

Re-doing the audit *

Isabel J. Cho

isabel.cho@marshall.usc.edu

University of Southern California

Clive Lennox

clennox@usc.edu

University of Southern California

Xiangyu Li

xiangyu.li@marshall.usc.edu

University of Southern California

June 2024

* We thank Katherine Breure, Jessie Cheong, Jonathan Craske, Mark DeFond, Suzanne Haley, Haizhu Hong, Taylor James, Huiping Ren, Yiqian Wang, and Ruike Zhang for their helpful comments. We thank Lori Smith for sharing her valuable experience as an audit partner. We thank Karthik Kancharla, Shital Nehete, Lakshita Shetty, and Connie Zhao for their excellent research assistance. We thank the Institute for Outlier Research in Business at the University of Southern California for financial support.

Re-doing the audit

Abstract

When a company changes its audit firm, the incoming auditor will sometimes re-audit the previous year's financial statements that were originally signed off by the company's predecessor auditor. We examine the benefits of performing a re-audit. We find an incoming auditor is more likely to re-audit when there are concerns about the quality of the predecessor's audit. However, a re-audit is not more likely when there are concerns with the company's ability to prepare fairly stated financial statements. A re-audit is more likely when the incoming auditor can expect to win more clients from the predecessor auditor by uncovering material misstatements that the predecessor missed. In addition, re-audits are strong predictors of subsequent restatements of the financial statements previously signed off by the predecessor auditor. We also examine the potential costs of re-audits. We find that re-audits are associated with longer audit delays which reduce the timeliness of financial reporting. However, incoming auditors are not paid higher audit fees for performing re-audits. Overall, we conclude that re-audits have important consequences for financial statement users, incoming auditors, and predecessor auditors.

1. Introduction

When a company changes its audit firm, the incoming auditor will sometimes re-audit the company's past financial statements. To our knowledge, there is no prior research on re-audits, despite that re-audits are fairly common when companies change auditor. The decision to perform a re-audit is important because the incoming auditor can thereby discover material misstatements that were missed by the company's predecessor auditor. In this study, we examine the benefits and costs of re-auditing the company's past financial statements.

Re-audits are important in the broader economy because they can provide additional assurance to investors and stakeholders about the fair presentation of a company's past financial statements. The primary reason for a re-audit is to detect and correct any past misstatements that were missed by the predecessor auditor. Accordingly, we hypothesize that a re-audit is more likely when there are concerns with the quality of the predecessor's audit (H1). To identify such audit-related concerns we examine whether: (1) there was a limitation on the scope of the audit by the predecessor auditor; (2) the predecessor auditor has issues with its Public Company Accounting Oversight Board (PCAOB) registration (i.e., revocation or suspension of registration, deregistration, or no registration); (3) the predecessor auditor is recently barred from conducting public company audits; (4) the predecessor auditor received an Securities and Exchange Commission (SEC) inquiry about the quality of its audits; or (5) questions were raised about the independence of the predecessor auditor.

We also examine whether re-audits occur when there are potential concerns with the company's ability to prepare fairly stated financial statements. We hypothesize that a re-audit is more likely when there are concerns with the company's financial reporting because a past undiscovered misstatement is more likely in this situation (H2). To identify such client-related

concerns, we examine whether: (1) there was an accounting disagreement between the predecessor auditor and the client; (2) the predecessor auditor concluded that the company's management is unreliable; (3) the predecessor auditor resigned from the client; (4) the company committed an illegal act; or (5) the company received an SEC inquiry about its financial reporting.

A re-audit can damage the reputation of the predecessor auditor by revealing material misstatements that the predecessor missed. The resulting restatements would cause some of the predecessor's clients to select other audit firms (Hennes et al. 2014; Swanquist and Whited 2015). We hypothesize that an incoming auditor has a stronger incentive to impose this reputation penalty on the predecessor auditor when the incoming auditor can expect to win more clients from the predecessor (H3). To test this hypothesis, we examine whether the incoming auditor is more likely to re-audit the predecessor's work when the incoming auditor can expect to win more clients from the predecessor auditor. We measure the incoming auditor's expected probability of winning clients from the predecessor using historical data on client switches between the two auditors.

Underpinning our three hypotheses is a maintained assumption that re-audits are helpful for detecting and correcting past material misstatements that were missed by the company's predecessor auditor. We verify this assumption by testing whether re-audits are associated with more future restatements of the financial statements that were originally signed off by the predecessor auditor.

In addition to the benefits of re-audits, there are likely to be important costs. We examine two such costs. First, a re-audit could delay the issuance of the company's current year financial statements due to the extra time taken by the incoming auditor to re-audit the company's past financial statements. Therefore, we test whether re-audits result in longer audit delays. A second

potential downside is that a re-audit could increase the cost of the audit due to the extra work performed by the incoming auditor. Therefore, we test whether companies pay higher audit fees when their past financial statements are re-audited by incoming auditors.

We assemble a sample of 5,299 auditor changes between 2005 and 2022. To determine whether the incoming auditor re-performs the final audit of the predecessor auditor, we hand-collect the final audit report of the predecessor and the first audit report of the incoming auditor in the years surrounding the auditor change. The re-audit variable is coded one if the predecessor's final report discloses that it audited the year $t-1$ financial statements and the incoming auditor's first report discloses that it audited the year t *and year $t-1$* financial statements. Conversely, the re-audit variable is zero if the predecessor's final report discloses that it audited the year $t-1$ financial statements, while the incoming auditor's first report discloses that it audited the year t financial statements but *not* year $t-1$. Of the 5,299 auditor changes in our sample, we find 748 cases of re-audits (14.11%).

