Audit committee strength and auditors' risk assessments: The moderating role of CEO narcissism

Zengin-Karaibrahimoglu, Y.; Emanuels, J.; Gold, A.; Wallage, P.

DOI
10.1111/ijau.12243

Publication date
2021

Document Version
Final published version

Published in
International Journal of Auditing

Received: 19 October 2020 | Revised: 30 April 2021 | Accepted: 16 June 2021

DOI: 10.1111/ijau.12243

ORIGINAL ARTICLE

WILEY

Audit committee strength and auditors' risk assessments: The moderating role of CEO narcissism

Yasemin Zengin-Karaibrahimoglu[1] | Jim Emanuels[1] | Anna Gold[2,3] | Philip Wallage[2,4]

[1]University of Groningen, The Netherlands
[2]Vrije Universiteit Amsterdam, The Netherlands
[3]Norwegian School of Economics, Norway
[4]Universiteit van Amsterdam, The Netherlands

Correspondence
Yasemin Zengin-Karaibrahimoglu, Department of Accountancy, University of Groningen, Groningen, The Netherlands.
Email: y.karaibrahimoglu@rug.nl

This paper examines the impact of two elements of the client's control environment on auditor's assessment of the risk of material misstatement: audit committee strength and CEO narcissism, the latter of which is a component of management philosophy, operating style, and tone at the top. We predict and find that auditors' risk assessments are adequately responsive to both elements; however, importantly, a strong audit committee decreases perceived risk assessments only when the client has a CEO with less narcissistic characteristics. In other words, our findings suggest that the presence of narcissistic CEOs' attitudes weakens the perceived audit committee effectiveness, leading auditors to rely less on a strong audit committee. Our findings contribute to the auditing literature by exploring auditors' responses to the complex dynamics between management boards and those charged with governance. From a practical perspective, our results suggest that auditing standards and practice guidance should consider making such complexities and the role of management attitudes and styles even more explicit.

KEYWORDS
audit committee strength, auditor risk assessments, CEO narcissism, control environment

1 | INTRODUCTION

Risk assessment is an integral part of every audit engagement, and understanding the client and its control environment is at the core of external auditors' risk assessment for a high-quality audit. Specifically, as part of assessing the entity's control environment, auditors are expected to evaluate (1) the participation of those charged with governance, especially the entity's board of directors and audit committee, and (2) management's philosophy, operating style, and tone at the top.[1] By doing so, auditors should obtain an adequate understanding of the client's monitoring structure and potential or realized approach towards the client's business risks, financial reporting, aggressive accounting practices, internal control and information processing. Indeed, recent high-profile corporate failures, such as Wirecard (Germany), Wells Fargo (United States), Steinhoff (South Africa), Carillion (United Kingdom) and Odebrecht (Brazil), have once again highlighted the importance for auditors to adequately understand the client and its control environment. Ultimately, these considerations should influence auditors' assessment of the risk of material misstatement (RMM). However, given the highly dynamic and integrated structure of the control environment, its understanding and translation into auditor risk assessments are not straightforward. In practice, rather than evaluating the governance structure and management attitudes separately, auditors are likely to consider the *combined* effect of these two control environment mechanisms in their risk assessments. In this study, we examine whether the response of auditors' risk assessment to audit committee strength—an indicator of the governance quality—is contingent on the client CEO's narcissism—an essential element of management philosophy and operating style, and reflecting the tone at the top.

Audit committees operate at the centre of the communication between management and external auditors, and they are considered a crucial constituent of an entity's overall corporate governance structure. According to prominent regulations worldwide (e.g., European Commission, 2006; Sarbanes–Oxley Act, 2002), an effective audit committee must be composed of independent members, financial and/or industry expertise and extensive experience. From an agency theory perspective, an effective ('strong') audit committee is essential to reduce the client's overall business risk and, in turn, should influence subsequent audit risk assessments (Bedard & Johnstone, 2004; Cohen et al., 2010). However, even after worldwide structural reforms in the post-SOX era regarding the qualifications of audit committee members and the restrictions on the direct involvement of CEOs in the nomination of audit committee members, audit committees' effectiveness remains an issue of debate. It is argued that audit committees might be strong in form, but they are frequently weak in substance due to, for example, the CEO's extensive influence (e.g., Beasley et al., 2009; Fiolleau et al., 2013; Gendron et al., 2004; Gendron & Bedard, 2006), and the audit committee's role being ceremonial rather than substantial (Cohen et al., 2010). Prior auditing research has established that auditors are responsive to the strength of the audit committee in their planning judgements, including risk assessments (e.g., Bedard & Johnstone, 2004; Sharma et al., 2008; Stewart & Munro, 2007). In the current study, we extend this literature by examining whether the presence of a narcissistic CEO will reduce auditors' perceived audit committee strength due to the potential malicious behaviour of CEOs, even when the audit committee is strong in form.

Narcissistic individuals are mostly characterized as self-centred, pursuing their own goals at the long-term cost of others (Campbell et al., 2005) and making impulsive, risky decisions (O'Reilly et al., 2014; Rosenthal & Pittinsky, 2006) that are harmful and costly for organizations (Campbell et al., 2004). As they believe that their actions are perfect, narcissists do not like to be accountable and transparent (Sedikides et al., 2002) and resist criticism. Consequently, to avoid criticism, judgement and monitoring, narcissists tend to influence and dominate others, for example, by restraining information sharing within the organization (Campbell & Miller, 2011; Nevicka et al., 2011). To avoid adequate monitoring over self-interested managerial activities, CEOs are likely to be either reluctant to share information with the audit committee or selective towards good news (Kothari et al., 2009), specifically when they are with a narcissistic personality trait. Consequently, such an information asymmetry between the CEO and audit committee is likely to restrain the monitoring ability of the audit committee over CEOs' activities (Adams & Ferreira, 2007; Chen et al., 2017; Harris & Raviv, 2008; Lisic et al., 2016).

We examine whether auditors' risk assessments are responsive to such complex dynamics between a narcissistic CEO and the audit committee. While prior auditing research documents that auditors incorporate evidence of their clients' CEO personality or management attitudes into their overall (fraud) risk assessments (Apostolou et al., 2001; Boyle et al., 2015; Johnson et al., 2013), the current study examines how CEO narcissism may mitigate the impact of audit committee strength on auditors' risk assessments. We predict that when the client's CEO is a narcissist, auditors' risk assessment response to audit committee strength will be reduced because they perceive the client's audit committees as less effective in monitoring due to the potential influence of a narcissistic CEO.[2]

To test our prediction, we conducted a 2×2 experiment among 112 Dutch auditors from Big 4 and non-Big 4 firms who assessed the RMM based on a scenario in which audit committee strength and the client's CEO narcissism were manipulated each at two levels (low and high). Consistent with our prediction and theory, we find that audit committee strength reduces RMM only when the client's CEO is less narcissistic. Hence, the presence of a narcissistic CEO not only weakens this desirable impact of the audit committee on auditors' assessed RMM but even eliminates the effect. Our findings suggest that, in their risk assessments, auditors are perceptive of the adverse influence of the client's CEO's narcissism on audit committee effectiveness. Follow-up interviews with eight senior audit partners from all Big 4 audit firms in the Netherlands confirm that, in practice, auditors consider the impact of a narcissistic CEO and the effectiveness of the audit committee as well as their interplay.

Our paper contributes to the existing literature, audit practice, and regulations in several ways. First, this paper is the first to examine the moderating impact of CEO narcissism on the relationship between audit committee strength and auditors' risk assessments. This is an essential extension to the auditing literature because recent studies in management explicitly indicate the need for research focusing on the role of the CEO's personality on the dynamics of CEO–board dyads and the consequences of such dyads for organizations (Samimi et al., 2020).[3] Although prior literature provides insights regarding the direct impact of CEO narcissism on auditors' judgements (e.g., Johnson et al., 2013), it does not consider the combined impact of governance structure and management attitude—two important control environment elements—on auditors' risk assessments. Second, our findings complement prior research on the effectiveness of the audit committee (e.g., Bruynseels & Cardinaels, 2014; Carcello et al., 2011; Cassell et al., 2018; Fiolleau et al., 2013; Kim et al., 2017; Lisic et al., 2016). We show that, even without explicit knowledge about the relationship between audit committee members and CEOs, auditors are likely to perceive audit committees as weaker in substance. This is, merely, because of the presence of a CEO with a distinct personality, which appears to be indicative of certain intended attitudes and behaviours in auditors' minds. Third, we contribute to the ongoing revisions of auditing standards on the assessment of RMM by documenting that auditors are indeed sensitive to the complex dynamics of the entity's control environment. Specifically, when the client has a highly narcissistic CEO, auditors put less emphasis on the potentially favourable impact of strong audit committees on monitoring and internal controls. Heiman-Hoffman et al. (1996) indicate that in the determination of misstatements in financial reporting, relative to *situational* factors like firm-specific conditions, *attitude* factors—*the management philosophy towards dishonest*, *hostile*, *aggressive and unreasonable behaviours*—are potentially more critical warning signs for auditors. Our findings confirm that, in auditors' risk assessment, CEO narcissism (an *attitude* factor) appears to dominate the effect of audit committee strength (a *situational* factor). Boyle et al. (2015) and Hammersley (2011) argue that the client CEO's personality should be incorporated into the auditors' risk model, specifically if the CEO is narcissistic (Craig & Amernic, 2011). In line with previous studies, our findings imply that the inclusion of the narcissistic personality trait is necessary because, via their potential influence over the monitoring ability of audit committees, narcissistic CEOs affect auditors' perceptions regarding audit committee strength in their risk assessment.

