawal, A. and S. Chadha. 2005. Corporate governance and accounting scandals. *The Journal of Law and Economics* 48 (2): 371-406.

Archambeault, D.S., F. T. DeZoort, and D. R. Hermanson. 2008. Audit committee incentive compensation and accounting restatements. *Contemporary Accounting Research* 25 (4): 965-992.

Armstrong, C. S., J. D. Kepler, and D. Tsui. 2017. Inelastic labor markets and directors' reputation incentives. Working paper: University of Pennsylvania and University of Southern California.

Audit Committee Leadership Network in North America. *Viewpoints for the Audit Committee Leadership Summit*. 2017. Available at: http://www.ey.com/Publication/vwLUAssets/EY-audit-chairs-share-practical-guidance-for-running-effective-meetings/$FILE/EY-audit-chairs-share-practical-guidance-for-running-effective-meetings.pdf.

Badolato, P.G., D. C. Donelson and M. Ege. 2014. Audit committee financial expertise and earnings management: The role of status. *Journal of Accounting and Economics* 58 (2): 208-230.

Baer, L., Y. Ertimur, and J. Zhang. 2017. Tainted executives as outside directors. Working paper: University of Colorado at Boulder and McGill University.

Barton, J., 2005. Who cares about auditor reputation? *Contemporary Accounting Research*, 22 (3):.549-586.

Beasley, M. S., J. V. Carcello, D. R. Hermanson, and T. L. Neal. 2009. The audit committee oversight process. *Contemporary Accounting Research* 26 (1): 65-122.

Biddle, G. C., G. Hilary, and R. S. Verdi. 2009. How does financial reporting quality relate to investment efficiency? *Journal of Accounting and Economics* 48 (2-3): 112-131.

Blue Ribbon Committee (BRC). 1999. *Report and recommendations of the Blue Ribbon Committee on Improving the Effectiveness of Corporate Audit Committees*. New York: BRC.

Bradley, D., S. Gokkaya, X. Liu, and F. Xie. 2017. Are all analysts created equal? Industry expertise and monitoring effectiveness of financial analysts. *Journal of Accounting and Economics* 63 (2):179-206.

Brochet, F. and S. Srinivasan. 2014. Accountability of independent directors: Evidence from firms subject to securities litigation. *Journal of Financial Economics* 111 (2): 430-449.

Bruynseels, L. and E. Cardinaels. 2013. The audit committee: Management watchdog or personal friend of the CEO? *The Accounting Review* 89 (1): 113-145.

Campbell, J.L., J. Hansen, C. A. Simon, and J. L. Smith. 2015. Audit committee stock options and financial reporting quality after the Sarbanes-Oxley Act of 2002. *Auditing: A Journal of Practice & Theory* 34 (2): 91-120.

Cao, Y., L. A. Myers, and T. C. Omer. 2012. Does company reputation matter for financial reporting quality? Evidence from restatements. *Contemporary Accounting Research* 29 (3): 956-990.

Carcello, J.V. and T. L. Neal. 2000. Audit committee composition and auditor reporting. *The Accounting Review* 75 (4): 453-467.

Carcello, J.V. and T. L. Neal. 2003. Audit committee characteristics and auditor dismissals following "new" going-concern reports. *The Accounting Review* 78 (1): 95-117.

Carcello, J. V., D. R. Hermanson, and Z. Ye. 2011a. Corporate governance research in accounting and auditing: Insights, practice implications, and future research directions. *Auditing: A Journal of Practice & Theory* 30 (3): 1-31.

Carcello, J. V., T.L. Neal, Z. Palmrose, and S. Scholz. 2011b. CEO involvement in selecting board members, audit committee effectiveness, and restatements. *Contemporary Accounting Research* 28 (2): 396-430.

Carter, R., and S. Manaster. 1990. Initial public offerings and underwriter reputation. *Journal of Finance* 45 (4): 1045-1067.

Carter, R., F. H. Dark, and A. K. Singh. 1998. Underwriter reputation, initial returns, and the long-run performance of IPO stocks. *Journal of Finance* 53 (1): 285-311.

Cassell, C. A., L. M. Dreher, and L. A. Myers. 2013. Reviewing the SEC's review process: 10-K comment letters and the cost of remediation. *The Accounting Review* 88 (6): 1875-1908

Cassell, C.A., L.A. Myers, R. Schmardebeck, and J. Zhou. 2017. The monitoring effectiveness of co-opted audit committees. *Contemporary Accounting Research* (Forthcoming).

Chung, H. and S. Kallapur. 2003. Client importance, nonaudit services, and abnormal accruals. *The Accounting Review* 78 (4): 931-955.

Clarke, J., A. Khorana, A. Patel, and P. R. Rau. 2007. The impact of all-star analyst job changes on their coverage choices and investment banking deal flow. *Journal of Financial Economics* 84 (3): 713-737.

Cohen, J., U. Hoitash, G. Krishnamoorthy, and A.M. Wright. 2014. The effect of audit committee industry expertise on monitoring the financial reporting process. *The Accounting Review* 89 (1): 243-273.

Costello, A. M., and R. Wittenberg-Moerman. 2011. The impact of financial reporting quality on debt contracting: Evidence from internal control weakness reports. *Journal of Accounting Research* 49 (1): 97-136.

Daske, H., L. Hail, C. Leuz, and R. Verdi. 2008. Mandatory IFRS reporting around the world: Early evidence on the economic consequences. *Journal of Accounting Research* 46 (5): 1085-1142.

Dhaliwal, D., V. Naiker, and F. Navissi. 2010. The association between accruals quality and the characteristics of accounting experts and mix of expertise on audit committees. *Contemporary Accounting Research* 27 (3): 787-827.

Dechow, P. M., R. G. Sloan, and A. P. Sweeney. 1995. Detecting earnings management. *The Accounting Review* 70 (2): 193-225.

Dechow, P., W. L. Ge, and C. Schrand. 2010. Understanding earnings quality: A review of the proxies, their determinants and their consequences. *Journal of Accounting and Economics* 50 (2-3): 344-401.

Dechow, P.M., W. Ge, C. R. Larson, and R. G. Sloan. 2011. Predicting material accounting misstatements. *Contemporary Accounting Research* 28 (1): 17-82.

DeHaan, E., F. Hodge, and T. Shevlin. 2013. Does voluntary adoption of a clawback provision improve financial reporting quality? *Contemporary Accounting Research* 30 (3): 1027-1062.

DeFond, M.L., R. N. Hann, and X. Hu. 2005. Does the market value financial expertise on audit committees of boards of directors? *Journal of Accounting Research* 43 (2): 153-193.

Desai, H., C. E. Hogan, and M. S. Wilkins. 2006. The reputational penalty for aggressive accounting: Earnings misstatements and management turnover. *The Accounting Review* 81 (1): 83-112.

Diamond, D.W. 1989. Reputation acquisition in debt markets. *Journal of Political Economy* 97 (4): 828-862.

Diamond, D.W. 1991. Monitoring and reputation: The choice between bank loans and directly placed debt. *Journal of Political Economy* 99 (4): 689-721.

Doyle, J. T., W. Ge, and S. McVay. 2007. Determinants of weaknesses in internal control over financial reporting. *Journal of Accounting and Economics* 44 (1): 193-223.

Engel, E., R. M. Hayes, X. Wang. 2010. Audit committee compensation and the demand for monitoring of the financial reporting process. *Journal of Accounting and Economics* 49 (1): 136-154.

Ertimur, Y., F. Ferri, and D. A. Maber. 2012. Reputation penalties for poor monitoring of executive pay: Evidence from option backdating. *Journal of Financial Economics* 104 (1): 118-144.

Fama, E. 1980. Agency problems and the theory of the firm. *Journal of Political Economy* 88 (2): 288-307.

Fama, E. F., and M. C. Jensen. 1983. Separation of ownership and control. *Journal of Law and Economics* 26 (2): 301-325.

Fang, L. and A. Yasuda. 2011. Are stars' opinions worth more? Evidence from stock recommendations 1994-2009. Working paper, INSEAD and University of California, Davis.

Feldmann, D. A., W. J. Read, and M. J. Abdolmohammadi. Financial restatements, audit fees, and the moderating effect of CFO turnover. *Auditing: A Journal of Practice and Theory* 28 (1): 205-223.

Ferris, S.P., M. Jagannathan, and A. C. Pritchard. 2003. Too busy to mind the business? Monitoring by directors with multiple board appointments. *The Journal of Finance* 58 (3): 1087-1111.

Fich, E. M., and A. Shivdasani. 2006. Are busy boards effective monitors? *The Journal of Finance* 61 (2): 689-724.

Fich, E. M., and A. Shivdasani. 2007. Financial fraud, director reputation, and shareholder wealth. *Journal of Financial Economics* 86 (2): 306-336.

Francis, J. R., R. LaFond, P.M. Olsson, and K. Schipper. 2004. Cost of Equity and Earnings Attributes. *The Accounting Review* 79 (4): 967-1010.

Garrett, J., R. Hoitash, and D. Prawitt. 2014. Trust and financial reporting quality. Journal of Accounting Research 52 (5): 1087-1125.

Gendron, Y., and J. Bèdard. 2006. On the constitution of audit committee effectiveness. *Accounting, Organizations, and Society* 31 (3): 211-239.

Gilson, S.C., 1990. Bankruptcy, boards, banks, and blockholders: Evidence on changes in corporate ownership and control when firms default. *Journal of Financial Economics* 27 (2): 355-387.

Gomes, A. 2000. Going public without governance: Managerial reputation effects. *Journal of Finance* 55 (2): 615-646.

Harford, J., 2003. Takeover bids and target directors' incentives: The impact of a bid on directors' wealth and board seats. *Journal of Financial Economics* 69 (1): 51-83.

Hermalin, B.E. and M. S. Weisbach. 1998. Endogenously chosen boards of directors and their monitoring of the CEO. *American Economic Review* 88 (1): 96-118.

Holmstrom, B. 1982. Moral hazards in teams. *The Bell Journal of Economics* 13 (2): 324-340.

Hribar, P. and D. W. Collins, D.W. 2002. Errors in estimating accruals: Implications for empirical research. *Journal of Accounting Research* 40(1):105-134.

Huang, H. H., G. J. Lobo, C. Wang, and J. Zhou. 2017. Do banks price independent directors' attention? *Journal of Financial and Quantitative Analysis* (Forthcoming).