We begin by examining the decision to perform a re-audit. Consistent with H1, we find that a re-audit is more likely when there are concerns with the quality of the audit by the company's predecessor auditor. We delve into the five indicator variables that make up the aggregated audit-related concerns to determine which ones have the largest relation to re-audits. All five indicator variables are positively associated with re-audits but not all five are statistically significant because some have small incidence rates. For example, there are only 11 auditor change observations in our sample of 5,299 where there are limitations on the scope of the audit by the predecessor auditor. The five indicator variables are highly significant when combined into an aggregate audit-related concerns variable and two of the five indicators are statistically significant when included individually. The significant individual variables are: 1) the

predecessor auditor had issues with its PCAOB registration, and 2) the predecessor auditor was barred from conducting public company audits. These events are highly salient audit-related concerns that increase the probability of a re-audit by the incoming auditor.

Surprisingly, we do not find that re-audits are more likely when there are client-related concerns relating to the company's ability to prepare fairly stated financial statements (H2). The five indicator variables for client-related concerns are statistically insignificant when they are combined into an aggregate measure. When we examine the five indicator variables individually, we find that three are positively associated with re-audits but two are negatively associated. Only one of the five indicator variables has a statistically significant positive association with re-audits. Specifically, a re-audit is more likely when predecessor auditors say the company's management is not reliable. In contrast, re-audits are not more likely when companies have accounting disagreements with their predecessor auditors, when predecessor auditors resign, or when there are illegal acts by the company. The insignificance of these variables could reflect that incoming auditors do not regard them as serious or lasting problems. For example, a company may tell the incoming auditor that its accounting disagreement with the predecessor auditor was the fault of the predecessor rather than a matter that the incoming auditor needs to worry about.

Overall, we find that incoming auditors conduct re-audits when there are concerns with the quality of the company's predecessor auditor (H1) but not when there are potential concerns with the company's financial reporting (H2). The inferences for these two hypotheses are further supported by our control variables. For example, we find that a re-audit is less likely when the company's predecessor auditor is a Big 4 firm, suggesting that Big 4 predecessors are perceived to be higher quality and therefore in less need of re-audits compared to non-Big 4 predecessors.

We find that restatements prior to the auditor change date do not have a significant effect on the decision to perform a re-audit, which is consistent with our main null result for H2.

We find strong evidence for our third hypothesis (H3) which predicts that an incoming auditor is more likely to re-do the audit when the incoming auditor can expect to win more clients from the predecessor. This finding suggests that incoming auditors are motivated to perform re-audits in order to win clients from predecessor auditors whose reputations are damaged by subsequent restatements. In an ex post analysis, we find that incoming auditors win significantly more clients from predecessor auditors after they re-audit the work of the predecessor auditors. This ex post analysis provides further support for our main ex ante test of H3, which is based on the incoming auditor's expected gains and losses of clients from the predecessor auditor. Further, we find strong evidence to support our maintained assumption that re-audits help to detect and correct past misstatements that the predecessor auditors missed. We show that re-audits are followed by significantly more future restatements of the financial statements that were originally signed off by the predecessor auditors.

Turning to the costs of re-audits, we find that re-audits result in significantly longer audit delays. This finding is consistent with incoming auditors spending extra time to re-audit the company's past financial statements concurrent with their audit of the company's current year financial statements. Surprisingly, we find that re-audits do not result in higher audit fees. This finding suggests that the costs of re-audits are borne by incoming auditors rather than being passed on to clients.

Overall, we conclude that re-audits have important consequences for financial statement users, incoming auditors, and predecessor auditors. Financial statement users benefit from re-audits because re-audits help to detect past misstatements that were missed by predecessor

auditors. At the same time, re-audits are costly to financial statement users because re-audits result in delays to the release of the current year's audited financial statements. Re-audits have consequences for predecessor auditors because a re-audit can damage the predecessor's reputation by uncovering material misstatements that the predecessor missed. There are also consequences for incoming auditors because re-audits help to reduce the risks of taking on new clients. Re-audits also help incoming auditors to win clients from predecessor auditors by uncovering material misstatements that the predecessor auditors missed. However, the costs of performing re-audits are borne by incoming auditors rather than being passed on to clients.

Our study makes three contributions to the literature. We contribute to the auditing literature by providing the first evidence on re-audits. There is a large literature on auditor changes (e.g., Chow and Rice 1982; Krishnan and Krishnan 1997; DeFond and Subramanyam 1998; Lennox 2000; Shu, 2000; Johnstone and Bedard, 2004; Hennes et al. 2014; Newton et al. 2016). However, we are not aware of any prior evidence on re-audits. We show that re-audits are an important tool that incoming auditors use to reduce the risks of taking on new clients and to identify past reporting errors that the predecessor auditors overlooked.

Second, our study contributes to the literature on accounting restatements. Numerous studies examine the characteristics of companies that restate (do not restate) their past financial statements (Palmrose and Scholz 2004; Efendi et al. 2007; Cheng and Farber 2008; Dechow et al. 2011; Lennox and Li 2014; Czerney et al. 2014; Guo et al. 2016). We contribute to this literature by showing that some restatements are triggered by the re-audits of incoming auditors. We also offer a new perspective on the relationship between audit quality and accounting restatements. It is usually assumed that high quality audits result in fewer accounting misstatements and therefore *fewer* restatements (Kinney et al. 2004; Stanley and DeZoort 2007; Chin and Chi 2009; Singer and

Zhang 2018). Our study offers a new perspective by showing that re-audits can result in *more* restatements because re-audits help to uncover material misstatements that the predecessor auditors missed.

Third, we contribute to the financial reporting literature by showing that re-audits lead to longer audit delays. This finding helps explain why delays are viewed negatively by investors (Alford et al. 1994; Griffin 2003; Impink et al. 2012; Bartov and Konchitchki 2017). Specifically, a reporting delay is bad news for investors because a delay is more likely when the incoming auditor is re-auditing the company's past financial statements and a re-audit increases the likelihood of a future restatement.²

2. Prior literature and hypotheses

2.1. What are re-audits?

Re-audits can occur when companies change their auditors. In a re-audit, the incoming auditor re-audits a company's past financial statements that were previously audited by the company's predecessor auditor. Re-audits can be initiated by the client company or the incoming auditor although an incoming auditor cannot perform a re-audit without the consent of the client. Later in the paper, we present evidence that re-audits are typically initiated by incoming auditors rather than by client companies.

