

Fee Pressure, Prospective Non-Audit Services and Audit Quality

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January 31, 2011

We are grateful for comments received from workshop participants at the University of Kentucky, Katholieke Universiteit Leuven, and Maastricht University.

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ABSTRACT

In this paper, we predict that economic incentives arising from the pressure to obtain future consulting engagements will negatively impact audit quality. We examine the relationship between *prospective* non-audit service fees, fee pressure, and audit quality where the latter is measured as: (a) performance-adjusted discretionary accruals, (b) the propensity to issue a going-concern audit opinion, and (c) the likelihood that reported earnings are subsequently restated. Using data from the pre-SOX period, we find that pressure to obtain non-audit fees and eventual realization of such fees are positively associated with earnings management. We find no association with going-concern opinions or earnings restatements. Additional results from the post-SOX period indicate audit quality is not influenced by fee pressure or prospective non-audit services for any of our metrics for audit quality. Current regulation bans certain NAS on the grounds they lead to poor audit quality, however, our results suggest that NAS adversely impacts audit quality only when auditors experience significant pressure to obtain future NAS fees. This suggest that the measures to limit partner compensation structure and performance evaluation considered in SOX and adopted by the Securities and Exchange Commission (SEC 2003) might effectively mitigate the independence impairing nature of NAS.

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1. Introduction

This research paper examines whether the *prospect* of receiving future non-audit service fees from audit clients influences audit quality. Specifically we examine if auditor's impair their independence when facing economic pressure to increase fee revenues by providing non-audit services. Auditor independence is essential to providing high quality audits and maintaining investor confidence in the financial reporting process. As a result, extensive regulatory attention has focused on ensuring that the auditor remains independent when making judgments about the presentation of their clients' financial reports. Regulators, including the Public Company Accounting Oversight Board (PCAOB) and State Boards of Public Accountancy influence General Accepted Auditing Standards (GAAS), ethical standards, and legal liability to collectively provide a framework that regulates auditor behavior. However, clients directly engage and compensate their auditor for audit and non-audit services. This creates potentially powerful economic incentives for auditors to compromise their independence.¹

In response, regulators addressed concerns that fees obtained from the provision of non-audit services can be detrimental to audit quality (Levitt 2000, SOX 2002). Driven in part by the scandalous affairs at Enron, who had paid large fees to their auditor for consulting work, regulators aggressively adopted policies that curb economic bonding between clients and their auditors from discretionary non-audit service fees. The Sarbanes Oxley Act of 2002 (SOX) embeds strict rules which ban auditors from providing most types of non-audit services (NAS) to their audit clients. The basic premise for the ban is that NAS are highly lucrative and provide a

¹ Extant literature provides extensive examination of the relationship between audit fees and audit quality (e.g., DeAngelo 1981; Simunic 1980; Francis 1984). We therefore focus specifically on NAS fees to address our research questions.

strong economic incentive for an auditor to acquiesce to client requests for more lenient treatment of reporting issues.

The banning of auditors providing non-audit services to their audit clients remains a very controversial aspect of SOX. A concern is the presence of other externalities such as potential loss in the economies of scope from the provision of professional services (Simunic 1984). Prior research indicates that joint provision of audit and non-audit services to audit clients provides richer and more complete information about the client, which in turn can be used by the auditor to produce more effective and efficient audits (Beck et al. 1984). Research indicates that auditor-provided NAS is associated with shorter audit report lags, which proxy for audit efficiency (Knechel and Payne 2001; Knechel and Sharma 2010). Paterson and Valencia (2009) find that recurring auditor-provided tax services lead to fewer earnings restatements. These results suggest that knowledge gained from provision of NAS can improve audit quality. Given these observed benefits it is important to investigate if NAS adversely affects audit quality by impairing auditor's independence. Moreover, although SOX strictly prohibits auditor's from providing a number of NAS to their publicly traded audit clients, the issue concerning NAS is of interest to other constituents where such services are still permitted, specifically the private sector and many international markets.²

The economic relationship between clients and auditors can threaten auditor independence (DeAngelo 1981; Simunic1984). However, empirical research has not substantiated the link between NAS fees and audit quality (DeFond et al. 2002; Ashbaugh et al. 2003; Larcker and Richardson 2004; Reynolds et al. 2004; Kinney et al. 2004).³ More specifically, prior archival

² For example, in Finland and Australia joint provision of audit and non-audit services is allowed (Salman and Carson 2009; Schadewitz and Vieru 2009)

³ Although most research finds no association, there is some evidence that auditor-provided NAS is associated with poor financial reporting quality including Frankel et al. (2002), Hoitash et al. (2005), Srinidhi and Gul (2007), and

research examines the relationship between the magnitude of NAS fees received from audit clients and various proxies of audit quality including earnings management (Frankel et al. 2002; Ashbaugh et al. 2003; Lim and Tan 2008), earnings conservatism (Ruddock et al. 2005), instances of earnings restatements (Kinney et al. 2004; Bloomfield and Shackman 2008), the propensity to issue going concern opinions (DeFond et al. 2002), and earnings response coefficients (Francis and Ke 2006). For the most part, the findings suggest that NAS fees do not appear to have an adverse impact on audit quality (Habib 2009; Defond and Francis 2005).

We extend this line of research in two ways. First, we focus on another aspect of the business relationship between an auditor and client: the prospect of future, potentially lucrative, NAS contracts that a client might use to reward an auditor who is willing to accept questionable financial reporting choices. We present the argument that the pressure can come from any client, not only the clients that currently pay high NAS fees. By simply comparing clients with low versus those with high NAS fees, prior literature does not acknowledge that even the low-NAS clients can exert pressure on the auditor simply by promising future business.⁴ Referring to the conflict of interest that might arise from future NAS fees, Coffee (2006) states that "...the real conflict lies not in the actual receipt of high fees, but in their expected receipt. Even the client currently paying low consulting revenues to its auditor might reverse this pattern if the auditor proved more cooperative." We suggest auditor independence is threatened by economic incentives created from the pursuit of additional service fees from current audit clients. This threat is potentially more salient than that created from current client NAS fees. We examine if

Elder et al. (2008). Moreover, Francis and Ke (2006) find that market perception of audit quality is negative when auditor provides NAS to its audit clients. Nevertheless, the majority of findings suggest no link between auditor-provided NAS and audit quality.

⁴ As Kinney and Libby (2002) note, "...more insidious effects on the economic bond may result from unexpected audit and non-audit service fees that more accurately be likened to attempted bribes."

prospective additional NAS fees adversely affects audit quality, while controlling for the current level of NAS fees.

Second, audit firms are under continuing pressure to expand their revenues. In response, prior to SOX, firms chose to increase the provision of, often very lucrative, NAS to existing clients. Audit services were affected by commodity type pricing with limited prospects for significant growth. It was suggested that many firms used the audit as a “loss leader” to more aggressively pursue growth opportunities in the area of NAS (Levitt 2000). Coffee (2006) suggests that compensation and promotions policies were used to reward partners who were able to cross-sell non-audit services. In many cases, partners who successfully attracted large NAS contracts through their salesmanship abilities replaced more technically proficient audit partners who failed to entice clients to purchase additional NAS.⁵

At the American Accounting Association Annual Meeting in 2003, Arthur Wyatt, a former FASB and IASB board member and former senior partner at Arthur Andersen stated that “Cross-selling of a range of consulting services to audit clients became one of the most important criteria in the evaluation of audit partners. Those with the technical skills previously considered so vital to internal firm advancement found themselves with relatively less important roles.” The pressure to obtain future business potentially makes the auditor more vulnerable to accepting future NAS in exchange for complacency. We therefore expect the prospective receipt of NAS to negatively affect audit quality when auditors find themselves under significant pressure to expand and increase future consulting engagements.

We argue that audit partners whose NAS fees from an audit client were relatively low in a given year are considered to be under significant pressure to obtain NAS fees in the future and

⁵ It is reported that at Arthur Andersen audit partners were expected to double the revenues obtained from their audit clients by cross-selling non-audit services (Brown and Dugan 2002).

thus are more likely to be affected by a NAS-based reward from a client. Based on this logic, we consider an auditor to be under pressure to increase NAS fees when their client's level of NAS fees in the current year is below the 50th percentile of such fees among the audit firm's clients in the same city and industry (PFEE). An audit firm's clients served by the same office and in the same industry are likely to be under the responsibility of the same partner. However, being under pressure is a necessary but not a sufficient condition for impaired independence; the partner must also have the opportunity to increase NAS fee revenue from the client in return for leniency in an audit dispute. The evidence of such an opportunity is unobservable, so our proxy for its existence is an observed significant increase in NAS fees in the following year (NY_PCT). We examine audit engagements characterized by two conditions: low NAS fees in the current year with an increase in NAS fees in the following year (PFEE*NY_PCT).

We investigate this expectation using data beginning with the time period before the passage of the Sarbanes Oxley Act of 2002 (SOX), when NAS were permitted. In the pre-SOX period, information systems design and implementation and services regarding internal audit were the most lucrative. We extend the analysis in the years after SOX to investigate the influence of allowed remaining NAS.⁶ We use three measures of audit quality found in prior research: (1) earnings management measured as the discretionary portion of current accruals (Ashbaugh et al. 2003; and Lim and Tan 2008); (2) propensity to issue going concern opinions (DeFond et al. 2002; Lim and Tan 2008) and (3) earnings restatements (Kinney et al. 2004; Paterson and Valencia 2009). Our goal is to identify engagements in which there was an increase in the following year's NAS fees and test whether the increase is associated with audit quality in the

⁶ SOX prohibits bookkeeping, information systems design and implementation, appraisals or valuation services, actuarial services, internal audits, management and human resources services, broker/dealer and investment banking services, legal or expert services unrelated to audit services. Other non-audit related services (e.g., tax services) are still allowed if approved by the Board.

current year and whether this association is more pronounced for auditors that we identify to be under significant pressure to obtain NAS fees.

