Shareholder Ratification of Auditors After PCAOB Censures

Vishal Munsif*
California State University San Bernardino

ABSTRACT
Prior research provides inconsistent evidence about the effect of PCAOB censures of U.S. Big 4 audit firms on investors' reactions. In this study, I use shareholder ratifications of the auditor as a direct measure of investor perceptions about audit quality. I find that first-time censures of Deloitte, Ernst & Young, and PwC by the PCAOB are associated with greater shareholder dissatisfaction, as measured by the percentage of shareholders not voting to ratify the auditor after the censure. However, repeat censures of Deloitte do not elicit significant shareholder reactions. In additional analyses of PCAOB censures of two second-tier audit firms, Grant Thornton and RSM, I also find no significant change in shareholder ratification voting following the censures**.** Overall, these results suggest that investors view PCAOB censures as signals of negative audit quality in some circumstances, particularly following the initial censure of a Big 4 audit firm. These findings are potentially relevant to regulators, audit committees, auditors, and investors.

Key Words: PCAOB censure, market response
JEL: M4

Contact. Email: Vmunsif@csusb.edu

1. INTRODUCTION

In this paper I provide empirical evidence about the following question: Does a censure by the Public Company Accounting Oversight Board (PCAOB) of an audit firm affect shareholders' perceptions about that auditor? Motivation for this paper comes from (a) the role of the PCAOB in ensuring investor confidence in the quality of independent audits, and (b) the differing results from prior studies addressing this issue. I use shareholder voting on auditor ratification to measure investor perceptions because it gives "shareholders a more direct stake in the audit process" (Mayhew 2017, 126).

The PCAOB is a nonprofit corporation established by Congress as part of the Sarbanes-Oxley Act (SOX 2002). The PCAOB notes on its website that it was established to "oversee the audits of public companies in order to protect investors and the public interest by promoting informative, accurate, and independent audit reports." As part of such oversight, the PCAOB inspects registered public accounting firms to assess compliance with SOX, the rules of the PCAOB and the SEC, and professional standards, in connection with the performance of audits.

The primary objective of the PCAOB's inspection program is to improve audit quality by monitoring auditor compliance with professional standards (CAQ 2012). One of the tools in the arsenal of the PCAOB is a disciplinary order (censure). A censure indicates that an auditor has violated PCAOB rules and auditing standards, failed to cooperate with a Board inspection, and/or failed to remediate audit deficiencies in a timely manner to the satisfaction of the PCAOB, and hence is punitive (Boone et al. 2019).

A censure is a rare occurrence, especially for the large international audit firms. From the start of the PCAOB's functioning in 2002 there have been only five censures involving the U.S. offices of the Big 4 firms until 2021. Hence, a censure by the PCAOB has the potential to damage the reputation of an audit firm particularly since auditing is a credence good.

Financial statement users cannot publicly observe the audit process, including the misstatements and errors detected by the auditor. Since the users can only observe the final audit report that does not provide much detail by way of measures of quality, the value of auditing is driven largely by the reputations established by the audit firms (DeAngelo 1981b; Watts and Zimmerman 1986). The value of independent audits to investors arises because of the assurance provided by the auditors, and such value is associated with the perceived quality of the audit provided by the external auditor (Francis and Wilson 1988; Barton 2005).[1] Hence, any damage to the reputation of the audit firm, which in turn can lead to reduced investor confidence in audit quality, can reduce the value of the audit (Wilson and Grimlund 1990).

Two prior studies find evidence consistent with the above argument that stakeholders view PCAOB censures as negative. Dee et al. (2011) and Boone et al. (2015) find that the PCAOB's very first censure of a Big 4 firm in 2007 was associated with significant costs to both SEC audit clients of Deloitte (in the form of stock price declines) and to Deloitte itself (in the form of more client switches and a lower audit fee growth), respectively. However, Boone et al. (2019) report that the negative response of investors and audit committees observed in Dee et al. (2011) and Boone et al. (2015) are not present for the censures of Ernst in 2012 and Deloitte again in 2013.

Measuring investor reactions to PCAOB censures through price changes has advantages and disadvantages. The advantage is that stock price change is the most basic metric of investor perceptions about a company. However, there also are some disadvantages to using stock prices to measure investor perceptions about audit quality and PCAOB censures. For example,

1 Investors can view external audits as a form of insurance (Menon and Williams 1994). A PCAOB censure can increase the litigation risk of the audit firm and reduce the value of such insurance provided by the audit firm.

Zimmerman (2013) asserts that financial reporting quality by itself has only a second order effect on valuations and, hence, the effects of audit quality on such valuations would be even more indirect. Further, the PCAOB censures occur after a drawn-out process; so precise measurement of stock price reactions to the censure event is difficult.[2]

I add to the research stream about shareholder perceptions of PCAOB censures using an alternative metric that enables direct measurement of investor reactions to PCAOB censures. I use shareholder votes against (or, abstaining from) ratification of the auditor as my measure of investor perceptions about the auditor. No empirical metric is perfect, and the shareholder ratification voting metric has its own problems (such as, a low proportion of votes not voting to ratify the auditor). But the advantage of this measure is that it is a relatively direct measure of investor perceptions that does not also impose costs on shareholders wanting to express their dissent. Thus, Raghunandan (2003, 162) notes "the unhappiest stockholders (those most concerned about the credibility of management's reports) may also be the most likely to sell their shares (as opposed to voting their shares). However, selling the shares may lead to significant costs to shareholders. Ultimately, it is a trade-off between the costs of selling the shares vs. putting pressure on management to … improve the credibility of financial statements." Also, Mayhew (2017, 125) summarizes prior research on auditor ratification and notes that evidence from prior studies shows that "votes against auditor ratification seem to matter to the firm and its shareholders even though the relative magnitude of the votes against auditor ratification is usually very small."

I examine the five censures of Big 4 audit firms from 2007 to 2019, using two different types of tests. Appendix A summarizes each censure, including the audit firm, date of the PCAOB action, nature of the violation, and disciplinary action imposed. In the first test, I compare the shareholder votes at clients of the censured audit firm immediately before and after the censure. Thus, I use each client as its own control to mitigate concerns about endogeneity and omitted variables. In the second test, I use clients of other (non-censured) Big 4 clients as the control sample. In both tests, I find that shareholders are more likely to vote against, or abstain from, ratifying an auditor immediately after the first PCAOB censure of a Big 4 audit firm. Consistent with Boone et al. (2019), I find that the second (third) censure of Deloitte in 2013 (2018) does not elicit a significant reaction from shareholders.

As additional analyses, I examine two censures of second-tier audit firms. However, I do not observe a significant reaction to such censures when examining shareholder votes to ratify the auditor at clients of such non-Big 4 firms.

In summary, I provide empirical evidence about the association between PCAOB censures and shareholder reactions. The evidence supports the argument that, in some instances, investors find PCAOB censures of audit firms as useful signals of audit quality. In the spirit of DeFond and Zhang (2014)'s suggestions for auditing researchers to triangulate using different metrics, I also confirm the inferences of Boone et al. (2019)—that repeat censures do not elicit investor reactions—using an alternative metric. More generally, I add to the research stream about the consequences of the PCAOB's disciplinary actions (Dee et al. 2011; DeFond and Lennox 2017; Aobdia and Shroff 2019; Boone et al. 2015, 2019).

The next section discusses the background and develops the research question. I then provide a description of method, including data and results. The paper concludes with a summary and discussion.

2 While such concerns are less relevant for analyses focusing on auditor changes and audit fees, audit committees can also be influenced by other factors that are not publicly observable by investors (such as, the identity of the members of the audit team [other than the signing partner, since 2017] and their personal characteristics, etc.).