² When a company issues a Form NT to notify investors that its 10-K filing will be late, the company typically does not disclose that the delay is due to the auditor performing a re-audit. Consequently, investors only know for sure that the past financial statements were re-audited when the incoming auditor's first audit report is disclosed in the delayed 10-K filing.

Not all the audit procedures available to the predecessor auditor on the original audit remain available to the incoming auditor on a subsequent re-audit. For example, the incoming auditor cannot go back in time to attend the previous year's inventory count. Moreover, audit confirmations of accounts receivable may not yield useful responses given that the receivable balances were from an earlier fiscal period. Nevertheless, the incoming auditor can still obtain reasonable assurance on such accounts by performing *alternative* audit procedures. For example, the incoming auditor can obtain competent evidential matter about inventory balances by testing the reliability of the client's perpetual inventory recording system and by tracing inventory purchase and sales transactions during the prior fiscal period. Similarly, the incoming auditor can test the existence and valuation of accounts receivables by examining cash collections from customers subsequent to the prior year-end.

Regardless of whether the incoming auditor performs a re-audit, the incoming auditor must always audit the company's opening balances (e.g., the opening inventory balance) as well as its closing balances. An opening balance in the current year is simply the closing balance from the previous year. However, auditing an opening balance is *not* equivalent to performing a re-audit. In a re-audit, the auditor tests and opines on the *entire* financial statements from the prior year, including the income statement and cash flow statement. Therefore, auditing the opening balances in the balance sheet is not equivalent to re-auditing the entire financial statements from the previous year. Similarly, a company's decision to include comparative financial figures from the previous year does not constitute a re-audit.³ In short, a re-audit occurs when the incoming

³ Public companies are required to report comparative financial figures from past years (years t-2, t-1) at the same time as reporting the current year's financial figures (year t). When there is a change of auditor, the past years are reported on by the predecessor auditor if the predecessor is willing to re-issue its past audit opinions. Alternatively, the past years are reported on by the successor auditor if they are re-audited by the successor auditor. If the predecessor auditor is not willing to re-issue its past audit opinions, the successor auditor can choose to re-audit them. Alternatively, the successor auditor can choose not to re-

auditor explicitly states in the audit report that it audited the entire financial statements from the previous year, where those past financial statements were originally audited by the company's predecessor auditor.

2.2. The riskiness of auditor change companies

Auditor change companies tend to be smaller and riskier than companies that do not change auditors. Companies change auditor after receiving qualified audit opinions, going-concern opinions, or adverse opinions on their internal controls over financial reporting (Chow and Rice 1982; Lennox 2000; Newton et al. 2016). Companies are more likely to change auditor after they report income-decreasing abnormal accruals during their final year under the predecessor auditor (DeFond and Subramanyam 1998). Overall, these findings are consistent with auditor change companies being risky and with companies changing their auditor in the hope of finding a more lenient incoming auditor.

Auditor changes also occur after it is discovered that a company has been using a low-quality auditor. Specifically, auditor changes are more likely when auditors are embroiled in financial reporting scandals (Weber et al. 2008; Skinner and Srinivasan 2012), when auditors are associated with accounting restatements (Hennes et al. 2014; Swanquist and Whited 2015), and when auditors receive negative reports from regulators about their audit quality (Hilary and Lennox 2005; Aobdia and Shroff 2017).

audit them even if the predecessor auditor is not willing to re-issue its past opinions. In this situation, the successor auditor must disclose in the year t audit opinion that the comparative financial statements from past years were previously audited by the predecessor auditor. For further information, see paragraph 74 of PCAOB (2016).

The main take-away from this literature is that auditor change companies pose high risks for incoming auditors. Such risks could motivate an incoming auditor to re-audit the past financial statements that were previously signed off by the company's predecessor auditor. We expect the incoming auditor to re-audit the predecessor's work if there is evidence that the predecessor may have performed a low-quality audit. For instance, the quality of the predecessor's audit would be in question if there was a limitation on the scope of the audit or concerns were raised about the predecessor's independence from the audit client. Regulatory actions can also cast doubt on the quality of the predecessor auditor. For instance, the predecessor auditor is likely to be a low-quality auditor if the predecessor's registration with the PCAOB was revoked or suspended, or the predecessor was barred by the SEC from conducting public company audits due to an enforcement action. Moreover, the quality of the predecessor auditor would be in question if the predecessor received an SEC inquiry about the quality of its audits. We expect more re-audits when such audit-related concerns are present. Therefore, we form the following hypothesis which is expressed in the alternative form.

H1: The incoming auditor is more likely to re-audit the predecessor's work when there are concerns that the predecessor auditor may have performed a low-quality audit.

Concerns with the company's ability to prepare fairly stated financial statements could also affect the decision to perform a re-audit. Such client-related concerns are likely to exist if the predecessor auditor had an accounting disagreement with the company's management or the predecessor auditor was unable to rely on the representations of the company's management. Whisenant et al. (2003) report significant negative market reactions when there are disagreements between predecessor auditors and client management. Whisenant et al. (2003) also find significant negative market reactions around auditor change announcements when auditors

resign rather than being dismissed. The negative signal conveyed by a resignation is consistent with predecessor auditors resigning from clients when they face a high liability risk due to client wrongdoing (Krishnan and Krishnan 1997; Shu 2000). Therefore, we expect that re-audits are more likely when predecessor auditors resign. Finally, there are likely to be concerns about the company's ability to prepare fairly stated financial statements when a company is found to have committed an illegal act or the company received an inquiry from the SEC about its financial reporting. We expect more re-audits when such client-related concerns are present. Therefore, we form the following hypothesis which is expressed in the alternative form.

H2: The incoming auditor is more likely to perform a re-audit when there are concerns with the company's ability to prepare fairly stated financial statements.