Our findings are summarized as follows: first, examining earnings management using an absolute measure, we find, consistent with our expectations, that the prospect of receiving NAS adversely affects audit quality when the pressure to obtain fees is high. Further examination reveals that prior to SOX, auditors who expected rewards from additional NAS allow managers to report more income increasing or income decreasing discretionary accruals as well. After SOX there is no association between NAS and earnings management. Second, we find no association between prospective NAS and the propensity to issue a going concern opinion, pre- or post-SOX. Third, we find no relationship, pre- or post-SOX, between prospective NAS and the likelihood that financial statements require restatement at a later date.

Overall, these results offer important insights that enhance our understanding of the relationship between auditor-provided NAS and audit quality. Mechanisms that seek to preserve audit quality such as concern for reputation and litigation are least powerful when considering accrual quality because the flexibility and subjectivity inherent in GAAP make it difficult to ascertain the quality of an audit. However, auditors are not likely to compromise the quality of their work if this quality can be more easily detected and punished (such as the case of using the more objective measures of audit quality like restatements or going concern opinions). Our findings are consistent with prior research that finds audit quality to be lower in settings with more accounting uncertainty. In this setting it is more difficult to detect audit quality problems and auditors are less likely to suffer reputational costs (Mayhew et al. 2001).

Our findings provide important contributions to the literature investigating the influence of auditor-provided NAS on audit quality. We relax an assumption held by prior research that

investigates current year NAS fees influence on audit quality. We investigate the potential effect that prospective NAS fees have on auditor independence. We introduce the idea that it is not just high current NAS fees that could impair auditor independence; rather, it is also audit partners facing firm pressure to sell NAS, and having an opportunity to sell future NAS fees to an audit client, that is also likely to impair auditor independence. Second, the study provides evidence that economic bonding arising from the prospect of future NAS is important only when auditors are under pressure to obtain fees. Thus, while current regulation bans certain NAS on the grounds that joint provision leads to poor audit quality, our results suggest that in order for NAS to adversely impact audit quality another condition must be present, that of auditors experiencing significant pressure to obtain NAS fees. This suggest that the measures to limit partner compensation structure and performance evaluation considered in SOX and adopted by the Securities and Exchange Commission (SEC 2003) might effectively mitigate the independence impairing nature of NAS. We leave this for future research to investigate.

The remainder of the paper is organized as follows: section 2 describes the research design and section 3 reports the main results. Section 4 concludes the paper.

2. Research Design and Sample

Regression Models

We test for a relationship between prospective NAS fees, fee pressure and audit quality using Models (1), (2), and (3) shown below:

$$\begin{aligned}
 ADCA_t = & \alpha_0 + \alpha_1 PFEE_t + \alpha_2 NY_PCT_t + \alpha_3 (PFEE \times NY_PCT)_t + \alpha_4 LNNASF_t + \\
 & \alpha_5 TENURE80_t + \alpha_6 CFO_t + \alpha_7 LEV_t + \alpha_8 LITIG_t + \alpha_9 MB_t + \alpha_{10} MV_t + \\
 & \alpha_{11} LOSS_t + \alpha_{12} FIN_t + \alpha_{13} LCA_t + \alpha_{14} SPEC_{t-1} + YearDummies + \varepsilon
 \end{aligned} \tag{1}$$

ADCA is our proxy for audit quality measured as the absolute value of discretionary accruals as specified in Lim and Tan (2008). Specifically, we generate discretionary accruals using a cross-sectional performance-matched Jones model (see Kothari, Leone, and Wasley 2005). We first use all COMPUSTAT companies available in our sample years with available data. Required data items include current accruals, equal to income plus depreciation, minus operating cash flows ($CA_t = IBC_t + DPC_t - OANCF_t$), change in sales ($SALE_t - SALE_{t-1}$), lagged income before extraordinary items (IB_{t-1}), and lagged total assets (AT_{t-1}). We winsorize all variables at the one percent tails before estimating the following regression within years and within 2-digit SIC codes (excluding industries with less than six members).

$$\frac{CA_t}{AT_{t-1}} = \lambda_1 \frac{1}{AT_{t-1}} + \lambda_2 \frac{\Delta SALE_t}{AT_{t-1}} + \lambda_3 \frac{IB_{t-1}}{AT_{t-1}} + \varepsilon$$

Discretionary accruals (DCA) are equal to the residual values from estimating this regression model as described above. Absolute discretionary accruals (ADCA) are equal to the absolute value of DCA. Consistent with prior studies, we eliminate observations with ADCA greater than one. We estimate regression (1) using all observations, and also separately for observations with income increasing and decreasing DCA.

The motivation for choosing earnings management as a proxy for audit quality comes from the regulators perspective that auditors were allowing their clients to engage in the aggressive management of earnings (Levitt 1998). For example, in his speech at NYU in 1998, titled “The Numbers Game” Levitt states that: “Too many corporate managers, auditors, and analysts are participating in a game of nods and winks. In the zeal to satisfy consensus earnings estimates and project a smooth earnings path, wishful thinking maybe winning the day over faithful representation”. Moreover, one of the primary goals of SOX was to limit earnings manipulations

because this is where the regulators believed that auditors were becoming more lax in their monitoring (SEC 2003). In addition, incentives to maintain independence such as concern for reputation or litigation costs are least powerful when considering earnings management because of the flexibility and subjectivity inherent in GAAP (see Mayhew et al. 2001). Therefore, if auditor independence is compromised, earnings management would be a likely metric to manifest the impairment.

PFEE is our proxy for the pressure to obtain non-audit fees. PFEE equals one if a client's non-audit service fees to the auditor are below the 50th percentile of those paid by clients of the company-year auditor in the same city and the same 1-digit SIC industry and zero otherwise. NY_PCT is the larger of (a) the percentage change in total NAS fees, and (b) the maximum change in any single NAS fee component (e.g., information systems design and implementation fees) scaled by total fees from year t to year $t+1$. This controls for settings where total NAS fee change is small due to an increase in one type of service combined with a decrease in another and allows the capture of subsequent increases in new service fees. Scaling by total fees ensures our results are not driven by client total fee size. The interaction term, PFEE*NY_PCT is our independent variable of interest. We expect that the coefficient on the interaction term is positive ($\alpha_3 > 0$) suggesting that the prospect of receiving future NAS fees is detrimental to audit quality only when auditors experience strong pressure to obtain additional fees from NAS contracts.

The control variables included in the models are obtained from prior research (Ashbaugh et al. 2002; Lim and Tan 2008). LNNASF is the natural log of non-audit service fees paid to the auditor in the current year. TENURE80 is auditor tenure in years, while CFO is equal to operating cash flow scaled by total assets. LEV, measuring leverage, is equal to total liabilities

scaled by lagged total assets. LITIG is a dummy variable equal to one if the company-year is in a high litigation industry including those with SIC codes: 2833-2836, 3570-3577, 3600-3674, 522-5961, 7370-7474 and zero otherwise. MB is the market-to-book ratio, MV is the natural log of the market value of equity at fiscal year-end, and LOSS is a dummy variable that equals one if net income is less than zero, zero otherwise. FIN is a dummy variable indicating new financing and equals one if COMPUSTAT footnote SALE_FN equals “AB”, or the percentage change in long-term debt is greater or equal to 20 percent, or the percentage change in common shares outstanding (adjusted for stock splits, etc.) is greater or equal to 10 percent, zero otherwise. LCA is the absolute value of lagged total accruals, and SPEC is a dummy variable that equals one if the company-year’s audit firm has the greatest market share in the company’s 2-digit SIC code, zero otherwise. Yearly dummy variables are included in the regression to control yearly fixed effects. The regression is run separately for pre-SOX (years 2000-2001) and post-SOX (years 2005-2007).

In addition to earnings management, we follow prior research and select additional proxies of audit quality which are considered more objective, including the decision to issue a going concern opinion and the likelihood that financial statements are restated at a later date. We use model (2) below to test for the association between prospective NAS fees, fee pressure, and the propensity to issue a going concern opinion:

$$\begin{aligned}
 OPIN_t = & \beta_0 + \beta_1 PFEE_t + \beta_2 NY_PCT_t + \beta_3 (PFEE \times NY_PCT)_t + \beta_4 LNNASF_t + \\
 & \beta_5 ZSCORE_t + \beta_6 BETA_t + \beta_7 RETURN_t + \beta_8 VOLA_t + \beta_9 LEV_t + \beta_{10} CLEV_t + \\
 & \beta_{11} LLOSS_t + \beta_{12} OCF_t + \beta_{13} REPLAG_t + \beta_{14} ASSET_t + \beta_{15} INVM_t + \beta_{16} AGE_t + \\
 & \beta_{17} FFIN_t + \beta_{18} SPEC + YearDummies + \varepsilon
 \end{aligned} \tag{2}$$

OPIN is the dependent variable obtained from Audit Analytics, that equals to 1 if the client receives a going concern opinion in the current year, zero otherwise. The control variables are

based on prior literature (Lim and Tan 2008) as follows. ZSCORE is the Altman's Z-score reported by Compustat, BETA is the systematic risk over the fiscal year, RETURN is the firm's stock return over the fiscal year, VOLA is the variance of the residual from the market model over the fiscal year, and CLEV is the change in LEV during the year. LLOSS is equal to 1 if the firm reports a loss in the previous year, REPLAG is the number of days between the fiscal year-end and earnings announcement date, ASSET is the natural log of total assets at fiscal year-end, INVM is cash, cash equivalents, and short-term and long-term investment securities deflated by total assets at fiscal year-end, AGE is the number of years since the company was listed on a stock exchange, and FFIN equals to 1 if the client issues equity or debt in the following year. Similar to equation (1), the variable of interest is the two-way interaction PFEE*NY_PCT which measures the differential effect of prospective NAS fees when auditors are under heavy pressure to obtain NAS contracts, on the decision to issue a going concern opinion. The hypothesis predicts that the coefficient on the two-way interaction term is negative ($\beta_3 < 0$) suggesting that auditors are less likely to issue a going concern opinion if appropriately rewarded by the client. All other variables are defined as in equation (1).

