“Paying for integrity: How cash-heavy audit committee compensation enhances earnings quality”

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PAYING FOR INTEGRITY: HOW CASH-HEAVY AUDIT COMMITTEE COMPENSATION ENHANCES EARNINGS QUALITY

Abstract

This study examines whether paying audit committee members a higher proportion of cash, rather than equity, improves the quality of financial oversight. Using 7,159 firm-year observations from publicly listed non-financial U.S. companies between 2005 and 2023, this paper focuses on firms with standardized financial disclosures and comparable audit committee structures. The sample begins in 2005 to reflect the regulatory environment following the implementation of Section 404 of the Sarbanes-Oxley Act, which requires companies to assess and disclose the effectiveness of internal controls. The results show that a higher proportion of cash compensation is significantly associated with lower discretionary accruals, indicating stronger earnings quality. This relationship holds across alternative model specifications and accrual quality measures. The findings suggest that cash-based pay may enhance audit committee independence by reducing incentives tied to stock performance. For companies and regulators, the study underscores the importance of compensation design – favoring cash over equity may help strengthen financial reporting oversight and reduce earnings management, particularly in complex or high-risk firms.

Keywords auditing, executive compensation, earnings quality, financial reporting, corporate governance

JEL Classification M41, M21, G30, M42

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INTRODUCTION

The integrity of financial reporting is a foundational concern in corporate governance. Audit committees are designed to serve as independent monitors, mitigating earnings management and ensuring the accuracy of financial disclosures. However, their ability to perform this function effectively is shaped not only by regulatory requirements but also by internal incentive structures, particularly how directors are compensated.

While corporate governance literature has extensively discussed the risks and benefits of equity-based compensation, less attention has been given to the role of fixed cash compensation in shaping the behavior of audit committee members. This omission is consequential. Unlike executives whose compensation is typically linked to firm performance, audit committee members are tasked with independent oversight, and the structure of their remuneration may either support or undermine this independence.

This study investigates the agency conflicts in audit committee compensation design, particularly focusing on the role of cash-based compensation in enhancing oversight independence. This paper addresses this gap by exploring the implications of audit committee compensation structures for financial reporting integrity.

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1. LITERATURE REVIEW

The structure of audit committee compensation has significant implications for corporate governance and financial oversight. While regulatory frameworks establish independence requirements, financial incentives can shape directors' monitoring behavior, influencing their diligence in overseeing financial reporting. Compensation mechanisms, particularly the balance between equity-based and cash-based incentives, have been widely debated in governance research. Some scholars argue that stock-based pay aligns directors' interests with shareholders, while others caution that it may compromise the audit committee's objectivity. Alternatively, cash-based compensation may reinforce independence by eliminating conflicts of interest tied to stock performance, but excessive fixed payments could introduce risks of passivity. Understanding how these incentive structures impact audit committee effectiveness is crucial for evaluating their role in mitigating earnings management and ensuring financial transparency.

Audit committees play a critical role in ensuring financial reporting integrity, regulatory compliance, and internal control effectiveness (Klein, 2002; Krishnan, 2005). As independent subcommittees of the board, audit committees are tasked with overseeing financial disclosures, internal controls, and external audits, thereby serving as key gatekeepers against opportunistic earnings management. Regulators have emphasized the importance of audit committee independence to strengthen investor confidence in financial reporting.

Under SEC Rule 10A-3, audit committee members must be independent directors, meaning they cannot be employed by the company or hold significant ownership stakes that could impair their objectivity (Deloitte, 2024). Additionally, NYSE and Nasdaq listing standards require audit committee members to have financial literacy, ensuring they possess the expertise necessary to assess financial reports and evaluate risk exposure. While these regulatory safeguards establish baseline independence requirements, they do not address the potential influence of compensation structures on audit committee oversight behavior. Research suggests that beyond independence rules, the incentive mechanisms embedded in audit committee compensation plans may significantly impact their effectiveness in monitoring financial reporting quality.