Although the predictions for H1 and H2 are intuitive, there is significant tension for them. By definition, an incoming auditor has agreed to become the company's new auditor. The incoming auditor should only take on this responsibility if the auditor believes the client is not excessively risky. Other auditors may turn down the opportunity to audit the client because of the perceived high risks, but the incoming auditor has shown by revealed preference that they do not consider the client to be too risky (a winner's curse problem). Therefore, the incoming auditor may see no need to re-audit the company's past financial statements.

In addition, the company's management may tell the incoming auditor that any problems with the predecessor auditor were the fault of the predecessor rather than the company. Auditors who are unpersuaded by such arguments would probably not agree to take on the client in the first place, while the incoming auditor may agree with the company's management which is why they take on the client. Thus, the incoming auditor may not perform a re-audit even when there are indicators of financial reporting problems at the company.

2.3. Accounting restatements and the reputation of the predecessor auditor

Restatements can damage the reputation of the predecessor firm that originally audited the materially misstated financial statements. Auditors whose reputations are damaged by restatements tend to lose clients to other audit firms subsequent to the restatement announcement (Hennes et al. 2014; Swanquist and Whited 2015). Thus, an incoming auditor can potentially benefit by winning new clients from the predecessor auditor. By re-doing the audit, the incoming auditor can find a material misstatement that the predecessor auditor missed and then win clients from the predecessor auditor whose reputation is damaged by the subsequent restatement. The incoming auditor has a stronger incentive to detect past misstatements that were missed by the predecessor auditor if the incoming auditor can expect to win more clients from the predecessor auditor. We therefore form the following hypothesis which is expressed in the alternative form.

H3: The incoming auditor is more likely to re-audit the predecessor's work when the incoming auditor expects to win more clients from the predecessor auditor.

A key assumption underpinning our three hypotheses (H1-H3) is that re-audits facilitate the detection of past misstatements that the predecessor auditors missed. We test this assumption by examining whether re-audits predict future restatements of the financial statements that were originally signed off by predecessor auditors as being fairly presented.

3. Research design and data

3.1. Tests of H1, H2 and H3

We test H1 to H3 by estimating the model of re-audits shown in eq. (1):

$$\begin{aligned}
Reaudit = & \beta_1 AuditConcerns + \beta_2 ClientConcerns + \beta_3 ClientWin + \beta_4 PredecessorBig4 + \beta_5 PriorRestate \\
& + \beta_6 GoingConcern + \beta_7 OfficerChange + \beta_8 AC_Change + \beta_9 Ln(TA) + \beta_{10} ROA + \beta_{11} Loss + \\
& IncomingAuditorFE + Year FE + Industry FE + u
\end{aligned} \tag{1}$$

The dependent variable (*Reaudit*) equals one if the incoming auditor issues an audit opinion on past financial statements that were previously audited by the company's predecessor auditor (zero otherwise). We estimate eq. (1) using a logit model.

Under H1, we expect a positive association between re-audits and concerns about the quality of the predecessor auditor (*AuditConcerns*); i.e., $\beta_1 > 0$. We construct *AuditConcerns* as an indicator variable that equals one if any of the following issues are disclosed in the 8-K filing announcing the auditor change: (1) there was a limitation on the scope of the audit performed by the predecessor auditor; (2) the predecessor auditor had problems with its PCAOB registration (i.e., revocation or suspension of registration, deregistration, or no registration); (3) the predecessor auditor was barred by the SEC from conducting public company audits; (4) the predecessor auditor received an SEC inquiry about the quality of one or more audits; (5) there are questions concerning the independence of the predecessor auditor. We aggregate the five indicator variables into a single *AuditConcerns* measure because some of the five groups have small sample sizes. Nevertheless, for completeness, we also report results using the five individual indicators of audit-related concerns; i.e., *ScopeLimitation*, *PCAOBRegistration*, *SECBan*, *SECInquiryAuditor*, and *LackIndependence*.

Under H2, we expect a positive association between re-audits and concerns with the quality of the company's financial reporting (*ClientConcerns*); i.e., $\beta_2 > 0$. We construct *ClientConcerns* as an indicator variable that equals one if any of the following issues are disclosed in the 8-K filing: (1) there was a disagreement between the predecessor auditor and the client; (2)

the predecessor auditor resigned from the engagement; (3) the predecessor auditor concluded that the company's management was not reliable; (4) the company committed an illegal act; or (5) the company received an SEC inquiry about its financial reporting. Again, we aggregate the five indicator variables into a single *ClientConcerns* measure because of the low frequency of some individual issues. Nevertheless, we also report results for the five individual indicators: *Disagreement*, *PredecessorResign*, *MgtNotReliable*, *IllegalActs*, and *SECInquiryClient*.

Under H3, we expect a positive association between re-audits and the probability that the incoming auditor can expect to win new clients from the predecessor auditor (*ClientWin*); i.e., $\beta_3 > 0$. We measure *ClientWin* based on the historical record of client switching between the two auditors because past switches capture the closeness of fit between the client portfolios of the incoming and predecessor auditors. Specifically, *ClientWin* is the number of client switches between the incoming auditor and the predecessor auditor, divided by the total number of client switches from and to the incoming auditor during the five-year window prior to the current switch. For example, suppose the incoming auditor (auditor A) gained a total of 20 clients and lost a total of 20 clients during the past five years. Suppose auditor A gained 5 of the 20 clients from auditor B and lost 5 of the 20 clients to auditor B. Then, the *ClientWin* variable is 25% ($= (5+5) / (20+20)$) when the predecessor auditor is auditor B. The *ClientWin* variable is calculated in the same way for other predecessor auditors. For instance, suppose auditor A gained 1 client from auditor C and lost 1 client to auditor C during the same five-year period. Then, the *ClientWin* variable is 5% ($= (1+1) / (20+20)$) when auditor C is the predecessor auditor. In this example, auditors A and B are closer substitutes than auditors A and C based on the past switches of their respective client portfolios. We expect that auditor A is more likely to re-do the audit when the predecessor is auditor B rather than auditor C because auditor A can expect to win more clients

from B than from C (i.e., 25% > 5%) given that A is a closer fit to B's clients than to C's clients. Both the numerator and denominator for the *ClientWin* variable are measured at the audit office level rather than the audit firm level because clients tend to choose audit offices that are located nearby rather than offices of a given audit firm that are located far away.