2. BACKGROUND AND RESEARCH QUESTION

The United States Congress created the Securities and Exchange Commission (SEC) in 1934, with a mandate to regulate the audits of SEC registrants. However, the SEC delegated such monitoring to the public accounting profession including the American Institute of Certified Public Accountants (AICPA) and its predecessor (American Institute of Accountants). After the US congressional hearings during the 1970s led by Representative Moss and Senator Metcalf, the AICPA created the SEC Practice Section (SECPS) and made it mandatory for any member firm that audited SEC registrants to belong to the SECPS. Member firms were subject to peer-reviews once every three years.

Thus, until 2002, individual auditors and audit firms certifying the financial statements of SEC registrants were subject to professional self-regulation. This changed after SOX. Section 101 of SOX established the PCAOB, and made the PCAOB the regulator of public company audits. Auditors of public companies have to register with the PCAOB, and are subject to the inspection process of the PCAOB.

The PCAOB issues reports following inspections of registered audit firms. Such inspection reports have two parts. Part 1 of the report is public, and provides information about problems found in inspected audit engagements. Thus, the information is at the audit engagement level. Since the problems are at the *client-level*, the identified problems do not necessarily reflect poorly about the audit quality of the overall audit firm. Further, almost all such inspection reports, especially of the large global and national firms, have such engagement-level deficiencies.

Hence, the data provided in Part 1 of the inspection reports is of limited use for researchers interested in examining cross-sectional differences in audit quality, or perceptions of such quality. Consistent with this assertion, Lennox and Pittman (2010) find that the information disclosures in Part 1 of the inspection reports show little by way of cross-sectional differences in Big 4 audit quality. Lennox and Pittman (2010) also show that audit clients do not perceive the inspection reports as valuable in terms of signaling audit quality. Similarly, Gunny and Zhang (2013) find that for audit firms subject to annual PCAOB inspection such inspection reports do not distinguish audit quality during the period inspected.[3]

However, Part II of the PCAOB's inspection reports are non-public. Part II of the reports relates to problems with the *firm-level* quality control problems. Even though such firm-level problems are arguably more informative to users and can serve as better signals of audit quality at the audit firm level, such information is not publicly available. This is because Section 104 of SOX states: "No portions of the inspection report that deal with criticisms of or potential defects in the quality control systems of the firm under inspection shall be made public if those criticisms or defects are addressed by the firm, to the satisfaction of the Board, not later than 12 months after the date of the inspection report."

Thus, the information in Part II of the PCAOB inspection reports can become public if and only if the defects are not addressed to the satisfaction of the PCAOB during the following 12 months. Usually, the audit firm resolves such issues to the PCAOB's satisfaction and, hence, the data remains non-public. In those rare instances when the audit firm has not addressed the problems to the satisfaction of the PCAOB, Part II of the inspection report becomes public.

Boone et al. (2019, 622) suggest that "given the rarity and intended punitive nature of a PCAOB disciplinary order, a censure can convey new information about the factual audit quality

3 Gunny and Zhang (2013) find that for the smaller (triennially-inspected) audit firms PCAOB inspections are associated with lower audit quality (higher abnormal accruals or restatements) when the reports are seriously deficient. However, my focus in this study is only on the annually inspected Big 4 and second-tier audit firms.

of the censured US Big 4 firm as well as harm the reputation of the censured firm by adversely affecting the perceived quality of the firm's audit services." Two prior studies find evidence consistent with the assertion that users react negatively to a PCAOB censure. Based on tests examining stock prices of Deloitte and non-Deloitte clients, Dee et al. (2011) conclude that the PCAOB censure revealed new information that was damaging to Deloitte's reputation or insurance value that led to negative stock market consequences for Deloitte clients. Boone et al. (2015) examine the consequences to Deloitte itself. If audit committees view the PCAOB censure negatively then it is likely that clients would be less likely to retain or hire Deloitte as their auditor. Boone et al. (2015) find evidence consistent with the above argument. Further, since Deloitte could, at the margin, make itself more attractive by offering lower audit fees, Boone et al. (2015) also examine the changes in audit fees. They find a decrease in growth-rate of audit fees for Deloitte, and conclude that the PCAOB censure imposed actual costs on Deloitte.

Subsequently, there have been four other instances of PCAOB censures of the US Big 4 firms: Ernst & Young in February 2012, Deloitte in October 2013 and May 2018, and PwC in August 2017. Boone et al. (2019) build upon an intriguing finding in their 2015 study—that there was little evidence of any difference in Deloitte's audit quality, when compared with the other Big 4 firms, over a three-year window surrounding the 2007 censure. Boone et al. (2019) document that the negative responses of investors and audit committees are not present for the next two Big 4 censures (Ernst in 2012 and Deloitte in 2013). Boone et al. (2019, 622) note that "the absence of any reputational harm to the auditor following a censure would suggest that PCAOB censures may not be having the intended punitive ('real consequences') effect on the censured US Big 4 firms."

DeFond and Zhang (2014), in their summary of archival auditing research, note the various measurement and inference issues associated with measures of audit quality such as accruals and measures of investor perceptions such as client stock price reactions to events related to their auditors. DeFond and Zhang (2014) recommend the use of multiple measures for questions related to audit quality and investor perceptions. My study uses shareholder ratification of the auditor as a more direct measure of investor perceptions of audit quality. Mayhew (2017, 125), in his summary of auditor ratification research, notes that results from auditor ratification voting "convey information to both the firm and to its current and future shareholders" and there is "value in shareholders ratifying the auditor as a way to link some of the auditors' incentives directly to the shareholders they are supposed to be serving."

2.1. Shareholder Ratification of the Auditor

Brown (2012) and Mayhew (2017) provide summaries of the regulatory and legal issues related to shareholder ratification of the auditor. I provide a very brief discussion of the relevant issues. In the standard corporate governance framework, shareholders (a) delegate responsibility to management to run the firm, and (b) elect a board of directors to monitor management and protect shareholders' interests. In turn, the board hires an external auditor to opine on the financial statements prepared by management. Mayhew (2017) notes that while in theory the audit committee has the power to select and set the compensation for the auditor, in practice management often exerts significant influence over the appointment and compensation of the auditor. Mayhew (2017, 126) states: "Management's influence over the auditor has long been recognized as a threat to independence and audit quality. It is, quite simply, difficult to believe that the auditor can objectively attest to the veracity of the financial statements prepared by the same party who hires and fires the auditor. Auditor ratification arose as a mechanism that quickly evolved to give shareholders a more direct stake in the audit process."

Neither federal nor state securities laws require shareholder ratification of the auditor.

Nevertheless, many companies offer shareholders the option to ratify the auditor as a matter of good corporate governance (Dao et al. 2012). Prior research shows that client size and governance-related variables are associated with having an auditor ratification vote (Krishnan & Ye 2005; Dao et al. 2012). Two prior studies, in an experimental setting (Mayhew & Pike 2004) and using archival data (Dao et al. 2012), show that providing investors with an opportunity to have a say on auditor selection is associated with greater auditor effort, higher audit fees, and better audit quality. Many prior studies have shown that shareholder dissatisfaction with the auditor (as measured by the proportion of votes not voting to ratify the auditor) is associated with factors that researchers and others have used as proxies for audit quality. Raghunandan (2003) and Mishra et al. (2005) rely on the SEC's (2000, 2003) assertions that disclosures about non-audit fees would be useful for shareholders in their decisions about ratifying the auditor selected by management. These two studies find that shareholders are more likely to vote against (or, abstain from) ratification in the presence of higher non-audit fee ratios. Another factor that regulators and legislators have suggested can impair audit quality is the length of the auditor-client relationship. Consistent with this argument, Dao et al. (2008) and Dunn et al. (2021) find that shareholders are more likely to vote against auditor ratification when the audit firm tenure is longer.[4] Other studies have found that the proportion of shareholder votes not voting to ratify the auditor is related to variables used as proxies for audit quality, including going-concern modified audit opinions (Sainty et al. 2002), internal control opinions, (Hermanson et al. 2009), and client financial restatements (Liu et al. 2009; Cassell et al. 2020).