2 | INSTITUTIONAL BACKGROUND, LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

2.1 | Audit committee requirements in the Netherlands

In the Netherlands, different from most other countries (such as the United States and the United Kingdom), most corporations have a 'two-tier board' structure that is composed of a management board, mainly responsible for the decision management (initiation and implementation), and a supervisory board, principally responsible for the decision control (ratification and monitoring). Dutch corporation law and the Dutch Corporate Governance Code (2016) require supervisory boards to consist of only non-executive members.[4] Supervisory boards of publicly listed companies are required to have an audit committee (a subcommittee of the supervisory board) of which more than half of the members, including the chairperson, are independent. The members of the audit committee are selected from the full supervisory board. According to Dutch law, the chair of the supervisory board or a former managing director of the company cannot be appointed as the chair of the audit committee.

Audit committees are in charge of the nomination and selection of the external auditors and the first point of contact for external auditors, specifically if the auditor identifies potential irregularities in the financial reporting. Regarding audit committee communication with auditors, the audit committee is required to meet with external auditors at least once a year, without the presence of the executive board, and more frequently if needed. Moreover, the audit committee is expected to monitor the integrity and quality of the financial reporting and assess the effectiveness of internal risk management and control systems.

In addition to the independence and meeting frequency requirements, and similar to requirements in other jurisdictions, and in line with the EU Statutory Audits Directive (European Commission, 2006), at least one of the members of the audit committee must have financial, accounting and/or auditing expertise.

2.2 | Audit committee strength and auditor-assessed risks of material misstatements

From an agency theory perspective, corporate governance with a strong board and an audit committee as monitoring tools are presumed to be efficient contractual mechanisms mitigating potential agency problems in an organization (Cohen et al., 2008). Specifically, an active, functional and well-structured audit committee is expected to limit potential misstatements (DeZoort et al., 2003; Xie et al., 2003).

Audit committees are responsible for the coordination and communication between internal and external auditors and for assuring the independence of external auditors. Consequently, they play a vital role in the financial reporting and audit quality through strong monitoring and overseeing of management and internal control of the financial reporting process (Beasley, 1996; Klein, 2002; Sarbanes–Oxley Act, 2002). Previous archival studies confirm that firms with strong audit committees (proxied by independence, experience, accounting, financial expertise and involvement) are more likely to have higher quality financial reporting, are less likely to engage in fraudulent financial reporting (e.g., Abbott et al., 2004; Beasley et al., 2000; Bedard et al., 2004; Cohen et al., 2013; Dhaliwal et al., 2010; Klein, 2002; Xie et al., 2003) and are less likely to be associated with internal control and disclosure problems (e.g., Hoitash et al., 2009; Johnstone et al., 2011; Krishnan, 2005; Naiker & Sharma, 2009; Zhang et al., 2007).

While in the pre-SOX period, auditors did not perceive audit committees as a strong monitoring mechanism in the financial reporting process (Cohen et al., 2002), in the post-SOX period, the role of audit committees has improved significantly (Cohen et al., 2010). Auditors are explicitly required to consider the governance structure of the audited entity when assessing the effectiveness of its control environment (e.g., ISA 315, International Standards of Auditing [ISA], 2019), and they consider effective audit committees as a source of internal control strength (Hines et al., 2015). Strong and effective corporate governance and audit committees reduce clients' overall business risk and, hence, should also influence the subsequent assessment of RMM (Bedard & Johnstone, 2004; Cohen et al., 2010). Stewart and Munro (2007) document that the existence of an audit committee decreases auditor-assessed RMM. Similarly, Sharma et al. (2008) find that strong corporate governance is associated with lower control environment risk. Furthermore, Contessotto and Moroney (2014) find that there is a negative association between the audit committee strength in substance and auditor-assessed RMM. In line with the above arguments and in an attempt to replicate the findings of previous studies, we expect auditors' risk assessments to be lower in response to a strong audit committee, and we hypothesize that:

> **Hypothesis 1.** Auditors' risk assessments are lower in response to a strong audit committee compared with a weak audit committee.

2.3 | CEO narcissism and auditor-assessed risks of material misstatements

While the audit committee, being the most prominent vehicle for the participation of those charged with governance, is an important component of the entity's control environment, auditors also consider other organizational factors, as prescribed by auditing standards (e.g., ISA 315, ISA, 2019). An important element of the control environment is that of management philosophy, operating style and tone at the top. Specifically, given that CEOs are among the main figures in the organizational decision-making process and all strategic choices are affected by their cognitive values (Hambrick & Mason, 1984), auditors are likely to consider the influence of CEOs in their assessment of the control environment and ultimately the RMM.

The Theory of Reasoned Action (Ajzen & Fishbein, 1980) states that individuals' behaviours are shaped by their intentions, which are linked to their personality traits. Auditors likely consider clients' behavioural intentions as strong predictors of a specific behaviour (Kaplan et al., 2011). In this paper, we are interested in the personality trait of CEO narcissism. On one hand, narcissism can be considered a desirable personality trait at the top of an organization and potentially a key ingredient for CEOs, because individuals with a narcissistic personality are more willing to pursue positions of power that require independent thinking, risk taking, passion, charisma and self-confidence (De Vries, 2004). On the other hand, extreme narcissistic traits of CEOs are commonly considered a 'toxic drug' (De Vries, 2004). Narcissists continuously search for affirmation, recognition and rewards (Resick et al., 2009) and are characterized by traits such as excessive self-focus, self-entitlement, dominance, self-confidence, a sense of entitlement, grandiosity and low empathy (Ham et al., 2017; O'Reilly et al., 2014).

Recent studies in management, finance and accounting suggest that a high level of narcissism is related to unethical conduct (Amernic & Craig, 2010) and that CEO narcissism increases risk taking and has negative consequences for the organization (Ham et al., 2017; Ham et al., 2018; Johnson et al., 2013; Young et al., 2015). More specifically, CEO narcissism is associated with real earnings management (Ham et al., 2017; Olsen et al., 2014), meeting or beating analyst forecasts (Olsen et al., 2014), firm performance volatility (Chatterjee & Hambrick, 2007), merger and acquisition decisions (Aktas et al., 2016), corporate tax avoidance (Olsen & Stekelberg, 2015), overinvestment (Ham et al., 2018), financial misreporting and fraud (Hales et al., 2011; Rijsenbilt, 2011; Rijsenbilt & Commandeur, 2013; Schrand & Zechman, 2012). Narcissistic CEOs exhibit excessive risk taking (Campbell et al., 2004; Foster et al., 2009) and misreporting (Hales et al., 2011; Rijsenbilt, 2011; Rijsenbilt & Commandeur, 2013; Schrand & Zechman, 2012).[5]

Based on the Theory of Reasoned Action and auditors' required focus on management philosophy, operating style and tone at the top as part of their required evaluation of the entity's control environment during audit planning, we suggest that the presence of a narcissistic CEO may have an adverse influence on auditors' risk assessment due to auditors' perceptions of the CEO's behavioural intentions. Our second hypothesis replicates prior auditing research that has documented that the clients' CEO personality trait is positively related to auditors' overall (fraud) risk assessments (Apostolou et al., 2001; Boyle et al., 2015; Hammersley, 2011; Heiman-Hoffman et al., 1996), and more recent studies directly associate it specifically with narcissism (Johnson et al., 2013; Judd et al., 2017).

> **Hypothesis 2.** Auditors' risk assessments are higher in response to the presence of a narcissistic CEO compared with its absence.

2.4 | The moderating effect of CEO narcissism

Given their positions in the organizations, CEOs have an information advantage regarding all strategic decisions of an organization relative to others (Beck & Mauldin, 2014; Compernolle & Richard, 2018; Fiolleau et al., 2013), including governance bodies, such as audit committees. As part of the head of the management board, the CEO has controlling power over what information is shared with the audit committee and auditors, including how and when this is done (Fiolleau et al., 2013).

Using this opportunity, together with the incentives derived from their personality, to avoid the costs of their actions, CEOs may purposefully be reluctant to share or be selective in sharing news regarding their actions (Kothari et al., 2009), mainly with the ones responsible for monitoring. Such opportunistic use of information power may generally cause a higher risk of both adverse selection (hidden information) and moral hazard (hidden action).