3.2. Control variables

Our study is the first to examine the decision to re-do the audit. Given the absence of prior research on re-audits, this section provides a detailed justification for each control variable in eq. (1). Appendix A provides formal definitions for the variables.

(1) *PredecessorBig4*

We control for whether the predecessor auditor is a Big 4 firm (*PredecessorBig4*). Prior research suggests that Big 4 firms provide higher quality audits than non-Big 4 firms (e.g., Becker et al. 1998; Francis and Maydew 1999; Francis and Wang 2008; Lennox and Pittman 2010). We expect the incoming auditor has more confidence in the predecessor and is less likely to re-audit the predecessor's work if the predecessor is a Big 4 firm. We predict a negative coefficient on the *PredecessorBig4* variable because we expect fewer re-audits by incoming auditors when the predecessor auditor is a Big 4 firm.

(2) *PriorRestate*

We control for the auditor change company's prior restatements. The *PriorRestate* variable equals one if the company announced a restatement within a one-year period prior to appointing the incoming auditor (zero otherwise). *Ex ante*, it is unclear whether a re-audit is more or less likely when the company has a prior restatement. A re-audit may be more likely because a prior

restatement reveals a problem with the company's past financial statements. On the other hand, a restatement implies that the problem has already been identified and corrected. Therefore, there may be less need for a re-audit following a prior restatement.

(3) *GoingConcern*

The *GoingConcern* variable equals one if the predecessor auditor previously issued a going concern modification in the company's audit report (zero otherwise). We expect a positive association between re-audits and prior going-concern opinions for a couple of reasons. First, a going-concern opinion shows that the company is financially distressed. In this situation, the incoming auditor may be more likely to re-do the audit because a distressed company poses a high level of risk. Second, a company could be engaged in opinion-shopping when it changes auditor after receiving a going-concern opinion from the predecessor auditor (Lennox 2000). For both reasons, we expect the incoming auditor to perform a re-audit when the company previously received a going-concern opinion.

(4) *OfficerChange* and *AC_Change*

The *OfficerChange* variable equals one if the company changed its CEO or CFO in the year prior to appointing the incoming auditor (zero otherwise). The *AC_Change* variable equals one if the company changed any of its audit committee members in the year prior to appointing the incoming auditor (zero otherwise). There are a couple of reasons why we expect a positive association between re-audits and the recent turnover of corporate officers and audit committee members. First, turnover is a sign of potential financial difficulties. The incoming auditor may re-do the audit in order to learn more about the company's difficulties that led to the turnover events. Second, a re-audit could result in a subsequent restatement of past financial statements and the ensuing restatement would likely damage the reputations of the company's officers and

audit committee members who were present at the company when it misstated its financial statements. New officers and new audit committee members were not present at that time and so do not face this reputational threat. Therefore, a re-audit poses less of a threat to the personal reputations of new officers and new audit committee members than a re-audit poses to the reputations of incumbent officers and incumbent audit committee members. Consequently, we expect that re-audits are more likely when the company has new officers or new audit committee members.

(5) $\ln(TA)$, ROA , $Loss$

We control for the size and profitability of the company because these risk factors could affect the decision to perform a re-audit. We control for size using the natural logarithm of the company's total assets in the year before the auditor change ($\ln(TA)$). We measure the company's return on assets (ROA) as net income divided by total assets in the year before the auditor change. We winsorize the continuous variables ($\ln(TA)$ and ROA) at the 1st and 99th percentiles to mitigate the influence of outliers. The $Loss$ indicator takes the value one if the company's net income is negative in the year before the auditor change (zero otherwise).

(6) $IncomingAuditorFE$, $YearFE$, $IndustryFE$

We include fixed effects for the incoming audit firms to control for time-invariant cross-sectional variation in the propensity for incoming auditors to perform re-audits.⁴ We also cluster the standard errors at the level of the incoming audit firm. We include year fixed effects to control

⁴ Within our sample, PricewaterhouseCoopers LLP re-audits 2.76% of its new engagements, Ernst & Young LLP re-audits 2.97%, Deloitte & Touche LLP re-audits 2.83%, and KPMG LLP re-audits 2.53%.

for yearly variation in re-audits. Finally, we include industry fixed effects to control for industry variation in re-audits across companies.⁵

3.3. Sample

We identify our sample using the auditor changes module from the Audit Analytics database. We merge the auditor changes with data on audit opinions, accounting restatements, and audit fees from Audit Analytics. Where available, we fill in missing data for the control variables (total assets, net income) using the Compustat database. For each auditor change, we cross-check the 8-K disclosures coded up in the Audit Analytics database with the original disclosures contained in the raw 8-K filings.⁶

In total, there are 21,910 auditor changes between 2005 and 2022.⁷ We exclude auditor changes involving non-U.S. companies or non-U.S. auditors, financial companies, pension plans, auditor changes that occur due to audit firm mergers, and auditor changes with missing data on the company's SIC code, missing data on the audit office, or missing data for other variables. This process leaves us with 9,921 auditor changes. For each auditor change, we hand-collect the company's audit reports in the years before and after the auditor change. When reading these reports, we further exclude auditor changes where there is a change in the company's name or fiscal year-end. Consequently, our final sample consists of 5,299 auditor changes for 3,812 unique

⁵ Most companies change their auditor only once during our sample period. Therefore, we do not include controls for company fixed effects.

⁶ The Audit Analytics database collects data on the disclosures found in 8-K filings. However, some of the disclosure variables in the Audit Analytics database contain errors. We manually collect each 8-K filing to ensure the accuracy of our data.