Thus, there is strong evidence from prior studies that when shareholders perceive that audit quality is lower they are more likely to vote against (or, abstain from) auditor ratification. In the context of the current study, this leads to the first research question:

RQ1: Are shareholders more likely to vote against (or, abstain from) auditor ratification if the auditor has been subject to PCAOB censure?

In my analyses, I examine only those instances where there is no auditor change. This is because initial year audits are unique (DeAngelo 1981a; Simon & Francis 1988; Gul et al. 2009; Barua et al. 2020) and because I use analyses of changes (in addition to levels analyses). Thus, I can compare the shareholder voting for the same auditor immediately before and after the PCAOB censure. One advantage of such an approach is that it enables us to sidestep concerns related to correlated omitted variables.

3. METHOD

As noted earlier, there have been five censures of a US-based Big 4 audit firm. I examine the shareholder voting on auditor ratification immediately after each of these five events. As discussed in detail below, I use two different comparisons. In the first test, I use each firm as its own control; thus, I compare shareholder voting immediately before and after the censure. In the second test, I use clients of the other Big 4 firms as the control sample. In this test, I compare shareholder votes at clients of the censured audit firm against votes at clients of other (non-censured) audit firms.

Test 1 - Sample

4 The positive correlation between auditor tenure and the proportion of shareholder votes not ratifying the auditor, while consistent with the concerns of legislators and regulators, is contrary to the evidence presented in many studies showing that audit quality is in fact lower in the initial years of an audit engagement.

Table 1 provides details about the sample selection process for the first test. I begin with 11,868 observations for audit clients with necessary data in the Audit Analytics database for the year before and after these five PCAOB censures. I restrict the sample to observations with December 31 fiscal year-end to alleviate concerns about the timing of the shareholder ratification vote, and the gap between PCAOB censure and such voting. I then remove 2,282 observations missing auditor ratification voting data in the Institutional Shareholder Services (ISS) database.[5] I do not rely on the Audit Analytics database for the shareholder voting data because such data are available only from 2010 in Audit Analytics. As noted earlier, the first PCAOB censure occurred in 2007 and prior research suggests that the first censure is unique and different from the subsequent PCAOB censures (Boone et al. 2019). Hence, since the ISS database includes information about shareholder ratification voting for the years prior to 2010 I use that database for all of my voting data.

Next, I delete 484 companies (968 observations) missing relevant financial statement data in Compustat. Consistent with most research in auditing, I remove 186 companies (372 observations) in the financial sector (SIC 6000 – 6999). Finally, I exclude 37 companies (74 observations) that had an auditor change. The final sample size for my first test—where I compare the voting immediately before and after the censure, and hence each client serves as its own control—is 1,698 companies (3,396 observations). Panel B of Table 1 presents the sample distribution by industry. I provide details about the sample for the second test—where I compare shareholder voting at the clients of the censured firm against shareholder voting at clients of other Big 4 firms—in a later sub-section.

Test 1 - Model

I use the following OLS regression model to examine the association between the PCAOB's censure of a Big 4 public auditing firm and subsequent shareholder ratification of the audit firm's appointment.

$$Ln(VOTE+1) = CENSURE + NAS + RESTATE + ICW + SPECIALIST + Ln(TENURE) + Ln(AT) + LEVERAGE + RETURN + Industry\ Dummies \quad (1)$$

The dependent variable, *Ln(VOTE + 1)*, is the natural logarithm of the *Vote* (in percent) plus 1; I add 1 because in some instances the *VOTE* measure is zero, and logarithm of zero is not defined. *VOTE* is the sum of shareholder votes "against" or "abstaining from" the ratification of the auditor divided by total shareholder votes (i.e., the sum of for, against, or abstain), expressed in percent form. I measure the dependent variable in the period before and after the vote. Hence, every company in the sample has a pre- and post-PCAOB censure firm-year observation.

In Test 1, the independent variable of interest, *CENSURE*, is an indicator variable that takes the value 1 for the shareholder vote occurring after the PCAOB censure, and 0 for the shareholder vote occurring before the PCAOB censure. I include several control variables shown in prior research to be correlated with the shareholder vote to ratify the auditor's appointment. I control for the proportion of non-audit fees received by the audit firm from the client (*NAS*) because higher non-audit fee ratios are associated with higher shareholder dissatisfaction (Raghunandan 2003; Mishra et al. 2005). I include indicator variables capturing whether the client had an accounting restatement (*RESTATE*) or material weakness in internal control over financial reporting (*ICW*) based on the results of Liu et al. (2009) and Hermanson et al. (2009), respectively.

5 As noted earlier, shareholder ratification is not a requirement under federal or state securities laws.

I control for whether the local audit office of the client is an auditor industry specialist (*SPECIALIST*). Generally, specialist audit offices have more resources and capability to provide a high level of assurance to investors regarding the quality of their audit services (Ferguson et al. 2003; Reichelt & Wang 2010). I expect shareholder dissatisfaction to be lower for audit offices that are industry specialists. Concerns about the effect of long-term auditor-client relationships on auditor independence may influence auditor ratification voting. Dao et al. (2008) and Dunn et al. (2021) show that longer auditor tenure is associated with higher shareholder dissatisfaction. Hence, I include auditor tenure as a control variable (*LN(TENURE*)).

I control for client size (*AT*), financial leverage (*LEVERAGE*), and stock price performance (*RETURN*). Activist shareholders generally pay more attention to large firms and are thus more likely to target these firms for symbolic votes against management and auditors (Dao et al. 2008). More generally, client size is used as a control variable in almost all accounting and auditing studies since it proxies for a variety of constructs. Leverage and stock performance capture the financial health of the company. I expect shareholders of companies in good financial condition to be generally satisfied with the management and auditor and, thus, less likely to express dissatisfaction (Raghunandan 2003). I include industry fixed effects and cluster standard errors at the firm-level.

Test 1 - Descriptive Statistics and Results

I present the summary statistics of the variables in Panel A of Table 2. The average proportion of shareholder votes against auditor ratification is about 1.77 percent. This is in line with the numbers reported in other recent auditor ratification studies (e.g., Barua et al. 2017; Tanyi & Roland 2017; Cassell et al. 2021; Dunn et al. 2021).

In Panel B, I present univariate analyses comparing the mean and median auditor ratification voting for each audit firm before and after the PCAOB censure. The tests show that shareholder votes against auditor ratification is significantly higher following the initial censures of the three Big 4 auditors by the PCAOB (Deloitte in 2007, Ernst in 2012, and PwC in 2017). However, the second and third censures of Deloitte do not elicit a significant shareholder reaction. The results related to the second and third Deloitte censures are consistent with the findings of Boone et al. (2019). Overall, preliminary evidence from the univariate analyses suggests that the initial censure of a Big 4 audit firm elicits higher shareholder dissatisfaction with the auditor.

Table 3 presents the Pearson correlation of the key variables in the model. None of the correlations exceeds 0.65, suggesting that multi-collinearity is unlikely to be a significant problem in my analyses.[6]

Table 4 reports the results from the OLS regression examining the association between PCAOB censure of an audit firm and the auditor ratification voting at clients of that audit firm. In the first column of Table, the independent variable of interest is *CENSURE*, an indicator variable that takes the value 1 for the vote that occurred immediately after the PCAOB censure of the audit firm, and 0 for the vote that occurred prior to the censure. The coefficient on *CENSURE* is positive and significant. After controlling for other factors, a PCAOB censure is associated with about a 4 percent higher shareholder dissatisfaction against the auditor's appointment.