We use model (3) below to test for the association between prospective NAS fees and the likelihood of a financial statement restatement:

$$\begin{aligned}
 RESTMT_t = & \delta_0 + \delta_1 PFEE_t + \delta_2 NY_PCT_t + \delta_3 (PFEE \times NY_PCT)_t + \delta_4 ACQUIS + \\
 & \delta_5 FEEAU_t + \delta_6 FEEIT_t + \delta_7 FEEAR_t + \delta_8 FEETAX_t + \delta_9 FEEBEN_t + \\
 & \delta_{10} FEEOTH_t + \delta_{11} MB_t + \delta_{12} LEV_t + \delta_{13} EXTFIN_t + \delta_{14} MV_t + \delta_{15} FCF_t + \\
 & \delta_{16} AQC_t + YearDummies + \varepsilon
 \end{aligned} \tag{3}$$

RESTMT is the dependent variable obtained from Audit Analytics, which equals 1 if the client restated its year t earnings at a later date, zero otherwise. The control variables are based on prior literature (Larcker et al. 2007) as follows. ACQUIS equals 1 if merger and acquisition

indicator in Compustat is “AA” or “AB”. FEEAU, FEEIT, FEEAR, FEETAX, FEEBEN, and FEEOTH are audit fees, IT fees, audit related fees, tax fees, benefit fees and other fees, respectively, each divided by the square root of total assets. EXTFIN is equal to net equity financing plus net debt financing all deflated by the beginning market value of equity. FCF is free cash flow and is measured as the difference between operating cash flow and average capital expenditures over the three prior years, and AQC is total cash spent on acquisitions during the fiscal period restated, deflated by beginning market value of equity; All other variables are defined as in equation (1). The hypothesis predicts that the coefficient on the interaction term, PFEE*NY_PCT, is positive ($\delta_3 > 0$) suggesting that the likelihood of a restatement is higher when clients promise future NAS to auditors that face significant economic pressure to obtain such fees.

Sample

We obtain data on Big-N clients regarding audit, non-audit fees, financial statement restatements, and going concern opinions from Audit Analytics, data on client characteristics from COMPUSTAT, and data on stock returns from CRSP.⁷ All continuous control variables are winsorized at the top and bottom 1 percent to remove extreme values. We eliminate company-years in SIC industry codes 6000 through 6999. In our tests, we report the results separately for two periods: 2000-2001 and 2005-2007. Most auditor-provided NAS were prohibited by SOX. We present results for the period 2005-2007 to examine the influence of this

⁷ We limit our investigation to Big-N firms (Arthur Andersen, Deloitte, Ernst & Young, KPMG, and Pricewaterhousecoopers) to be consistent with prior literature that identifies these firms as having differential audit quality and pricing (e.g., Francis and Wang 2005).

prohibition on the potential for an economic bond to form between the auditor and their clients, potentially impairing auditor independence.⁸

Table 1, panel A summarizes the sample size by year for each of the models. The accruals model (1) uses 4,093 firm-year observations for years 2000-2001 and 4,989 firm-year observations for years 2005-2007. The going concern model (2) uses 1,348 firm-year observations for years 2000-2001 and 954 firm-year observations for year 2005-2007. The restatement model (3) uses 887 firm-year observations for years 2000-2001 and 1,565 firm-year observations for years 2005-2007. It is possible for financial statement restatements to affect more than one quarter's or fiscal year's previously reported balances. In cases where multiple years were affected, we classify the restatement as occurring in the first year that was restated. The differences in sample sizes are the result of the different dependent and control variable requirements of each model. For example, the going-concern opinion sample is limited to companies with financial reports that indicate financial distress (either net income or operating cash flows less than zero). The restatement sample is limited by the availability of the restatement data and the need for quite a few lagged values to calculate the fee and control variables. Panel B summarizes frequency distribution of firms in each model by industry.

3. Results

Prospective non-audit services and earnings management

Descriptive Statistics

Table 2 presents descriptive statistics (Panel A) and correlation coefficients of the variables (Panel B) in the accruals model (1). We present the descriptive statistics in Panel A separately for the pre-SOX (2000-2001) and post-SOX periods (2005-2007). The mean (median) value of

⁸ We do not include the years 2002-2004 as these represent the transition years into SOX where NAS fees were declining and audit fees were increasing dramatically in response to the new regulation.

ADCA is 0.09 (0.05) during pre-SOX which are similar to the values reported in Lim and Tan (2008), but it drops to 0.06 (0.04) after SOX, which is consistent with the finding that SOX limited earnings management (Cohen et al. 2008). The mean value of NY_PCT prior to SOX is 0.22 indicating that non-audit fees scaled by total fees increased on average by 22 percent of total fees in 2001 compared to year 2000, suggesting that audit firms were actively pursuing NAS fees just prior to SOX. The value of NY_PCT drops to 0.05 after SOX. On average, about 40 percent of firms prior to SOX and 36 percent of firms after SOX had non-audit fees below the 50th percentile for the same combination of city and 1-digit SIC industries, as measured by PFEE. The average magnitude of NASF (000's) prior to SOX is 1488.06 dropping to 723.53 after SOX consistent with the banning of many forms of NAS. Note that NAS does not fall to zero, as many forms on NAS, mainly tax services, are still allowed under SOX. The mean value of auditor tenure is about 9 years (pre-SOX), and 11 years (after SOX). Finally, 28 percent of firms in the pre-SOX are audited by the specialist auditor, increasing to 33 percent after SOX.

In Panel B Pearson correlations show that prior to SOX, PFEE is positively and significantly correlated with ADCA providing some evidence that pressure to obtain fees may reduce audit quality, measured by higher absolute value of discretionary accruals. The relationship between ADCA and PFEE is not significant post-SOX, suggesting that the pressure to obtain fees does not affect accrual quality during this time. The relationship between ADCA and NY_PCT is negative and significant suggesting that an increase in prospective NAS is associated with lower discretionary accruals in only the pre-SOX period. Consistent with some prior literature, NAS fees are negatively correlated with absolute values of discretionary accruals. However, simple correlations do not simultaneously control for all variables that might influence ADCA. We

examine this in a multivariate form below. Other variables do not show significant correlations that might affect the inferences from our multivariate analysis.

Multivariate results

Table 3 presents the regression results of the accruals model (1) separately for years 2000-2001 (Panel A) and years 2005-2007 (Panel B). In Panel A, three separate results are shown, using total, income-increasing, and income-decreasing accruals. The OLS results in panels (A) and (B) have adjusted R-square ranging from 21 to 37 percent, suggesting a reasonably good fit and are comparable to levels reported in prior research. LNNASF is not a significant determinant of ADCA which suggests the current level of NAS obtained from the client does not affect audit quality (see Ashbaugh et al. 2003; Habib 2009). There is mild significance indicating less income increasing discretionary accruals as NAS increases. This indicates more conservative financial reporting in the presence of higher NAS fees which is contrary to the concerns of regulators.

The coefficients on PFEE and NY_PCT are negative and significant ($\alpha_1 = -0.016$ and $\alpha_2 = -0.014$, respectively) suggesting that simply being under pressure to obtain fees or obtaining an increase in future NAS fees does not necessarily lead to earnings management. To the contrary, the results suggest that auditors with high pressure to obtain fees or those who experience an increase in NAS fees are associated with reduced absolute accruals. Consistent with our expectations, the coefficient on the interaction term PFEE*NY_PCT, is positive and significant ($\alpha_3 = 0.018$, one tailed $p < 0.01$, t-statistic = 2.46). This suggests that when auditors are under significant pressure to obtain future NAS fees, an increase in prospective non-audit service fees is associated with more earnings management. We obtain a similar result when ADCA is equal to both income increasing ($\alpha_3 = 0.017$, one tailed $p < .05$, t-statistic = 1.81) and

income decreasing ($\alpha_3 = 0.019$, one tailed $p < .05$, t-statistic = 1.91) discretionary accruals. The sign and significance of the remaining control variables are consistent with prior research.

In order to provide a benchmark to our main results, we also test whether the relationship between prospective NAS, fee pressure, and audit quality remains during 2005-2007, after the implementation of the SOX prohibitions on NAS. The results in Panel B suggest that an increase in prospective NAS fees in the presence of significant pressure to obtain such fees is not associated with earnings management. This provides some evidence that the NAS allowed by SOX do not appear to affect auditor independence regarding decisions on reported accrual balances.

Overall, our results suggest that prior SOX, the presence of significant pressure to sell NAS, in combination with an opportunity to provide additional NAS services to an audit client, can cause a reduction in auditor independence resulting in lower reporting quality. In addition, although SOX still allows the joint provision of some NAS, these do not appear to adversely affect audit quality.⁹ Most importantly, in the pre-SOX period, the prospect of receiving additional NAS impairs audit quality only in those cases in which auditors are under significant pressure to increase their NAS revenues from their audit clients.