Institutional Shareholder Services (ISS). 2015a. 2015-2016 ISS Global Policy Survey. Available at: https://www.issgovernance.com/file/publications/ISS2015-2016PolicySurveyResultsReport.pdf.

Institutional Shareholder Services (ISS). 2015b. Executive Summary: Proxy Voting Guideline Updates and Process. Available at: https://www.issgovernance.com/file/policy/executive-summary-of-key-2016-updates- and-policy.pdf.

Jackson, A. R. 2005. Trade generation, reputation, and sell-side analysts. *Journal of Finance* 60 (2): 673-717.

Jensen, M., 2006. Should we stay or should we go? Accountability, status anxiety, and client defections. *Administrative Science Quarterly* 51 (1): 97-128.

Jo, H., Y. Kim, and M. S. Park. 2007. Underwriter choice and earnings management: Evidence from seasoned equity offerings. *Review of Accounting Studies* 12 (1): 23-59.

Jones, J.J., 1991. Earnings management during import relief investigations. *Journal of Accounting Research* 29 (2):193-228.

Kaplan, S.N. and D. Reishus. 1990. Outside directorships and corporate performance. *Journal of Financial Economics* 27 (2): 389-410.

Klein, A., 2002. Audit committee, board of director characteristics, and earnings management. *Journal of Accounting and Economics* 33 (3): 375-400.

Kose, J., and D. C. Nachman. 1985. Risky debt, investment incentives, and reputation in a sequential equilibrium. *Journal of Finance* 40 (3): 863-878.

Kothari, S. P., A. Leone, and C. Wasley. 2005. Performance matched discretionary accrual measures. *Journal of Accounting and Economics* 39 (1): 163-197.

KPMG. 2015. *Audit Committee Workload*. Available at: https://home.kpmg.com/content/dam/kpmg/pdf/2015/10/audit-committee-workload.pdf.

Krishnan, J., 2005. Audit committee quality and internal control: An empirical analysis. *The Accounting Review* 80 (2): 649-675.

Krishnan, G.V. and G. Visvanathan. 2008. Does the SOX definition of an accounting expert matter? The association between audit committee directors' accounting expertise and accounting conservatism. *Contemporary Accounting Research* 25 (3): 827-858.

Krishnan, J., Y. Wen, and W. Zhao. 2011. Legal expertise on corporate audit committees and financial reporting quality. *The Accounting Review* 86 (6): 2099-2130.

LaCroix, K. 2014. Liability Exposure of Audit Committee Chairs. Available at: https://www.dandodiary.com/2014/04/articles/director-and-officer-liability/liability-exposures-of-audit-committee-chairs/.

Larcker, D. F., and S. A. Richardson. 2004. Fees paid to audit firms, accrual choices, and corporate governance. *Journal of Accounting Research* 42 (3): 625-658.

Linck, J.S., J. M. Netter, and T. Yang. 2008. The effects and unintended consequences of the Sarbanes-Oxley Act on the supply and demand for directors. *The Review of Financial Studies* 22 (8): 3287-3328.

Lisic, L.L., T. L. Neal, I. X. Zhang, and Y. Zhang. 2016. CEO power, internal control quality, and audit committee effectiveness in substance versus in form. *Contemporary Accounting Research* 33 (3): 1199-1237.

Ljungqvist, A., F. Marston, L. T. Starks, K. D. Wei, and H. Yan. 2007. Conflicts of interest in sell-side research and the moderating role of institutional investors. *Journal of Financial Economics* 85 (2): 420-456.

Masulis, R. W., and S. Mobbs. 2014. Independent director incentives: Where do talented directors spend their limited time and energy? *Journal of Financial Economics* 111 (2): 406-429.

Mayhew, B.W. 2001. Auditor reputation building. *Journal of Accounting Research* 39 (3): 599-617.

Myers, J. N., L. A. Myers, and T. C. Omer. 2003. Exploring the term of the auditor-client relationship and the quality of earnings: A case for mandatory auditor rotation? *The Accounting Review* 78 (3): 779-799.

Naiker, V. and D. S. Sharma. 2009. Former audit partners on the audit committee and internal control deficiencies. *The Accounting Review* 84 (2): 559-587.

National Association of Corporate Directors (NACD). 2014. Audit Committee Chair Advisory Council: Summary of Proceedings. Available at: http://www.acc.com/_cs_upload/vl/membersonly/Article/1388890_1.pdf.

Palmrose, Z. V., V. J. Richardson, and S. Scholz. 2004. Determinants of market reactions to misstatement announcements. *Journal of Accounting and Economics* 37 (1): 59-89.

Palmrose, Z-V., and S. Scholz. 2004. The circumstances and legal consequences of non-GAAP reporting: Evidence from restatements. *Contemporary Accounting Research* 21 (1): 139-180.

Pittman, J., and Y. Zhao. 2017. The impact of financial statement audits on non-income-increasing misreporting: Evidence from restatements. Working paper: Memorial University of Newfoundland and University of Houston.

Reichelt, K., and D. Wang. 2010. National and office-specific measures of auditor industry expertise and effects on audit quality. *Journal of Accounting Research* 48 (3): 647-686.

Reynolds, J.K. and J. R. Francis. 2000. Does size matter? The influence of large clients on office-level auditor reporting decisions. *Journal of Accounting and Economics* 30 (3): 375-400.

Sarbanes-Oxley Act (SOX) of 2002. 2002. Public L. no. 107-204, 116 Stat. 745.

Stiglitz, J., and A. Weiss. 1983. Incentive effects of terminations: Applications to the credit and labor markets. *American Economic Review* 75 (5): 912-927.

Sharma, V., and E. Iselin. 2012. The association between audit committee multiple-directorships, tenure, and financial misstatements. *Auditing: A Journal of Practice & Theory* 31 (3): 149-175.

Spencer Stuart. 2015. Spencer Stuart Board Index 2015. Available at: https://www.spencerstuart.com/~/media/pdf%20files/research%20and%20insight%20pdfs/ssbi-2015_110215-web.pdf.

Srinivasan, S. 2005. Consequences of financial reporting failure for outside directors: Evidence from accounting restatements and audit committee members. *Journal of Accounting Research* 43 (2): 291-333.

Tan, C. E. L. and S.M. Young. 2015. An analysis of 'little r" restatements. *Accounting Horizons* 29 (3): 667-693.

Tanyi, P. N. and D.B. Smith. 2015. Busyness, expertise, and financial reporting quality of audit committee chairs and financial experts. *Auditing: A Journal of Practice & Theory* 34 (2): 59-89.

Vafeas, N., 2005. Audit committees, boards, and the quality of reported earnings. *Contemporary Accounting Research* 22 (4): 1093-1122.

Wang, C., F. Xie, and M. Zhu. 2015. Industry expertise of independent directors and board monitoring. *Journal of Financial and Quantitative Analysis* 50 (5): 929-962.

Weigelt, K., and C. Camerer. 1988. Reputation and corporate strategy: A review of recent theory and applications. *Strategic Management Journal* 9 (5): 443-454.

Wilson, R. 1985. Reputations in games and markets. In *Game –theoretic models of bargaining,* ed. A. E. Roth. New York: Cambridge University Press.

Wilson, R.J., 2009. An examination of corporate tax shelter participants. *The Accounting Review* 84 (3): 969-999.

Wooldridge, J. M. 2010. *Econometric Analysis of Cross Section and Panel Data*. 4th edition: MIT press.

Xie, B., W. N. Davidson, and P. J. DaDalt. 2003. Earnings management and corporate governance: the role of the board and the audit committee. *Journal of Corporate Finance* 9 (3): 295-316.

Yermack, D. 2004. Remuneration, retention, and reputation incentives for outside directors. *Journal of Finance* 59 (5): 2281-2308

APPENDICES

Appendix A
Variable Definitions

Variable	Source	Definition
Dependent Variables:		
ABSDA	Compustat	The absolute value of performance adjusted discretionary accruals calculated using the modified Jones model (Dechow et al. 1995) as adapted by Kothari et al. (2005)
HIGH_FSCORE	Compustat	Indicator variable equal to one if the firm's F-Score, as calculated in model 1 in Dechow et al. (2011), is greater than 1.85, and zero otherwise
MISSTATE	Audit Analytics	Indicator variable equal to one if core accounting issues ("res_acc_res_fkey_list" includes 1, 3, 4, 6, 7, 12, 14, 20, 21 23, 29, or 42) in annual financial statements were misstated during year *t*, as evidenced by a subsequent restatement in the Non-Reliance database, and zero otherwise
MWEAK	Audit Analytics	Indicator variable equal to one if the auditor issued a material weakness opinion in year *t*, and zero otherwise
Variable of Interest:		
HIGH_REP	BoardEx	Indicator variable equal to one if the directorship is the largest directorship, or within 10% of the largest, that the director holds (as measured by market capitalization of the firm), and zero otherwise
Control Variables		
AC_SIZE	BoardEx	Number of members on audit committee
AGE	Compustat	The natural log of years the firm has existed in Compustat

AR_INV	Compustat	Receivables and inventory, divided by total assets [(RECT+INVT)/AT]
AUD_IMPORT	Audit Analytics	Total fees paid by firm *i* to the auditor in year *t* divided by the total revenue of the auditor local office that issues the audit report.
BIG4	Audit Analytics	Indicator variable equal to one if the auditor is from the Big 4, and zero otherwise
BD_INDEP	BoardEx	Proportion of the board that is independent, measured as the number of independent directors divided by board size
BD_SIZE	BoardEx	Board size, measured by number of board members
BUS_SEG	Compustat	Square root of the number of business segments
DIR_TENURE	BoardEx	Director *d*'s tenure at firm *i* in year *t*
EARLY_TENURE	BoardEx	Indicator variable equal to one if the director *d* is in year 1 or 2 of their tenure at the directorship in year *t,* and zero otherwise
FOREIGN	Compustat	Indicator variable equal to one if firm has foreign operations (FCA not equal to zero and not missing), and zero otherwise
IND_SPECIAL	Audit Analytics	Indicator variable equal to one if the auditor has the largest market share of a two-digit SIC category in the local MSA and if its market share is at least 10% greater than the second largest industry leader in the local MSA's audit market, and zero otherwise (Reichelt and Wang 2010)
LAG_ABSDA	Compustat	Lagged discretionary accruals, measured as *ABSDA* in year *t-1*
LEV	Compustat	Long term debt divided by total assets [(DLTT+DLC)/AT]
LOSS	Compustat	Indicator variable equal to one if the firm reports a net loss (NI less than zero), and zero otherwise