Equity-based compensation is commonly used to align directors' incentives with shareholder value. Stock-based pay, including restricted stock grants and stock options, is designed to encourage long-term governance engagement by tying directors' wealth to firm performance (Beasley, 1996). However, this argument is more applicable to executive compensation than to audit committee incentives, given their fundamentally different responsibilities. Audit committee members are not responsible for driving firm performance, but rather for ensuring the accuracy and reliability of financial reporting. If their compensation is tied to stock price fluctuations, their incentives may shift from enforcing financial transparency to supporting earnings management strategies that boost short-term stock performance. This potential misalignment raises concerns about whether equity-based pay compromises audit committee independence and reduces its ability to constrain opportunistic financial reporting.

Empirical studies provide evidence that equity-based compensation is associated with weaker financial oversight. Archambeault et al. (2008) find that audit committees with higher equity-based pay are more likely to oversee firms that issue financial restatements, suggesting a reduced capacity to prevent misreporting. Similarly, Campbell et al. (2015) document that firms where audit committee members receive stock-based compensation exhibit a higher likelihood of meeting or narrowly exceeding analyst earnings forecasts, a behavior typically linked to earnings management. Brick et al. (2006) further highlight that stock-based incentives may weaken board oversight, leading to CEO overcompensation and governance failures.

Unlike stock-based incentives, cash compensation provides a fixed, predictable financial reward, ensuring that audit committee members are not financially influenced by stock price movements. This structure can enhance independence by eliminating incentives to prioritize stock performance over transparent reporting. Several studies argue that cash-based pay strengthens gover-

nance by reinforcing audit committee vigilance. Ye (2014) suggests that higher cash compensation attracts more experienced and financially independent directors, who are better equipped to exercise strong oversight. Murphy (2013) further posits that cash retainers provide stable incentives that encourage long-term monitoring commitments rather than short-term stock performance considerations.

While cash-based incentives offer several governance advantages, some researchers caution that excessively high cash compensation could introduce new agency risks. Vafeas (2000) argues that directors who receive large cash retainers may feel obligated to management, potentially reducing their willingness to challenge aggressive financial reporting practices. This concern aligns with reciprocity theory, which suggests that individuals who receive generous compensation may develop a psychological inclination to reciprocate the favor by adopting a more lenient stance on oversight matters (Brick et al., 2006). From this perspective, if cash retainers become too large, audit committee members may shift from being independent monitors to passive overseers. Instead of reinforcing governance effectiveness, excessive fixed compensation could lead to reduced director engagement, lower scrutiny of financial disclosures, and increased tolerance for earnings management. Thus, while moderate cash compensation may strengthen independence, excessive payments could potentially undermine it, presenting a governance trade-off.

In summary, the existing literature highlights that compensation structures significantly impact audit committee independence and oversight effectiveness. However, there remains limited empirical evidence on whether cash-based compensation enhances earnings quality in practice. The structure of audit committee compensation influences oversight quality, raising critical questions about how cash-heavy remuneration aligns with earnings quality and financial transparency.

The purpose of this study is to evaluate whether a cash-heavy audit committee compensation structure supports financial reporting transparency by mitigating earnings management.

2. RESEARCH METHOD

The following Model (1) is to examine the relation between the audit committee's cash compensation ratio and earnings quality:

$$\begin{aligned} AbsDA_{i,t} &= \beta_0 + \beta_1 CCAC\%_{i,t} + \beta_2 SIZE_{i,t} \\ &+ \beta_3 ROA_{i,t} + \beta_4 BTM_{i,t} + \beta_5 LEV_{i,t} \\ &+ \beta_6 IN\_CAPITAL_{i,t} + \beta_7 OCF_{i,t} + \beta_8 Big4_{i,t} \\ &+ \beta_9 LOSS_{i,t} + \beta_{10} LIT_{i,t} + Industry_{FE} \\ &+ YEAR_{FE} + \varepsilon_{i,t}, \end{aligned} \quad (1)$$

For the dependent variable, this paper measures earnings quality using the absolute value of discretionary accruals obtained from the residuals of the Jones model following Kothari et al. (2005). The Jones (1991) model is estimated cross-sectionally by each industry-year group. Given that earnings manipulation encompasses both extremely positive and negative values of discretionary accruals (Klein, 2002), this paper employs the absolute value of discretionary accruals as the proxy for earnings management. The test variable CCAC% measures the cash compensation ratio of audit committee members. This is calculated as the total cash compensation received by all audit committee members divided by the total compensation of all audit committee members of the firm in a certain year.