Prospective non-audit services and the likelihood of going concern opinions

Descriptive Statistics

Table 4 provides descriptive statistics of the sample used to test the going concern opinion model (2). As before, statistics are presented separately for pre and post-SOX time periods. In the pre-SOX sample, about 9 percent of sample companies on average received a going concern

⁹ Note that the SEC (2003) regulation mentioned earlier regarding partner compensation and evaluation might have reduced the pressure of the permitted NAS for the 2005-2007 time period.

opinion compared to about 5 percent after SOX. These statistics are comparable to Lim and Tan (2008). The pre-SOX mean value of NY_PCT is 0.19, dropping to 0.05 after SOX, suggesting that prior to SOX, on average NAS fees scaled by total fees increased by 19 percent, whereas the increase is only 5 percent after SOX. The mean PFEE is 0.49 (pre-SOX) and 0.44 (post-SOX). Panel B presents the Pearson correlations between the variables in the going concern model (2). The correlation between PFEE and OPIN is not significant pre- or post-SOX. NY_PCT is negatively and significantly correlated with OPIN prior to SOX, but not related to it after SOX. Other variables do not show significant correlations that might affect the inferences from our multivariate analysis.

Multivariate results

Table 5 presents the results of the going concern opinion logit regression related to model (2) separately for years 2000-2001 and years 2005-2007. In both regression outcomes, the adjusted R-square ranges from 14 to 16 percent which is comparable to levels reported in prior research (Lim and Tan 2008). The coefficients on PFEE and NY_PCT are not significant at conventional levels. Moreover, the coefficient on the interaction term PFEE*NY_PCT is not significant either prior to SOX ($\beta_3=0.150$, p-value = 0.87) or after SOX ($\beta_3=7.401$, p-value =0.33) suggesting that receipt of prospective NAS does not lead to a lower likelihood of issuing a going concern opinion even when the auditor is under pressure to increase NAS fees from audit clients. This result supports the results in DeFond et al. 2002 who find no association between NAS fees and the propensity to issue a going concern opinion. We extend this result by showing that the pressure created from prospective NAS fees likewise does not affect decisions regarding the issuance of going concern opinions.

Prospective non-audit services and the likelihood of restatements

Descriptive Statistics

Table 6 provides descriptive statistics of the sample used to test the restatement model (3). As before, statistics are presented separately for pre and post-SOX time periods. In the pre-SOX sample, about 8 percent of sample company years are affected by a restatement compared to about 3 percent after SOX. The pre-SOX mean value of NY_PCT is 0.25, dropping to 0.04 after SOX, suggesting that prior to SOX, on average the year-to-year increase in NAS fees was about 25 percent, whereas the increase was only 4 percent after SOX. The mean PFEE is 0.35 pre-SOX and 0.38 post-SOX. Panel B presents the Pearson correlations between the variables in the restatement model (3). The correlation between RESTMT and PFEE, and that between RESTMT and NY_PCT is not significant both before and after SOX. Other variables do not show significant correlations that might affect the inferences from our multivariate analysis.

Multivariate results

Table 7 presents the results of the restatement logit regression related to model (3) separately for years 2000-2001 and years 2005-2007. In both regression outcomes, the adjusted R-square ranges from 1 to 2 percent which is comparable to levels reported in prior research (Larcker et al. 2007). The coefficients on PFEE and NY_PCT are not significant at conventional levels. Moreover, the coefficient on the interaction term PFEE*NY_PCT is not significant either prior to SOX ($\beta_3=0.154$, p-value = 0.79) or after SOX ($\delta_3=-7.248$, p-value =0.22) suggesting that receipt of prospective NAS do not lead to an increase in the likelihood of a restatement even when the auditor is under pressure to increase NAS fees from audit clients. Our results are consistent with prior research which finds no association between NAS fees and the likelihood of a restatement. (eg. Kinney et al. 2004).

To summarize, our findings suggest that future NAS-based rewards are associated with GAAP-based earnings management only when auditors find themselves under significant pressure to obtain additional revenue. We obtain this result during pre-SOX periods when compensation practices led to increased pressure for partners to pursue aggressive growth in business and become more lenient towards their clients' reporting practices. In contrast, we do not obtain any significant association between NAS-based future rewards and earnings management post-SOX. This can be explained from the banning of certain NAS and potentially from the changes in compensation practices which banned audit partners from directly sharing the profits from NAS sales to audit clients. In addition, there seems to be no association between fee pressure and future NAS fees and more objective measures of audit quality including the likelihood of reporting earnings that require subsequent restatement and the issuance of going concern opinions either pre- or post-SOX.

Conclusion

In this paper we predict that auditor independence is threatened when auditors are under pressure to increase revenue generated from existing audit clients and when clients respond to this pressure by rewarding the auditor with future NAS contracts. Consistent with our expectations, we find that future receipt of non-audit service fees adversely affects accrual quality when the pressure to obtain new NAS fees is high in periods before the enactment of SOX. Absolute discretionary accruals are larger, comprising an increase from both income increasing and income decreasing discretionary accruals. In the post-SOX periods examined, discretionary accruals are not influenced by pressure to increase revenues or the receipt of future NAS fees. Our investigation of the propensity of the auditor to issue a going concern opinion or

financial statements to require future restatement finds that auditors do not appear to be influenced by the future receipt of NAS fees, regardless of the economic pressure imposed on the auditor in both pre- and post-SOX periods.

Overall, our results provide several interesting insights that enhance our understanding of the relationship between NAS and audit quality. First, we introduce the idea that potential future NAS fees are a potential threat to auditor independence. Therefore, the threat to auditor independence posed by NAS fees can come from clients that currently pay little or no NAS fees to their auditor. Second, we introduce the idea of selling pressure as an important interacting factor in the role of NAS fees and auditor independence. We find that it is the combination of selling pressure and the potential for future NAS fees, that creates the environment for impairment of auditor independence. This is the key finding that distinguishes our analysis from prior research. Our findings indicate little support for prohibiting NAS in the absence of fee pressure or based on the current level of NAS fees (as shown in most prior research). Fee pressure, not simply the receipt of NAS fees, seems to be the dominate factor that threatens auditor independence. In addition, our findings support prior research (Mayhew et al. 2001) which argues that auditors have more incentives to maintain high audit quality if the latter can be more easily observed, via financial statement restatements or inappropriate going concern opinions, but they are more willing to compromise when audit quality is uncertain.

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TABLE 1
Sample Size and Industry Distribution

Panel A: Distribution of sample companies by year

Year	Accruals Model	Going Concern Model	Restatement Model
2000	1,595	483	351
2001	<u>2,498</u>	<u>865</u>	<u>536</u>
Total company-years	4,093	1,348	887
Total companies	2,810	1,076	634
2005	1,778	354	511
2006	1,659	311	517
2007	<u>1,552</u>	<u>289</u>	<u>537</u>
Total company-years	4,989	954	1,565
Total companies	2,163	601	813

Panel B: Distribution of sample companies by industry

SIC Industry	<u>Accruals Model</u>				<u>Going Concern Model</u>				<u>Restatement Model</u>			
	<u>2000 – 2001</u>		<u>2005 – 2007</u>		<u>2000 – 2001</u>		<u>2005 – 2007</u>		<u>2000 – 2001</u>		<u>2005 – 2007</u>	
	N	%	N	%	N	%	N	%	N	%	N	%
13 Oil and gas extraction	166	4.06	199	3.76	17	1.26	15	1.57	28	3.16	58	3.71
20 Food and kindred prod.	82	2.00	139	2.63	10	0.74	10	1.05	26	2.93	64	4.09
28 Chemical and allied proc.	433	10.58	594	10.65	204	15.13	257	26.94	69	7.78	131	8.37
35 Industrial machinery/equip.	268	6.55	300	6.29	91	6.75	55	5.77	60	6.76	93	5.94
36 Electronic/other electric	334	8.16	375	8.15	144	10.68	92	9.64	47	5.30	91	5.81
37 Transportation equip.	111	2.71	152	2.78	28	2.08	20	2.10	39	4.40	55	3.51
38 Instruments and related	284	6.94	309	6.61	104	7.72	68	7.13	58	6.54	107	6.84
48 Communication	197	4.81	219	4.34	86	6.38	64	6.71	23	2.59	44	2.81
49 Electric/gas/sanitary serv.	205	5.01	321	5.70	14	1.04	15	1.57	138	15.56	233	14.89
50 Durable goods – whsl.	97	2.37	140	2.71	33	2.45	29	3.04	17	1.92	39	2.49

59 Miscellaneous retail	83	2.03	130	2.51	33	2.45	26	2.73	9	1.01	48	3.07
73 Business services/software	620	15.15	517	11.11	292	21.66	102	10.69	75	8.46	94	6.01
87 Engineering/mgmt. serv.	98	2.39	110	2.24	40	2.97	28	2.94	8	0.90	15	0.96
Other	<u>1,115</u>		<u>27.24</u>	<u>1,484</u>	<u>30.52</u>	<u>252</u>	<u>18.69</u>	<u>173</u>	18.13	<u>290</u>	<u>32.69</u>	<u>493</u>
<u>31.50</u>												
Total	4,093		4,989		1,348		954			887		1,565

TABLE 2

Descriptive Statistics and Correlation between Variables Used in the Accruals Model