Prior research argues that the CEO's extensive influence may weaken the substantive effectiveness of audit committees even when they are strong in form (e.g., Beasley et al., 2009; Fiolleau et al., 2013; Gendron et al., 2004; Gendron & Bedard, 2006). CEOs may dominate over audit committees through informal involvement in the selection of committee members via co-option (Cassell et al., 2018), involvement in the auditor selection process (Fiolleau et al., 2013), their social ties with committee members (Bruynseels & Cardinaels, 2014) and their overall power (Lisic et al., 2016). While these prior studies have examined CEO influence on the effectiveness of audit committees, we argue that the presence of a narcissistic CEO will reduce the effect of audit committee strength on auditors' risk assessment, as a result of the *potential* malicious behaviour of CEOs. Prior research shows that narcissistic CEOs have a lower tolerance for monitoring (Young et al., 2015) and a strong preference to use information power and dominance to limit the criticism and judgement abilities of others (Nevicka et al., 2011). Therefore, they are likely to be less inclined to share information with the audit committee, to avoid extensive questioning which may cause them to be accountable and responsible to make explanations for their choices. The primary incentive for narcissists to have a lower tolerance for extensive monitoring stems from the deterrence of attitudes such as being accountable, the expectation to explain, rationalize and defend one's self-evaluations to another person (Sedikides et al., 2002). Moreover, narcissistic CEOs may also be reluctant to share information to avoid reporting by audit committees on their performance arisen from risky operations, because of their focus on strong success and achievement orientation and avoidance of fear and failure (Elliot & Thrash, 2001).

Given that a less informed audit committee will be unable to conduct high-quality monitoring over CEOs' self-interested managerial activities, auditors' assessed risks are less likely to be alleviated even if the audit committee is strong in form. With a narcissistic CEO, auditors are likely to attribute greater salience to the CEO's personality relative to audit committee strength. Hence, we expect that, in the presence of a narcissistic CEO, due to the information asymmetry arising from the CEOs' potential attitudes and intentions, auditors perceive audit committees to be less effective even though they are strong in form. Therefore, we expect the effect of audit committee strength on the auditor-assessed RMMs to be weakened by CEO narcissism in our final hypothesis (see also Figure 1).

Hypothesis 3. The effect of audit committee strength on auditors' risk assessments is weaker when the CEO‘s narcissism is high compared with low.

3 | RESEARCH METHOD

3.1 | Procedure and participants

To test our hypothesis, we designed and administered an experiment by using a 2 *CEO NARCISSISM* (high vs. low) by 2 *Audit Committee (AC) STRENGTH* (high vs. low) between-participants design. We randomly assigned participants to one of the four treatment conditions. The experimental case used in this study is an adaptation of the Johnson et al. (2013) case with the permission of the author team. The case was carefully adapted to fit our research objectives and contextually and linguistically translated into Dutch. The case centres on a construction company (Groenendijk Construction N.V.), which has problems in the timely delivery of a project within budget. One of the prominent adjustments we made to the original case was the introduction of the client's CEO instead of the general manager, to reflect our purpose of investigating auditors' response to the CEO's narcissistic traits.

Participants were Dutch audit professionals from the Big 4 audit firms and one smaller audit firm. Audit professionals at the senior staff level and higher were invited to participate by the researchers and the research assistants through personal requests. Auditors at these ranks are considered to be core audit team members who, following Dutch and International Standards on Auditing, are required to be involved in audit and fraud risk assessments in the planning stage of the audit (ISA 315, ISA, 2019). Each participant received an email with a link to a Qualtrics survey containing a (1) brief introduction to the research project, (2) information about the hypothetical audit engagement and client (including the description of our manipulations), (3) the dependent variable measures, (4) manipulation checks and (5) postexperimental questionnaires. To mitigate the risk of participants sharing and discussing information about the case and, thereby, discovering manipulations, the email only referred to an audit judgement case and urged participants to complete the questionnaire in one sitting. Furthermore, reading the case and answering took no longer than 25 min, the window between the distribution of the emails and closing Qualtrics was short (6 days), and once completed, the questionnaire could not be submitted again. Once responses were submitted, all participants received an email to verify that they completed the survey themselves, and after the closing of Qualtrics, all participants were thanked for their effort and debriefed about the experimental nature of the survey. The experimental protocol in which the aforementioned measures are embedded was independently reviewed and approved by the Ethics Committee of one of the authors' universities.

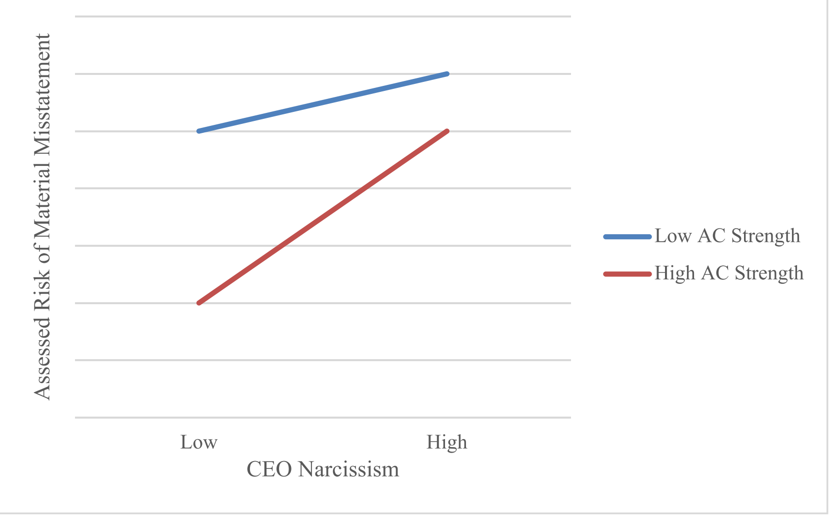

FIGURE 1 Predicted interaction: CEO narcissism by audit committee strength on auditors' assessed risk of material misstatement [Colour figure can be viewed at wileyonlinelibrary.com]

3.2 | Independent variables

To manipulate *CEO NARCISSISM*, we followed Johnson et al. (2013) and Chatterjee and Hambrick (2007) by using a composite measure including (1) the prominence of the CEO's photograph in the company's annual report, (2) a dialogue between the auditor (the participant) and the client manager that included (in the high narcissism condition) or did not include (in the low narcissism condition) conversational cues by the CEO that were consistent with narcissism and (3) the CEO's use of first-person singular pronouns in conversation.[6] The resulting manipulation is presented in Table 1.

TABLE 1 *CEO NARCISSISM* manipulation (translated from Dutch)

CEO NARCISSISM treatment attribute	High *CEO NARCISSISM*	Low *CEO NARCISSISM*
CEO photograph	CEO in the middle of the management team and the foreground	CEO as a part of the management team (second from left in the picture, not in the foreground)
CEO's conversational cues and the use of first-person singular pronouns	'I make sure things get done on time, and let me tell you, it is not always easy. I'll give you an example. The first quarter close this year was a real nightmare. My contract supervisor dropped the ball on getting some change orders processed, and construction in progress [CIP] was way out of line compared to the latest progress estimates, thanks to one of my accounting clerks not getting the job done. I worked like a dog to get the change orders and CIP in shape for closing—I must have put 80 hours in that week. After that debacle, I had a meltdown and told my staff that they had better follow my procedures to the letter from now on, our heads would roll. I have got my hands full keeping this place running—I do not have time to do their work for them'.	'The team has a history of stepping up when it counts to make sure things get done on time. I'll give you an example. Our first-quarter close this year was on a tight deadline. We got a little behind on getting subcontractor change orders to processed, and we had not completed reconciling construction in progress [CIP] to the latest progress estimates. The team knew we had to get the change orders and CIP account detail in shape for closing, and everyone stayed late to get the job done. After things settled down, we had a meeting to go over our quarter-end procedures. The team came up with great suggestions to streamline the process and make it easier to meet deadlines in the future'.

To manipulate *AC STRENGTH*, we used a composite of (1) audit committee financial and accounting expertise (high vs. low), (2) the number of audit committee meetings (six vs. two per year) and (3) audit committee and CEO social ties (absent vs. present), which is consistent with prior research. Financial or accounting expertise may enhance financial reporting quality and reduce fraud and restatements (Abbott et al., 2004). The number of audit committee meetings is expected to increase the audit committee effectiveness (Davidson et al., 2005; DeZoort et al., 2002) and diligence, which is negatively associated with the occurrence of financial statement fraud (Abbott et al., 2004; Abbott & Parker, 2000). Finally, Bruynseels and Cardinaels (2014) provide evidence that intense social ties between the CEO and audit committee members influence the audit committee's effectiveness because these induce feelings of reciprocity from the audit committee members towards the CEO (Côté et al., 2007; Gibbons, 2004). Our *AC STRENGTH* manipulation is provided in Table 2. Despite the manipulated variation in strength, we ensured that the audit committee in both conditions is in compliance with the Dutch Corporate Governance Code (2016).

In all four conditions of the experiment, all other information regarding Groenendijk Construction was held constant. Compared

TABLE 2 *AC STRENGTH* manipulation

AC STRENGTH treatment	High *AC STRENGTH*	Low *AC STRENGTH*
Audit committee financial and accounting expertise Audit committee and CEO social ties Number of audit committee meetings	The audit committee is composed of Bram Zegveld, *a former Big 4 accounting firm partner*; Yvonne de Raas who has a *background in banking*; Petra van Opeinde who, as a compliance officer, manages the legal department of a large bank; and the fourth member Dreef de Vries, a very experienced director from the construction industry. Yearly, *the audit committee has six meetings*.	The audit committee is composed of Bram Zegveld, an experienced purchase manager and *a golf buddy of Michel van Beek*; Yvonne de Raas, a retired HR consultant; Petra van Opeinde who, as a compliance officer, manages the legal department of a large bank; and the fourth member Dreef de Vries, a very experienced director from the construction industry, *who joins Michel van Beek in several social networks*. On average, *the audit committee meets twice every year*.

with (particularly fraud) cases used in existing research (see, e.g., Asare & Wright, 2004), and following the approach of Johnson et al. (2013), the information in our case was limited to relevant (high level) information regarding the financial position and the construction projects of Groenendijk, in order to avoid any undesirable noise.