Following the prior literature, this study controls for firm size, as prior studies suggest that larger firms are expected to have better accounting quality (Dechow et al., 2010; Dechow & Dichev, 2002). In addition, this paper controls firm performance (*ROA*), profitability (*LOSS*), leverage (*LEV*), book-to-market ratio (*BTM*) and capital intensity (*IN_CAPITAL*) as prior research finds that firms with poor performance, negative earnings, high leverage, better growth opportunities are more likely to have greater incentives in earnings management (Becker et al., 1998; Dechow & Dichev, 2002). This paper also controls litigation risks (*LIT*). Prior studies suggest that companies with high litigation risk are less likely to manage earnings to avoid negative earnings surprises (Matsumoto, 2002). Whether the firm utilizes a Big 4 audit (*BIG4*) is also controlled in the model, as external auditors play a significant role in overseeing prop-

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er financial reporting (Becker et al., 1998; Chen et al., 2007). In addition to the above variables, this paper also controls for year and industry fixed effects to adjust for potential macroeconomic and industry-specific factors on earnings quality in all regression models.

3. SAMPLE AND DATA

The dataset used in this study was compiled from BoardEx and Compustat.[1]

3.1. Sample selection

Prior research suggests that financial reporting quality has improved following the enactment of the Sarbanes-Oxley Act (SOX) (Rice & Weber, 2012). One of the key provisions, SOX Section 404, mandates that both management and external auditors assess and publicly disclose the effectiveness of a company's internal controls in each annual report. Given that SOX 404 became effective on November 15, 2004, this study begins the sample period in 2005 to account for its potential impact on financial reporting practices.

The initial dataset consists of 1,569,501 board role observations obtained from BoardEx for the period 2005–2023. This study then merges this dataset with compensation data from BoardEx and excludes observations with missing salary information, reducing the sample to 254,959 observations. Next, this paper filters for audit-related committees by retaining only those observations where the committee's name contains the term "audit", resulting in 13,314 unique firm-year observations.

To integrate financial data, this paper merges the dataset with Compustat North America and excludes firms in the financial services industry, as their financial reporting characteristics differ significantly from other industries. This step reduces the sample to 7,810 firm-year observations. Finally, this paper excludes observations with missing values for control variables, yielding a final sample of 7,159 firm-year observations. Overall, this selection process ensures that the sample is comprehensive and reflective of firms with relevant audit committee structures and financial reporting characteristics while maintaining consistency with prior research.

3.2. Descriptive statistics

Table 1 presents the summary statistics of the variables used in the analysis. Panel A reports the descriptive statistics for all variables included in the main models. The mean audit committee cash compensation ratio is 0.40, closely aligning with the 0.4133 mean reported in Liu et al. (2021), indicating consistency with prior research. Additionally, the sample of this study shows that over 98% of firms are audited by one of the Big Four accounting firms, reflecting a strong external governance framework. Furthermore, 13.17% of firm-year observations report a loss, while 26.69% operate in industries characterized by high litigation risk, underscoring variations in financial performance and regulatory exposure across firms.

Panel B of Table 1 details the distribution of audit committee cash compensation ratios across industries, categorized by two-digit SIC codes. The Agriculture, Forestry, and Fishing industry exhibits the highest average cash compensation ratio of 44.1%, suggesting a greater reliance on cash-based incentives to attract and retain independent audit committee members. In contrast, the Retail Trade industry has the lowest average cash compensation ratio at 31.7%, highlighting potential industry-specific differences in compensation structures.