⁷ We use auditor change data going back to 2000 to measure the *ClientWin* variable, which is calculated using historical auditor switches during the five-year window prior to the current switch.

companies. There are 616 (559) unique predecessor (incoming) audit firms, and 1,304 (1,294) unique predecessor (incoming) audit offices.

We identify whether the incoming auditor re-audits the work of the predecessor auditor using information found in the company's audit reports during the years surrounding the auditor change. Specifically, we identify the fiscal year(s) audited in the first audit report issued by the incoming auditor and compare those years to the fiscal years reported in the predecessor auditor's final report. We code the auditor change as a re-audit if the incoming auditor issued an audit opinion on financial statements that had previously been audited by the predecessor auditor. For example, the re-audit variable is coded as one if the predecessor audited the year $t-1$ financial statements, while the new auditor's first report discloses that it the year t and year $t-1$ financial statements. Conversely, the re-audit variable is coded as zero if the predecessor audited the year $t-1$ financial statements, while the new auditor's first report discloses that it audited the year t financial statements but *not* the year $t-1$ financial statements.⁸

3.4. Descriptive statistics

Panel A of Table 1 provides descriptive statistics. The incoming auditor performs a re-audit in 14.1% of auditor changes (*Reaudit*). Prior to the auditor change, 3.5% of observations have potential concerns relating to the predecessor auditor (*AuditConcerns*), while 22.4% have potential concerns relating to the client company (*ClientConcerns*). In 17.3% of observations, there are

⁸ Unfortunately, the Audit Analytics database does not provide sufficient information for researchers to identify re-audits which is why we identified re-audits manually from audit reports. We determined that the only reliable method to obtain accurate and comprehensive data on re-audits is by manually verifying the audit opinions issued before and after every auditor change. Upon publication of this manuscript, we will make our hand-collected re-audit data publicly available to other researchers.

accounting restatements in the year *prior* to the appointment of the incoming auditor (*PriorRestate*). In 7.1% of observations, the company's past financial statements that were originally signed off by the predecessor auditor are restated *after* the company's appointment of the incoming auditor (*FutureRestate*). In later analyses, we examine whether these future restatements of past financial statements are associated with the incoming auditor having re-audited the company's past financial statements.

[INSERT TABLE 1 HERE]

Panel A shows that 40.1% of observations have going concern modifications in the audit reports issued by predecessor auditors (*GoingConcern*). This high percentage reflects that many auditor change companies are financially distressed. Changes in corporate officers and changes in audit committee members are quite common too. We find that 29.7% of companies have a change in the CEO or CFO in the period from the signature date of the final financial statements under the predecessor auditor up to the signature date of the first financial statements audited by the incoming auditor (*OfficerChange*). Over the same event window, we find that 12.2% of companies experience a change in audit committee membership (*AC_Change*). On average, auditor change companies have total assets of \$424.7 million, a return on assets of -9.5%, and 70.9% report losses in the year prior to the auditor change. Thus, auditor change companies are relatively small and have poor performance, reflecting that they are high-risk engagements for incoming auditors.

Panel B of Table 1 reports the pair-wise correlations between the variables. Re-audits are associated with more future restatements, longer audit delays, and smaller audit fees. Consistent with H1 and H2, re-audits are more likely when there are concerns about the predecessor auditor (*AuditConcerns*) or concerns about the company (*ClientConcerns*). However, the correlation with

re-audits is much larger for *AuditConcerns* than *ClientConcerns* (0.26 versus 0.06). Consistent with H3, re-audits are more likely when the incoming auditor has a higher probability of winning clients from the predecessor auditor (*ClientWin*).

Turning to the control variables, we find that re-audits are less likely when the predecessor auditor is a Big 4 firm (*PredecessorBig4*). However, re-audits are not significantly related to prior restatements (*PriorRestate*). Companies that receive going concern modifications from predecessor auditors (*GoingConcern*) are more likely to be re-audited. Larger companies and more profitable companies are significantly less likely to be re-audited ($\ln(TA)$, ROA) while loss-making companies are more likely to be re-audited (*Loss*). These findings are corroborated by the univariate comparisons shown in Panel C of Table 1.

4. Multivariate results

4.1. Determinants of re-audit

Table 2 reports the regression results for eq. (1), which examines the determinants of re-audits. In Col. (1), the coefficient on *AuditConcerns* is positive and highly significant (z-stat. = 10.081). Consistent with H1, this result shows that an incoming auditor is more likely to re-audit the company's past financial statements when there are concerns with the quality of the predecessor's audit. Contrary to our prediction in H2, concerns with the company's ability to prepare fairly stated financial statements do not have a significant positive impact on the re-audit decision, as evidenced by the insignificant negative coefficient on *ClientConcerns*. This result could reflect that the incoming auditor has revealed through their decision to accept the new client that the incoming auditor does not consider the company to be excessively risky. It is also possible that the company told the incoming auditor that its disagreements with the predecessor auditor were

the fault of the predecessor rather than the company. Thus, the incoming auditor may not consider accounting disagreements or resignations to be strong signals of financial reporting problems at the company.

[INSERT TABLE 2 HERE]

Col. (2) of Table 2 reports the results for the individual components of the aggregate measures of *AuditConcerns* and *ClientConcerns*. The five individual components of *AuditConcerns* are all found to have positive coefficients, indicating that re-audits are more likely when there are concerns with the quality of the predecessor auditor. Two of the individual components are statistically significant. Specifically, the incoming auditor is more likely to re-do the audit when the predecessor auditor has issues with its PCAOB registration (*PCAOBRegistration*; z-stat. = 8.255) or the predecessor is barred by the SEC from conducting public company audits (*SECBan*; z-stat. = 4.635). The five components of *ClientConcerns* have mixed results as two components have negative coefficients (*Disagreement*, *PredecessorResign*) while three components have positive coefficients (*MgtNotReliable*, *IllegalActs*, and *SECInquiryClient*). Only the concern about management reliability (*MgtNotReliable*) shows up as having a positive coefficient that is statistically significant at the 5% level or better. The coefficients for *Disagreement* and *PredecessorResign* are negative and insignificant, suggesting that incoming auditors do not consider accounting disagreements or resignations as situations that warrant a re-audit.