Given the differences between the Big 4 firms, pooling the clients of the three Big 4 firms into a single sample may not be the most appropriate way for the analyses. Hence, in Table 5, I separately examine each of the censured audit firms. Thus, I examine the effect of the PCAOB censure on subsequent shareholder ratification of the auditor's appointment using a within-audit

6 None of the variance inflation factors exceed 4 suggesting that multicollinearity is not a concern.

firm design. In this approach each client and audit firm serve as their own control. In the first two columns, I compare the auditor ratification votes just before the censures of Deloitte to the auditor ratification vote outcomes after the censures. In the first column, I combine all three Deloitte censures and find that, on average, shareholder dissatisfaction with Deloitte increases significantly after the PCAOB censures. In the second column, I separately examine the first, second, and third censures of Deloitte. I find that the PCAOB censure has a significant effect on auditor ratification vote outcomes only in the first censure (effect size = 7.4 percent) but not in the second or third censures of Deloitte.

In the third and fourth columns of Table 5, I examine the effect of the PCAOB censure only on EY and PwC clients, respectively. I find a significantly positive association between these two censures and shareholder dissatisfaction; the effect sizes are 5.8 percent and 6.9 percent for the Ernst and PwC censures, respectively. Overall, the empirical evidence suggests that the initial censures by the PCAOB of the Big 4 audit firms is associated with subsequent increases in the proportion of shareholders not voting to ratify the reappointment of that audit firm. However, repeat censures do not elicit such reactions from shareholders.

Test 2

For Test 2, I augment the sample of clients of the censured Big 4 audit firm with clients of the other Big 4 audit firms that were not subject to the PCAOB censure associated with the particular event. For each censure event, I require observations for both the pre-censure and post-censure periods for the censured firm's clients and for the control firms' clients. The pre- and post-censure periods for the control observations correspond to those of the censured audit firm.

In Test 2, CENSURE equals 1 for observations of clients of the censured Big 4 audit firm in the post-censure period and 0 otherwise. Thus, observations for clients of the censured audit firm in the pre-censure period and observations for clients of the non-censured Big 4 control firms receive a value of 0**.** The coefficient on CENSURE therefore captures the incremental shareholder dissatisfaction associated with the censured auditor following the PCAOB censure relative to the comparison observations. With this approach, my sample size for the five censure events is 8,866. I use the same model as in Table 1.

Table 6 presents the results of the regression for Test 2. The overall regression is significant, and the adjusted R-square is similar to that reported in Table 4 as well as in prior studies. The *CENSURE* variable is positive and significant, indicating that compared to the other Big 4 firm the censured Big 4 firm had a higher proportion of shareholder dissatisfaction. After controlling for other factors, a PCAOB censure is associated with about a 3 percent higher shareholder dissatisfaction against the auditor's appointment. Consistent with expectations, the results show that shareholder dissatisfaction is higher when there is (a) higher non-audit fee ratio, (b) longer audit firm tenure, and (c) a restatement.

Next, as in Test 1, I separately examine each of the five censures. In such analyses, I make one additional change. The EY censure occurred in 2012 and the second Deloitte censure occurred in 2013. Hence, there is overlap—Deloitte clients would be in the control sample when examining the EY censure while EY clients would be in the control sample when examining the second Deloitte censure. Hence, to prevent contamination, I restrict the control sample to include only KPMG and PWC clients for the 2012 EY censure and the 2013 (second) Deloitte censure events. Using similar logic, I include only KPMG and EY clients as controls when examining the PWC censure in 2017 and the third Deloitte censure in 2018.

Table 7 presents the results from separate analyses of the five censure events. The *CENSURE* variable is positive and significant for the first Deloitte censure, as well as the EY and

PWC censure events. However, *CENSURE* is not significant for the second and third Deloitte censure events. These results reinforce the inferences from the univariate analyses, as well as the results from Test 1. In terms of the control variables, consistent with expectations, the coefficients of *NAS* and *LN(TENURE)* are positive and significant in each of the five regressions.

Censures of Second-Tier Firms

The PCAOB censured Grant Thornton in December 2017 and RSM in March 2019. As additional analyses, I examine shareholder reactions to these two censures of second-tier US audit firms. For such analyses, for Test 1, I have data for 103 and 50 clients (i.e., 206 and 100 observations, since I examine pre- and post-censure) of GT and RSM, respectively. In univariate analyses, neither of the two censures elicits a significant reaction from shareholders. I then use the same two types of tests as used to examine shareholder voting at clients of the Big 4.

Table 8 presents the results from the two tests, pooling observations of the clients of the two non-Big 4 firms. The first regression in Table 8 presents the results from the regression where each client acts as its own control, and I use the voting data for each client before and after the censure. The *CENSURE* variable is not significant in the model. In untabulated analyses, I analyze GT and RSM clients separately. In each of these regressions, the *CENSURE* variable is not significant.

The last column of Table 8 presents the results from Test 2. For this test, the control sample includes the clients of non-censured non-Big 4 firms. Thus, my analyses is not restricted to only RSM and Grant Thornton clients for this test—i.e., all other non-Big 4 clients are included in the analyses. In this regression also, the *CENSURE* variable is not significant. In untabulated sensitivity analyses, I restrict the sample to include only RSM and Grant Thornton clients so that only RSM clients constitute the control sample when examining the Grant Thornton censure and vice-versa; my inferences remain unchanged.

Thus, I obtain consistent evidence, using both univariate and multiple regression analyses, that PCAOB censures of non-Big 4 firms does not appear to elicit a significant reaction from shareholders in the context of auditor ratification.[7]

Changes Regression

A changes model that measures variables as first differences is less subject to omitted variable bias and thus allows parsimonious models (Tinkelman and Neely 2011). As a robustness test, I estimate a changes regression that examines the effect of a PCAOB censure on changes in the outcome of auditor ratification votes. The dependent variable, *CHG_VOTE*, is the change in the percentage of shareholder disapproval from before the censure of the audit firm to after the censure. For the non-censured control firms, I use the same time periods as for the censured firm. Thus, I am comparing the change in voting at clients of the censured audit firm versus the change in voting at clients of other audit firms. I perform such analyses separately for the Big 4 and non-Big 4 firms.

Table 9 presents the results from two regressions, one each for the Big 4 and non-Big 4 firms. The control variables are changes in the variables used in the levels model. The results of the first regression show that a PCAOB censure is associated with an increase in the proportion of shareholders not voting to ratify the auditor, for clients of the Big 4 auditors. The second regression shows that a PCAOB censure is not associated with a significant increase in shareholder dissatisfaction when examining the clients of non-Big 4 firms. Overall, these results are consistent

7 The results are consistent with the suggestion that PCAOB censures matter only for Big 4 auditors because of their reputation for higher quality audits.

with those in earlier Tables of this paper.

4. SUMMARY AND DISCUSSION

There have been five instances when the PCAOB has publicly censured US Big 4 audit firms for audit quality failures at the firm level. Two prior studies find that the PCAOB's first-ever censure of a US Big 4 firm resulted in negative consequences for investors, clients, and the audit firm. However, Boone et al. (2019) report that the two subsequent censures of US Big 4 audit firms by the PCAOB are not associated with negative consequences.