Panel C of Table 1 presents the distribution of cash compensation ratios over time (2005–2023). The trend indicates a gradual decline in cash compensation ratios over this period, with the highest average observed in 2008 (46.5%) and the lowest levels recorded in 2020 and 2021 (35.9%). This pattern aligns with findings from Farrell et al. (2008), which document an increasing shift toward equity-based compensation in corporate governance roles over the past decade, reflecting evolving compensation strategies and market conditions.

Additionally, an unreported correlation matrix provides pairwise correlation coefficients among

1 In response to the principle of open data, the data for the analysis have been deposited in an open-access repository and are available at Zenodo: https://doi.org/10.5281/zenodo.15369177.

Table 1. Summary statistics

Panel A: Descriptive statistics							
	N	Mean	SD	p25	Median	p75	p90
Abs DA	7159	0.415	1.303	0.023	0.072	0.252	0.748
CCAC%	7159	0.4	0.225	0.255	0.382	0.492	0.669
SIZE	7159	9.327	1.548	8.571	9.424	10.239	11.081
ROA	7159	0.136	0.140	0.092	0.135	0.187	0.251
LEV	7159	0.263	0.220	0.141	0.246	0.347	0.458
BTM	7159	0.372	0.569	0.189	0.333	0.535	0.763
IN_CAPITAL	7159	0.31	0.243	0.11	0.22	0.485	0.707
OCF	7159	0.105	0.113	0.068	0.103	0.15	0.203
BIG4	7159	0.982	0.132	1	1	1	1
LOSS	7159	0.132	0.338	0	0	0	1
LIT	7159	0.267	0.442	0	0	1	1

Panel B: Distribution of the mean of Cash compensation ratio by industry (2-digit SIC code)			
	Cash (000)	Total rem (000)	Cash ratio
Agriculture, Forestry, and Fishing	525.55	1297.7	0.441
Mining	501.872	1698.418	0.402
Construction	411.249	1431.323	0.389
Manufacturing	419.144	1545.058	0.396
Transportation	538.987	1702.578	0.433
Wholesale Trade	371.549	1305.221	0.383
Retail Trade	506.333	1610.167	0.317

Panel C: Distribution of Cash compensation ratio by year			
	Cash(000)	Total rem(000)	Cash ratio
2005	223.964	1025.978	0.393
2006	308.472	1519.802	0.434
2007	347.979	1177.104	0.448
2008	375.353	1074.157	0.465
2009	425.847	1814.018	0.393
2010	415.607	1274.037	0.398
2011	461.081	1690.014	0.418
2012	450.926	1298.186	0.397
2013	476.322	1517.558	0.374
2014	497.058	1430.233	0.393
2015	579.374	1869.573	0.407
2016	490.41	1433.413	0.381
2017	504.515	1523.265	0.373
2018	496.227	1446.642	0.414
2019	524.828	1533.656	0.382
2020	546.168	2299.147	0.359
2021	517.994	1682.311	0.359
2022	542.969	2049.838	0.380
2023	563.524	2612.189	0.375

Note: This table presents the descriptive statistics for the test sample. Panel A presents the descriptive statistics of all variables used in the main models. Panel B presents the distribution of the audit committee cash compensation ratio across different industries. Industries are defined based on a 2-digit SIC code. Panel C presents the distribution of cash compensation ratios by years. All variables are defined in Appendix B. *Abs DA* and *BTM* are winsorized at the 1% level at both tails of the distribution due to significant outliers.

key variables. The correlation between the test variable (CCAC%) and the dependent variable (Abs DA) is 0.003, which is statistically significant, indicating a direct association between audit committee cash compensation and earnings quality at the univariate level. Moreover, most independent variables exhibit significant correlations with the dependent variable, except for LOSS. The variance inflation factor (VIF) is 3.49, suggesting that multicollinearity is not a concern in regression models.

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4. RESULTS

Table 2 presents the baseline results of Model (1). The first column reports the univariate regression of the absolute value of discretionary accruals (DA) on the audit committee cash compensation percentage (CCAC%). Across all model specifications, the coefficient for CCAC% remains significantly positive, indicating a consistent and robust association between higher cash-based compensation for audit committees and improved earnings quality.