Consistent with H3, we find positive and highly significant coefficients for the *ClientWin* variable (z-stats. = 3.734, 3.343). Therefore, re-audits are more likely when the incoming auditor can expect a higher probability of winning clients from the predecessor auditor. This finding suggests that incoming auditors have a stronger incentive to impose a reputation penalty on the

predecessor auditor when the incoming auditor can expect to win more clients from the predecessor auditor by uncovering a material misstatement that the predecessor overlooked.

Turning to the control variables, we find that re-audits are significantly less likely when the predecessor auditor is a Big 4 firm (*PredecessorBig4*; z-stats. = -3.356 , -5.052). This finding suggests that incoming auditors regard Big 4 firms as being in less need of a re-audit, which is consistent with prior evidence that Big 4 firms are higher quality than non-Big 4 firms (Becker et al. 1998; Francis and Maydew 1999; Francis and Wang 2008; Lennox and Pittman 2010). This finding further supports our inference from H1 that re-audits are less likely when there are fewer concerns with the quality of the predecessor auditor.

Consistent with our main null result for H2, we find that re-audits are not significantly associated with prior restatements (*PriorRestate*). However, re-audits are more likely if the company previously received a going-concern opinion (*GoingConcern*; z-stats. = 1.834 , 2.496). Re-audits are more likely for companies that experience recent changes in corporate officers (*OfficerChange*) or changes in audit committee members (*AC_Change*), although the coefficients on these turnover variables are not statistically significant at the 5% level or better. Finally, the company size coefficients are significantly negative ($\ln(TA)$; z-stats. = -7.489 , -9.079), suggesting that incoming auditors regard larger companies as less risky and therefore in less need of a re-audit.

4.2. Future restatements and re-audits

Our hypothesis development assumes that the primary motivation for a re-audit is to allow the incoming auditor to discover a material misstatement that was not detected and corrected by the company's predecessor auditor. In this section, we examine the plausibility of this assumption by

examining whether re-audits are followed by more future restatements of the financial statements that were previously signed off by the predecessor auditor. The model of future restatements is shown in eq. (2):

$$\begin{aligned}
 FutureRestate = & \beta_1 Reaudit + \beta_2 AuditConcerns + \beta_3 ClientConcerns + \beta_4 ClientWin + \beta_5 PredecessorBig4 \\
 & + \beta_6 PriorRestate + \beta_7 GoingConcern + \beta_8 OfficerChange + \beta_9 AC_Change + \beta_{10} Ln(TA) + \beta_{11} ROA \\
 & + \beta_{12} Loss + Incoming Auditor FE + Year FE + Industry FE + u
 \end{aligned} \tag{2}$$

The dependent variable (*FutureRestate*) equals one if the company restates the financial statements that were originally audited by the predecessor auditor. We require the restatement announcement to occur after the incoming auditor is appointed to ensure that the *FutureRestate* variable captures restatements that are plausibly affected by the re-audit by the incoming auditor.⁹ We expect re-audits to uncover errors in past financial statements that were overlooked by the predecessor auditor. Therefore, we expect *Reaudit* to have a positive coefficient in eq. (2); $\beta_1 > 0$. We include the same control variables as before to ensure that the correlation between *FutureRestate* and *Reaudit* is not capturing other risk factors that affect the decision to have a re-audit. Importantly, we control for restatements announced prior to the appointment of the incoming auditor (*PriorRestate*) because there could be persistence in a company's general level of restatements.

The results for eq. (2) are shown in Table 3. We find significant positive coefficients on *Reaudit* (z-stats. = 7.990, 7.912). Therefore, re-audits are followed by significantly more future restatements of the past financial statements that were originally audited by the company's

⁹ We do not observe the date that the incoming auditor starts to re-audit the company's past financial statements. We only have the date of the incoming auditor's appointment and the date of the incoming auditor's first audit report in which it is revealed that the past financial statements were re-audited.

predecessor auditor. This finding is consistent with our assumption that incoming auditors re-do the audit in order to find any material misstatements that the predecessor auditors might have missed. Nevertheless, we acknowledge that the decision to re-audit is endogenously affected by a company's risks (as shown in Table 2). Therefore, we refrain from drawing strong causal inferences from the statistical correlation between re-audits and future restatements in Table 3.

[INSERT TABLE 3 HERE]

4.3. Audit delays and re-audits

Our findings suggest that re-audits are beneficial to financial statement users because re-audits help to detect and correct past material misstatements that were missed by the company's predecessor auditor. However, re-audits are also potentially costly to financial statement users because the incoming auditor has to spend additional time checking the company's past financial statements. The extra time taken could delay the issuance of the current year's audit opinion, meaning that financial statement users would have access to less timely audited information.

To test whether re-audits are associated with longer audit delays, we estimate the model shown in eq. (3):

$$\begin{aligned}
 \text{Delay} = & \beta_1 \text{Reaudit} + \beta_2 \text{AuditConcerns} + \beta_3 \text{ClientConcerns} + \beta_4 \text{ClientWin} + \beta_5 \text{PredecessorBig4} + \beta_6 \\
 & \text{PriorRestate} + \beta_7 \text{GoingConcern} + \beta_8 \text{OfficerChange} + \beta_9 \text{AC_Change} + \beta_{10} \text{Ln(TA)} + \beta_{11} \text{ROA} + \\
 & \beta_{12} \text{Loss} + \text{Incoming Auditor FE} + \text{Year FE} + \text{Industry FE} + u
 \end{aligned} \tag{3}$$

The dependent variable (*Delay*) is the natural logarithm of the number of days it takes for the incoming auditor to issue its first audit report. We focus on the date of the first *newly-audited* fiscal year to ensure that we are capturing delays to the current year's audit opinion; i.e., the first fiscal year following the incoming auditor's appointment. We expect that re-audits are associated

with increased audit delays due to the increased workload from re-auditing the past financial statements. Therefore, we expect *Reaudit* to have a positive coefficient in the model of audit delays; $\beta_1 > 0$. Eq. (3) includes the same control variables as Table 2 to ensure that the correlation between *Delay* and *Reaudit* is not capturing risk factors that affect the decision to have a re-audit. Importantly, we control for the audit delay in the previous reporting period (*PriorDelay*) because there could be persistence in a company's audit delays from one year to the next.