Panel A: Descriptive statistics

Variable	2000 – 2001					2005 – 2007				
	Mean	SDT. Dev.	1 st Qrtl.	Median	3 rd Qrtl.	Mean	SDT. Dev.	1 st Qrtl.	Median	3 rd Qrtl.
<i>ADCA</i>	0.09	0.11	0.02	0.05	0.10	0.06	0.08	0.02	0.04	0.07
<i>NY_PCT</i>	0.22	0.38	0.00	0.09	0.31	0.05	0.12	0.00	0.01	0.06
<i>PFEE</i>	0.40	0.49	0	0	1	0.36	0.48	0	0	1
<i>NASF(000's)</i>	1488.06	5023.56	83.55	256.24	856.46	723.53	2042.47	72.25	229.13	614.90
<i>TENURE80</i>	8.95	6.38	4	7	12	10.92	7.45	5	9	16
<i>CFO</i>	0.02	0.22	-0.02	0.06	0.13	0.08	0.14	0.04	0.09	0.15
<i>LEV</i>	0.57	0.31	0.36	0.57	0.73	0.58	0.26	0.41	0.56	0.71
<i>LITIG</i>	0.34	0.47	0	0	1	0.31	0.44	0	0	1
<i>MB</i>	2.58	4.56	0.86	1.72	3.22	2.94	4.26	1.47	2.25	3.63
<i>MV</i>	5.56	2.24	3.91	5.59	7.06	7.00	1.79	5.80	6.99	8.13
<i>LOSS</i>	0.44	0.50	0	0	1	0.24	0.43	0	0	0
<i>FIN</i>	0.43	0.49	0	0	1	0.35	0.48	0	0	1
<i>LCA</i>	0.07	0.10	0.02	0.04	0.08	0.05	0.07	0.01	0.03	0.05
<i>SPEC</i>	0.28	0.45	0	0	1	0.33	0.47	0	0	1

Panel B: Pearson Correlations

(2000 – 2001 above diagonal; 2005 – 2007 below diagonal)

	<i>ADCA</i>	<i>NY_PCT</i>	<i>PFEE</i>	<i>LNNASF</i>	<i>TENURE80</i>	<i>CFO</i>	<i>LEV</i>	<i>LITIG</i>	<i>MB</i>	<i>MV</i>	<i>LOSS</i>	<i>FIN</i>	<i>LCA</i>	<i>SPEC</i>
<i>ADCA</i>		-0.07**	0.04**	-0.15**	-0.17**	-0.34**	0.09**	0.20**	0.04**	-0.22**	0.27**	0.20**	0.32**	0.01
<i>NY_PCT</i>	-0.01		0.01	-0.01	0.00	0.089**	-0.04**	-0.01	0.03	0.15**	-0.13**	-0.02	-0.06**	0.02
<i>PFEE</i>	0.01	-0.03*		-0.60**	-0.11**	-0.13**	0.00	0.03	-0.04**	-0.37**	0.13**	-0.04*	0.10**	-0.01
<i>LNNASF</i>	-0.11**	-0.01	-0.54**		0.25**	0.23**	0.10**	-0.09**	0.06**	0.70**	-0.20**	0.00	-0.19**	0.02
<i>TENURE80</i>	-0.09**	-0.05**	-0.08**	0.22**		0.222**	0.06**	-0.16**	0.03	0.26**	-0.26**	-0.11**	-0.14**	-0.00
<i>CFO</i>	-0.24**	0.05**	-0.09**	0.22**	0.09**		0.07**	-0.24**	-0.01	0.30**	-0.50**	-0.27**	-0.27**	0.00
<i>LEV</i>	0.10**	-0.03*	-0.01	0.13**	-0.01	-0.16**		-0.17**	-0.16**	-0.12**	0.09**	0.02	0.13**	-0.02
<i>LITIG</i>	0.12**	-0.00	0.03*	-0.11**	-0.04**	-0.17**	-0.13**		0.10**	-0.05**	0.21**	0.11**	0.17**	0.00
<i>MB</i>	0.00	0.02	-0.00	0.02	0.00	0.10**	-0.09**	0.05**		0.25**	-0.04**	0.04**	0.02	0.02
<i>MV</i>	-0.21**	0.02	-0.09**	0.54**	0.23**	0.39**	-0.03*	-0.08**	0.20**		-0.35**	-0.00	-0.24**	0.04**
<i>LOSS</i>	0.29**	-0.04**	0.07**	-0.19**	-0.14**	-0.56**	0.19**	0.18**	-0.08**	-0.41**		0.18**	0.19**	0.02
<i>FIN</i>	0.16**	0.01	-0.02	-0.06**	-0.08**	-0.18**	0.04**	0.05**	-0.01	-0.10**	0.14**		0.13**	0.02
<i>LCA</i>	0.33**	-0.00	0.04**	-0.16**	-0.09**	-0.25**	0.08**	0.10**	-0.02	-0.25**	0.25**	0.10**		-0.02
<i>SPEC</i>	0.02	0.01	0.00	-0.04**	0.03	-0.07**	-0.02	0.00	0.01	-0.03**	0.04**	0.02	0.03*	

Notes for Table 2

<i>ADCA</i>	=	Absolute value of discretionary accruals; observations with $ADCA > 1.0$ have been deleted.
<i>NY_PCT</i>	=	Percentage change in non-audit-services fees scaled by total fees from year t to $t+1$; winsorized at the 99 th percentile.
<i>PFEE</i>	=	Dummy variable equal to one if the company's non-audit-services fees are below the 50 th percentile of those paid by clients of the company-year's auditor in the same city and 1-digit SIC industry; zero otherwise.
<i>NASF</i>	=	Total non-audit service fees (000's)
<i>LNNASF</i>	=	Natural log of total non-audit-service fees.
<i>TENURE80</i>	=	Auditor tenure measured in years.
<i>CFO</i>	=	Operating cash flows scaled by lagged total assets .
<i>LEV</i>	=	Leverage; total liabilities scaled by current total assets.
<i>LITIG</i>	=	Dummy variable equal to one if the company-year is in a high litigation SIC code: 2833-2836, 3570-3577, 3600-3674, 5200-5961, 7370-7374; zero otherwise.
<i>MB</i>	=	Market-to-book ratio.
<i>MV</i>	=	Natural log of market value of equity at fiscal-year-end.
<i>LOSS</i>	=	Dummy variable equal to one if net income is less than zero; zero otherwise.
<i>FIN</i>	=	Dummy variable indicating new financing. Equal to one if COMPUSTAT footnote SALE_FN equals "AB", or the percentage change in long-term debt is greater or equal to 20 percent, or the percentage change in common shares outstanding (adjusted for stock splits, etc.) is greater or equal to 10 percent; zero otherwise.
<i>LCA</i>	=	Absolute value of lagged total accruals.
<i>SPEC</i>	=	Dummy variable equal to one if the company-year's audit firm has the greatest market share in the company's 2-digit SIC code; zero otherwise.

All continuous control variables are winsorized at the 1 percent tails.

** and * denote statistical significance at the 1 and 5 percent levels, respectively.

TABLE 3

Regression of Absolute Discretionary Accruals on Fee Variables and Controls

Panel A: Years 2000 - 2001

$$ADCA_t = \alpha_0 + \alpha_1 PFEE_t + \alpha_2 NY_PCT_t + \alpha_3 (PFEE \times NY_PCT)_t + \alpha_4 LNNASF_t + \alpha_5 TENURE80_t + \alpha_6 CFO_t + \alpha_7 LEV_t + \alpha_8 LITIG_t + \alpha_9 MB_t + \alpha_{10} MV_t + \alpha_{11} LOSS_t + \alpha_{12} FIN_t + \alpha_{13} LCA_t + \alpha_{14} SPEC_{t-1} + \alpha_{15} Y(0) + \varepsilon$$

ADCA=	Total discretionary accruals		Income increasing discretionary accruals		Income decreasing discretionary accruals	
	Estimated Coefficient	t-statistic	Estimated Coefficient	t-statistic	Estimated Coefficient	t-statistic
Variable						
Intercept	0.088***	5.19	0.138***	5.45	0.060***	2.73
<i>PFEE</i>	-0.016***	-3.34	-0.016***	-2.67	-0.016***	-2.46
<i>NY_PCT</i>	-0.014***	-2.54	-0.016**	-2.42	-0.012	-1.58
<i>PFEE x NY_PCT</i>	0.018***	2.46	0.017**	1.81	0.019**	1.91
<i>LNNASF</i>	-0.000	-0.15	-0.004*	-1.73	-0.000	-0.01
<i>TENURE80</i>	-0.001***	-4.09	-0.001**	-2.17	-0.001***	-4.04
<i>CFO</i>	-0.091***	-5.62	-0.240***	-11.38	0.014	0.59
<i>LEV</i>	0.022***	2.84	-0.006	-0.65	0.043***	4.00
<i>LITIG</i>	0.023***	5.71	-0.003	-0.60	0.037***	6.68
<i>MB</i>	0.002***	3.07	-0.000	-0.37	0.002***	3.24
<i>MV</i>	-0.006***	-4.29	-0.001	-0.84	-0.006***	-3.51
<i>LOSS</i>	0.011***	2.64	-0.053***	-8.53	0.052***	9.82
<i>FIN</i>	0.022***	6.73	0.022***	5.29	0.021***	4.76
<i>LCA</i>	0.216***	7.30	0.322***	8.21	0.122***	3.38
<i>SPEC</i>	-0.005	-1.55	0.004	0.88	0.004	0.80
Adjusted R ²	0.212		0.371		0.216	
N	4,093		1,755		2,338	

TABLE 3

Regression of Absolute Discretionary Accruals on Fee Variables and Controls

Panel B: Years 2005 - 2007

$$ADCA_t = \alpha_0 + \alpha_1 PFEE_t + \alpha_2 NY_PCT_t + \alpha_3 (PFEE \times NY_PCT)_t + \alpha_4 LNNASF_t + \alpha_5 TENURE80_t + \alpha_6 CFO_t + \alpha_7 LEV_t + \alpha_8 LITIG_t + \alpha_9 MB_t + \alpha_{10} MV_t + \alpha_{11} LOSS_t + \alpha_{12} FIN_t + \alpha_{13} LCA_t + \alpha_{14} SPEC_{t-1} + \alpha_{15} Y_t + \varepsilon$$