The results in Table 2 provide strong empirical findings that audit committee cash compensation reduces earnings management. The statistical significance of CCAC% suggests that cash-based remuneration enhances financial oversight by mitigating opportunistic managerial behaviors, thereby strengthening financial reporting integrity. These findings align with prior research (Alkebsee et al., 2022; Ye, 2014), which emphasizes the governance benefits of cash incentives in fostering independent and objective monitoring.

Furthermore, the analysis demonstrates that this relationship persists even after controlling for firm-specific characteristics, industry effects, and other governance-related variables. The explanatory power of the audit committee cash compensation ratio in predicting earnings management underscores the importance of compensation structures in shaping director incentives. Given the consistency and magnitude of these results, this study proved that audit committee cash compensation has no impact on financial reporting quality.

Table 2. Relationship between earnings management and AC cash-based compensation ratio (N = 7,159)

Variables	Dependent variable = Abs DA(Jones)		
	Univariate Model	With Control Model	With Control and FE Model
CCAC%	0.0195***	0.0627***	0.0373**
	(3.0757)	(2.9798)	(2.3718)
SIZE		0.0284***	0.0303**
		(3.0096)	(2.1121)
ROA		–0.233	–0.108
		(–0.329)	(–0.305)
LEV		–0.0916*	–0.0930
		(–1.7521)	(–0.0629)
BTM		0.0113	0.0155
		(0.0234)	(0.0228)
IN_CAPITAL		0.161**	0.413**
		(1.9681)	(2.183)
OCF		0.0106	0.216
		(0.386)	(0.356)
BIG4		–0.281	–0.0330
		(–0.171)	(–0.164)
LOSS		0.240***	0.102*
		(2.6718)	(1.7567)
LIT		–0.0694**	–0.218***
		(–2.0322)	(–2.0709)
Constant	0.408***	0.378**	0.0753**
	(3.0334)	(2.179)	(2.206)
Year FE	No	No	Yes
Industry FE	No	No	Yes
R-squared	0.075	0.182	0.314

Note: This table presents OLS estimates of the baseline regressions on the impact of the audit committee cash ratio on earnings quality. Column (1) reports the univariate regression. Column (2) reports the estimates after adding control variables. Column (3) reports the estimates with control variables and industry, and year fixed effects. *, **, and *** denote significance at the 10 percent, 5 percent, and 1 percent levels, respectively. Coefficient estimates are presented above the p-value. All variables are defined in Appendix B. Abs DA and BTM are winsorized at the 1% level at both tails of the distribution due to significant outliers.

To ensure the reliability of the findings, this study conducted robustness tests using an alternative measure of earnings management. Following Call et al. (2017), this study employed the standard deviation of residuals from years t-4 to t, obtained from cross-sectional estimations of the modified Dechow-Dichev (McNichols, 2002) model (Modified DD), as a proxy for earnings quality. This approach validates whether the primary results hold under different earnings quality specifications.

The unreported results confirm the robustness of the main findings. Specifically, the coefficient of the test variable, CCAC%, remains significantly positive when employing the Modified DD approach, reinforcing the conclusion that a higher proportion of cash compensation in audit committee remuneration is associated with improved financial reporting quality. This consistency across different model specifications suggests that the findings are not driven by the choice of earnings quality measure but rather reflect a robust underlying relationship.

Additionally, the persistence of significant results under an alternative model aligns with prior research that underscores the reliability of the Modified DD model in capturing accrual quality variations (Dechow et al., 2010). These findings strengthen the argument that cash-based incentives enhance audit committee oversight by reducing opportunistic earnings management and promoting financial transparency.

5. DISCUSSION

This study provides empirical evidence that a higher proportion of cash compensation in audit committee pay is associated with improved earnings quality. The findings are consistent across alternative model specifications and robust to different measures of accrual quality. This suggests that cash-heavy compensation structures can play a positive role in enhancing audit committee oversight by reducing incentives linked to stock price fluctuations.