In this study, I examine shareholders' reactions to PCAOB censures of US Big 4 audit firms using data from shareholder ratifications of the auditor before and after each such censure. As in Boone et al. (2019, 653), my expectation is that "the censures may be expected to hurt the reputations of the censured firms." I find that the initial instances of the PCAOB's censures (Deloitte in 2007, EY in 2012, and PwC in 2017) elicit negative reactions from shareholders. However, the second and third censures of Deloitte (in 2013 and 2018) are not associated with significant increases in the percent of shareholders not voting to ratify the auditor. Overall, these results provide empirical evidence about the effect of PCAOB censures on shareholders' perceptions of audit quality.

The results are subject to the following caveat. As with prior studies examining shareholder ratification of the auditor, the proportion of votes against ratification are quite small. Nevertheless, many prior studies have documented that small changes in shareholder votes can have significant consequences in monitoring and governance (Del Guercio et al. 2008; Cai et al. 2009; Ertimur et al. 2013: Brochet and Srinivasan 2014). Former SEC Commissioner Grundfest (1993) asserts that because of the reputational concerns of the independent directors, even small changes in shareholder votes can lead to significant policy changes. Similarly, Dao et al. (2012) cite evidence from shareholder activists and auditors and suggest that small changes in shareholder votes against ratification can lead to significant changes in audit firms' behavior.

This paper adds to three distinct research streams and suggests some avenues for future research. First, I add to the emerging literature about the effects of PCAOB censures. While Dee et al. (2011) and Boone et al. (2015, 2019) have focused on the censures of Big 4 firms, my preliminary evidence from two censures of second-tier firms suggests that the results do not necessarily transfer to non-Big 4 settings. Future research can examine if such differences exist with respect to other consequences (such as, audit quality, auditor changes, and fees to auditors) of PCAOB censures of non-Big 4 firms. Second, I add to the emerging literature about the PCAOB's oversight process and the consequences associated with the PCAOB's disciplinary actions (DeFond & Lennox 2017; Krishnan et al. 2017; Aobdia & Shroff 2019). My approach, namely using shareholder voting on auditor ratification, can be a useful method in the context of examining other actions of the PCAOB (such as, requiring disclosures about audit quality, audit participants, etc.). Third, I add to the literature about shareholder ratification of the auditor. One notable feature of research in this area is that almost all published studies have used data from the USA. While shareholder ratification of the auditor is not mandatory in the USA, it is a requirement in some countries. It would be interesting to examine the effects of regulatory actions using auditor ratification data in countries other than the USA, and to examine if there are differences based on whether or not such voting is mandatory.

References

Aobdia, D., and N. Shroff. 2019. Regulatory oversight and auditor market share. *Journal of Accounting and Economics* 63(2–3): 262–87.

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

Barua, A., C. Lennox, and A. Raghunandan. 2020. Are audit fees discounted in initial year audit engagements? *Journal of Accounting and Economics 69*(2-3): p.101282.

Barua, A., K. Raghunandan, and D. V. Rama. 2017. Shareholder Votes on Auditor Ratification and Subsequent Auditor Dismissals. *Accounting Horizons 31*(1): 129-139.

Boone, J., I. Khurana, and K. Raman. 2015. Did the 2007 PCAOB disciplinary order against Deloitte impose actual costs on the firm or improve its audit quality?. *The Accounting Review*, *90*(2): 405–441.

____, _____, and _____. 2019. Audit market response to PCAOB censures of US Big 4 firms. *European Accounting Review 28*(4): 621-658.

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

Brown, J. R. 2012. The politicization of corporate governance: Bureaucratic discretion, the SEC, and shareholder ratification of auditors. *Harvard Business Law Review 2*(1): 60–94.

Cai, J., J. Garner, and R. Walkling. 2009. Electing directors. *Journal of Finance* 64: 2387-2419.

Cassell, C., T. Kleppe, and J. Shipman. 2021. Retail Shareholders and the Efficacy of Proxy Voting: Evidence from Auditor Ratification. Available at: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3113807.

Center for Audit Quality (CAQ). 201). *A guide to PCAOB inspections*. Washington, DC: The CAQ.org.

Dao, M., S. Mishra, and K. Raghunandan. 2008. Auditor tenure and shareholder ratification of the auditor. *Accounting Horizons 22*(3): 297-314.

Dee, C., A. Lulseged, and T. Zhang. 2011. Client stock market reaction to PCAOB sanctions against a Big 4 auditor. *Contemporary Accounting Research*, *28*(1): 263–291.

DeAngelo, L. E. 1981a. Auditor independence, 'low balling', and disclosure regulation. *Journal of Accounting and Economics 3*(2): 113–127.

_____. 1981b. Auditor size and audit quality. *Journal of Accounting and Economics 3* (3): 183–99.

DeFond, M., and C. S. Lennox. 2017. Do PCAOB inspections improve the quality of internal control audits? *Journal of Accounting Research* 55(3): 591–627.

DeFond, M., and J. Zhang. 2014. A review of archival auditing research. *Journal of Accounting*

and Economics 58(2): 275–326.

Del Guercio, D., L. Seery, and T. Woidtke. 2008. Do boards pay attention when institutional investors 'just vote no'? *Journal of Financial Economics* 90: 84-103.

Department of the Treasury (DoT). 2008. *Report of the Advisory Committee on the Auditing Profession to the U.S. Department of the Treasury*. Washington, DC: U.S. DoT.

Dunn, R., N. Lundstrom, and M. Wilkins. 2021. The impact of mandatory auditor tenure disclosures on ratification voting, auditor dismissal, and audit pricing. *Contemporary Accounting Research*, *38*(4): 2871-2917.

Ertimur, Y., F. Ferri, and D. Oesch. 2013. Shareholder votes and proxy advisors: Evidence from say on pay. *Journal of Accounting Research 51*(4): 951-996.

Ferguson, A., J. R. Francis and D. J. Stokes. 2003. The effects of firm-wide and office-level industry expertise on audit pricing. *The Accounting Review 78*(2): 429-448.

Francis, J. R., and E. Wilson. 1988. Auditor changes: A joint test of theories relating to agency costs and auditor differentiation. *The Accounting Review 63*(4): 663–82.

Grundfest, J. A. 1993. Just vote no: a minimalist strategy for dealing with barbarians inside the gates. *Stanford Law Review 45*(4): 857-937.

Gul, F. A., S. Y. K. Fung, and B. Jaggi. 2009. Earnings quality: Some evidence on the role of auditor tenure and auditors' industry expertise. *Journal of Accounting and Economics* 47(3): 265–287.

Gunny, K., and T. Zhang. 2013. PCAOB inspection reports and audit quality. *Journal of Accounting and Public Policy*, *32*(2), 136–160.

Hermanson, D. R., J. Krishnan, and Z. Ye. 2009. Adverse Section 404 opinions and shareholder dissatisfaction toward auditors. *Accounting Horizons* 23 (4): 391-409.

Krishnan, J., J. Krishnan, and H. Song. 2017. PCAOB international inspections and audit quality. *The Accounting Review* 92(5): 143–66.

Lennox, C. and J. Pittman. 2010. Auditing the auditors: Evidence on the recent reforms to the external monitoring of audit firms. *Journal of Accounting and Economics*, *49*(1-2), pp.84-103.

Liu, L., K. Raghunandan, and D. V. Rama. 2009. Financial restatements and shareholder ratifications of the auditor. *AUDITING: A Journal of Practice & Theory* 28 (1): 225-240.

Mayhew, B. W. 2017. Introduction and Commentary on Ratification Research Forum. *Accounting Horizons* 31(1): 125-128.

Menon, K., and D. Williams. 1994. The insurance hypothesis and market prices. *The Accounting Review* 69 (2): 327–42.

Mishra, S., K. Raghunandan, and D. V. Rama. 2005. Do investors' perceptions vary with types of nonaudit fees? Evidence from auditor ratification voting? *Auditing: A Journal of Practice & Theory* 24(2): 9-25.

