**CEOs with accounting backgrounds have an impact on:**
- Firms’ earnings management behavior
- Level of accounting conservatism

**Earnings management happens when:**
Managers use judgment in financial reporting and in structuring transactions to alter financial reports to either:
- Mislead some stakeholders about the underlying economic performance of the company; or
- Influence contractual outcomes that depend on reporting accounting number

**Accounting conservatism**
- Accountants’ tendency to require a higher degree of verification for recognizing good news in earnings than for recognizing bad news.
- Gains and losses are treated differently using accounting conservatism.

**Methodology**
- Review existing literature and develop the following hypotheses
  - CEOs with accounting backgrounds are less likely to engage in income-increasing discretionary accruals.
  - CEOs with accounting backgrounds are more likely to be associated with a lower level of accounting conservatism.
- Data Collection and Empirical Models
  - Obtain educational backgrounds from BoardEx database.
  - Collect the financial-related information for the companies from the Compustat database and the stock return data from the Center for Research in Security Prices (CRSP).
- For each firm-year, to identify the accounting background for its CEO, we take a three-step approach, which requires merging the inside trading data with the BoardEx data:
  - Step 1. Based on the inside trading data from Thomson Financial, we identify the inside trading transactions conducted by CEOs by using the ROLECODE variable.
  - Step 2. Since CEOs of a given company might not conduct inside trading every year, we use his or her first inside trading year as the year he or she starts to work for that company and his or her last inside trading year as the year he or she leaves that company. Any years in between are classified as the years that CEO works for that firm. This is a more conservative way of identifying the years a CEO works for one particular firm.
  - Step 3. We match CEOs’ first and last names from BoardEx with those from inside trading to identify the backgrounds for each CEO.

**Research model**
- Link CEOs backgrounds to discretionary accruals, while controlling for other factors that are likely to influence earnings management.

**Model 1**
\[
DA_t = \alpha + \beta_1 \cdot \text{Accounting} + \beta_2 \cdot \text{Lev}_{t-1} + \beta_3 \cdot \text{Market} - \text{to} - \text{Book}_{t-1} + \beta_4 \cdot \text{Operating}\ 
- \text{Cycle} + \beta_5 \cdot \text{Capital} - \text{intensity} + \beta_6 \cdot \text{cash} - \text{flow} + \beta_7 \cdot \text{Size} + \beta_8 \cdot \text{Loss}
+ \sum_{i=1}^{3} \gamma_i \cdot \text{Other}_i
\]
- To determine whether CEOs with accounting backgrounds are less likely to be conservative, we first need to estimate the accounting conservatism of each firm. Estimate the C-score(Model 2), which is the firm-year measure of conservatism or incremental bad news timelines, and the total-score(Model 3), which is the total bad news timeline, as indicators of accounting conservatism.

**Model 2**
\[
c_{\text{score}} = \alpha + \beta_1 \cdot \text{Accounting} + \beta_2 \cdot \text{Gender} + \beta_3 \cdot \text{Age} + \beta_4 \cdot \text{Time}_\text{To_Retire}
+ \beta_5 \cdot \text{Time} - \text{in} - \text{Role} + \beta_6 \cdot \text{Time} - \text{on} - \text{Board} + \beta_7 \cdot \text{Time} - \text{in} - \text{Org}
+ \beta_8 \cdot \text{Time} - \text{in} - \text{Other} - \text{Org} + \beta_9 \cdot \text{Num}_\text{Qualifications}
\]

**Model 3**
\[
t_{\text{total-score}} = \alpha + \beta_1 \cdot \text{Accounting} + \beta_2 \cdot \text{Gender} + \beta_3 \cdot \text{Age} + \beta_4 \cdot \text{Time}_\text{To_Retire}
+ \beta_5 \cdot \text{Time} - \text{in} - \text{Role} + \beta_6 \cdot \text{Time} - \text{on} - \text{Board} + \beta_7 \cdot \text{Time} - \text{in} - \text{Org}
+ \beta_8 \cdot \text{Time} - \text{in} - \text{Other} - \text{Org} + \beta_9 \cdot \text{Num}_\text{Qualifications}
\]

- For robust check purpose, we also use market-to-book ratio as the other accounting conservatism measures (Model 4).

**Model 4**
\[
\text{Market} - \text{to} - \text{Book} = \alpha + \beta_1 \cdot \text{Accounting} + \beta_2 \cdot \text{Gender} + \beta_3 \cdot \text{Age} + \beta_4 \cdot \text{Time}_\text{To_Retire}
+ \beta_5 \cdot \text{Time} - \text{in} - \text{Role} + \beta_6 \cdot \text{Time} - \text{on} - \text{Board} + \beta_7 \cdot \text{Time} - \text{in} - \text{Org}
+ \beta_8 \cdot \text{Time} - \text{in} - \text{Other} - \text{Org} + \beta_9 \cdot \text{Num}_\text{Qualifications} + \sum_{i=1}^{3} \gamma_i \cdot \text{Other}_i
\]

**Conclusion**
CEOs who have accounting backgrounds are associated with lower levels of accounting conservatism, but not with higher levels of income-increasing discretionary accruals.

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