Compared to prior studies highlighting the risks of equity-based incentives (Archambeault et al., 2008; Campbell et al., 2015; Brick et al., 2006), this study suggests that shifting toward cash-based compensation may mitigate these conflicts and reinforce audit committee independence. In contrast to the findings of Vafeas (2000) and Brick et al. (2006), who caution that excessive cash pay may impair director vigilance, this study finds no evidence of such negative effects within the observed range of compensation ratios. Instead, the positive association supports the view proposed by Ye (2014) and Alkebsee et al. (2022), who argue that fixed compensation can attract more experienced and independent directors.

These results offer new insights by isolating the governance impact of cash compensation, rather than treating it merely as the inverse of stock-based pay. This study extends the literature by focusing on the audit committee – governance body with oversight duties distinct from those of the broader board – and by using a continuous ratio variable to capture the composition of committee pay. While prior studies often assess the presence or absence of equity grants, this research quantifies the proportion of cash pay, offering a more nuanced understanding of incentive design.

From a policy perspective, these findings suggest that regulators and firms should pay closer attention to the structure, not just the level, of audit committee compensation. Encouraging a balanced or cash-heavy pay structure may enhance the independence and monitoring effectiveness of audit committees, particularly in high-risk or high-complexity environments.

However, caution is warranted in interpreting the results. While this research does not observe a decline in oversight effectiveness at higher cash compensation levels, further research is needed to test for potential non-linear effects or threshold points beyond which cash incentives might reduce vigilance. Moreover, future studies could explore how external governance mechanisms, such as investor activism or auditor stringency, interact with compensation structures to jointly affect earnings quality.

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CONCLUSION

This study investigates whether the structure of audit committee compensation, specifically the proportion of cash-based pay, affects the quality of financial reporting. By analyzing a large panel of U.S. firms over nearly two decades, the study provides new evidence on how incentive design can shape audit committee behavior and governance outcomes.

Rather than viewing compensation structure as a routine administrative matter, this study highlights its strategic importance in enhancing oversight capacity. This underscores the need for firms and regulators to reassess existing remuneration practices, with particular attention to how fixed compensation may promote or undermine audit independence.

Beyond contributing to academic debates on director incentives, the study offers practical implications for board design and regulatory policy. Encouraging transparency and discipline in compensation decisions may strengthen audit committee performance, particularly in contexts where monitoring credibility is critical. Future research should build on this foundation by testing cross-country variations, institutional moderators, and potential non-linearities in the relationship between pay structure and oversight effectiveness. Expanding this line of inquiry will support a more comprehensive understanding of how governance design influences financial integrity.

AUTHOR CONTRIBUTIONS

Conceptualization: Tianyingkuo Yang, Lihong Zhao, Ruixue Sun, Sing Lui So, Hideyuki Hao Sun, Yuki Gong.
Data curation: Tianyingkuo Yang.
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Writing – review & editing: Tianyingkuo Yang, Lihong Zhao, Ruixue Sun, Sing Lui So, Hideyuki Hao Sun, Yuki Gong.

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APPENDIX A

Director Compensation

The Compensation Committee periodically reviews the regular annual retainer paid to non-employee directors and makes recommendations for adjustments, as appropriate, to the full Board. Our objective for compensation to non-employee directors is to award the majority of compensation in equity and to make meaningful adjustments every few years, rather than smaller adjustments that are more frequent. There was no change in fiscal year 2023. Our CEO, Mr. Nadella does not receive pay for serving as a director or as Board Chairman.

Fiscal Year 2023 Compensation Structure for Non-Employee Directors

Regular Retainers	
Annual Base Retainer (TOTAL)	$360,000
Cash	$125,000
Stock Award	$235,000
Committee Retainers (cash except stock award for Governance and Nominating Committee)	
Annual Audit Committee Chair Retainer	$45,000
Annual Audit Committee Non-Chair Member Retainer	$15,000
Annual Compensation Committee Chair Retainer	$35,000
Annual Environmental, Social, and Public Policy Committee Chair Retainer	$25,000
Annual Governance and Nominating Committee Chair Retainer	$25,000
Lead Independent Director Retainer (stock award in addition to other retainers)	$40,000

The Company reimburses reasonable expenses incurred for Board-related activities. Directors may participate in our corporate matching gift program for charitable donations.