Public Company Accounting Oversight Board (PCAOB). 2013a. Standing Advisory Group Meeting. Discussion – Audit Quality Indicators. May 15-16.

_____. 2013b. Report from the Working Group on Audit Quality Indicators. October.

_____. 2013c. Audit Quality Indicators update. November 14, 2013.

Raghunandan, K. 2003. Non-audit services and shareholder ratification of auditors. *AUDITING: A Journal of Practice & Theory* 22 (1): 155-163.

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

Sainty, B., G. Taylor, and D. Williams. 2002. Investor dissatisfaction toward auditors. *Journal of Accounting, Auditing, and Finance* 17 (2): 111-136.

Simon, D. T., and J. R. Francis. 1988. The Effects of Auditor Change on Audit Fees: Tests of Price Cutting and Price Recovery. *The Accounting Review* 63(2), 255-269.
Tanyi, P. N., and K. C. Roland. 2017. Market reaction to auditor ratification vote tally. *Accounting Horizons* 31 (1): 141-157.
Watts, R. and J. Zimmerman. 1986. *Positive Accounting Theory*. Prentice-Hall Inc.
Wilson, T., and R. Grimlund. 1990. An examination of the importance of an auditor's reputation. *Auditing: A Journal of Practice and Theory* 9 (2): 43–59.

Ye, Z., D. R. Hermanson, and J. Krishnan. 2013. Shareholder voting in director elections and initial SOX Section 404 reports. *Journal of Accounting, Auditing & Finance* 28 (2): 103-127.

Zimmerman, J. L. 2013. Myth: External Financial Reporting Quality Has a First-Order Effect on Firm Value. *Accounting Horizons* 27(4): 887–894.

Appendix A: PCAOB Censures of Big 4 Audit Firms

Accounting Firm	Date	PCAOB Violation	PCAOB Disciplinary Action
Deloitte & Touche LLP	Dec 10, 2007	Violation of auditing standards in connection with Deloitte's 2003 audit of Ligand Pharmaceuticals Incorporated. Deloitte failed to perform appropriate and adequate audit procedures related to Ligand's reported revenue from sales of products and did not perform procedures that adequately took into account the existence of factors indicating that Ligand's ability to make reasonable estimates of product returns.	Deloitte consented to an order imposing a $1 million civil money penalty. James L. Fazio, the Deloitte partner on the audit was barred from being an associated person of a public accounting firm that is registered with the PCAOB
Ernst & Young LLP	Feb 8, 2012	The Board found that E&Y and its partners failed to properly evaluate a material component of the company's financial statements — its sales returns reserve, in the audits of Medicis's Dec. 31, 2005, 2006 and 2007 financial statements.	EY consented to an order imposing a $2 million civil money penalty and the sanctioning of four of its current and former partners for violating PCAOB rules and standards who are all barred from being an associated person of a public accounting firm that is registered with the PCAOB
Deloitte & Touche LLP	Oct 22, 2013	Violation of the Sarbanes-Oxley Act and PCAOB rules on not permitting a former partner to perform or continue to perform activities as an "associated person" that were prohibited while they are a subject to a PCAOB suspension order.	Deloitte consented to an order imposing a $2 million civil money penalty.

PricewaterhouseCoopers LLP	Aug 2, 2017	PwC issued audit and examination reports without obtaining sufficient evidence about Merrill's compliance assertions, as required by PCAOB auditing and attestation standards. he SEC's Customer Protection Rule requires a broker-dealer to hold certain customer securities in lien-free segregated accounts to protect them from creditor claims should the broker's business fail. Merrill Lynch reported that it had complied with the rule in fiscal year 2014 and that its internal control over compliance with the rule was effective.	PwC consented to an order imposing a $2 million civil money penalty.
Deloitte & Touche LLP	May 23, 2018	Deloitte violated PCAOB rules and standards in connection with its integrated audits of Jack Henry & Associates, Inc. for the fiscal years ended June 30, 2014, 2013, and 2012. Deloitte's failed in auditing Jack Henry's recognition of software license revenue from multiple-element software arrangements.	PCAOB imposed a civil money penalty in the amount of $500,000 on Deloitte.

Appendix B: Variable Definitions

VOTE%	total shareholder "against" and "abstain" votes divided by total shareholder "for", "against", and "abstain" votes;
CENSURE	1 if the client's audit firm is censured by the PCAOB in year t, 0 otherwise;
NAS	fees for non-audit services paid to audit firm scaled by total fees paid to the same audit firm;
RESTATE	1 if the company disclosed a financial statement restatement, 0 otherwise;
ICW	1 if company reports material weakness in internal controls over financial reporting, 0 otherwise;
SPECIALIST	1 if the local audit-office of the client is audit industry leader in the client's industry, 0 otherwise;
TENURE	tenure in years of the auditor with the client;
AT	total assets of the client (in millions of $);
LEVERAGE	the total amount of long-term debt scaled by total assets;
RETURN	12-month holding period return on the firm's stocks beginning from January 1st to December 31st;

Table 1

Panel A: Sample Construction

Clients of PCAOB censured Big 4 auditors with auditor data in Audit Analytics (AA) database in the year before and after the audit firm is censured by PCAOB	11,868
Less: observations with non-December 31 fiscal year-end	4,816
Less: missing auditor ratification vote data in Institutional Shareholder Services (ISS)	2,282
Less: missing financial statement data in Compustat	968
Less: observations in the financial sector (SIC 6000 – 6999)	332
Less: observations that had an auditor change before or after the PCAOB censure	74
Final Sample Size (1,698 unique firms)	**3,396**

Panel B: Sample Distribution by Industry[8]

Industry	Frequency	Percent
Chemicals	56	3.30
Computers	232	13.66
Durable Manufacturers	410	24.15
Extractive	51	3.00
Food	40	2.36
Mining and Construction	60	3.53
Others	66	3.89
Pharmaceuticals	124	7.30
Retail	193	11.37
Services	205	12.07
Textiles & Printing	64	3.77
Transportation	83	4.89
Utilities	114	6.71
Total	1,698	100.00

8 Chemicals (SIC 2800 – 2824, 2840 – 2899); Computers (SIC 3570 – 3579, 3670 – 3679, 7370 – 7379), Durable Manufacturers (3000 – 3569, 3580 – 3669, 3680 – 3999); Extractive (1300 – 1399, 2900 – 2999); Food (2000 – 2111); Mining and Construction (1000 – 1300, 1399 – 1999); Others (0000 – 0999, 9000 – 9999); Pharmaceuticals (2830 – 2836); Retail (5000 – 5999); Services (7000 – 7369; 7380 – 8999); Textiles & Printing (2200 – 2799); Transportation (4000 – 4899); and Utilities (4900 – 4999).

Table 2

Panel A: Summary Statistics

	Obs.	Mean	Median	Lower Quartile	Upper Quartile	Std Dev
VOTE %	3,396	1.717	1.157	0.495	2.112	2.547
CENSURE	3,396	0.500	0.000	0.000	1.000	0.500
NAS	3,396	0.152	0.130	0.0529	0.237	0.133
RESTATE	3,396	0.073	0.000	0.000	0.000	0.265
ICW	3,396	0.032	0 .000	0.000	0.000	0.180
SPECIALIST	3,396	0.392	0.000	0.000	1.000	0.493
TENURE	3,396	14.533	12.000	7.000	21.00	10.273
AT ($ Million)	3,396	8,677.24	1,888.33	565.279	6121.00	25623.25
LEVERAGE	3,396	0.230	0.218	0.051	0.348	0.203
RETURN	3,396	0.199	0.125	-0.073	0.347	0.589

Note: This table provides summary statistics about the variables in the model to examine the association between PCAOB censures and auditor ratification vote outcomes. See Appendix B for variable definitions. All ratio variables are winsorized at the 1st and 99th percentiles.