3.3 | Dependent variable

We asked participants to assess the RMMs on a 7-point scale ranging from 'very low' to 'very high' in response to the following statement: 'Based on the information I received in the case, my estimate of the risk of a material misstatement in Groenendijk's financial statements over 2017 is …'.[7]

4 | RESULTS

4.1 | Sample

A total of 125 auditors participated in this study; however, 13 participants were eliminated for being extreme outliers (using the interquartile range rule) and/or highly influential observations (according to Cook's distance), resulting in a final sample of 112 participants. Of these, 55 (49.1%) are senior staff, while 57 participants (50.9%) hold manager or higher positions in their firm. The mean audit experience is 11.6 years. The majority (92%) of the participants work at a Big 4 audit firm, and 50 participants (44.6%) hold a Dutch 'Register Accountant' (equivalent to CPA) certification. Of note, the majority of participants (64.3%) have never experienced any fraud, while 39 participants (34.8%) have encountered fraud on at least one engagement. Hence, the mean number of engagements on which participants experienced fraud is below 1. See Table 3 for more demographic details about the participants. None of the measured demographic variables varies significantly across treatment conditions, suggesting that randomization in our experiment was successful.

To reduce overall experimental error, we checked for potential demographic covariates to be included in our analysis. Audit experience, CPA and rank all correlate with our primary dependent variable and with each other. The correlation with the dependent variable is strongest for rank (measured as senior staff vs. manager or higher); hence, we include *RANK* as a covariate in our analysis. Gender, firm type (Big 4 vs. non-Big 4), sector experience and fraud experience are not significantly associated with our dependent measure. We further measured participants' risk aversion (based on Young, 1985) and their own narcissism (using the Dutch translation of the short 16-item NPI [NPI-16] questionnaire by Ames et al., 2006) to understand whether these measures have a significant impact on auditors' judgements. Neither measure is associated with the dependent variable, so we do not include them as covariates.

4.2 | Manipulation checks

Following Johnson et al. (2013), we employ six items based on the NPI to measure the effectiveness of the *CEO NARCISSISM* manipulation. For example, one item reads, 'The CEO demands respect'; another reads, 'The CEO has a high opinion of himself'. Participants indicated their agreement with each item on a scale from 1 (*strongly disagree*) to 7 (*strongly agree*). As the six items loaded onto a single factor that captures over 40% of the variance of the items, we computed an unweighted average index of the six items. The mean of the index

TABLE 3 Sample demographics

	Mean (SD)	%	n[a]
Gender			112
Male		78.6%	
Female		21.4%	
Age	34.28 (9.08)		111
Employing audit firm			112
Big 4		92%	
Non-Big 4		8%	
Audit experience	11.60 (9.12)		111
In possession of Dutch CPA ('RA') licence		44.6%	112
Current rank			112
Senior staff		49.1%	
Manager or higher		50.9%	
Participants reporting fraud experience on at least one engagement		34.8%	
Number of engagements on which fraud was experienced	0.92 (1.77)		111
Number of engagements in the construction sector	2.24 (3.35)		111

[a]Data are missing where $n < 112$.

for participants in the high *CEO NARCISSISM* treatment (4.95) is significantly higher than the index means of the low narcissism treatment (4.53; $p < 0.05$, one tailed). Consistent results were obtained from five of the six individual items.[8] We conclude that our narcissism manipulation was successful.[9]

The manipulation check of *AC STRENGTH* consisted of four items measuring the perceived level of the audit committee's independence, financial and accounting expertise, diligence and overall committee quality. Participants indicated their agreement with each item on a scale from 1 (*strongly disagree*) to 7 (*strongly agree*). The four items loaded onto a single factor capturing over 80% of the variance of the items, so we again computed an unweighted average index. The mean of the index for participants in the high *AC STRENGTH* treatment condition (4.52) is significantly greater than the index means in the low *AC STRENGTH* condition (2.95; $p < 0.01$). We obtain consistent results from all four individual items; hence, we conclude that our manipulation of *AC STRENGTH* was successful.

4.3 | Hypothesis testing

Table 4 reports the overall analysis of our experiment. The dependent variable is the participants' assessment of the RMM in the client's financial statements. The ANCOVA in Table 4, Panel A, demonstrates that the overall model is highly significant at conventional levels ($F(1,106) = 7.27$, $p < 0.001$). Panel B reports the means adjusted for the effect of the covariate (*RANK*) included in the ANCOVA.

TABLE 4 Risk of material misstatement

Panel A: Results of a 2 × 2 ANCOVA for risk of material misstatement per *CEO NARCISSISM* and *AC STRENGTH*

Source	SS	df	MS	*F* value	*p* value
Corrected model	9.51	4	2.38	7.43	<0.001
CEO NARCISSISM	1.84	1	1.84	5.75	0.018
AC STRENGTH	2.24	1	2.24	7.00	0.009
CEO NARCISSISM × *AC STRENGTH*	1.65	1	1.65	5.16	0.025
RANK	2.65	1	2.65	8.28	0.005
Error	34.21	107	0.32		

Panel B: Adjusted means (SE) for risk of material misstatement

	AC STRENGTH condition		
***CEO NARCISSISM* condition**	**High**	**Low**	**Total**
High	5.75 (0.11) $n = 27$	5.79 (0.11) $n = 29$	5.77 (0.08) $n = 56$
Low	5.25 (0.11) $n = 28$	5.78 (0.11) $n = 28$	5.51 (0.08) $n = 56$
Total	5.50 (0.08) $n = 55$	5.78 (0.08) $n = 57$	5.64 (0.05) $n = 112$

Panel C: Contrast coefficients

High *CEO NARCISSISM*; high *AC STRENGTH*	High *CEO NARCISSISM*; low *AC STRENGTH*	Low *CEO NARCISSISM*; high *AC STRENGTH*	Low *CEO NARCISSISM*; low *AC STRENGTH*
+1	+1	−2	0

Panel D: Planned contrast tests

Source	*df*	*F* statistic	*p* value (one tailed)
Contrast weights (+1, +1, −2 and 0)	107	15.55	<0.001

Panel E: Planned pairwise mean comparisons

Condition	Mean comparison	Mean difference	SE	*p* value
Low *CEO NARCISSISM*	High versus low *AC STRENGTH*	−0.53	0.15	<0.001 (one tailed)
High *CEO NARCISSISM*	High versus low *AC STRENGTH*	−0.03	0.15	0.400 (one tailed)
Low *AC STRENGTH*	High versus low *CEO NARCISSISM*	0.01	0.15	0.93 (two tailed)
High AC STRENGTH	High versus low *CEO NARCISSISM*	0.5	0.15	0.002 (two tailed)

Note: The dependent variable is the auditor-assessed risk of material misstatement. *CEO NARCISSISM* and *AC STRENGTH* are each manipulated between subjects as high or low. In all panel tests, we control and adjust for participants' *RANK* (senior staff vs. manager or higher).

Hypothesis 1 predicts a main effect of *AC STRENGTH* on auditors' risk assessments. As shown in Table 4, Panel A, the main effect is significant ($p < 0.01$), and adjusted means in Panel B reveal that, as predicted, auditors' risk assessments are lower when the audit committee is strong (5.50) compared with weak (5.78), supporting Hypothesis 1.

Hypothesis 2 predicts that auditors assess a higher RMM when the client has a narcissistic CEO. The effect is also significant ($p < 0.5$), such that a narcissistic CEO leads to higher risk assessments (5.77), compared with a nonnarcissistic CEO (5.51), supporting Hypothesis 2. Given the significant interaction term and our interaction prediction, these main effects should, however, be interpreted with caution.

Our primary interest in the current study is the interaction between *CEO NARCISSISM* and *AC STRENGTH*, as predicted in Hypothesis 3. Figure 2 depicts the interaction plot employing adjusted means. The overall pattern suggests that auditor-assessed RMM is consistently high, except when *CEO NARCISSISM* is low and *AC STRENGTH* is high, in which case risk assessments are lower.

Hypothesis 3 predicts that *AC STRENGTH* reduces auditors' assessments of the RMM more strongly for clients with a less compared with a more narcissistic CEO. To test Hypothesis 3, we use a planned contrast test (adjusted for covariates *RANK* and *CEO LIKEABILITY*) because we predict a nonsymmetrical, ordinal interaction (Buckless & Ravenscroft, 1990). As illustrated in Table 4, Panel C, we use contrast weights $+1$, $+1$, -2 and 0 because Hypothesis 3 predicts a stronger decreasing effect of *AC STRENGTH* when *CEO NARCISSISM* is low. The contrast shown in Table 4, Panel D, is statistically significant ($F(1,107) = 15.55$; $p < 0.001$), providing overall strong support for our interaction prediction.