Note: The Fiscal 2023 Director Compensation from Microsoft Corporation's Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934 https://www.sec.gov/Archives/edgar/data/789019/000119312523259247/d356108ddef14a.htm

Figure A1. Director compensation - Example 1

COMPENSATION OF DIRECTORS

For fiscal 2023, each non-employee director earned $37,000 per year for serving on the Board. Directors are reimbursed for travel expenses incurred in connection with their duties. In fiscal 2023, each non-employee director received a grant of restricted stock units ("RSUs"), with a value of $270,000. Based on the closing share price at the time of grant, each director received 565 restricted stock units. RSUs vest one-third annually, beginning on the first anniversary of the date of grant and are subject to accelerated vesting upon the director's retirement: 50% and 100% after five and ten years of service, respectively. Stock ownership requirements mandate that within five years of joining the Board a non-executive board member shall own and retain shares of Company common stock worth at least $1 million based on the value at the time of acquisition. All non-executive board members are in compliance.

FISCAL 2023 DIRECTOR COMPENSATION

The following table summarizes compensation for the non-employee directors of the Company for fiscal 2023.

Name	Fees Earned or Paid in Cash ($)	Stock Awards ($)[1]	Total ($)
Hamilton E. James	37,000	265,754	302,754
Susan L. Decker	37,000	265,754	302,754
Kenneth D. Denman	37,000	265,754	302,754
Helena B. Foulkes[2]	—	—	—
Sally Jewell	37,000	265,754	302,754
Charles T. Munger	37,000	265,754	302,754
Jeffrey S. Raikes	37,000	265,754	302,754
John W. Stanton	37,000	265,754	302,754
Mary Agnes (Maggie) Wilderotter	37,000	265,754	302,754

(1) Represents the grant-date fair value of the RSUs granted in October 2022. The value is calculated as the market value of the common stock on the grant date less the present value of the expected dividends forgone during the vesting period. These amounts thus do not reflect the amount of compensation actually received during the fiscal year. For a description of the assumptions used in calculating the fair value of equity awards, see Note 1 of our financial statements in our Form 10-K for the year ended September 3, 2023.
(2) Ms. Foulkes was elected in August 2023 and accordingly did not receive compensation for fiscal 2023.

Note: The Fiscal 2023 Director Compensation from Costco Wholesale Corporation's Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934 https://www.sec.gov/Archives/edgar/data/909832/000090983223000058/cost-20231206.htm

Figure A2. Director compensation - Example 2

APPENDIX B

Table B1. Variables definition

Dependent variable	
Abs DA	Absolute value of discretionary accruals measured by the Jones model (Kothari Leone & Wasley, 2005)
DA_SD	Accruals quality computed using the standard deviation of residuals from years t-4 to t obtained from cross-sectional estimations of the modified Dechow-Dichev (2002) model of accruals quality
Independent variable	
CCAC%	Cash compensation ratio of audit committee members
Control variables	
SIZE	Natural log of total assets
ROA	Return on assets, estimated as earnings before interest divided by total assets
BTM	Book-to-market ratio, which equals the book value of common equity divided by the market value of equity
LEV	Leverage measured as long-term debt divided by total assets
LIT	An indicator variable equal to 1 if the firm's SIC code is 2833–2836, 3570–3577, 3600–3674, 5200–5961, or 7370–7370, 0 otherwise
BIG4	An indicator variable equal to 1 if the firm-year is audited by a Big 4 auditor and 0 otherwise
LOSS	An indicator variable equal to 1 if the firm made a loss during the year and 0 otherwise
IN_CAPITAL	The intensity of capital assets, defined as Net Property, Plant, and Equipment, is divided by total assets
OCF	Cash flow from operating activities divided by total assets
Fixed effects	
FIRMFE	Control for industry fixed effects using Fama Fama-French 12 industries classification
IndustryFE	Control for industry fixed effects (FYEAR)

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