Panel B: Univariate Analysis

All Observations										
	Before PCAOB Censure			After PCAOB Censure			*Test of Difference in Means*		*Test of Difference in Medians*	
	N	Mean	Median	N	Mean	Median	t Value		Wilcoxon Z	
VOTE%	1,698	1.597%	1.074%	1,698	1.837%	1.261%	2.75	***	4.08	***
First Deloitte Censure (2007)										
	Before PCAOB Censure			After PCAOB Censure			*Test of Difference in Means*		*Test of Difference in Medians*	
	N	Mean	Median	N	Mean	Median	t Value		Wilcoxon Z	
VOTE%	221	1.365%	0.984	221	1.822%	1.165%	1.99	**	1.76	*
E&Y Censure (2012)										
	Before PCAOB Censure			After PCAOB Censure			*Test of Difference in Means*		*Test of Difference in Medians*	
	N	Mean	Median	N	Mean	Median	t Value		Wilcoxon Z	
VOTE%	499	1.781%	1.065%	499	2.014%	1.247%	2.26	**	2.31	**
Second Deloitte Censure (2013)										
	Before PCAOB Censure			After PCAOB Censure			*Test of Difference in Means*		*Test of Difference in Medians*	
	N	Mean	Median	N	Mean	Median	t Value		Wilcoxon Z	
VOTE%	268	1.601%	1.260%	268	1.874%	1.240%	1.48		1.33	
PwC Censure (2017)										
	Before PCAOB Censure			After PCAOB Censure			*Test of Difference*		*Test of Difference*	

							in Means		*in Medians*	
	N	Mean	Median	N	Mean	Median	t Value		Wilcoxon Z	
VOTE%	388	1.464%	1.068%	388	1.691%	1.370%	2.29	**	2.85	***

Third Deloitte Censure (2018)

	Before PCAOB Censure			After PCAOB Censure			*Test of Means*	*Test of Median*
	N	Mean	Median	N	Mean	Median	t Value	Wilcoxon Z
VOTE%	322	1.628%	1.022%	322	1.713%	1.203%	0.44	0.75

Note: In this table I report the results of univariate analyses examining the association between PCAOB censures and shareholder ratification vote outcomes. See Appendix B for variable definition. The t-statistic tests whether the mean VOTE% differs between the pre- and post-censure periods. The Wilcoxon Z statistic tests whether the distributions/median VOTE% differ between the pre- and post-censure periods

Table 3: Pearson Correlation Coefficients, N = 3,396
Prob > |r| under H0: Rho=0

		2)	3)	4)	5)	6)	7)	8)	9)	10)
1)	*VOTE%*	0.054	0.175	0.012	0.007	-0.008	0.124	0.029	-0.054	-0.040
		0.008	<.0001	0.567	0.733	0.689	<.0001	0.149	0.007	0.048
2)	*CENSURE*		-0.001	-0.013	-0.030	-0.030	0.046	0.010	0.023	-0.081
			0.965	0.512	0.141	0.140	0.023	0.616	0.251	<.0001
3)	*NAS*			-0.006	-0.025	0.007	0.085	0.094	0.054	0.005
				0.757	0.220	0.738	<.0001	<.0001	0.007	0.790
4)	*RESTATE*				0.201	0.001	0.049	-0.026	0.089	0.002
					<.0001	0.946	0.015	0.193	<.0001	0.934
5)	*ICW*					-0.003	-0.041	-0.037	0.021	-0.013
						0.870	0.045	0.071	0.305	0.508
6)	*SPECIALIST*						0.039	0.018	0.039	-0.012
							0.052	0.364	0.053	0.545
7)	*TENURE*							0.237	0.036	-0.021
								<.0001	0.075	0.293
8)	*AT*								0.043	-0.023
									0.035	0.249
9)	*LEVERAGE*									0.046
10)	*RETURN*									

Table 4
PCAOB Censure and Auditor Ratification Vote Outcome

	Exp. Sign	Coeff. (t stat)	
CENSURE	+	0.040	**
		(2.23)	
NAS	+	0.803	***
		(10.41)	
RESTATE	+	0.003	
		(0.10)	
ICW	+	0.072	
		(1.23)	
SPECIALIST	-	-0.004	**
		(2.03)	
LN(TENURE)	+	0.199	***
		(14.70)	
LN(AT)	?	0.003	
		(0.55)	
LEVERAGE	?	-0.172	***
		(3.17)	
RETURN	?	-0.003	
		(0.16)	
CONSTANT	?	-0.076	
		(0.55)	
Industry Fixed Effects		Yes	
Adj. R-Square		0.188	
F-Value		92.38	***
Obs		3,396	

Note: This table presents results from the OLS regression to examine the association between PCAOB censure of a Big 4 audit firm and auditor ratification vote outcomes All other variables are defined in Appendix B. Associated p-values are reported using ***, **, and *, representing significance at the 1%, 5%, and 10% levels, respectively. The model is estimated with industry fixed effects and clustered standard errors.

Table 5
PCAOB Censure and Auditor Ratification Vote Outcome

***LN* (1 + *VOTE*%)**

		DT Clients				EY Clients		PwC Clients	
	Exp. Sign	Coeff. (t Value)		Coeff. (t Value)		Coeff. (t Value)		Coeff. (t Value)	
CENSURE	+	0.041	**			0.056	**	0.067	**
		(2.58)				(2.51)		(2.14)	
DT_CENSURE (2007)	+			0.071	**				
				(2.00)					
DT_CENSURE (2013)	+			0.034					
				(0.80)					
DT_CENSURE (2018)				0.020					
				(0.63)					
NAS		0.934	***	0.932	***	0.625	***	1.144	***
		(7.31)		(7.31)		(4.65)		(6.72)	
RESTATE		0.052		0.052		0.092		0.039	
		(0.79)		(0.79)		(1.17)		(0.79)	
ICW		0.024		0.023		0.042		0.012	
		(0.34)		(0.32)		(0.44)		(0.11)	
SPECIALIST		-0.025		-0.023		-0.030		-0.008	
		(0.80)		(0.76)		(0.84)		(0.23)	
LN(TENURE)		0.273	***	0.277	***	0.343	***	0.330	***
		(9.71)		(9.39)		(8.37)		(11.84)	
LN(AT)		0.004		0.003		-0.011		0.012	

	(0.04)	(0.03)	(0.96)		(0.90)
LEVERAGE	-1.298	-1.126	-0.242	***	-0.069

	(1.47)		(1.42)		(2.79)		(1.04)	
RETURN	-1.210	***	-1.114	***	-0.021		-0.009	
	(3.93)		(3.52)		(0.67)		(0.37)	
CONSTANT	-0.208		-0.212		0.199		0.175	
	(1.45)		(1.48)		(1.47)		(1.18)	
Industry Fixed Effects	Yes		Yes		Yes		Yes	
Adj. R-Square	0.243		0.242		0.176		0.373	
F-Value	44.00	***	77.60	***	78.74	***	49.54	***
Obs	1,622		1,622		998		776	

Note: This table presents results from an OLS regression to examine the association between PCAOB censure of a Big 4 audit firm and auditor ratification vote outcome. *DT_CENSURE* (2007) is 1 for Deloitte clients if vote is after PCAOB censure of Deloitte in 2007, and 0 otherwise; *DT CENSURE* (2013) is 1 for Deloitte clients if vote is after PCAOB censure of Deloitte in 2013, and 0 otherwise; *DT CENSURE* (2018) is 1 for Deloitte clients if vote is after PCAOB censure of Deloitte in 2018, and 0 otherwise. All other variables are defined in Appendix B. Associated p-values are reported using ***, **, and *, representing significance at the 1%, 5%, and 10% levels, respectively. The model is estimated with industry fixed effects and clustered standard errors.