M&A	Compustat	Indicator variable equal to one if firm is involved in mergers or acquisitions (i.e., if any of the following are non-zero: AQA, AQC, AQD, AQEPS), and zero otherwise
MTB	Compustat	Market-to-book[(PRCC_F*CSHO)/CEQ]
NUM_AC	BoardEx	The number of audit committees that director *d* serves on in year *t*
ROA	Compustat	Net Income divided by lagged total assets (NI/AT)
RESTRUCTURE	Compustat	Restructuring charges in year *t* scaled by total assets in year *t* [(RCA)/AT]
SALES_GROWTH	Compustat	Year-over-year sales growth [(SALE in year *t* - SALE in year *t*-1) / SALE in year *t*-1]
SIZE	Compustat	Natural logarithm of total assets [log(AT)]
THREE_OR_MORE	BoardEx	Indicator variable equal to one if director *d* holds more than two audit committee seats in year *t*, and zero otherwise
VOL_CF_OP	Compustat	Volatility of cash flows. Measured as standard deviation of variable *CFO* over years [*t-4* to *t-1]*

Appendix B
Measurement of Relative Reputation Incentives (*HIGH_REP)*

Firm	**Director**	**Market Cap**	**Difference**	***HIGH_REP***
Y	John Doe	$500 M	-	1
Z	John Doe	$300 M	40%	0

Firm	**Director**	**Market Cap**	**Difference**	***HIGH_REP***
A	Jane Smith	$500 M	-	1
B	Jane Smith	$475 M	5%	1
C	Jane Smith	$200 M	60%	0

Notes: This appendix serves as an example of how my variable of interest, *HIGH_REP,* is measured. In the first example, John Doe's audit committee seats are ranked by the market capitalization of the firms at which he serves as audit committee chair or designated financial expert. His audit committee seat at his largest firm is automatically a high reputation incentive directorship. His second audit committee seat is over 10% smaller than the largest (it is 40% smaller), so it is not a high reputation incentive directorship. In the second example, Jane Smith's audit committee seats are also ranked by the market capitalization of the firms at which she serves as audit committee chair or designated financial expert. Her audit committee seat at her largest firm is automatically a high reputation incentive directorship. Her second audit committee seat is only 5% smaller than her largest audit committee seat (within 10%), so it is also a high reputation incentive directorship. Her third audit committee seat is 60% smaller than her largest audit committee seat (more than 10% smaller), so it is not a high reputation incentive directorship.

Appendix C
Tables

Table 1
Sample Selection

Misstatement Sample	**Observations**
Firms covered by AA, BoardEx, and Compustat with AC CHAIR or FINEXP that serves on multiple audit committees	8,991
Drop regulated firms	(1,161)
Drop directors that no longer have multiple audit committees in the sample	(820)
Less: firms missing data to estimate Equation (1)	(3,870)
Final Sample in Misstatements Analysis	3,140

F-Score Sample	**Observations**
Firms covered by AA, BoardEx, and Compustat with AC CHAIR or FINEXP that serves on multiple audit committees	8,991
Drop regulated firms	(1,161)
Drop directors that no longer have multiple audit committees in the sample	(820)
Less: firms missing data to calculate F-Score	(1,046)
Less: firms missing data to estimate Equation (4)	(3,217)
Final Sample in F-Score Analysis	2,747

Table 1 Continued
Sample Selection

Material Weakness Sample	**Observations**
Firms covered by AA, BoardEx, and Compustat with AC CHAIR or FINEXP that serves on multiple audit committees	8,991
Drop regulated firms	(1,161)
Drop directors that no longer have multiple audit committees in the sample	(820)
Less: firms not covered by AA SOX 404(B) database	(2,390)
Less: firms missing data to estimate Equation (2)	(2,491)
Final Sample in Material Weakness Analysis	2,129

Accruals Sample	**Observations**
Firms covered by AA, BoardEx, and Compustat with AC CHAIR or FINEXP that serves on multiple audit committees	8,991
Drop regulated firms	(1,161)
Drop directors that no longer have multiple audit committees in the sample	(820)
Less: firms missing data to calculate accruals	(876)
Less: firms missing data to estimate Equation (3)	(3,355)
Final Sample in Accruals Analysis	2,779

Table 2
Descriptive Statistics

Panel A

Variable	N	Mean	Median	Std. Dev.	25%	75%
MISSTATE	3,140	0.10	0.00	0.30	0.00	0.00
F_SCORE	2,747	1.15	0.91	5.21	0.57	1.36
HIGH_FSCORE	2,747	0.08	0.00	0.27	0.00	0.00
MWEAK	2,129	0.05	0.00	0.21	0.00	0.00
ABSDA	2,779	0.05	0.04	0.06	0.02	0.07
HIGH_REP	3,140	0.48	0.00	0.50	0.00	1.00
SIZE	3,140	6.56	6.57	1.87	5.31	7.82
MTB	3,140	3.72	2.22	7.95	1.45	3.76
ROA	3,140	-0.01	0.04	0.23	-0.01	0.08
LOSS	3,140	0.28	0.00	0.45	0.00	1.00
LEV	3,140	0.19	0.17	0.18	0.01	0.32
AR_INV	3,140	0.25	0.23	0.19	0.11	0.36
BIG4	3,140	0.84	1.00	0.36	1.00	1.00
AUD_IMPORT	3,140	0.09	0.03	0.15	0.01	0.09
IND_SPECIALIST	3,140	0.24	0.00	0.43	0.00	0.00
BUSSEG_SR	3,140	2.15	1.73	1.05	1.73	3.00
RESTRUCTURE	3,140	0.32	0.00	0.47	0.00	1.00
M&A	3,140	0.04	0.00	0.21	0.00	0.00
FOREIGN	3,140	0.30	0.00	0.46	0.00	1.00
BDINDEP	3,140	0.76	0.80	0.13	0.67	0.88
BDSIZE	3,140	8.29	8.00	2.11	7.00	10.00
ACSIZE	3,140	3.57	3.00	0.86	3.00	4.00
NUM_AC	3,140	2.42	2.00	0.66	2.00	3.00
DIR_TENURE	3,140	6.73	5.20	5.91	2.40	9.30
CO_AGE	2,129	23.80	17.00	17.24	10.00	36.00
SALES_GROWTH	2,129	0.18	0.08	1.42	0.00	0.20
VOL_CF_OP	2,779	0.07	0.03	0.44	0.02	0.06
LAG_ABSDA	2,779	0.06	0.04	0.06	0.02	0.07

Notes: This table presents descriptive statistics for my sample. All variables are defined as in Appendix A

Table 2 Continued
Descriptive Statistics

Panel B					
Director-Year Level Descriptives					
Variable	Mean	Median	Std. Dev.	25%	75%
NUM_AC	2.37	2.00	0.62	2.00	3.00
NUM_HIGH_REP	1.00	1.00	0.00	1.00	1.00
PROP_HIGH_REP	0.44	0.50	0.09	0.33	0.50
NUM_NOT_HIGH_REP	1.37	1.00	0.62	1.00	2.00
PROP_NOT_HIGH_REP	0.56	0.50	0.09	0.50	0.67
Director-Year Observations	1,494				

Notes: This table presents descriptive statistics for unique director years. All variables are defined as in Appendix A

Table 3
Univariate Tests

Panel A	**MISSTATE SAMPLE**			**F_SCORE SAMPLE**		
	HIGH_REP = 0	***HIGH_REP = 1***	**p-val**	***HIGH_REP = 0***	***HIGH_REP = 1***	**p-val**
MISSTATE	0.06	0.06	(0.708)			
HIGH_FSCORE				0.09	0.08	(0.068)*
SIZE	5.77	7.41	(0.000)***	5.82	7.46	(0.000)***
MTB	3.44	4.03	(0.020)**	3.32	3.93	(0.025)**
ROA	-0.04	0.02	(0.000)***	-0.03	0.04	(0.000)***
LOSS	0.37	0.19	(0.000)***	0.35	0.17	(0.000)***
LEV	0.18	0.21	(0.000)***	0.17	0.22	(0.000)***
AR_INV	0.27	0.24	(0.000)***	0.29	0.25	(0.000)***
BIG4	0.79	0.90	(0.000)***	0.81	0.91	(0.000)***
AUD_IMPORT	0.08	0.10	(0.000)***	0.08	0.11	(0.000)***
IND_SPECIAL	0.23	0.26	(0.023)**	0.24	0.27	(0.048)**
BUSSEG_SR	2.04	2.18	(0.000)***	2.09	2.24	(0.000)***
RESTRUCTURE	0.31	0.33	(0.133)	0.33	0.35	(0.335)
M&A	0.04	0.05	(0.174)	0.05	0.05	(0.167)
FOREIGN	0.29	0.32	(0.081)*	0.3	0.32	(0.068)*
BDINDEP	0.75	0.77	(0.000)***	0.76	0.78	(0.000)***
BDSIZE	7.92	8.70	(0.000)***	8.01	8.80	(0.000)***
ACSIZE	3.50	3.64	(0.000)***	3.53	3.66	(0.000)***
NUM_AC	2.46	2.37	(0.000)***	2.46	2.38	(0.000)***
DIR_TENURE	6.69	6.77	(0.642)	7.03	7.04	(0.522)
Observations	1,636	1,504		1,429	1,322	

Notes: This table presents a test of differences in means between higher reputation incentive firms (*HIGH_REP* = 1) and firms that are not high reputation incentive firms (*HIGH_REP* = 0) in a director's portfolio of audit committee seats. All variables are defined as in Appendix A. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels (two-sided).