Next, we examine planned pairwise mean comparisons (adjusted for *RANK*) in Table 4, Panel E. Results demonstrate that the negative effect of *AC STRENGTH* is significant only when *CEO NARCISSISM* is low (*AC STRENGTH* high $= 5.25$ vs. low $= 5.78$; $\Delta = -0.53$, $p < 0.001$, one tailed) but not when *CEO NARCISSISM* is high (*AC STRENGTH* high $= 5.75$ vs. low $= 5.79$; $\Delta = -0.03$, $p = 0.40$, one tailed). Hence, in the presence of a narcissistic CEO, the effect of *AC STRENGTH* on auditors' risk assessment is not only weakened but is also eliminated altogether. Results provide partial support for Hypothesis 3.

For completeness, in two-tailed post hoc tests, we also examine the simple effects of *CEO NARCISSISM* holding *AC STRENGTH* high or low (see Table 4, Panel E). When *AC STRENGTH* is low, we observe no significant effect of *CEO NARCISSISM* (*CEO NARCISSISM* high $= 5.79$ vs. low $= 5.78$; $\Delta = 0.01$, $p = 0.93$, two tailed), suggesting that risk assessments are consistently high in the presence of a relatively weak audit committee. In contrast, when *AC STRENGTH* is high, low CEO narcissism reduces auditors' risk assessments (*CEO NARCISSISM* high $= 5.75$ vs. low $= 5.25$; $\Delta = 0.5$, $p < 0.01$, two tailed). Concluding, we find support for our prediction that the presence of a narcissistic CEO undermines the perceived effectiveness of the client entity's audit committee, to the extent that auditors' risk assessments are not at all affected by audit committee strength when the client has a narcissistic CEO, supporting Hypothesis 3.

4.4 | Supplemental analyses

Employing the NPI-16 questionnaire by Ames et al. (2006), we measured participants' narcissistic personality to understand whether auditors' perception regarding the consequences of CEO narcissism possibly changes with the level of their own narcissism. The NPI-16 consists of 16 paired and opposing items that participants select. One example of such a pair is 'I really like to be the center of attention' versus 'It makes me uncomfortable to be the center of attention'. The 16 pairs are scored 0 or 1, and the score on the scale is the mean of all the answers, resulting in a final score between 0 and 1. Our sample's mean (SD) response is 0.28 (1.65). Nontabulated results indicate that auditor narcissism does not correlate with auditors' risk assessments, neither does it have a significant moderating impact on the effect of CEO narcissism on risk assessments. Further, based on

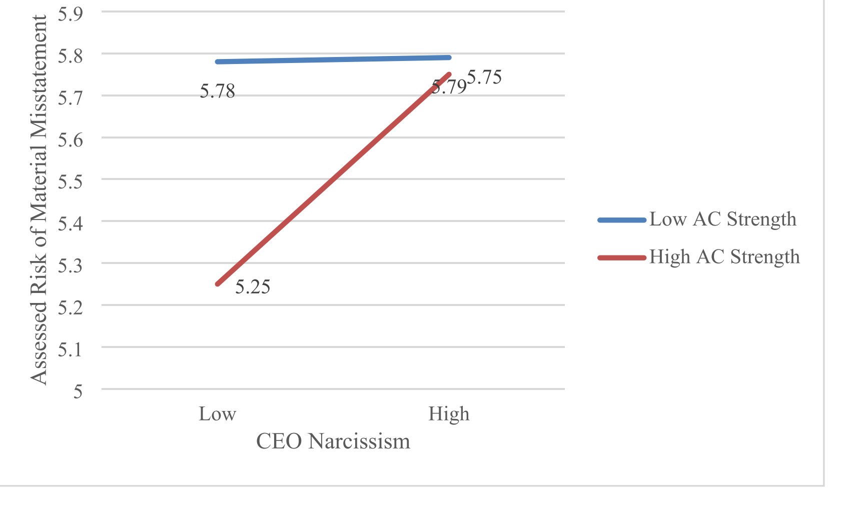

FIGURE 2 Observed interaction plot: *CEO NARCISSISM* by *AC STRENGTH* on auditors' assessed risk of material misstatement (adjusted means) [Colour figure can be viewed at wileyonlinelibrary.com]

Young (1985), we examined participants' risk aversion; however, this measure does not correlate with auditors' risk assessments either or moderate the impact of either of our two main independent variables.

4.5 | Interview findings

To corroborate and add to our experimental results, as anecdotal evidence, we interviewed eight senior audit partners from different Big 4 audit firms in the Netherlands regarding their thoughts on how audit committee strength influences auditors' assessment of RMM and whether the CEOs' personality potentially moderates the effect of audit committee strength on their risk assessments in their practice experience.[10] Table 5 provides the interview protocol employed.

All but one of the audit partners indicated they consider the audit committee as important but depending on several conditions. Specifically, while the presence of an audit committee is important, it does not ensure a strong control environment per se. The audit committee members' lack of financial and accounting expertise affects auditors' RMM assessments. Most partners mention an average of four to six audit committee meetings per year to be common and emphasize that the quality of the audit committee agenda is more important than the number of meetings.

We further asked how they incorporate the personality of the CEO into their risk assessments. Most of the auditors confirm the importance of the personality of a client's CEO as a risk factor. Although a narcissistic CEO in itself is not necessarily bad, they suggest that a strong CFO must be a countervailing power able to withstand the CEO's pressure. Only when out of balance, the risk of management override in combination with other factors (poor financial position, bonus plans, growth through acquisitions, private equity pressure, etc.) will lead to increased RMM and additional substantive testing (accounting estimates, tax position and target journal entry testing).

TABLE 5 Interview protocol

1. Could you indicate if and how, generally speaking, the composition of the audit committee influences your assessment of RMM?
2. How do the following factors specifically impact your assessment of the audit committees' strength?
   a. Social relationships between the CEO and audit committee members
   b. Financial and accounting expertise of audit committee members
   c. The frequency of audit committee meetings
3. Could you indicate how, generally speaking, important the personality of clients' CEO is in your risk assessment? More specifically, is a *dominant CEO* a factor you would take into account in assessing RMM?
4. Do you believe that a dominant CEO impacts the monitoring ability of the Audit Committee, and if so, how and why?
5. If you believe that a dominant CEO negatively impacts the monitoring ability of the CEO, and thus is an important factor affecting your risk assessment (RMM) adversely, in practice, do you have additional guidance on how to assess such risks and perform specific (substantive) audit procedures?

When it comes to the interplay between CEO and audit committee, in our interviewees' view, social relationships between the CEO and audit committee members could indeed influence the assessment of the audit committees' strength although auditors do not actively search for such relationships. As one of the partners indicated that 'it can have an (indirect) influence as it creates an unpleasant feeling'. Most partners believe, however, that a dominant CEO impacts the monitoring ability of the audit committee due to potentially withholding information. One of the partners stated that 'A narcissistic CEO makes me nervous. Then a strong audit committee is less relevant, although a good audit committee can partially mitigate the risk'.

Finally, our interviewees comment on the fact that no guidance is available when it comes to translating the potential risks of a narcissistic CEO to the extent and nature of audit procedures. As one of the partners noticed 'you cannot perform targeted substantive tests with just a dominant CEO unless there are [direct] signals'. However, auditors should also be careful in drawing conclusions, as one of the partners notices that 'with a narcissistic CEO, you tend to dig deeply into the wrong things'.

5 | CONCLUSION AND DISCUSSION

This paper examines the relationship between audit committee strength and auditor-assessed RMMs and whether this relationship is moderated by CEO narcissism. As predicted, we find that auditors respond adequately to situations of increased risk, as manipulated in our experiment, both when this is due to a perceived weakness in the audit committee and the potential dominance of narcissistic CEO. Most importantly, we find that in the presence of a narcissistic CEO, the audit committee strength's impact on auditors' risk assessment is not only weakened but also altogether eliminated. This implies that the presence of a CEO having a strong and dominant personality trait such as narcissism, ex ante, leads an audit committee to be perceived as weak by auditors due to the potential malicious behaviour of CEOs driven from their personality, even when the audit committee is strong in form. As the principal agent, CEOs have the opportunity to control the extent of the information and narcissistic CEOs further have incentives to limit the information sharing with audit committees. These findings provide evidence on the salience of *attitude* factors in auditors' judgements—that is, the management philosophy towards dishonest, hostile, aggressive and unreasonable behaviours—relative to *situational* factors like firm-specific conditions, which is in line with Heiman-Hoffman et al. (1996) and Apostolou et al. (2001). This implies that the client CEO's narcissism, as a strong personality trait, is a crucial element evaluated by auditors and should be incorporated into the auditor risk assessment model, as suggested by Boyle et al. (2015) and Hammersley (2011). Therefore, from a regulatory perspective, based on our findings, we suggest that rather than leaving auditors with implicit choices, the explicit inclusion of CEO personality as a contingency factor in auditor-assessed risks of material misstatement appears to be essential in the ISAs.

Our study's results have several implications for audit practice. For instance, Chen et al. (2017) argue that independent directors do not necessarily have better monitoring abilities than nonindependent directors due to the information disadvantages. Extending this argument to a two-tier board setting, non-executive directors on the audit committee, a subcommittee of the supervisory board, are likely to have an information disadvantage compared with the executive directors on the management board. One implication of our findings is that auditors may need to be made explicitly aware of audit committee members' factual independence and strength to counteract the perceived problems arising from a potentially narcissistic top manager in the client firm. Our findings suggest that 'formal' independence does not fulfil this objective. In the case of narcissistic CEOs, to prevent an increase in the RMMs, companies should ensure that independent audit committee members have access to strategic and operational information directly and be less influenced by narcissistic CEOs' potential biases in information sharing attempts. In this respect, both the CFO and the chair of the audit committee play a key role in providing countervailing power. At the same time, our findings imply that in order to increase the effectiveness of the audit committee, auditors should report their concerns of potential management override or manipulation by a narcissistic CEO to the audit committee.