ADCA= Variable	Total discretionary accruals		Income increasing discretionary accruals		Income decreasing discretionary accruals	
	Estimated Coefficient	t-statistic	Estimated Coefficient	t-statistic	Estimated Coefficient	t-statistic
Intercept	0.050	5.01	0.056***	2.97	0.010	0.78
<i>PFEE</i>	-0.004*	-1.68	-0.002	-0.39	-0.005	-1.45
<i>NY_PCT</i>	-0.003	-0.25	-0.004	-0.19	-0.000	-0.00
<i>PFEE x NY_PCT</i>	0.003	0.18	0.017	0.57	-0.006	-0.37
<i>LNNASF</i>	-0.001	-0.68	0.001	0.84	-0.000	-0.28
<i>TENURE80</i>	-0.000	-1.34	-0.001***	-2.67	0.000	0.17
<i>CFO</i>	-0.019	-1.04	-0.222***	-9.72	0.191***	5.87
<i>LEV</i>	0.015***	2.54	0.011	1.53	0.023***	2.62
<i>LITIG</i>	0.009***	3.51	0.002	0.39	0.012***	3.65
<i>MB</i>	0.001**	1.93	0.001**	2.22	0.000	0.27
<i>MV</i>	-0.002***	-2.91	-0.004***	-2.91	-0.002**	-2.21
<i>LOSS</i>	0.028***	6.03	-0.043***	-8.25	0.076***	12.68
<i>FIN</i>	0.016***	7.08	0.017***	5.17	0.009***	3.55
<i>LCA</i>	0.278***	8.37	0.300***	6.81	0.244***	5.41
<i>SPEC</i>	-0.001	-0.28	-0.009***	-2.56	0.005*	1.89
Adjusted R ²	0.228		0.394		0.214	

N

4,989

1,909

3,080

Notes for Table 3

<i>ADCA</i>	=	Absolute value of discretionary accruals; observations with $ADCA > 1.0$ have been deleted.
<i>NY_PCT</i>	=	Percentage change in non-audit-services fees scaled by total fees from year t to $t+1$; winsorized at the 99 th percentile.
<i>PFEE</i>	=	Dummy variable equal to one if the company's non-audit-services fees are below the 50 th percentile of those paid by clients of the company-year's auditor in the same city and 1-digit SIC industry; zero otherwise.
<i>LNNASF</i>	=	Natural log of total non-audit-service fees.
<i>TENURE80</i>	=	Auditor tenure measured in years.
<i>CFO</i>	=	Operating cash flows scaled by lagged total assets .
<i>LEV</i>	=	Leverage; total liabilities scaled by current total assets.
<i>LITIG</i>	=	Dummy variable equal to one if the company-year is in a high litigation SIC code: 2833-2836, 3570-3577, 3600-3674, 5200-5961, 7370-7374; zero otherwise.
<i>MB</i>	=	Market-to-book ratio.
<i>MV</i>	=	Natural log of market value of equity at fiscal-year-end.
<i>LOSS</i>	=	Dummy variable equal to one if net income is less than zero; zero otherwise.
<i>FIN</i>	=	Dummy variable indicating new financing. Equal to one if COMPUSTAT footnote SALE_FN equals "AB", or the percentage change in long-term debt is greater or equal to 20 percent, or the percentage change in common shares outstanding (adjusted for stock splits, etc.) is greater or equal to 10 percent; zero otherwise.
<i>LCA</i>	=	Absolute value of lagged total accruals.
<i>SPEC</i>	=	Dummy variable equal to one if the company-year's audit firm has the greatest market share in the company's 2-digit SIC code; zero otherwise.
<i>Y(n)</i>	=	Yearly dummy variables.

All continuous control variables are winsorized at the 1 percent tails.

t-statistics are calculated based on the Huber-White method (Diggle et al. 1994)

***, ** and * denote statistical significance at the 1, 5 and 10 percent levels, respectively, using one-tailed test for the hypothesized variables and two-tailed for the control variables.

TABLE 4

Descriptive Statistics and Correlation between Variables Used in the Going Concern Opinion Model

Panel A: Descriptive statistics

Variable	2000 – 2001					2005 – 2007				
	Mean	SDT. Dev.	1 st Qrtl.	Median	3 rd Qrtl.	Mean	SDT. Dev.	1 st Qrtl.	Median	3 rd Qrtl.
<i>OPIN</i>	0.09	0.28	0	0	0	0.05	0.21	0	0	0
<i>NY_PCT</i>	0.19	0.33	0.00	0.06	0.26	0.05	0.11	0.00	0.00	0.05
<i>PFEE</i>	0.49	0.50	0	0	1	0.44	0.50	0	0	1
<i>NASF</i>	596.16	1813.15	61.23	150.00	445.00	323.36	666.11	36.00	111.71	302.90
<i>ZSCORE</i>	1.20	0.89	0	2	2	1.29	0.85	0	2	2
<i>BETA</i>	1.09	0.83	0.45	0.94	1.63	1.13	0.66	0.69	1.13	1.56
<i>RETURN</i>	-0.19	0.70	-0.66	-0.35	0.06	-0.05	0.52	-0.38	-0.15	0.14
<i>VOLA</i>	0.00	0.00	0.00	0.00	0.01	0.00	0.00	0.00	0.00	0.00
<i>LEV</i>	0.56	0.40	0.28	0.52	0.74	0.63	0.37	0.37	0.57	0.80
<i>CLEV</i>	0.07	0.24	-0.01	0.04	0.12	0.06	0.17	-0.01	0.03	0.10
<i>LLOSS</i>	0.66	0.47	0	0	1	0.67	0.47	0	1	1
<i>OCF</i>	-0.13	0.30	-0.18	-0.03	0.04	-0.10	0.26	-0.16	-0.01	0.05
<i>REPLAG</i>	53.58	27.41	36.00	50.00	70.50	60.44	47.25	41.00	57.00	70.00
<i>ASSET</i>	5.04	1.67	3.82	4.88	6.11	5.72	1.62	4.47	5.62	6.79
<i>INVM</i>	0.29	0.29	0.04	0.17	0.47	0.33	0.30	0.06	0.23	0.59
<i>AGE</i>	9.55	6.14	5	7	13	13.58	7.25	8	12	19
<i>FFIN</i>	0.71	0.45	0	1	1	0.79	0.41	1	1	1
<i>SPEC</i>	0.29	0.45	0	0	1	0.38	0.49	0	0	1

Panel B: Pearson Correlations

(2000 – 2001 above diagonal; 2005 – 2007 below diagonal)

	<i>OPIN</i>	<i>NY_PCT</i>	<i>PFEE</i>	<i>LNNASF</i>	<i>ZSCORE</i>	<i>BETA</i>	<i>RETURN</i>	<i>VOLA</i>	<i>LEV</i>	<i>CLEV</i>	<i>LLOSS</i>	<i>OCF</i>	<i>REPLAG</i>	<i>ASSET</i>	<i>INVM</i>	<i>AGE</i>	<i>FFIN</i>	<i>SPEC</i>
<i>OPIN</i>		-0.09**	0.05	-0.10**	0.18**	-0.08**	-0.10**	0.26**	0.18**	0.15**	0.15**	-0.28**	0.28**	0.21**	-0.08**	-0.05	0.00	-0.03
<i>NY_PCT</i>	-0.04		0.03	-0.04	-0.12**	-0.03	0.15**	-0.14**	-0.01	-0.06*	-0.04	0.08**	-0.05	0.10**	0.01	0.04	0.09**	0.02
<i>PFEE</i>	0.01	0.00		-0.60**	0.02	-0.16**	0.01	0.15**	0.00	0.03	0.10**	-0.10**	0.13**	-0.33**	0.04	-0.03	-0.08**	-0.01
<i>LNNASF</i>	-0.05	-0.00	-0.57**		0.07**	0.24**	-0.05	-0.26**	0.07**	-0.02	-0.21**	0.21**	-0.22**	0.72**	-0.15**	0.11**	0.12**	0.02
<i>ZSCORE</i>	0.14**	-0.01	0.02	0.04		-0.09**	-0.22**	0.25**	0.47**	0.28**	0.11	-0.18**	0.18**	0.02	-0.26**	-0.01	-0.05	0.02
<i>BETA</i>	-0.07*	0.05	0.00	0.16**	0.07*		-0.12**	0.15**	-0.19**	0.05*	0.21**	-0.20**	-0.30**	0.20**	0.40**	-0.27**	0.14**	-0.00
<i>RETURN</i>	-0.10**	0.07*	0.02	-0.03	-0.21**	0.04		-0.19**	-0.04	-0.22**	0.05	0.14**	-0.06*	0.01	0.03	0.11**	0.13**	0.04
<i>VOLA</i>	0.28**	-0.06*	0.07*	-0.24**	0.20**	-0.11**	-0.13**		0.14**	0.18**	0.30**	0.41**	0.23**	-0.46**	0.10**	-0.30**	-0.07**	-0.03
<i>LEV</i>	0.15**	0.04	-0.06*	0.24**	0.45**	0.04	-0.03	0.08*		0.56**	-0.00	-0.10**	0.24**	0.03	-0.38**	0.14**	0.05	-0.03
<i>CLEV</i>	0.21**	-0.02	-0.05	0.04	0.25**	-0.02	-0.21**	0.18**	0.47**		0.10**	-0.26**	0.12**	-0.10**	-0.08**	-0.10**	0.02	-0.03
<i>LLOSS</i>	0.09**	0.02	0.08*	-0.20**	0.26**	0.05	0.08**	0.29**	0.10**	0.06*		-0.33**	0.05	-0.26**	0.36**	-0.35**	0.07*	0.00
<i>OCF</i>	-0.37**	0.05	-0.10**	0.29**	-0.19**	0.01	0.10**	-0.37**	-0.10**	-0.29**	-0.34**		-0.07**	0.46**	-0.36**	0.28**	-0.01	-0.01
<i>REPLAG</i>	0.08**	-0.05	0.06*	0.04	0.08*	-0.11**	-0.06	0.11**	0.08*	0.08*	0.01	-0.03		-0.28**	-0.18**	0.07*	-0.04	-0.05
<i>ASSET</i>	-0.20**	0.06	-0.14**	0.58**	0.08**	0.30**	0.03	-0.41**	0.22**	-0.08*	-0.29**	0.50**	-0.07*		-0.20**	0.18**	0.12**	0.04
<i>INVM</i>	0.03	0.06	0.11**	-0.37**	0.09**	0.13**	0.01	0.23**	-0.16**	0.05	0.39**	-0.51**	-0.09**	-0.41**		-0.31**	0.02	0.09**
<i>AGE</i>	-0.00	0.03	-0.12**	0.26**	-0.11**	0.05	0.02	-0.27**	0.09**	-0.09**	-0.29**	0.24**	-0.01	0.29**	-0.32**		-0.00	-0.05
<i>FFIN</i>	0.06	0.03	0.00	-0.05	0.04	0.01	0.10**	0.03	0.06	0.07*	0.05	-0.13**	-0.06	-0.08**	0.03	0.01		0.07*
<i>SPEC</i>	-0.08*	0.00	0.00	-0.09**	-0.00	-0.07*	0.04	0.04	-0.07*	-0.02	0.07*	-0.06	0.00	-0.05	0.15**	-0.05	0.04	