Table 3 Continued
Univariate Tests

Panel B	**MWEAK SAMPLE**			**ABSDA SAMPLE**		
	HIGH_REP = 0	***HIGH_REP = 1***	**p-val**	***HIGH_REP = 0***	***HIGH_REP = 1***	**p-val**
MWEAK	0.06	0.04	(0.015)**			
ABSDA				0.06	0.05	(0.010)**
SIZE	6.35	7.87	(0.000)***	5.94	7.59	(0.000)***
MTB	3.65	4.5	(0.001)***	3.54	4.31	(0.001)***
ROA	-0.03	0.04	(0.000)***	-0.06	0.02	(0.000)***
LOSS	0.36	0.18	(0.000)***	0.41	0.23	(0.000)***
LEV	0.18	0.2	(0.012)**	0.17	0.19	(0.000)***
AR_INV	0.24	0.22	(0.000)***	0.25	0.22	(0.000)***
BIG4	0.87	0.94	(0.000)***	0.82	0.90	(0.000)***
AUD_IMPORT	0.08	0.10	(0.001)***	0.08	0.10	(0.000)***
IND_SPECIAL	0.25	0.27	(0.215)	0.23	0.23	(0.447)
BUSSEG_SR	2.09	2.22	(0.000)***	2.06	2.17	(0.001)***
RESTRUCTURE	0.38	0.38	(0.400)	0.33	0.35	(0.145)
M&A	0.05	0.06	(0.183)	0.05	0.05	(0.224)
FOREIGN	0.34	0.37	(0.004)***	0.31	0.34	(0.020)**
BDINDEP	0.78	0.79	(0.034)**	0.76	0.78	(0.000)***
BDSIZE	8.22	8.92	(0.000)***	7.82	8.58	(0.000)***
ACSIZE	3.50	3.64	(0.000)***	3.39	3.53	(0.000)***
NUM_AC	2.50	2.42	(0.002)***	2.52	2.39	(0.000)***
DIR_TENURE	6.98	7.25	(0.150)	6.68	6.85	(0.224)
CO_AGE	2.75	2.89	(0.000)***			
SALES_GROWTH	0.34	0.19	(0.141)			
VOL_CF_OP				0.08	0.06	(0.018)**
LAG_ABSDA				0.07	0.06	(0..000)***
Observations	1,105	1,024		1,447	1,332	

Notes: This table presents a test of differences in means between higher reputation incentive firms (*HIGH_REP* = 1) and firms that are not high reputation incentive firms (*HIGH_REP* = 0) in a director's portfolio of audit committee seats. All variables are defined as in Appendix A. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels (two-sided).

Table 4
Main Multivariate Analysis

Panel A

	Column 1			Column 2		
	MISSTATE			*HIGH_FSCORE*		
VARIABLES	**coef**	**p-value**		**coef**	**p-value**	
Constant	0.402	(0.000)	***	0.082	(0.356)	
HIGH_REP	**-0.004**	**(0.714)**		**-0.027**	**(0.089)**	*
SIZE	0.013	(0.518)		0.035	(0.000)	***
MTB	0.001	(0.630)		-0.001	(0.038)	**
ROA	0.030	(0.323)		-0.034	(0.334)	
LOSS	0.036	(0.002)	***	-0.029	(0.102)	
LEV	0.071	(0.058)	*	0.190	(0.001)	***
AR_INV	0.032	(0.597)		0.417	(0.000)	***
BIG4	0.004	(0.849)		0.013	(0.629)	
AUD_IMPORT	-0.079	(0.562)		0.014	(0.745)	
IND_SPECIALIST	0.021	(0.232)		0.003	(0.865)	
BUSSEG_SR	-0.004	(0.693)		-0.010	(0.176)	
RESTRUCTURE	0.019	(0.278)		-0.036	(0.021)	**
M&A	0.008	(0.766)		0.130	(0.000)	***
FOREIGN	0.033	(0.344)		-0.007	(0.616)	***
BDINDEP	-0.063	(0.281)		-0.221	(0.001)	***
BDSIZE	-0.002	(0.739)		-0.001	(0.851)	
ACSIZE	-0.008	(0.479)		-0.015	(0.072)	*
NUM_AC	0.004	(0.819)		0.010	(0.499)	
DIR_TENURE	0.002	(0.137)		0.000	(0.677)	
Year FE		Yes			Yes	
Industry FE		Yes			Yes	
Director FE		Yes			Yes	
Adj R-Squared		0.14			0.23	
Observations		3,140			2,747	

Notes: Panel A presents the results from estimating Equation (1). Column 1 presents a linear probability model examining the effect of the relative reputation incentives that a firm offers to the director on the likelihood of a misstatement, *MISSTATE*. Column 2 presents a linear probability model examining the effect of the relative reputation incentives that a firm offers to the director on the likelihood that the firm's F-Score is greater than 1.85, *HIGH_FSCORE*. P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 4 Continued
Main Multivariate Analysis

Panel B

	MWEAK		
VARIABLES	**coef**	**p-value**	
Constant	0.034	(0.720)	
HIGH_REP	**-0.021**	**(0.061)**	*
SIZE	0.011	(0.174)	
MTB	0.000	(0.698)	
ROA	-0.056	(0.283)	
LOSS	0.027	(0.096)	*
LEV	0.067	(0.097)	*
AR_INV	0.039	(0.528)	
BIG4	0.000	(0.798)	
AUD_IMPORT	0.045	(0.181)	
IND_SPECIALIST	0.015	(0.356)	
BUSSEG_SR	-0.015	(0.023)	**
RESTRUCTURE	0.022	(0.171)	
M&A	0.013	(0.499)	
FOREIGN	0.018	(0.187)	
BDINDEP	-0.055	(0.289)	
BDSIZE	-0.003	(0.281)	
ACSIZE	0.011	(0.581)	
NUM_AC	-0.003	(0.943)	
DIR_TENURE	-0.001	(0.027)	**
CO_AGE	0.020	(0.023)	**
SALES_GROWTH	0.001	(0.691)	
Year FE		Yes	
Industry FE		Yes	
Director FE		Yes	
Adj R-Squared		0.15	
Observations		2,129	

Notes: Panel B presents the results from estimating Equation (2) using a linear probability model. The model examines the effect of the relative reputation incentives that a firm offers to the director on the likelihood of a material weakness in internal controls over financial reporting, *MWEAK*. P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 4 Continued
Main Multivariate Analysis

Panel C

	ABSDA		
VARIABLES	**coef**	**p-value**	
Constant	0.030	(0.031)	***
HIGH_REP	**-0.004**	**(0.094)**	*
SIZE	-0.003	(0.037)	**
MTB	0.000	(0.483)	
ROA	0.014	(0.079)	*
LOSS	-0.003	(0.299)	*
LEV	0.020	(0.004)	***
AR_INV	0.026	(0.015)	
BIG4	0.001	(0.828)	
AUD_IMPORT	0.018	(0.002)	***
IND_SPECIALIST	0.001	(0.534)	
BUSSEG_SR	-0.002	(0.015)	**
RESTRUCTURE	-0.003	(0.272)	
M&A	0.001	(0.742)	
FOREIGN	-0.001	(0.650)	
BDINDEP	-0.009	(0.289)	
BDSIZE	0.002	(0.026)	**
ACSIZE	-0.002	(0.270)	
NUM_AC	-0.001	(0.807)	
DIR_TENURE	0.000	(0.483)	
VOL_CFO	0.073	(0.003)	***
LAG_ABSDA	0.037	(0.096)	*
Year FE	Yes		
Industry FE	Yes		
Director FE	Yes		
Adj R-Squared	0.17		
Observations	2,779		

Notes: Panel C presents the results from estimating Equation (3) using an OLS model. The model examines the effect of the relative reputation incentives that a firm offers to the director on the absolute value of performance-adjusted discretionary accruals, *ABSDA*. P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 5
Director Descriptive Statistics by Busyness Level

Directors with Two Audit Committee Seats					
Variable	Mean	Median	Std. Dev.	25%	75%
NUM_AC	2.00	2.00	0.00	2.00	2.00
NUM_HIGH_REP	1.00	1.00	0.00	1.00	1.00
PROP_HIGH_REP	0.50	0.50	0.00	0.50	0.50
NUM_NOT_HIGH_REP	1.00	1.00	0.00	1.00	1.00
PROP_NOT_HIGH_REP	0.50	0.50	0.00	0.50	0.50
Director-Year Observations	1,041				

Notes: This table presents descriptive statistics for director-years in which the director holds two audit committee seats. All variables are defined as in Appendix A

Directors with Three or More Audit Committee Seats					
Variable	Mean	Median	Std. Dev.	25%	75%
NUM_AC	3.21	3.00	0.49	3.00	3.00
NUM_HIGH_REP	1.00	1.00	0.00	1.00	1.00
PROP_HIGH_REP	0.32	0.33	0.04	0.33	0.33
NUM_NOT_HIGH_REP	2.21	2.00	0.49	2.00	2.00
PROP_NOT_HIGH_REP	0.68	0.67	0.04	0.67	0.67
Director-Year Observations	452				

Notes: This table presents descriptive statistics for director-years in which the director holds three or more audit committee seats. All variables are defined as in Appendix A

Table 6
Busyness Level Interaction Analysis

Panel A						
	Column 1			**Column 2**		
	MISSTATE			*HIGH_FSCORE*		
VARIABLES	**coef**	**p-value**		**coef**	**p-value**	
Constant	0.467	(0.000)	***	0.051	(0.607)	
HIGH_REP	-0.006	(0.657)		-0.021	(0.247)	
THREE_OR_MORE	0.058	(0.099)	*	-0.018	(0.643)	
HIGH_REP*THREE_OR_MORE	**0.005**	**(0.766)**		**-0.017**	**(0.444)**	
SIZE	0.001	(0.948)		0.058	(0.001)	***
MTB	-0.001	(0.699)		-0.002	(0.064)	*
ROA	0.054	(0.180)		-0.033	(0.452)	
LOSS	0.074	(0.009)	***	-0.027	(0.098)	*
LEV	0.078	(0.047)	**	0.184	(0.001)	***
AR_INV	0.063	(0.239)		0.402	(0.000)	***
BIG4	-0.014	(0.650)		0.020	(0.529)	
AUD_IMPORT	-0.035	(0.401)		0.014	(0.748)	
IND_SPECIALIST	0.032	(0.250)		0.002	(0.874)	
BUSSEG_SR	-0.011	(0.519)		-0.011	(0.172)	
RESTRUCTURE	0.014	(0.585)		-0.036	(0.021)	**
M&A	-0.038	(0.418)		0.130	(0.000)	***
FOREIGN	0.018	(0.276)		-0.006	(0.592)	
BDINDEP	-0.015	(0.866)		-0.222	(0.001)	***
BDSIZE	-0.003	(0.637)		-0.001	(0.883)	
ACSIZE	-0.002	(0.925)		-0.015	(0.070)	*
DIR_TENURE	0.001	(0.669)		0.000	(0.695)	
Year FE		Yes			Yes	
Industry FE		Yes			Yes	
Director FE		Yes			Yes	
Adj R-Squared		0.14			0.23	
Observations		3,140			2,747	
Joint Test of Coefficients						
Coefficients	coef	p-value		coef	p-value	
$\alpha_1 + \alpha_3 = 0$	-0.001	(0.950)		-0.038	(0.160)	