Table 6
PCAOB Censure and Auditor Ratification – Censured Big 4 vs. Non-Censured Big 4

LN (1 + *VOTE*%)

	Exp. Sign	Coeff. (t stat)	
CENSURE	+	0.025	***
		(3.84)	
NAS	+	0.770	***
		(16.31)	
RESTATE	+	0.039	*
		(1.81)	
ICW	+	0.018	
		(0.63)	
SPECIALIST	-	-0.001	
		(0.07)	
LN(TENURE)	+	0.254	***
		(26.80)	
LN(AT)	?	0.006	
		(1.63)	
LEVERAGE	?	-0.064	**
		(2.52)	
RETURN	?	0.007	
		(0.63)	
CONSTANT	?	0.936	***
		(4.23)	
Industry Fixed Effects		Yes	
Adj. R-Square		0.167	
F-Value		333.73	***
Obs		8,866	

Note: This table presents results from the OLS regression examining auditor ratification voting for clients of censured Big 4 audit firms relative to clients of non-censured Big 4 audit firms. For each censure event, the control sample consists of clients of the other Big 4 firms during the corresponding pre- and post-censure periods. CENSURE equals 1 for clients of the censured Big 4 audit firm in the post-censure period and 0 otherwise. All other variables are defined in Appendix B. Associated p-values are reported using ***, **, and *, representing significance at the 1%, 5%, and 10% levels, respectively. The model is estimated with industry fixed effects and firm-clustered standard errors.

Table 7
PCAOB Censure and Auditor Ratification Vote Outcome

***LN* (1 + *VOTE*%)**

		DT (2007)		DT (2013)		DT (2018)		EY Clients		PwC Clients	
	Exp. Sign	Coeff. (t Value)		Coeff. (t Value)		Coeff. (t Value)		Coeff. (t Value)		Coeff. (t Value)	
CENSURE	+	0.021	***	0.013		0.040		0.074	**	0.043	**
		(2.62)		(0.43)		(1.12)		(2.55)		(2.36)	
NAS		0.694	***	1.053	***	0.862	***	0.605	***	0.959	***
		(5.49)		(10.36)		(7.00)		(5.79)		(7.81)	
RESTATE		0.068		0.025		0.028		0.042		0.021	
		(1.18)		(0.63)		(0.31)		(0.92)		(0.29)	
ICW		0.121		0.043		0.003		0.072		0.008	
		(1.64)		(0.71)		(0.04)		(1.06)		(0.12)	
SPECIALIST		-0.006		-0.037		-0.002		-0.018		-0.004	
		(0.21)		(1.49)		(0.08)		(0.66)		(0.13)	
LN(TENURE)		0.169	***	0.158	***	0.270	***	0.274	***	0.319	***
		(5.88)		(8.34)		(11.80)		(10.65)		(13.00)	
LN(AT)		0.071	***	-0.055	***	-0.011		0.001		0.001	
		(7.64)		(6.75)		(0.91)		(0.17)		(0.04)	
LEVERAGE		-1.744	***	0.043		-0.010		-1.703	***	-0.058	
		(3.14)		(0.08)		(0.14)		(3.01)		(0.91)	
RETURN		-0.024		-0.045	*	-0.014		-0.016		-0.029	
		(0.57)		(1.78)		(0.74)		(0.76)		(1.08)	
CONSTANT		1.326	***	1.508	***	-0.108		1.393	***	0.295	***
		(14.02)		(21.88)		(1.11)		(16.32)		(3.32)	
Industry Fixed Effects		Yes		Yes		Yes		Yes		Yes	

Adj. R-Square	0.28	0.23	0.322	0.24	0.254

F-Value	37.95	***	29.34	***	60.60	***	6.12	***	26.44	***
Obs	1,468		2,158		1,360		1,726		1,372	

Note: This table presents results from an OLS regression to examine the association between PCAOB censure of a Big 4 audit firm and auditor ratification vote outcome. *DT_CENSURE* (2007) is 1 for Deloitte clients if vote is after PCAOB censure of Deloitte in 2007, and 0 otherwise; *DT CENSURE* (2013) is 1 for Deloitte clients if vote is after PCAOB censure of Deloitte in 2013, and 0 otherwise; *DT CENSURE* (2018) is 1 for Deloitte clients if vote is after PCAOB censure of Deloitte in 2018, and 0 otherwise. All other variables are defined in Appendix B. Associated p-values are reported using ***, **, and *, representing significance at the 1%, 5%, and 10% levels, respectively. The model is estimated with industry fixed effects and clustered standard errors.

Table 8
PCAOB Censure and Auditor Ratification Vote Outcome – Non Big 4 Firms

***LN* (1 + *VOTE*%)**

	Exp. Sign	TEST 1 Coeff. (t stat)		TEST 2 Coeff. (t stat)	
CENSURE	+	0.104		0.001	
		(1.55)		(0.02)	
NAS	+	0.175	**	0.398	***
		(2.44)		(3.74)	
RESTATE	+	0.157		0.086	
		(0.96)		(1.60)	
ICW	+	0.162	*	0.095	*
		(2.01)		(1.72)	
SPECIALIST	-	-0.271	*	-0.001	
		(1.90)		(0.01)	
LN(TENURE)	+	0.042		0.039	**
		(0.76)		(2.32)	
LN(AT)	?	-0.127	**	-0.080	***
		(4.49)		(10.18)	
LEVERAGE	?	-0.108		-0.023	***
		(1.02)		(2.95)	
RETURN	?	-0.016		-0.015	
		(038)		(1.76)	
CONSTANT	?	0.936	***	0.001	
		(4.93)		(0.02)	
Industry Fixed Effects		Yes		Yes	
Adj. R-Square		0.167		0.093	
F-Value		333.73	***	8.60	***
Obs		306		1,567	

Note: This table presents results from the OLS regression to examine the association between PCAOB censure of a non-Big 4 audit firm and auditor ratification vote outcomes. All other variables are defined in Appendix B. Associated p-values are reported using ***, **, and *, representing significance at the 1%, 5%, and 10% levels, respectively. The model is estimated with industry fixed effects and clustered standard errors.

Table 9 – Changes Analyses

	Exp. Sign	*LN* (1 + *VOTE%*)			
		Big 4 Firms		Non-Big 4 Firms	
		Coeff. (t Value)		Coeff. (t Value)	
CENSURE	+	0.058	***	0.009	
		(3.46)		(1.44)	
CHG_NAS	+	0.119	**	0.364	***
		(2.24)		(2.80)	
CHG_RESTATE	+	0.011	**	0.207	**
		(2.46)		(2.54)	
CHG_ICW	+	0.037		0.116	
		(0.87)		(1.23)	
CHG LN(AT)	?	-0.057		-0.207	**
		(1.26)		(2.23)	
CHG_LEVERAGE	?	-0.173	*	-0.097	
		(1.65)		(0.26)	
CHG_RETURN	-	-0.005		-0.029	
		(0.35)		(0.89)	
CONSTANT	?	-0.084		-0.129	
		(0.55)		(0.70)	
Industry Fixed Effects		Yes		Yes	
Adj. R-Square		0.022		0.018	
F-Value		2.27	***	3.10	***
Obs		8,866		1,567	

Note: All other variables are defined in Appendix B. Associated p-values are reported using ***, **, and
*, representing significance at the 1%, 5%, and 10% levels, respectively. The model is estimated with industry fixed effects and clustered standard errors.