Notes for Table 4

OPIN	=	Dummy variable equal to one if the client receives a going concern opinion, zero otherwise.
NY_PCT	=	Percentage change in non-audit-services fees scaled by total fees from year t to t+1; winsorized at the 99 th percentile.
PFEE	=	Dummy variable equal to one if the company's non-audit-services fees are below the 50 th percentile of those paid by clients of the company-year's auditor in the same city and 1-digit SIC industry; zero otherwise.
NASF	=	Total non-audit service fees (000's).
LNNASF	=	Natural log of total non-audit-service fees.
ZSCORE	=	Altman's Z-score reported by Compustat.
BETA	=	Systematic risk over the fiscal year.
RETURN	=	Firm's stock return over the fiscal year.
VOLA	=	Variance of the residual from the market model over the fiscal year.
LEV	=	Leverage; total liabilities scaled by current total assets.
CLEV	=	Change in LEV during the year.
LLOSS	=	Dummy variable equal to one if last year's net income is less than zero; zero otherwise.
OCF	=	Operating cash flow scaled by total assets at fiscal year-end.
REPLAG	=	Number of days between the fiscal year-end and earnings announcement date.
ASSET	=	Natural log of total assets at fiscal year-end.
INVM	=	cash, cash equivalents, and short-term and long-term investment securities deflated by total assets at fiscal year-end.
AGE	=	Number of years since the company was listed on a stock exchange.
FFIN	=	Dummy variable equal to one if the client issues equity or debt in the following year; zero otherwise.
SPEC	=	Dummy variable equal to one if the company-year's audit firm has the greatest market share in the company's 2-digit SIC code; zero otherwise.

All continuous control variables are winsorized at the 1 percent tails.

** and * denote statistical significance at the 1 and 5 percent levels, respectively.

TABLE 5

Logit Regression of Going Concern Opinion on Fee Variables and Controls

$$\begin{aligned}
 OPIN_t = & \beta_0 + \beta_1 PFEE_t + \beta_2 NY_PCT_t + \beta_3 (PFEE \times NY_PCT)_t + \beta_4 LNNASF_t + \\
 & \beta_5 ZSCORE_t + \beta_6 BETA_t + \beta_7 RETURN_t + \beta_8 VOLA_t + \beta_9 LEV_t + \beta_{10} CLEV_t + \\
 & \beta_{11} LLOSS_t + \beta_{12} OCF_t + \beta_{13} REPLAG_t + \beta_{14} ASSET_t + \beta_{15} INVM_t + \\
 & \beta_{16} AGE_t + \beta_{17} FFIN_t + \beta_{18} SPEC_{t-1} + \beta_{19} Yt + \varepsilon
 \end{aligned}$$

Sample Period:	2000-2001		2005-2007	
Variable	Estimated Coefficient	Wald statistic	Estimated Coefficient	Wald statistic
Intercept	-5.712***	12.93	-6.541***	7.66
PFEE	-0.126	0.16	0.083	0.03
NY_PCT	-0.689	0.89	-6.553	0.85
PFEE*NY_PCT	0.150	0.02	7.401	0.94
LNNASF	0.132	0.89	0.139	0.44
ZSCORE	0.317*	2.96	0.848**	5.42
BETA	-0.514***	7.25	-0.387	1.46
RETURN	-0.217	1.22	-0.483	1.14
VOLA	62.106**	4.23	482.80***	11.25
LEV	0.306	0.72	-0.286	0.21
CLEV	0.133	0.07	0.722	0.41
LLOSS	1.288***	14.46	0.251	0.19
OCF	-1.993***	23.92	-3.555***	19.95
REPLAG	0.027***	31.95	0.003	0.99
ASSET	-0.196	2.31	-0.275	1.95
INVM	2.373***	13.75	-2.421***	6.31
AGE	-0.009	0.17	0.095***	8.68
FFIN	0.264	1.09	0.203	0.14
SPEC	-0.190	0.53	-1.049**	5.71
Adjusted R ²	0.163		0.138	
N	1,348		954	

Notes for Table 5

OPIN	=	Cumulative abnormal return equal to the three-day cumulated raw return over days -1, 0, and 1 around the earnings announcement date, less the three-day cumulated CRSP value-weighted market return over the same period.
NY_PCT	=	Percentage change in non-audit-services fees scaled by total fees from year t to t+1; winsorized at the 99 th percentile.
PFEE	=	Dummy variable equal to one if the company's non-audit-services fees are below the 50 th percentile of those paid by clients of the company-year's auditor in the same city and 1-digit SIC industry; zero otherwise.
LNNASF	=	Natural log of total non-audit-service fees.
ZSCORE	=	Altman's Z-score reported by Compustat.
BETA	=	Systematic risk over the fiscal year.
RETURN	=	Firm's stock return over the fiscal year.
VOLA	=	Variance of the residual from the market model over the fiscal year.
LEV	=	Leverage; total liabilities scaled by current total assets.
CLEV	=	Change in LEV during the year.
LLOSS	=	Dummy variable equal to one if last year's net income is less than zero; zero otherwise.
OCF	=	Operating cash flow scaled by total assets at fiscal year-end.
REPLAG	=	Number of days between the fiscal year-end and earnings announcement date.
ASSET	=	Natural log of total assets at fiscal year-end.
INVM	=	cash, cash equivalents, and short-term and long-term investment securities deflated by total assets at fiscal year-end.
AGE	=	Number of years since the company was listed on a stock exchange.
FFIN	=	Dummy variable equal to one if the client issues equity or debt in the following year; zero otherwise.
SPEC	=	Dummy variable equal to one if the company-year's audit firm has the greatest market share in the company's 2-digit SIC code; zero otherwise.

All continuous control variables are winsorized at the 1 percent tails.

***, ** and * denote statistical significance at the 1, 5 and 10 percent levels, respectively, using one-tailed test for the hypothesized variables and two-tailed for the control variables.

TABLE 6

Descriptive Statistics and Correlation between Variables Used in the Restatement Model

Panel A: Descriptive statistics

Variable	2000 – 2001					2005 – 2007				
	Mean	SDT. Dev.	1 st Qrtl.	Median	3 rd Qtrl.	Mean	SDT. Dev.	1 st Qrtl.	Median	3 rd Qtrl.
<i>RESTMT</i>	0.08	0.27	0	0	0	0.03	0.18	0	0	0
<i>NY_PCT</i>	0.25	0.40	0.00	0.11	0.34	0.04	0.10	0.00	0.01	0.04
<i>PFEE</i>	0.35	0.48	0	0	1	0.38	0.48	0	0	1
<i>ACQUIS</i>	0.16	0.37	0	0	0	0.15	0.35	0	0	0
<i>FEEAU</i>	18.94	13.44	9.92	15.89	24.48	58.00	47.36	30.14	47.76	75.00
<i>FEEIT</i>	3.72	20.49	0	0	0	0.00	0.00	0.00	0.00	0.00
<i>FEEAR</i>	3.41	10.04	0	0	0	4.67	9.57	0.33	1.81	4.81
<i>FEETAX</i>	4.49	13.18	0	0	0	7.17	11.51	0.40	2.74	9.55
<i>FEEBEN</i>	0.26	3.41	0	0	0	0.02	0.20	0	0	0
<i>FEEOTH</i>	20.49	31.01	3.30	9.70	25.08	0.53	3.56	0.00	0.00	0.07
<i>MB</i>	2.35	2.99	0.95	1.70	2.91	2.78	3.71	1.51	2.22	3.59
<i>LEV</i>	0.62	0.25	0.46	0.63	0.76	0.60	0.22	0.45	0.61	0.72
<i>EXTFIN</i>	-0.02	0.33	-0.07	-0.01	0.06	0.01	0.18	-0.06	-0.02	0.03
<i>MV</i>	6.23	2.39	4.50	6.48	7.91	7.46	1.84	6.34	7.45	8.63
<i>FCF</i>	156.75	642.47	-8.98	7.53	101.57	336.48	1135.11	-4.00	49.26	224.91
<i>AQC</i>	0.04	0.11	0.00	0.00	0.02	0.03	0.09	0.00	0.00	0.02