Notes: Panel A presents the results from estimating Equation (1) using a linear probability model. It examines the moderating effect of the director's level of busyness on the effect of *HIGH_REP* on FRQ. P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 6 Continued
Busyness Level Interaction Analysis

Panel B			
		MWEAK	
VARIABLES	**coef**	**p-value**	
Constant	-0.018	(0.936)	
HIGH_REP	-0.020	(0.068)	*
THREE_OR_MORE	0.008	(0.735)	
HIGH_REP*THREE_OR_MORE	**-0.009**	**(0.639)**	
SIZE	-0.011	(0.553)	
MTB	0.001	(0.713)	
ROA	-0.113	(0.199)	
LOSS	0.026	(0.387)	
LEV	0.098	(0.211)	
AR_INV	0.078	(0.442)	
BIG4	-0.006	(0.859)	
AUD_IMPORT	0.075	(0.265)	
IND_SPECIALIST	0.032	(0.181)	
BUSSEG_SR	-0.042	(0.005)	***
RESTRUCTURE	0.036	(0.183)	
M&A	0.037	(0.446)	
FOREIGN	0.002	(0.925)	
BDINDEP	-0.096	(0.296)	
BDSIZE	0.002	(0.761)	
ACSIZE	0.020	(0.178)	
DIR_TENURE	0.001	(0.506)	
CO_AGE	0.020	(0.022)	**
SALES_GROWTH	-0.001	(0.366)	
Year FE		Yes	
Industry FE		Yes	
Director FE		Yes	
Adj R-Squared		0.15	
Observations		2,129	
Joint Test of Coefficients			
Coefficients	coef	p- value	
$\beta_1 + \beta_3 = 0$	-0.029	(0.060)	*

Notes: Panel B presents the results from estimating Equation (2) using a linear probability model. It examines the moderating effect of the director's level of busyness on the effect of *HIGH_REP* on FRQ. P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 6 Continued
Busyness Level Interaction Analysis

Panel C

		ABSDA	
VARIABLES	**coef**	**p-value**	
Constant	0.016	(0.316)	
HIGH_REP	-0.004	(0.080)	*
THREE_OR_MORE	-0.008	(0.213)	
HIGH_REP*THREE_OR_MORE	**0.000**	**(0.951)**	
SIZE	-0.003	(0.043)	**
MTB	0.001	(0.494)	
ROA	0.012	(0.093)	*
LOSS	-0.004	(0.290)	
LEV	0.020	(0.004)	***
AR_INV	0.027	(0.012)	**
BIG4	0.001	(0.817)	
AUD_IMPORT	0.018	(0.002)	***
IND_SPECIALIST	0.000	(0.552)	
BUSSEG_SR	-0.003	(0.015)	**
RESTRUCTURE	-0.002	(0.285)	
M&A	0.014	(0.186)	
FOREIGN	-0.002	(0.554)	
BDINDEP	-0.002	(0.903)	
BDSIZE	0.002	(0.026)	**
ACSIZE	-0.001	(0.807)	
DIR_TENURE	-0.001	(0.309)	
VOL_CFO	0.072	(0.003)	***
LAG_ABSDA	0.037	(0.094)	*
Year FE		Yes	
Industry FE		Yes	
Director FE		Yes	
Adj R-Squared		0.17	
Observations		2,779	

Joint Test of Coefficients

Coefficients	coef	p- value	
$\chi_1 + \chi_3 = 0$	-0.004	(0.098)	*

Notes: Panel C presents the results from estimating Equation (3) using an OLS model. It examines the moderating effect of the director's level of busyness on the effect of *HIGH_REP* on FRQ. P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 7
Director-Firm-Year Descriptive Statistics on Tenure

MISSTATE SAMPLE

Variable	Mean	Median	Std. Dev.	25%	75%
EARLY_TENURE	0.30	0.00	0.46	0.00	1.00
Director-Firm-Year Observations	3,140				

Notes: This table presents descriptive statistics for director-firm-years in the *MISSTATE* sample All variables are defined as in Appendix A

F_SCORE SAMPLE

Variable	Mean	Median	Std. Dev.	25%	75%
EARLY_TENURE	0.27	0.00	0.46	0.00	1.00
Director-Firm-Year Observations	2,747				

Notes: This table presents descriptive statistics for director-firm-years in the *FSCORE* sample All variables are defined as in Appendix A

MWEAK SAMPLE

Variable	Mean	Median	Std. Dev.	25%	75%
EARLY_TENURE	0.26	0.00	0.44	0.00	1.00
Director-Firm-Year Observations	2,129				

Notes: This table presents descriptive statistics for director-firm-years in the *MWEAK* sample All variables are defined as in Appendix A

ABSDA SAMPLE

Variable	Mean	Median	Std. Dev.	25%	75%
EARLY_TENURE	0.29	0.00	0.47	0.00	1.00
Director-Firm-Year Observations	2,779				

Notes: This table presents descriptive statistics for director-firm-years in the *ABSDA* sample All variables are defined as in Appendix A

Table 8
Early Tenure Interaction Analysis

Panel A

	Column 1			Column 2		
	MISSTATE			*HIGH_FSCORE*		
VARIABLES	**coef**	**p-value**		**coef**	**p-value**	
Constant	0.392	(0.000)	***	0.087	(0.322)	
HIGH_REP	-0.001	(0.931)		-0.020	(0.228)	
EARLY_TENURE	0.005	(0.759)		0.012	(0.568)	
HIGH_REP*EARLY_TENURE	**-0.012**	**(0.560)**		**-0.021**	**(0.415)**	
SIZE	0.002	(0.905)		0.055	(0.000)	***
MTB	-0.001	(0.716)		-0.002	(0.091)	*
ROA	0.053	(0.192)		-0.030	(0.490)	
LOSS	0.074	(0.003)	***	-0.025	(0.256)	
LEV	0.077	(0.047)	**	0.118	(0.110)	
AR_INV	0.175	(0.229)		0.390	(0.000)	***
BIG4	-0.015	(0.645)		0.022	(0.514)	
AUD_IMPORT	-0.185	(0.385)		0.103	(0.176)	
IND_SPECIALIST	0.032	(0.243)		0.053	(0.033)	**
BUSSEG_SR	-0.011	(0.514)		-0.013	(0.205)	
RESTRUCTURE	0.014	(0.590)		-0.042	(0.113)	
M&A	-0.037	(0.420)		0.081	(0.097)	*
FOREIGN	0.066	(0.279)		-0.008	(0.652)	
BDINDEP	-0.014	(0.879)		-0.233	(0.008)	***
BDSIZE	-0.003	(0.646)		0.006	(0.369)	
ACSIZE	-0.003	(0.901)		-0.018	(0.198)	
NUM_AC	0.015	(0.607)		-0.018	(0.414)	
Year FE		Yes			Yes	
Industry FE		Yes			Yes	
Director FE		Yes			Yes	
Adj R-Squared		0.14			0.23	
Observations		3,140			2,747	

Joint Test of Coefficients

Coefficients	coef	p- value	coef	p- value
$\alpha_1 + \alpha_3 = 0$	-0.013	(0.509)	-0.041	(0.116)

Notes: Panel A presents the results from estimating Equation (1) using a linear probability model. It examines the moderating effect of the tenure of the director on the effect of *HIGH_REP* on FRQ. P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 8 Continued
Early Tenure Interaction Analysis

Panel B			
		MWEAK	
VARIABLES	**coef**	**p-value**	
Constant	-0.075	(0.710)	
HIGH_REP	-0.020	(0.085)	*
EARLY_TENURE	0.032	(0.092)	*
HIGH_REP*EARLY_TENURE	**-0.016**	**(0.531)**	
SIZE	-0.016	(0.384)	
MTB	0.001	(0.730)	
ROA	-0.111	(0.209)	
LOSS	0.024	(0.429)	
LEV	0.097	(0.224)	
AR_INV	0.074	(0.467)	
BIG4	-0.007	(0.827)	
AUD_IMPORT	0.074	(0.273)	
IND_SPECIALIST	0.034	(0.162)	
BUSSEG_SR	-0.016	(0.028)	**
RESTRUCTURE	0.038	(0.164)	
M&A	0.040	(0.402)	
FOREIGN	0.003	(0.906)	
BDINDEP	-0.098	(0.284)	
BDSIZE	0.001	(0.822)	
ACSIZE	0.002	(0.175)	
NUM_AC	0.020	(0.831)	
CO_AGE	0.022	(0.015)	**
SALES_GROWTH	0.001	(0.744)	
Year FE		Yes	
Industry FE		Yes	
Director FE		Yes	
Adj R-Squared		0.14	
Observations		2,129	
Joint Test of Coefficients			
Coefficients	coef	p- value	
$\beta_1 + \beta_3 = 0$	-0.036	(0.089)	*

Notes: Panel A presents the results from estimating Equation (2) using a linear probability model. It examines the moderating effect of the tenure of the director on the effect of *HIGH_REP* on FRQ. P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 8 Continued
Early Tenure Interaction Analysis