The Dutch Corporate Governance Code currently requires audit committees to have at least one meeting with the auditor, without the presence of the CEO. Our experimental and interview results suggest that, in the case of a CEO with a narcissistic personality, audit firms should consider requiring the auditor to discuss the potential risks due to the CEO's personality with the audit committee in private meetings, to review the effectiveness of the oversight measures taken by the audit committee to share concerns with respect to strategic and operational risks that are not reported or underreported.

As with any research, our findings are subject to certain limitations that suggest avenues for future research. One limitation is that our study only focuses on CEO narcissism as a personality characteristic. Future research could extend our work to examine whether auditors are sensitive to other client management (including the CFO's) personality characteristics that might be harmful to corporate governance effectiveness. Another important limitation of our experiment is that we are unable to observe the actual mechanisms or dynamics causing audit committees to be effective or ineffective. Future field research may focus on the actual processes involved in cases in which an audit committee is confronted with a narcissistic CEO, ultimately strengthening board oversight and reducing the RMMs. Finally, while our study focuses on auditors' risk assessments, future research may examine other auditor planning judgements and decisions, such as the nature, timing and extent of planned audit procedures, in response to client management integrity concerns.

ACKNOWLEDGEMENTS

We appreciate comments received from Arnold Wright from Northeastern University, Robert Knechel from University of Florida, Chun Keung (Stan) Hoi from Rochester Institute of Technology and participants of the 2019 European Accounting Association Congress (Paphos). This research received no specific grant from any funding agency in the public, commercial or not-for-profit sectors. The conference participation was funded by the School of Management at the University of Groningen.

CONFLICT OF INTEREST

No conflict of interest has been declared by the author(s).

ETHICS STATEMENT

The authors confirm that the ethical policies of the journal, as noted on the journal's author guidelines page, have been adhered to and the appropriate ethical review committee approval has been received by the Ethics Committee of the Faculty of Economics and Business at the University of Groningen.

ENDNOTES

[1] In December 2019, to improve audit quality globally, the International Auditing and Assurance Standards Board (IAASB) revised ISA 315 (ISA, 2019)—Identifying and Assessing the Risks of Material Misstatement and explicitly referred to the factors that should be considered in the risk of material misstatements.

[2] We reason that the combination of a strong audit committee and a narcissistic CEO is plausible given the two-tier governance structure in which the supervisory board (rather than the CEO) selects the members of the audit committee.

[3] The current literature on CEO–board dynamics merely focuses on CEO demographic characteristics, but CEO personality may explain such relations better (Engelen et al., 2016; Nadkarni & Herrmann, 2010).

[4] The Dutch Corporate Governance Code (2016), which applies to all listed companies, is in accordance with legal requirements and European guidelines and contains best-practice provisions subject to the 'comply or explain' approach.

[5] Among other factors that enter into risk taking (such as locus of control, experience and dominance), narcissism is prominent (Chatterjee & Hambrick, 2011).

[6] The narcissism manipulation that Johnson et al. (2013) developed is based on an analysis of selected items from the Narcissistic Personality Inventory (NPI) by Raskin and Hall (1981).

[7] Following Johnson et al. (2013), we also asked for participants' assessment of the financial reporting fraud risk as a secondary dependent measure, using the same scale: 'Based on the information I received in the case, my estimate of the risk of fraud related to Groenendijk's financial statements over 2017 is …'. However, our (nontabulated) analyses using this alternative dependent measure did not produce any significant results.

[8] The manipulation check did not produce significant results for the item 'The CEO is an integer person', where the mean in both conditions is 4.02.

[9] We also measured the extent to which participants perceived the CEO to be competent, successful in his career and likeable. Perceptions of CEO competence and career success do not vary significantly across the narcissism manipulation, but participants in the high narcissism condition perceive the CEO as significantly less likeable (3.45) than participants in the low narcissism condition (3.91; $p < 0.040$, two tailed).

[10] Despite the fact that we consider these interviews anecdotal, we applied for and obtained approval from the Ethics Board of one of the authors' universities for holding the interviews.

AUTHOR CONTRIBUTIONS

Yasemin Zengin-Karaibrahimoglu: Conceptualization; writing - original draft; review and editing. **Anna Gold:** Conceptualization; formal analysis; writing - review, and editing; Software; Methodology. **Jim Emanuels** and **Philip Wallage:** Conceptualization; Data collection. Conceptualization of the experiment, organizing the team/ coordinating/ conducting the experiment & the interviews.

DATA AVAILABILITY STATEMENT

The data that support the findings of this study are openly available in DataverseNL at https://doi.org/10.34894/0A5XQH. Reference to Data: Gold, Anna; Zengin-Karaibrahimoglu, Yasemin; Emanuels, Jim; Wallage, Philip, 2020, 'Replication Data for: EGKW Audit Committee Strength and Auditors' Risk Assessments: The Moderating Role of CEO Narcissism', https://doi.org/10.34894/0A5XQH, DataverseNL, V1.

ORCID

Yasemin Zengin-Karaibrahimoglu https://orcid.org/0000-0003-1885-1025
Jim Emanuels https://orcid.org/0000-0002-2037-7708
Anna Gold https://orcid.org/0000-0002-1754-7673
Philip Wallage https://orcid.org/0000-0002-7447-0019

REFERENCES

Abbott, L., & Parker, S. (2000). Auditor selection and audit committee characteristics. *Auditing: A Journal of Practice & Theory*, *19*(2), 47–66. https://doi.org/10.2308/aud.2000.19.2.47

Abbott, L., Parker, S., & Peters, G. (2004). Audit committee characteristics and restatements: A study of the efficacy of certain Blue Ribbon Committee recommendations. *Auditing: A Journal of Practice & Theory*, *23*, 69–87. https://doi.org/10.2308/aud.2004.23.1.69

Adams, R. B., & Ferreira, D. (2007). A theory of friendly boards. *The Journal of Finance*, *62*(1), 217–250. https://doi.org/10.1111/j.1540-6261.2007.01206.x

Ajzen, I., & Fishbein, M. (1980). *Understanding attitudes and predicting social behavior*. Prentice-Hall.

Aktas, N., de Bodt, E., Bollaert, H., & Roll, R. (2016). CEO narcissism and the takeover process: From private initiation to deal completion. *Journal of Financial and Quantitative Analysis*, *51*(1), 113–137. https://doi.org/10.1017/S0022109016000065

Amernic, J. H., & Craig, R. J. (2010). Accounting as a facilitator of extreme narcissism. *Journal of Business Ethics*, *96*(1), 79–93. https://doi.org/10.1007/s10551-010-0450-0

Ames, D. R., Rose, P., & Anderson, C. P. (2006). The NPI-16 as a short measure of narcissism. *Journal of Research in Personality*, *40*(4), 440–450. https://doi.org/10.1016/j.jrp.2005.03.002

Apostolou, B. A., Hassell, J. M., Webber, S. A., & Sumners, G. E. (2001). The relative importance of management fraud risk factors. *Behavioral Research in Accounting*, *13*(1), 1–24. https://doi.org/10.2308/bria.2001.13.1.1

Asare, S., & Wright, A. (2004). The effectiveness of alternative risk assessment and program planning tools in a fraud setting. *Contemporary Accounting Research*, *21*(2), 325–352. https://doi.org/10.1506/L20L-7FUM-FPCB-7BE2

Beasley, M. S. (1996). An empirical analysis of the relation between the board of director composition and financial statement fraud. *The Accounting Review*, *71*(4), 443–465.

Beasley, M. S., Carcello, J. V., Hermanson, D. R., & Lapides, P. D. (2000). Fraudulent financial reporting: Consideration of industry traits and corporate governance mechanisms. *Accounting Horizons*, *14*(4), 441–454. https://doi.org/10.2308/acch.2000.14.4.441

Beasley, M. S., Carcello, J. V., Hermanson, D. R., & Neal, T. L. (2009). The audit committee oversight process. *Contemporary Accounting Research*, *26*(1), 65–122. https://doi.org/10.1506/car.26.1.3

Beck, M. J., & Mauldin, E. G. (2014). Who's really in charge? Audit committee versus CFO power and audit fees. *The Accounting Review*, *89*(6), 2057–2085. https://doi.org/10.2308/accr-50834

Bedard, J., Chtourou, S. M., & Courteau, L. (2004). The effect of audit committee expertise, independence, and activity on aggressive earnings management. *Auditing: A Journal of Practice & Theory*, *23*(2), 13–35. https://doi.org/10.2308/aud.2004.23.2.13

Bedard, J. C., & Johnstone, K. M. (2004). Earnings manipulation risk, corporate governance risk, and auditors' planning and pricing decisions. *The Accounting Review*, *79*(2), 277–304. https://doi.org/10.2308/accr.2004.79.2.277

Boyle, D. M., DeZoort, F. T., & Hermanson, D. R. (2015). The effect of alternative fraud model use on auditors' fraud risk judgments. *Journal of Accounting and Public Policy*, *34*(6), 578–596. https://doi.org/10.1016/j.jaccpubpol.2015.05.006

Bruynseels, L., & Cardinaels, E. (2014). The audit committee: Management watchdog or personal friend of the CEO? *The Accounting Review*, *89*(1), 113–145. https://doi.org/10.2308/accr-50601

Buckless, F. A., & Ravenscroft, S. P. (1990). Contrast coding: A refinement of ANOVA in behavioral analysis. *The Accounting Review*, *65*(4), 933–945.