Panel B: Pearson Correlations

(2000 – 2001 above diagonal; 2005 – 2007 below diagonal)

	<i>RESTMT</i>	<i>NY_PCT</i>	<i>PFEE</i>	<i>ACQUIS</i>	<i>FEEAU</i>	<i>FEEIT</i>	<i>FEEAR</i>	<i>FEETAX</i>	<i>FEEBEN</i>	<i>FEEOTH</i>	<i>MB</i>	<i>LEV</i>	<i>EXTFIN</i>	<i>MV</i>	<i>FCF</i>	<i>AQC</i>
<i>RESTMT</i>		0.02	0.01	0.02	0.01	0.00	-0.02	-0.00	-0.01	-0.03	-0.02	0.03	-0.04	-0.05	0.03	0.01
<i>NY_PCT</i>	-0.01		-0.06	0.01	-0.08**	-0.04	-0.04	-0.05	-0.02	-0.02	0.09**	-0.04	0.06	0.10**	0.01	0.09**
<i>PFEE</i>	0.01	-0.03		-0.08*	0.08*	-0.13**	-0.19**	-0.19**	-0.05	-0.33**	-0.14**	-0.02	-0.13**	-0.46**	-0.14**	-0.09**
<i>ACQUIS</i>	-0.02	0.05*	-0.05		-0.01	-0.03	0.06*	0.03	0.02	0.06	0.01	-0.03	0.16**	0.10**	0.05	0.40**
<i>FEEAU</i>	0.06*	-0.07**	0.02	0.03		0.09**	0.22**	0.29**	0.06	0.30**	0.07*	0.20**	-0.03	0.00	0.19**	-0.01
<i>FEEIT</i>	.	.	.	.	.		0.02	0.08*	0.01	0.28**	0.01	0.01	0.01	-0.16**	0.09**	-0.03
<i>FEEAR</i>	0.00	0.00	-0.27**	0.04	0.23**	.		0.42**	0.02	-0.01	0.09**	0.10**	0.05	0.24**	0.11**	0.09**
<i>FEETAX</i>	-0.02	0.08	-0.36**	0.06*	0.38**	.	0.27**		0.11**	-0.05	0.07*	0.01	-0.01	0.20**	0.18**	-0.01
<i>FEBEN</i>	-0.02	0.03	-0.00	-0.00	-0.00	.	-0.03	-0.03		0.01	0.01	0.02	-0.01	0.07*	0.05	-0.02
<i>FEEOTH</i>	0.03	-0.01	-0.10**	0.02	0.20**	.	0.05*	0.07**	-0.01		0.18**	0.07*	0.01	0.34**	0.29**	0.02
<i>MB</i>	-0.02	0.04	-0.05*	0.01	-0.09**	.	0.00	0.00	0.02	-0.02		-0.11**	0.02	0.39**	0.25**	-0.02
<i>LEV</i>	0.03	-0.05*	0.01	-0.10**	0.15**	.	0.06**	0.03	0.02	0.08**	-0.11**		0.00	-0.07*	0.01	0.11**
<i>EXTFIN</i>	0.06**	-0.01	-0.00	0.17**	-0.01	.	0.02	-0.04	-0.02	-0.03	-0.07**	0.07**		0.16**	-0.04	0.38**
<i>MV</i>	-0.05*	0.03	-0.14**	0.04	0.03	.	0.12**	0.12**	-0.03	0.01	0.22**	-0.10**	-0.13**		0.42**	0.07*
<i>FCF</i>	-0.04	0.02	-0.13**	0.02	0.06*	.	0.16**	0.17**	-0.03	0.04	0.11**	-0.07**	-0.10**	0.53**		0.00
<i>AQC</i>	0.01	0.03	-0.04	0.37**	0.02	.	0.06**	0.07**	-0.03	0.01	-0.05*	0.04	0.48**	-0.04	-0.01	

Notes for Table 6

RESTMT	=	Dummy variable equal to one if the client restated its year t earnings; zero otherwise.
NY_PCT	=	Percentage change in non-audit-services fees scaled by total fees from year t to t+1; winsorized at the 99 th percentile.
PFEE	=	Dummy variable equal to one if the company's non-audit-services fees are below the 50 th percentile of those paid by clients of the company-year's auditor in the same city and 1-digit SIC industry; zero otherwise.
ACQUIS	=	Dummy variable equal to one if merger and acquisition indicator in Compustat is "AA" or "AB"; zero otherwise.
FEEAU	=	Audit fees divided by the square root of total assets and fiscal year-end.
FEEIT	=	IT fees divided by the square root of total assets and fiscal year-end. This variable is equal to zero for years 2005-2007.
FEEAR	=	Audit related fees divided by the square root of total assets and fiscal year-end.
FEETAX	=	Tax fees divided by the square root of total assets and fiscal year-end.
FEEBEN	=	Benefit fees divided by the square root of total assets and fiscal year-end.
FEEOTH	=	Other fees divided by the square root of total assets and fiscal year-end.
MB	=	Market-to-book ratio.
LEV	=	Leverage; total liabilities scaled by current total assets.
EXTFIN	=	Net equity financing plus net debt financing all deflated by the beginning market value of equity.
MV	=	Natural log of market value of equity at fiscal-year-end.
FCF	=	Free cash flow and is measured as the difference between operating cash flow and average capital expenditures over the three prior years.
AQC	=	Total cash spent on acquisitions during the fiscal period restated, deflated by beginning market value of equity.

All continuous control variables are winsorized at the 1 percent tails.

** and * denote statistical significance at the 1 and 5 percent levels, respectively.

TABLE 7

Logit Regression of Restatements on Fee Variables and Controls

$$RESTMT_t = \delta_0 + \delta_1 PFEE_t + \delta_2 NY_PCT_t + \delta_3 (PFEE \times NY_PCT)_t + \delta_4 ACQUIS_t + \delta_5 FEEAU_t + \delta_6 FEEIT_t + \delta_7 FEEAR_t + \delta_8 FEETAX_t + \delta_9 FEEBEN_t + \delta_{10} FEEOTH_t + \delta_{11} MB_t + \delta_{12} LEV_t + \delta_{13} EXTFIN_t + \delta_{14} MV_t + \delta_{15} FCF_t + \delta_{16} AQC_t + \delta_{17} Y_t + \varepsilon$$

Variable	2000-2001		2005-2007	
	Estimated Coefficient	Wald statistic	Estimated Coefficient	Wald Statistic
Intercept	-1.774***	8.67	-3.369***	74.70
PFEE	-0.312	0.74	0.180	0.24
NY_PCT	0.172	0.20	0.983	0.41
PFEE*NY_PCT	0.154	0.07	-7.248	1.51
ACQUIS	0.245	0.45	-0.284	0.35
FEEAU	0.002	0.03	0.004	2.95
FEEIT	0.003	0.31	.	.
FEEAR	-0.007	0.19	0.003	0.03
FEETAX	-0.002	0.03	-0.022	1.19
FEEBEN	-0.008	0.02	-33.370	0.01
FEEOTH	-0.005	0.71	0.018	0.54
MB	0.000	0.00	0.011	0.11
LEV	0.264	0.30	0.069	0.01
EXTFIN	-0.308	0.80	1.395**	4.46
MV	-0.126*	3.08	-0.077	0.73
FCF	0.000*	3.51	-0.000	3.89
AQC	0.573	0.23	-0.551	0.12
Adjusted R ²	0.011		0.023	
N	887		1,565	

Notes for Table 7

RESTMT	=	Dummy variable equal to one if the client restated its year t earnings; zero otherwise.
NY_PCT	=	Percentage change in non-audit-services fees scaled by total fees from year t to t+1; winsorized at the 99 th percentile.
PFEE	=	Dummy variable equal to one if the company's non-audit-services fees are below the 50 th percentile of those paid by clients of the company-year's auditor in the same city and 1-digit SIC industry; zero otherwise.
ACQUIS	=	Dummy variable equal to one if merger and acquisition indicator in Compustat is "AA" or "AB"; zero otherwise.
FEEAU	=	Audit fees divided by the square root of total assets and fiscal year-end.
FEEIT	=	IT fees divided by the square root of total assets and fiscal year-end.
FEEAR	=	Audit related fees divided by the square root of total assets and fiscal year-end.
FEETAX	=	Tax fees divided by the square root of total assets and fiscal year-end.
FEEBEN	=	Benefit fees divided by the square root of total assets and fiscal year-end.
FEEOTH	=	Other fees divided by the square root of total assets and fiscal year-end.
MB	=	Market-to-book ratio.
LEV	=	Leverage; total liabilities scaled by current total assets.
EXTFIN	=	Net equity financing plus net debt financing all deflated by the beginning market value of equity.
MV	=	Natural log of market value of equity at fiscal-year-end.
FCF	=	Free cash flow and is measured as the difference between operating cash flow and average capital expenditures over the three prior years.
AQC	=	Total cash spent on acquisitions during the fiscal period restated, deflated by beginning market value of equity.

All continuous control variables are winsorized at the 1 percent tails.

***, ** and * denote statistical significance at the 1, 5 and 10 percent levels, respectively, using one-tailed test for the hypothesized variables and two-tailed for the control variables.