Panel C			
		ABSDA	
VARIABLES	**coef**	**p-value**	
Constant	0.030	(0.188)	
HIGH_REP	-0.004	(0.085)	*
EARLY_TENURE	0.003	(0.338)	
HIGH_REP*EARLY_TENURE	**0.000**	**(0.925)**	
SIZE	-0.001	(0.878)	
MTB	0.001	(0.039)	**
ROA	0.013	(0.168)	
LOSS	-0.005	(0.305)	
LEV	-0.002	(0.848)	
AR_INV	0.030	(0.098)	*
BIG4	0.009	(0.077)	*
AUD_IMPORT	0.041	(0.006)	***
IND_SPECIALIST	0.000	(0.954)	
BUSSEG_SR	-0.002	(0.182)	
RESTRUCTURE	-0.007	(0.077)	*
M&A	0.015	(0.085)	*
FOREIGN	-0.002	(0.615)	
BDINDEP	-0.001	(0.912)	
BDSIZE	-0.001	(0.797)	
ACSIZE	-0.001	(0.904)	
NUM_AC	-0.003	(0.747)	
VOL_CFO	0.137	(0.000)	***
LAG_ABSDA	0.076	(0.001)	***
Year FE		Yes	
Industry FE		Yes	
Director FE		Yes	
Adj R-Squared		0.17	
Observations		2,779	
Joint Test of Coefficients			
Coefficients	coef	p- value	
$\chi_1 + \chi_3 = 0$	-0.004	(0.093)	*

Notes: Panel A presents the results from estimating Equation (3) using an OLS model. It examines the moderating effect of the tenure of the director on the effect of *HIGH_REP* on FRQ. P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 9
Threshold Analysis

Panel A

	Column 1			Column 2		
	MISSTATE			*MISSTATE*		
VARIABLES	**coef**	**p-value**		**coef**	**p-value**	
Constant	0.385	(0.000)	***	0.300	(0.001)	***
HIGH_REP_20	**-0.005**	**(0.727)**				
HIGH_REP_50				**0.021**	**(0.216)**	
SIZE	0.010	(0.414)		-0.002	(0.847)	
MTB	0.001	(0.972)		-0.001	(0.202)	
ROA	0.017	(0.166)		0.016	(0.555)	
LOSS	0.040	(0.005)	***	0.025	(0.148)	
LEV	0.100	(0.034)	**	-0.035	(0.370)	
AR_INV	0.165	(0.163)		0.005	(0.926)	
BIG4	0.019	(0.466)		0.024	(0.199)	
AUD_IMPORT	-0.052	(0.217)		-0.077	(0.056)	*
IND_SPECIALIST	0.003	(0.824)		-0.001	(0.993)	
BUSSEG_SR	0.001	(0.866)		0.003	(0.434)	
RESTRUCTURE	-0.001	(0.530)		-0.009	(0.665)	
M&A	0.000	(0.997)		-0.011	(0.747)	
FOREIGN	0.066	(0.939)		0.031	(0.043)	**
BDINDEP	-0.031	(0.164)		-0.022	(0.742)	
BDSIZE	-0.002	(0.702)		-0.001	(0.855)	
ACSIZE	-0.012	(0.538)		-0.008	(0.456)	
NUM_AC	-0.011	(0.615)		-0.007	(0.739)	
DIR_TENURE	0.000	(0.519)		0.001	(0.579)	
Year FE		Yes			Yes	
Industry FE		Yes			Yes	
Director FE		Yes			Yes	
Adj R-Squared		0.13			0.12	
Observations		3,012			2,357	

Notes: Panel A presents the results from estimating Equation (1) using different thresholds for the main variable of interest, *HIGH_REP*. Columns 1 and 2 present linear probability models examining the effect of the relative reputation incentives that a firm offers to the director on the likelihood of a misstatement, *MISSTATE*. Columns 1 and 2 use a 20% relative size threshold and a 50% relative size threshold, respectively, to measure *HIGH_REP*. P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 9 Continued
Threshold Analysis

Panel B

	Column 1			Column 2		
	HIGH_FSCORE			*HIGH_FSCORE*		
VARIABLES	**coef**	**p-value**		**coef**	**p-value**	
Constant	0.091	(0.334)		0.071	(0.488)	
HIGH_REP_20	**-0.028**	**(0.087)**	*			
HIGH_REP_50				**-0.068**	**(0.081)**	*
SIZE	0.036	(0.000)	***	0.035	(0.001)	***
MTB	-0.001	(0.033)	**	-0.001	(0.067)	*
ROA	-0.035	(0.345)		-0.029	(0.492)	
LOSS	-0.031	(0.087)	*	-0.025	(0.242)	
LEV	0.185	(0.011)	**	0.155	(0.008)	***
AR_INV	0.439	(0.000)	***	0.321	(0.000)	***
BIG4	0.014	(0.613)		0.020	(0.530)	
AUD_IMPORT	0.083	(0.754)		0.100	(0.184)	
IND_SPECIALIST	0.019	(0.387)		0.016	(0.388)	
BUSSEG_SR	-0.010	(0.196)		-0.012	(0.256)	
RESTRUCTURE	-0.036	(0.019)	**	-0.039	(0.031)	**
M&A	0.128	(0.000)	***	0.101	(0.005)	***
FOREIGN	-0.011	(0.463)		-0.008	(0.646)	
BDINDEP	-0.216	(0.002)	**	-0.203	(0.005)	***
BDSIZE	-0.001	(0.780)		0.001	(0.920)	
ACSIZE	-0.017	(0.046)	**	-0.018	(0.042)	**
NUM_AC	0.005	(0.723)		-0.013	(0.949)	
DIR_TENURE	-0.001	(0.617)		0.000	(0.959)	
Year FE		Yes			Yes	
Industry FE		Yes			Yes	
Director FE		Yes			Yes	
Adj R-Squared		0.22			0.23	
Observations		2,632			2,052	

Notes: Panel B presents the results from estimating Equation (1) using different thresholds for the main variable of interest, *HIGH_REP*. Columns 1 and 2 present linear probability models examining the effect of the relative reputation incentives that a firm offers to the director on the likelihood that the firm's F-Score is greater than 1.85, *HIGH_FSCORE*. Columns 1 and 2 use a 20% relative size threshold and a 50% relative size threshold, respectively, to measure *HIGH_REP*. P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 9 Continued
Threshold Analysis

Panel C

	Column 1			Column 2		
	MWEAK			*MWEAK*		
VARIABLES	**coef**	**p-value**		**coef**	**p-value**	
Constant	0.001	(0.994)		0.128	(0.368)	
HIGH_REP_20	**-0.025**	**(0.064)**	*			
HIGH_REP_50				**-0.008**	**(0.051)**	*
SIZE	0.012	(0.152)		0.020	(0.125)	
MTB	0.000	(0.744)		0.001	(0.678)	
ROA	-0.046	(0.405)		-0.064	(0.386)	
LOSS	0.038	(0.110)		0.037	(0.096)	*
LEV	0.086	(0.068)	*	0.038	(0.597)	
AR_INV	0.111	(0.122)		0.065	(0.426)	
BIG4	0.036	(0.242)		0.013	(0.772)	
AUD_IMPORT	0.065	(0.170)		0.043	(0.442)	
IND_SPECIALIST	0.018	(0.276)		0.068	(0.001)	
BUSSEG_SR	-0.017	(0.023)	**	-0.018	(0.034)	***
RESTRUCTURE	0.027	(0.183)		0.032	(0.204)	
M&A	-0.004	(0.876)		0.012	(0.600)	
FOREIGN	0.012	(0.939)		0.004	(0.870)	
BDINDEP	-0.050	(0.424)		-0.069	(0.378)	
BDSIZE	-0.004	(0.392)		-0.005	(0.396)	
ACSIZE	0.007	(0.333)		0.015	(0.045)	**
NUM_AC	-0.004	(0.861)		0.007	(0.802)	
DIR_TENURE	-0.001	(0.516)		-0.001	(0.400)	
CO_AGE	0.022	(0.012)	**	0.010	(0.354)	
SALES_GROWTH	0.001	(0.537)		-0.005	(0.507)	
Year FE		Yes			Yes	
Industry FE		Yes			Yes	
Director FE		Yes			Yes	
Adj R-Squared		0.15			0.14	
Observations		2,013			1,508	

Notes: Panel C presents the results from estimating Equation (2) using different thresholds for the main variable of interest, *HIGH_REP*. Columns 1 and 2 present linear probability models examining the effect of the relative reputation incentives that a firm offers to the director on the likelihood of a material weakness in internal controls over financial reporting, *MWEAK*. Columns 1 and 2 use a 20% relative size threshold and a 50% relative size threshold, respectively, to measure *HIGH_REP*. P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 9 Continued
Threshold Analysis

Panel D

	Column 1			Column 2		
	ABSDA			*ABSDA*		
VARIABLES	**coef**	**p-value**		**coef**	**p-value**	
Constant	0.029	(0.038)	**	0.027	(0.116)	
HIGH_REP_20	**-0.004**	**(0.065)**	*			
HIGH_REP_50				**-0.008**	**(0.056)**	*
SIZE	-0.003	(0.033)	**	-0.001	(0.376)	
MTB	0.000	(0.453)		0.001	(0.040)	**
ROA	0.013	(0.143)		0.012	(0.840)	
LOSS	-0.002	(0.570)		-0.004	(0.627)	
LEV	0.021	(0.003)	***	0.018	(0.036)	**
AR_INV	0.025	(0.045)	**	0.023	(0.057)	*
BIG4	0.002	(0.579)		0.008	(0.101)	
AUD_IMPORT	0.018	(0.005)	***	0.016	(0.026)	**
IND_SPECIALIST	-0.002	(0.538)		0.000	(0.925)	
BUSSEG_SR	-0.022	(0.033)	**	-0.002	(0.200)	
RESTRUCTURE	-0.004	(0.122)		-0.008	(0.080)	*
M&A	0.005	(0.443)		0.014	(0.186)	
FOREIGN	-0.002	(0.650)		-0.002	(0.401)	
BDINDEP	-0.001	(0.438)		-0.002	(0.342)	
BDSIZE	0.002	(0.030)	**	0.002	(0.084)	*
ACSIZE	-0.001	(0.952)		-0.001	(0.838)	
NUM_AC	-0.005	(0.136)		-0.001	(0.473)	
DIR_TENURE	-0.001	(0.125)		-0.001	(0.300)	
VOL_CFO	0.067	(0.006)	***	0.095	(0.001)	***
LAG_ABSDA	0.038	(0.111)		0.040	(0.172)	
Year FE		Yes			Yes	
Industry FE		Yes			Yes	
Director FE		Yes			Yes	
Adj R-Squared		0.17			0.14	
Observations		2,604			2,042	