Campbell, W. K., Bush, C. P., Brunell, A. B., & Shelton, J. (2005). Understanding the social costs of narcissism: The case of the tragedy of the commons. *Personality and Social Psychology Bulletin*, *31*(10), 1358–1368. https://doi.org/10.1177/0146167205274855

Campbell, W. K., Goodie, A. S., & Foster, J. D. (2004). Narcissism, confidence, and risk attitude. *Journal of Behavioral Decision Making*, *17*(4), 297–311. https://doi.org/10.1002/bdm.475

Campbell, W. K., & Miller, J. D. (2011). *The handbook of narcissism and narcissistic personality disorder: Theoretical approaches, empirical findings, and treatments*. John Wiley & Sons. https://doi.org/10.1002/9781118093108

Carcello, J. V., Neal, T. L., Palmrose, Z. V., & Scholz, S. (2011). CEO involvement in selecting board members, audit committee effectiveness, and restatements. *Contemporary Accounting Research*, *28*(2), 396–430. https://doi.org/10.1111/j.1911-3846.2010.01052.x

Cassell, C. A., Myers, L. A., Schmardebeck, R., & Zhou, J. (2018). The monitoring effectiveness of co-opted audit committees. *Contemporary Accounting Research*, *35*(4), 1732–1765. https://doi.org/10.1111/1911-3846.12429

Chatterjee, A., & Hambrick, D. C. (2007). It's all about me: Narcissistic chief executive officers and their effects on company strategy and performance. *Administrative Science Quarterly*, *52*, 351–386. https://doi.org/10.2189/asqu.52.3.351

Chatterjee, A., & Hambrick, D. C. (2011). Executive personality, capability cues, and risk taking: How narcissistic CEOs react to their successes and stumbles. *Administrative Science Quarterly*, *56*(2), 202–237. https://doi.org/10.1177/0001839211427534

Chen, J. Z., Cussatt, M., & Gunny, K. A. (2017). When are outside directors, more effective monitors? Evidence from real activities manipulation. *Journal of Accounting, Auditing & Finance*, *35*(1), 26–52.

Cohen, J., Krishnamoorthy, G., & Wright, A. (2010). Corporate governance in the post-Sarbanes-Oxley era: Auditors' experiences. *Contemporary Accounting Research*, *27*(3), 751–786. https://doi.org/10.1111/j.1911-3846.2010.01026.x

Cohen, J., Krishnamoorthy, G., & Wright, A. M. (2002). Corporate governance and the audit process. *Contemporary Accounting Research*, *19*(4), 573–594. https://doi.org/10.1506/983M-EPXG-4Y0R-J9YK

Cohen, J. R., Hoitash, U., Krishnamoorthy, G., & Wright, A. M. (2013). The effect of audit committee industry expertise on monitoring the financial reporting process. *The Accounting Review*, *89*(1), 243–273.

Cohen, J. R., Krishnamoorthy, G., & Wright, A. M. (2008). Form versus substance: The implications for auditing practice and research of alternative perspectives on corporate governance. *Auditing: A Journal of Practice & Theory*, *27*(2), 181–198. https://doi.org/10.2308/aud.2008.27.2.181

Compernolle, T., & Richard, C. (2018). The audit committee as an interactive process: Insights on the AC chairperson's power. *European Accounting Review*, *27*(4), 623–647. https://doi.org/10.1080/09638180.2017.1367315

Contessotto, C., & Moroney, R. (2014). The association between audit committee effectiveness and audit risk. *Accounting & Finance*, *54*(2), 393–418. https://doi.org/10.1111/acfi.12010

Côté, R., Plickert, G., & Wellmann, B. (2007). It's not who you know, it's how you know them: Who exchanges what with whom? *Social Networks*, *29*(3), 405–429.

Craig, R., & Amernic, J. (2011). Detecting linguistic traces of destructive narcissism at-a-distance in a CEO's letter to shareholders. *Journal of Business Ethics*, *101*(4), 563–575. https://doi.org/10.1007/s10551-011-0738-8

Davidson, R., Goodwin-Stewart, J., & Kent, P. (2005). Internal governance structures and earnings management. *Accounting & Finance*, *45*(2), 241–267. https://doi.org/10.1111/j.1467-629x.2004.00132.x

De Vries, M. K. (2004). Organizations on the couch: A clinical perspective on organizational dynamics. *European Management Journal*, *22*(2), 183–200.

DeZoort, F. T., Hermanson, D. R., Archambeault, D. S., & Reed, S. A. (2002). Audit committee effectiveness: A synthesis of the empirical audit committee literature. *Journal of Accounting Literature*, *21*, 38–75.

DeZoort, F. T., Hermanson, D. R., & Houston, R. W. (2003). Audit committee member support for proposed audit adjustments: A source credibility perspective. *Auditing: A Journal of Practice & Theory*, *22*(2), 189–205. https://doi.org/10.2308/aud.2003.22.2.189

Dhaliwal, D. A. N., Naiker, V. I. C., & Navissi, F. (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. https://doi.org/10.1111/j.1911-3846.2010.01027.x

Dutch Corporate Governance Code, Monitoring Commissie Corporate Governance, 2016. Available at: https://www.mccg.nl/?page=4738

Elliot, A. J., & Thrash, T. M. (2001). Narcissism and motivation. *Psychological Inquiry*, *12*(4), 216–219.

Engelen, A., Neumann, C., & Schmidt, S. (2016). Should entrepreneurially oriented firms have narcissistic CEOs? *Journal of Management*, *42*(3), 698–721. https://doi.org/10.1177/0149206313495413

European Commission. (2006). DIRECTIVE 2006/43/EC of the European Parliament and of the Council of 17 May 2006 on statutory audits of annual accounts and consolidated accounts, amending Council Directives 78/660/EEC and 83/349/EEC and repealing Council Directive 84/253/EEC. Published in the Official Journal of the European Union, L.157/87. http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2006:157:0087:0107:EN:PDF

Fiolleau, K., Hoang, K., Jamal, K., & Sunder, S. (2013). How do regulatory reforms to enhance auditor independence work in practice? *Contemporary Accounting Research*, *30*(3), 864–890. https://doi.org/10.1111/1911-3846.12004

Foster, J. D., Shenesey, J. W., & Goff, J. S. (2009). Why do narcissists take more risks? Testing the roles of perceived risks and benefits of risky behaviors. *Personality and Individual Differences*, *47*(8), 885–889. https://doi.org/10.1016/j.paid.2009.07.008

Gendron, Y., & Bedard, J. (2006). On the constitution of audit committee effectiveness. *Accounting, Organizations and Society*, *31*(3), 211–239. https://doi.org/10.1016/j.aos.2005.03.002

Gendron, Y., Bedard, J., & Gosselin, M. (2004). Getting inside the black box: A field study of practices in "effective" audit committees. *Auditing: A Journal of Practice & Theory*, *23*(1), 153–171. https://doi.org/10.2308/aud.2004.23.1.153

Gibbons, D. (2004). Friendship and advice networks in the context of changing professional values. *Administrative Science Quarterly*, *49*(2), 238–262.

Hales, J., Hobson, J. L., & Resutek, R. J. (2011). The dark side of socially mediated rewards: How social status and narcissism affect managerial reporting. Working paper, Georgia Institute of Technology.

Ham, C., Lang, M., Seybert, N., & Wang, S. (2017). CFO narcissism and financial reporting quality. *Journal of Accounting Research.*, *55*(5), 1089–1135. https://doi.org/10.1111/1475-679X.12176

Ham, C., Seybert, N., & Wang, S. (2018). Narcissism is a bad sign: CEO signature size, investment, and performance. *Review of Accounting Studies*, *23*(1), 234–264. https://doi.org/10.1007/s11142-017-9427-x

Hambrick, D. C., & Mason, P. A. (1984). Upper echelons: The organization as a reflection of its top managers. *Academy of Management Review*, *9*(2), 193–206. https://doi.org/10.5465/amr.1984.4277628

Hammersley, J. S. (2011). A review and model of auditor judgments in fraud-related planning tasks. *Auditing: A Journal of Practice & Theory*, *30*(4), 101–128. https://doi.org/10.2308/ajpt-10145

Harris, M., & Raviv, A. (2008). A theory of board control and size. *The Review of Financial Studies*, *21*(4), 1797–1832. https://doi.org/10.1093/rfs/hhl030

Heiman-Hoffman, V. B., Morgan, K. P., & Patton, J. M. (1996). The warning signs of fraudulent financial reporting. *Journal of Accountancy*, *182*(4), 75.

