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The 'Dark Side' of Managers With Audit Background – by Tatyana Shumsky

Handing large paychecks to corporate executives with audit-firm experience could raise the risk of financial misstatements, according to new research.

Companies that gave top managers above-average compensation and whose executives had an audit-firm background were about 30% more likely than those with lower-paid counterparts to misstate financial results, according to a study in the November issue of The Accounting Review. The study examined more than 3,000 public companies over a 10-year period.

The combination of audit-firm experience and excess pay brought out this "dark side" of accounting competence and raised the risk of misstatements, **said Anne Albrecht, an assistant professor of accounting at the Neeley School of Business at Texas Christian University, who is one of the study's authors.**

"Accounting competence is good because they're able to generate more reliable financial statements," she said. "But it's bad because the knowledge of accounting procedures allows them to make the misstatements in the first place, and their knowledge of the auditing process allows them to hide it."

Moreover, executives with an audit background were more likely to engender trust from the company's current auditors, resulting in a higher rate of clean audit opinions, the study found.

"That shared background generates trust so that auditors aren't necessarily as skeptical of management as perhaps they should be," Ms. Albrecht said.

Researchers looked at corporate officers, such as finance chiefs or chief executives, to determine accounting competence. If the executive had prior experience as an audit partner or manager at a public accounting firm, they were considered competent.

The authors then compared pay among executive teams to establish an average compensation, adjusted for factors such as accounting competence, executive tenure at the company, and company performance within its industry. If the actual compensation was above the predicted amount, the management team was deemed to have received "excess compensation."

In any given year, about 12% of the companies had one or more top executive with prior audit experience as partner or manager at an accounting firm. Of those executives, roughly 60% were CFOs and 9% were CEOs.

Overall, the financial restatement rate was about 10% for all the companies analyzed during the 10-year period. For firms that had executives with an audit-firm background, the restatement rate was 9.5%.

However, companies that had executives with both an audit-firm background and high excess compensation, the restatement rate was 11% during the 10 year period, compared to 8% for firms that had managers with accounting competency and low excess compensation.

For board members and audit committees, the study shines a spotlight on a potential risk, said Howard Brownstein, president of the Philadelphia chapter of the National Association of Corporate Directors and a NACD board leadership fellow.

“If there’s a risk that you have very competent people who know how to game the system, you need very strong systems and controls,” Mr. Brownstein said. “It’s not about accusing them of being dishonest, it’s about keeping them from being tempted.”

November 20, 2018
Charging your holiday shopping may prove riskier than rewarding – by Lauren Jakalik

A recent report from Nerd Wallet showed about 39.4 million Americans who charged their holiday shopping last year are still paying it off.

For Karen Wallace, opening bills these days is no biggie, but it used to bring her big-time anxiety.

“Looking at my Target bill one day, I looked at how long it would take me to pay it off if I just made minimum payments—and it was in my 50s,” Wallace said.

She is one of the millions of Americans who’ve opened credit cards or store cards, attracted by the promise of rewards or discounts. She was in her 20s when it happened, before marriage and motherhood.

After charging $11,000, Wallace realized her debt outweighed any benefit she might’ve received. “I would pay one and not the other because I couldn’t afford it,” she said. “It was just terrifying.”

Thomas Moeller is an associate professor of finance at Texas Christian University. “Generally those store cards come with very high interest rates,” he told WFAA. “So you might save 5 percent on

your purchase, but then if you have a 25 percent interest rate, if you keep a balance a little over two months, you're losing the 5 percent."

Moeller says stores are counting on people this holiday season to open cards and not pay their bills in full, or to keep spending. A recent report from Nerd Wallet showed about 39.4 million Americans who charged their holiday shopping last year are still paying it off. "I think it's a real problem," Moeller said.

He says debit cards or cash is key. If you don't have the discipline or money to pay your charge cards, don't use them. According to Wallet Hub, one in six people plan to apply for a new credit card just for holiday shopping.

Times have changed for Fort Worth teacher Karen Wallace. "Black Friday, if I don't have the cash, we just don't do it," she said. She ended up having to take out a loan and paid off her credit card debt in five years. She said she plans to keep it that way.