Notes: Panel D presents the results from estimating Equation (3) using different thresholds for the main variable of interest, *HIGH_REP*. Columns 1 and 2 present OLS models examining the effect of the relative reputation incentives that a firm offers to the director on the absolute value of performance-adjusted discretionary accruals, *ABSDA*. Columns 1 and 2 use a 20% relative size threshold and a 50% relative size threshold, respectively, to measure *HIGH_REP*. P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 10
Additional Misstatement Type Analysis

	Column 1		Column 2		Column 3	
	BIG_R		*BIG_R*		*BIG_R*	
VARIABLES	**coef**	**p-value**	**coef**	**p-value**	**coef**	**p-value**
HIGH_REP	**0.001**	**(0.917)**				
HIGH_REP_20			**-0.001**	**(0.972)**		
HIGH_REP_50					**0.012**	**(0.546)**
Intercept and Controls		Yes		Yes		Yes
Year FE		Yes		Yes		Yes
Industry FE		Yes		Yes		Yes
Director FE		Yes		Yes		Yes
Adj R-Squared		0.23		0.23		0.24
Observations		3,140		3,012		2,357

Notes: This table presents the results from estimating Equation (1) using different thresholds for the main variable of interest, *HIGH_REP*. Columns 1-3 present linear probability models examining the effect of the relative reputation incentives that a firm offers to the director on the likelihood of a misstatement that is accompanied with an 8-K announcement, *BIG_R*. Column 1 uses a 10% relative size threshold to measure *HIGH_REP,* Column 2 uses a 20% relative size threshold to measure *HIGH_REP,* and Column 3 uses a 50% threshold to measure *HIGH_REP*. Coefficients for control variables are suppressed for brevity. P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 11
F-Score Continuous Measure Analysis

	Column 1			Column 2			Column 3		
	FSCORE			*FSCORE*			*FSCORE*		
VARIABLES	**coef**	**p-value**		**coef**	**p-value**		**coef**	**p-value**	
HIGH_REP	**-0.244**	**(0.089)**	*						
HIGH_REP_20				**-0.266**	**(0.097)**	*			
HIGH_REP_50							**-0.607**	**(0.071)**	*
Intercept and Controls		Yes			Yes			Yes	
Year FE		Yes			Yes			Yes	
Industry FE		Yes			Yes			Yes	
Director FE		Yes			Yes			Yes	
Adj R-Squared		0.19			0.19			0.20	
Observations		2,747			2,632			2,052	

Notes: This table presents the results from estimating Equation (1) using different thresholds for the main variable of interest, *HIGH_REP*. Columns 1-3 present OLS models examining the effect of the relative reputation incentives that a firm offers to the director on the continuous measure of the F-Score, *FSCORE*. Column 1 uses a 10% relative size threshold to measure *HIGH_REP,* Column 2 uses a 20% relative size threshold to measure *HIGH_REP,* and Column 3 uses a 50% threshold to measure *HIGH_REP.* P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 12
Firm Fixed Effects

Panel A	**Column 1**		**Column 2**		**Column 3**	
	MISSTATE		*MISSTATE*		*MISSTATE*	
VARIABLES	**coef**	**p-value**	**coef**	**p-value**	**coef**	**p-value**
HIGH_REP	**-0.020**	**(0.296)**				
HIGH_REP_20			**-0.015**	**(0.501)**		
HIGH_REP_50					**0.010**	**(0.764)**
Intercept and Controls		Yes		Yes		Yes
Year FE		Yes		Yes		Yes
Firm FE		Yes		Yes		Yes
Director FE		Yes		Yes		Yes
Adj R-Squared		0.27		0.26		0.23
Observations		3,140		3,012		2,357

Notes: Panel A presents the results from estimating Equation (1) using different thresholds for the main variable of interest, *HIGH_REP*. Columns 1-3 present linear probability models examining the effect of the relative reputation incentives that a firm offers to the director on the likelihood of a misstatement, *MISSTATE*. Column 1 uses a 10% relative size threshold to measure *HIGH_REP,* Column 2 uses a 20% relative size threshold to measure *HIGH_REP,* and Column 3 uses a 50% threshold to measure *HIGH_REP*. Coefficients for control variables are suppressed for brevity. The model is estimated using firm fixed effects. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 12 Continued
Firm Fixed Effects

Panel B	**Column 1**			**Column 2**			**Column 3**		
	HIGH_FSCORE			*HIGH_FSCORE*			*HIGH_FSCORE*		
VARIABLES	**coef**	**p-value**		**coef**	**p-value**		**coef**	**p-value**	
HIGH_REP	**-0.023**	**(0.068)**	*						
HIGH_REP_20				**-0.020**	**(0.121)**				
HIGH_REP_50							**-0.048**	**(0.054)**	*
Intercept and Controls		Yes			Yes			Yes	
Year FE		Yes			Yes			Yes	
Firm FE		Yes			Yes			Yes	
Director FE		Yes			Yes			Yes	
Adj R-Squared		0.26			0.28			0.33	
Observations		2,747			2,632			2,052	

Notes: Panel B presents the results from estimating Equation (1) using different thresholds for the main variable of interest, *HIGH_REP*. Columns 1-3 present linear probability models examining the effect of the relative reputation incentives that a firm offers to the director on the likelihood that the firm's F-Score is greater than 1.85, *HIGH_FSCORE*. Column 1 uses a 10% relative size threshold to measure *HIGH_REP,* Column 2 uses a 20% relative size threshold to measure *HIGH_REP,* and Column 3 uses a 50% threshold to measure *HIGH_REP.* Coefficients for control variables are suppressed for brevity. The model is estimated using firm fixed effects. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 12 Continued
Firm Fixed Effects

Panel C	**Column 1**		**Column 2**		**Column 3**	
	MWEAK		*MWEAK*		*MWEAK*	
VARIABLES	**coef**	**p-value**	**coef**	**p-value**	**coef**	**p-value**
HIGH_REP	**-0.017**	**(0.449)**				
HIGH_REP_20			**-0.029**	**(0.259)**		
HIGH_REP_50					**-0.043**	**(0.374)**
Intercept and Controls		Yes		Yes		Yes
Year FE		Yes		Yes		Yes
Firm FE		Yes		Yes		Yes
Director FE		Yes		Yes		Yes
Adj R-Squared		0.29		0.29		0.24
Observations		2,129		2,013		1,508

Notes: Panel C presents the results from estimating Equation (1) using different thresholds for the main variable of interest, *HIGH_REP*. Columns 1-3 present linear probability models examining the effect of the relative reputation incentives that a firm offers to the director on the likelihood of a material weakness in internal controls over financial reporting, *MWEAK*. Column 1 uses a 10% relative size threshold to measure *HIGH_REP,* Column 2 uses a 20% relative size threshold to measure *HIGH_REP,* and Column 3 uses a 50% threshold to measure *HIGH_REP*. Coefficients for control variables are suppressed for brevity. The model is estimated using firm fixed effects. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 12 Continued
Firm Fixed Effects

Panel D	**Column 1**			**Column 2**			**Column 3**		
	ABSDA			*ABSDA*			*ABSDA*		
VARIABLES	**coef**	**p-value**		**coef**	**p-value**		**coef**	**p-value**	
HIGH_REP	**-0.006**	**(0.094)**	*						
HIGH_REP_20				**-0.010**	**(0.021)**	**			
HIGH_REP_50							**-0.027**	**(0.000)**	***
Intercept and Controls		Yes			Yes			Yes	
Year FE		Yes			Yes			Yes	
Firm FE		Yes			Yes			Yes	
Director FE		Yes			Yes			Yes	
Adj R-Squared		0.25			0.26			0.25	
Observations		2,779			2,604			2,042	

Notes: Panel D presents the results from estimating Equation (1) using different thresholds for the main variable of interest, *HIGH_REP*. Columns 1-3 present OLS models examining the effect of the relative reputation incentives that a firm offers to the director on the absolute value of performance-adjusted discretionary accruals, *ABSDA*. Column 1 uses a 10% relative size threshold to measure *HIGH_REP,* Column 2 uses a 20% relative size threshold to measure *HIGH_REP,* and Column 3 uses a 50% threshold to measure *HIGH_REP*. Coefficients for control variables are suppressed for brevity. The model is estimated using firm fixed effects. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 13
Continuous Measure of Reputation Incentives

	Column 1		Column 2			Column 3			Column 4		
VARIABLES	*MISSTATE*		*HIGH_FSCORE*			*MWEAK*			*ABSDA*		
DIST_FROM_MEDIAN	**0.012**	**(0.332)**	**-0.005**	**(0.073)**	*****	**-0.004**	**(0.060)**	*****	**-0.001**	**(0.065)**	*****
Intercept and Controls	Yes		Yes			Yes			Yes		
Year FE	Yes		Yes			Yes			Yes		
Industry FE	Yes		Yes			Yes			Yes		
Director FE	Yes		Yes			Yes			Yes		
Adj R-Squared	0.14		0.23			0.28			0.26		
Observations	3,140		2,747			2,129			2,779		

Notes: This table presents the results from estimating Equation (1)-(3) using a different measure of reputation incentives, *DIST_FROM_MEDIAN*. *DIST_FROM_MEDIAN* is defined as the difference between the *SIZE* variable of firm *i* and the median of the *SIZE* variable of all the firms that director d serves in year *t*. Columns 1-3 present linear probability models examining the effect of the relative reputation incentives that a firm offers to the director on FRQ. Column 4 presents an OLS model examining the effect of the relative reputation incentives that a firm offers to the director on the FRQ. P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 14
Means of *HIGH_REP* by Size Distribution

Panel A

Lower Half

Variable	Mean	Median	Std. Dev.	25%	75%
HIGH_REP	0.30	0.00	0.46	0.00	1.00
Observations	1,572				

Notes: This table presents descriptive statistics for firms in the sample below or equal to the median of size. All variables are defined as in Appendix A

Upper Half

Variable	Mean	Median	Std. Dev.	25%	75%
HIGH_REP	0.66	1.00	0.47	0.00	1.00
Observations	1,568				

Notes: This table presents descriptive statistics for firms in the sample above the median of size. All variables are defined as in Appendix A

Table 14 Continued
Means of *HIGH_REP* by Size Distribution

Panel B

Bottom Tercile

Variable	Mean	Median	Std. Dev.	25%	75%
HIGH_REP	0.23	0.00	0.42	0.00	0.00
Observations	1,047				