Hines, C. S., Masli, A., Mauldin, E. G., & Peters, G. F. (2015). Board risk committees and audit pricing. *Auditing: A Journal of Practice & Theory*, *34*(4), 59–84. https://doi.org/10.2308/ajpt-51035

Hoitash, U., Hoitash, R., & Bedard, J. C. (2009). Corporate governance and internal control over financial reporting: A comparison of regulatory regimes. *The Accounting Review*, *84*(3), 839–867. https://doi.org/10.2308/accr.2009.84.3.839

International Standards of Auditing. (2019). (Revised) Identifying and assessing the risks of material misstatement (ISA 315). https://www.ifac.org/system/files/publications/files/ISA-315-Full-Standard-and-Conforming-Amendments-2019-.pdf

Johnson, E. N., Kuhn, J. R. Jr., Apostolou, B. A., & Hassell, J. M. (2013). Auditor perceptions of client narcissism as a fraud attitude risk factor. *Auditing: A Journal of Practice & Theory*, *32*(1), 203–219. https://doi.org/10.2308/ajpt-50329

Johnstone, K., Li, C., & Rupley, K. H. (2011). Changes in corporate governance associated with the revelation of internal control material weaknesses and their subsequent remediation. *Contemporary Accounting Research*, *28*(1), 331–383. https://doi.org/10.1111/j.1911-3846.2010.01037.x

Judd, J. S., Olsen, K. J., & Stekelberg, J. (2017). How do auditors respond to CEO narcissism? Evidence from external audit fees. *Accounting Horizons*, *31*(4), 33–52. https://doi.org/10.2308/acch-51810

Kaplan, S. E., Pope, K. R., & Samuels, J. A. (2011). An examination of the effect of inquiry and auditor type on reporting intentions for fraud. *Auditing: A Journal of Practice & Theory*, *30*(4), 29–49. https://doi.org/10.2308/ajpt-10174

Kim, H., Kwak, B., Lim, Y., & Yu, J. (2017). Audit committee accounting expertise, CEO power, and audit pricing. *Asia-Pacific Journal of Accounting & Economics*, *24*(3–4), 421–439. https://doi.org/10.1080/16081625.2015.1105753

Klein, A. (2002). Audit committee, board of director characteristics, and earnings management. *Journal of Accounting and Economics*, *33*(3), 375–400. https://doi.org/10.1016/S0165-4101(02)00059-9

Kothari, S. P., Shu, S., & Wysocki, P. D. (2009). Do managers withhold bad news? *Journal of Accounting Research*, *47*(1), 241–276. https://doi.org/10.1111/j.1475-679X.2008.00318.x

Krishnan, J. (2005). Audit committee quality and internal control: An empirical analysis. *The Accounting Review*, *80*(2), 649–675. https://doi.org/10.2308/accr.2005.80.2.649

Lisic, L. L., Neal, T. L., Zhang, I. X., & Zhang, Y. (2016). CEO power, internal control quality, and audit committee effectiveness in substance versus in form. *Contemporary Accounting Research*, *33*(3), 1199–1237. https://doi.org/10.1111/1911-3846.12177

Nadkarni, S., & Herrmann, P. O. L. (2010). CEO personality, strategic flexibility, and firm performance: The case of the Indian business process outsourcing industry. *Academy of Management Journal*, *53*(5), 1050–1073. https://doi.org/10.5465/amj.2010.54533196

Naiker, V., & Sharma, D. S. (2009). Former audit partners on the audit committee and internal control deficiencies. *The Accounting Review*, *84*(2), 559–587. https://doi.org/10.2308/accr.2009.84.2.559

Nevicka, B., Ten Velden, F. S., De Hoogh, A. H., & Van Vianen, A. E. (2011). Reality at odds with perceptions: Narcissistic leaders and group performance. *Psychological Science*, *22*(10), 1259–1264. https://doi.org/10.1177/0956797611417259

Olsen, K. J., Dworkis, K. K., & Young, S. M. (2014). CEO narcissism and accounting: A picture of profits. *Journal of Management Accounting Research*, *26*(2), 243–267. https://doi.org/10.2308/jmar-50638

Olsen, K. J., & Stekelberg, J. (2015). CEO narcissism and corporate tax sheltering. *The Journal of the American Taxation Association*, *38*(1), 1–22.

O'Reilly, C. A., Doerr, B., Caldwell, D. F., & Chatman, J. A. (2014). Narcissistic CEOs and executive compensation. *The Leadership Quarterly*, *25*(2), 218–231. https://doi.org/10.1016/j.leaqua.2013.08.002

Raskin, R., & Hall, C. (1981). The Narcissistic Personality Inventory: Alternate form reliability and further evidence of construct validity. *Journal of Personality Assessment*, *45*(2), 159–162. https://doi.org/10.1207/s15327752jpa4502_10

Resick, C. J., Whitman, D. S., Weingarden, S. M., & Hiller, N. J. (2009). The bright side and the dark side of CEO personality: Examining core self-evaluations, narcissism, transformational leadership, and strategic influence. *Journal of Applied Psychology*, *94*(6), 1365–1381. https://doi.org/10.1037/a0016238

Rijsenbilt, A., & Commandeur, H. (2013). Narcissus enters the courtroom: CEO narcissism and fraud. *Journal of Business Ethics*, *117*(2), 413–429. https://doi.org/10.1007/s10551-012-1528-7

Rijsenbilt, J. A. (2011). CEO Narcissism: Measurement and Impact (No. EPS-2011-238-STR). ERIM Ph.D. Series Research in Management. Erasmus Research Institute of Management, Available at: https://repub.eur.nl/pub/23554/

Rosenthal, S. A., & Pittinsky, T. L. (2006). Narcissistic leadership. *The Leadership Quarterly*, *17*(6), 617–633. https://doi.org/10.1016/j.leaqua.2006.10.005

Samimi, M., Cortes, A. F., Anderson, M. H., & Herrmann, P. (2020). What is strategic leadership? Developing a framework for future research. *The Leadership Quarterly*. https://doi.org/10.1016/j.leaqua.2019.101353

Sarbanes-Oxley Act of 2002. (2002). The Public Company Accounting Reform and Investor Protection Act, Pub. L. no. 107-204. Available at https://pcaobus.org/About/History/Documents/PDFs/Sarbanes_Oxley_Act_of_2002.pdf

Schrand, C. M., & Zechman, S. L. (2012). Executive overconfidence and the slippery slope to financial misreporting. *Journal of Accounting and Economics*, *53*(1), 311–329. https://doi.org/10.1016/j.jacceco.2011.09.001

Sedikides, C., Herbst, K. C., Hardin, D. P., & Dardis, G. J. (2002). Accountability as a deterrent to self-enhancement: The search for mechanisms. *Journal of Personality and Social Psychology*, *83*(3), 592–605. https://doi.org/10.1037/0022-3514.83.3.592

Sharma, D. S., Boo, E. F., & Sharma, V. D. (2008). The impact of non-mandatory corporate governance on auditors' client acceptance, risk and planning judgments. *Accounting and Business Research*, *38*(2), 105–120. https://doi.org/10.1080/00014788.2008.9663324

Stewart, J., & Munro, L. (2007). The impact of audit committee existence and audit committee meeting frequency on the external audit: Perceptions of Australian auditors. *International Journal of Auditing*, *11*(1), 51–69. https://doi.org/10.1111/j.1099-1123.2007.00356.x

Xie, B., Davidson, W. N. III, & DaDalt, P. J. (2003). Earnings management and corporate governance: The role of the board and the audit committee. *Journal of Corporate Finance*, *9*(3), 295–316. https://doi.org/10.1016/S0929-1199(02)00006-8

Young, R. (1985). Participative budgeting: The effects of risk aversion and asymmetric information on budgetary slack. *Journal of Accounting Research*, *23*(2), 829–842. https://doi.org/10.2307/2490840

Young, S. M., Du, F., Dworkis, K. K., & Olsen, K. J. (2015). It's all about all of us: The rise of narcissism and its implications for management control system research. *Journal of Management Accounting Research*, *28*(1), 39–55.

Zhang, Y., Zhou, J., & Zhou, N. (2007). Audit committee quality, auditor independence, and internal control weaknesses. *Journal of Accounting and Public Policy*, *26*(3), 300–327. https://doi.org/10.1016/j.jaccpubpol.2007.03.001

AUTHOR BIOGRAPHIES

Yasemin Zengin-Karaibrahimoglu is an assistant professor in the Department of Accountancy at the University of Groningen, the Netherlands. Yasemin's research area of interest is on the effects of regulatory changes in auditing, financial reporting and corporate governance on organizational outcomes.

Jim Emanuels is a professor in the Department of Accountancy at the University of Groningen, the Netherlands. Jim's research interests are in the internal control and accounting information systems.

Anna Gold is a professor at the Vrije Universiteit Amsterdam (VU), adjunct professor at NHH and editor at *The Accounting Review*. Anna's research interests are in the judgement and decision-making area, primarily applied to the field of auditing.

Philip Wallage is a professor at the Vrije Universiteit Amsterdam (VU) and Universiteit van Amsterdam. Philip's research focuses on auditing, with a specific interest in auditing professionals' roles for organizations.

How to cite this article: Zengin-Karaibrahimoglu, Y., Emanuels, J., Gold, A., & Wallage, P. (2021). Audit committee strength and auditors' risk assessments: The moderating role of CEO narcissism. *International Journal of Auditing*, *25*(3), 661–674. https://doi.org/10.1111/ijau.12243