Notes: This table presents descriptive statistics for firms in the sample that are in the bottom tercile of size. All variables are defined as in Appendix A

Middle Tercile

Variable	Mean	Median	Std. Dev.	25%	75%
HIGH_REP	0.49	0.00	0.50	0.00	1.00
Observations	1,046				

Notes: This table presents descriptive statistics for firms in the sample that are in the middle tercile of size. All variables are defined as in Appendix A

Top Tercile

Variable	Mean	Median	Std. Dev.	25%	75%
HIGH_REP	0.73	1.00	0.45	0.00	1.00
Observations	1,047				

Notes: This table presents descriptive statistics for firms in the sample that are in the top tercile of size. All variables are defined as in Appendix A

Table 15
Size Distribution Analysis

Panel A	**Column 1**		**Column 2**		**Column 3**		**Column 4**	
TOP HALF								
	MISSTATE		***HIGH_FSCORE***		***MWEAK***		***ABSDA***	
VARIABLES	**coef**	**p-value**	**coef**	**p-value**	**coef**	**p-value**	**coef**	**p-value**
HIGH_REP	**0.010**	**(0.648)**	**-0.019**	**(0.476)**	**0.010**	**(0.520)**	**-0.002**	**(0.504)**
Intercept and Controls		Yes		Yes		Yes		Yes
Industry FE		Yes		Yes		Yes		Yes
Year FE		Yes		Yes		Yes		Yes
Director FE		Yes		Yes		Yes		Yes
Adj R-Squared		0.12		0.27		0.20		0.31
Observations		1,049		908		674		903

Notes: This table presents the results from estimating Equation (1)-(3) on a sample of directors that only serve companies in the top half of the distribution of firm size. Columns 1 and 2 present linear probability models examining the effect of the relative reputation incentives that a firm offers to the director on the likelihood of a misstatement, *MISSTATE*, and the likelihood that the firm's F-Score is greater than 1.85, *HIGH_FSCORE*, respectively. Column 3 presents a linear probability model examining the effect of the relative reputation incentives that a firm offers to the director on the likelihood of the firm having a material weakness in internal control, *MWEAK*. Column 4 presents an OLS model examining the effect of the relative reputation incentives that a firm offers to the director on the absolute value of performance-adjusted discretionary accruals, *ABSDA*. P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 15 Continued
Size Distribution Analysis

Panel B	**Column 1**			**Column 2**			**Column 3**			**Column 4**		
BOTTOM HALF												
	MISSTATE			***HIGH_FSCORE***			***MWEAK***			***ABSDA***		
VARIABLES	**coef**	**p-value**		**coef**	**p-value**		**coef**	**p-value**		**coef**	**p-value**	
HIGH_REP	**-0.033**	**(0.062)**	*	**-0.013**	**(0.653)**		**-0.068**	**(0.036)**	**	**-0.010**	**(0.029)**	**
Intercept and Controls		Yes			Yes			Yes			Yes	
Industry FE		Yes			Yes			Yes			Yes	
Year FE		Yes			Yes			Yes			Yes	
Director FE		Yes			Yes			Yes			Yes	
Adj R-Squared		0.238			0.262			0.189			0.204	
Observations		974			851			622			826	

Notes: This table presents the results from estimating Equation (1)-(3) on a sample of directors that only serve companies in the bottom half of the distribution of firm size. Columns 1 and 2 present linear probability models examining the effect of the relative reputation incentives that a firm offers to the director on the likelihood of a misstatement, *MISSTATE*, and the likelihood that the firm's F-Score is greater than 1.85, *HIGH_FSCORE*, respectively. Column 3 presents a linear probability model examining the effect of the relative reputation incentives that a firm offers to the director on the likelihood of the firm having a material weakness in internal control, *MWEAK*. Column 4 presents an OLS model examining the effect of the relative reputation incentives that a firm offers to the director on the absolute value of performance-adjusted discretionary accruals, *ABSDA*. P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 16
Regressions by Tercile

Panel A

TOP TERCILE

	Column 1		Column 2		Column 3		Column 4	
	MISSTATE		*HIGH_FSCORE*		*MWEAK*		*ABSDA*	
VARIABLES	**coef**	**p-value**	**Coef**	**p-value**	**coef**	**p-value**	**coef**	**p-value**
HIGH_REP	**-0.048**	**(0.222)**	**-0.026**	**(0.495)**	**-0.009**	**(0.444)**	**-0.001**	**(0.846)**
Intercept and Controls	Yes		Yes		Yes		Yes	
Year FE	Yes		Yes		Yes		Yes	
Industry FE	Yes		Yes		Yes		Yes	
Director FE	Yes		Yes		Yes		Yes	
Adj R-Squared	0.17		0.30		0.26		0.10	
Observations	562		493		368		479	

Notes: This table presents the results from estimating Equation (1) -(3) on a sample of directors that only serve companies in the top tercile of firm size. Columns 1 and 2 present linear probability models examining the effect of the relative reputation incentives that a firm offers to the director on the likelihood of a misstatement, *MISSTATE,* and the likelihood that the firm's F-Score is greater than 1.85*, HIGH_FSCORE,* respectively. Column 3 presents a linear probability model examining the effect of the relative reputation incentives that a firm offers to the director on the likelihood that the firm having a material weakness in internal control, *MWEAK*. Column 4 presents an OLS model examining the effect of the relative reputation incentives that a firm offers to the director on the absolute value of performance-adjusted discretionary accruals, *ABSDA*. P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 16 Continued
Regressions by Tercile

Panel B

MIDDLE TERCILE

	Column 1		Column 2		Column 3		Column 4	
	MISSTATE		*HIGH_FSCORE*		*MWEAK*		*ABSDA*	
VARIABLES	**coef**	**p-value**	**Coef**	**p-value**	**coef**	**p-value**	**coef**	**p-value**
HIGH_REP	**0.067**	**(0.272)**	**0.108**	**(0.206)**	**0.004**	**(0.959)**	**0.003**	**(0.775)**
Intercept and Controls	Yes		Yes		Yes		Yes	
Year FE	Yes		Yes		Yes		Yes	
Industry FE	Yes		Yes		Yes		Yes	
Director FE	Yes		Yes		Yes		Yes	
Adj R-Squared	0.30		0.40		0.59		0.25	
Observations	330		304		249		310	

Notes: Panel B presents the results from estimating Equation (1) -(3) on a sample of directors that only serve companies in the middle tercile of firm size. Columns 1 and 2 present linear probability models examining the effect of the relative reputation incentives that a firm offers to the director on the likelihood of a misstatement, *MISSTATE,* and the likelihood that the firm's F-Score is greater than 1.85*, HIGH_FSCORE,* respectively. Column 3 presents a linear probability model examining the effect of the relative reputation incentives that a firm offers to the director on the likelihood that the firm having a material weakness in internal control, *MWEAK*. Column 4 presents an OLS model examining the effect of the relative reputation incentives that a firm offers to the director on the absolute value of performance-adjusted discretionary accruals, *ABSDA.* P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 16 Continued
Regressions by Tercile

Panel C

BOTTOM TERCILE	**Column 1**			**Column 2**			**Column 3**			**Column 4**		
	MISSTATE			***HIGH_FSCORE***			***MWEAK***			***ABSDA***		
VARIABLES	**coef**	**p-value**		**Coef**	**p-value**		**coef**	**p-value**		**coef**	**p-value**	
HIGH_REP	**-0.064**	**(0.027)**	**	**-0.025**	**(0.766)**		**-0.062**	**(0.087)**	*	**-0.001**	**(0.078)**	*
Intercept and Controls	Yes			Yes			Yes			Yes		
Year FE	Yes			Yes			Yes			Yes		
Industry FE	Yes			Yes			Yes			Yes		
Director FE	Yes			Yes			Yes			Yes		
Adj R-Squared	0.30			0.38			0.47			0.28		
Observations	480			428			334			403		

Notes: Panel C presents the results from estimating Equation (1) -(3) on a sample of directors that only serve companies in the bottom tercile of firm size. Columns 1 and 2 present linear probability models examining the effect of the relative reputation incentives that a firm offers to the director on the likelihood of a misstatement, *MISSTATE,* and the likelihood that the firm's F-Score is greater than 1.85*, HIGH_FSCORE,* respectively. Column 3 presents a linear probability model examining the effect of the relative reputation incentives that a firm offers to the director on the likelihood that the firm having a material weakness in internal control, *MWEAK*. Column 4 presents an OLS model examining the effect of the relative reputation incentives that a firm offers to the director on the absolute value of performance-adjusted discretionary accruals, *ABSDA*. P-values reported in parentheses are based on robust standard errors clustered by firm. *, **, and *** indicate statistical significance at the 10%, 5%, and 1% levels, respectively (two-sided). All variables are defined as in Appendix A.

Table 17
Descriptive Statistics on the Addition of Audit Committee Seats by Directors

Panel A: Full Panel of AC Chairs and FEs	
Variable	Mean
ADD1	0.051
BECOME_2	0.034
BECOME_3ORMORE	0.017
ADD_SIMILAR_OR_LARGER	0.032
ADD_SMALLER	0.019
Director-Year Observations	29,791

Notes: This table provides descriptive statistics on the addition of board seats by directors

Panel B: Directors Ending up with Two Audit Committee Seats	
Variable	Mean
ADD_SIMILAR_OR_LARGER	0.45
ADD_SMALLER	0.55
Director-Firm-Year Observations	1,012

Notes: This table provides descriptive statistics on the addition of board seats by directors

Panel C: Directors Ending up with Three or More Audit Committee Seats	
Variable	Mean
ADD_SIMILAR_OR_LARGER	0.92
ADD_SMALLER	0.08
Director-Firm-Year Observations	508

Notes: This table provides descriptive statistics on the addition of board seats by directors

VITA

Justin C. Short obtained a Bachelor's and a Master's degree in Accountancy from the University of Tennessee, Knoxville. He worked for two years in the audit practice of Ernst & Young in the firm's Nashville, TN office. He audited public and private companies in multiple industries including insurance, manufacturing, healthcare, and utilities. He is a licensed CPA in the state of Tennessee. He started the doctoral program at the University of Tennessee in 2014 and has research and teaching interests in corporate governance, auditing, and financial reporting. After graduating with a Doctor of Philosophy degree in May, Justin will begin his academic career at Emory University in Atlanta, GA in the fall of 2018.