Table 4 reports the results for eq. (3). As expected, we find significant positive coefficients on the *Reaudit* variable (t-stats. = 5.248, 6.211). Therefore, audit delays are significantly longer when the incoming auditor re-audits the company's past financial statements. This finding suggests that re-audits are costly to financial statement users because re-audits result in delays that make the audited financial information less timely. This finding is interesting because prior research shows that audit delays are viewed negatively by investors (Alford et al. 1994; Griffin 2003; Impink et al. 2012; Bartov and Konchitchki 2017). Our findings suggest that delays transmit a negative signal to investors because delays occur when the company's past financial statements are being re-audited (Table 4), and re-audits are, in turn, a leading indicator of future restatements (Table 3).¹⁰

[INSERT TABLE 4 HERE]

4.4. Audit fees and re-audits

Our findings suggest that an incoming auditor can mitigate the risks of taking on a new client by re-auditing the client's past financial statements. In addition, incoming auditors can expect to win

¹⁰ Typically, companies do not disclose whether a filing delay is attributable to a re-audit of the company's financial statements. Therefore, delays provide investors with noisy signals of re-audits which are, in turn, noisy leading indicators of future accounting restatements.

clients from predecessor auditors if the predecessors are found to have overlooked material misstatements in the company's past financial statements. However, re-audits are also potentially costly to incoming auditors because the incoming auditors have to spend additional time and effort on checking the company's past financial statements. In this section, we examine whether these additional costs are passed on to clients in the form of higher audit fees.

We test the association between audit fees and re-audits by estimating eq. (4):

$$\begin{aligned}
 Ln(AF) = & \beta_1 Reaudit + \beta_2 AuditConcerns + \beta_3 ClientConcerns + \beta_4 ClientWin + \beta_5 PredecessorBig4 + \\
 & \beta_6 PriorRestate + \beta_7 GoingConcern + \beta_8 OfficerChange + \beta_9 AC_Change + \beta_{10} PriorLn(AF) \\
 & + \beta_{11} AuditPeriod + \beta_{12} Ln(TA) + \beta_{13} ROA + \beta_{14} Loss + Incoming AuditorFE + Year FE \\
 & + Industry FE + u
 \end{aligned} \tag{4}.$$

The dependent variable ($Ln(AF)$) is the natural logarithm of the audit fee paid to the incoming auditor in the first year of the engagement. We expect re-audits to increase the costs of the audit. This would cause the audit fee to increase if the incoming auditor can pass on some of the extra costs to their client. Therefore, we predict a positive coefficient on *Reaudit* in the audit fee model; $\beta_1 > 0$. Eq. (4) includes the same control variables as before to ensure that the correlation between $Ln(AF)$ and *Reaudit* is not capturing risk factors that affect the decision to have a re-audit. In addition, we control for the audit fee in the previous reporting period ($PriorLn(AF)$) because there could be persistence in audit fees from one year to the next. Barua et al. (2020) shows that the audit fee is significantly higher if the incoming auditor is appointed earlier in the fiscal year. We therefore control for *AuditPeriod*, which equals the number of days between the date of the incoming auditor's appointment and the incoming auditor's first audit report, divided by the

number of days between the beginning of the fiscal year and the incoming auditor's first audit report.

Table 5 reports the results for eq. (4). Surprisingly, we find that re-audits do not result in higher audit fees, as evidenced by the insignificant negative coefficients on *Reaudit*. This result suggests the costs of re-audits are borne by incoming auditors rather than passed on to companies in the form of increased fees. Results for the control variables are consistent with prior research. For instance, Table 5 shows that the incoming auditor receives a higher audit fee when the company is larger ($\ln(TA)$), when the company is less profitable (ROA , $Loss$), and when the incoming auditor is appointed earlier in the fiscal year (*AuditPeriod*).

[INSERT TABLE 5 HERE]

Any money paid to the incoming audit firm for performing a re-audit should be disclosed in the audit fee (Barua et al. 2020). However, it is possible that some companies disclose the extra amount as an audit-related other service rather than as part of the standard audit fee. To address this concern, we construct an alternative dependent variable equal to the natural logarithm of the incoming auditor's audit fee plus any fees received by the incoming auditor for other audit-related services. Using this alternative dependent variable, we find in untabulated tests that the coefficients on the *Reaudit* variable remain statistically insignificant (t-stats. = 0.305, 0.540). Thus, we find no evidence that incoming auditors are able to charge higher fees in return for re-auditing their client's past financial statements.

5. Additional analyses

5.1. The timing of the decision to re-do the audit

In this section, we explore whether the decision to re-do the audit is taken before the incoming auditor is appointed or afterwards. Relatedly, we also consider whether the decision is made by the incoming auditor, the company, or (more likely) a combination of both.

One scenario is that the company changes its auditor because the company wants its past financial statements to be re-audited by a new auditor. Under this scenario, the re-audit decision is pre-planned by the company. To evaluate how often this first scenario plays out in the data, we examine each 8-K filing to determine whether the company discloses at the time of the auditor change that the incoming auditor will re-audit the company's past financial statements. Out of our full sample of 5,299 auditor changes, we find only 34 instances (0.6%) of future re-audits being pre-announced in 8-K filings.¹¹ This figure is relatively small compared to actual re-audits performed (748 instances; 14%). Therefore, we do not find strong evidence to support the notion that most re-audits are pre-planned by companies. It is important to note, however, that re-audits are not a required disclosure in 8-K filings. Therefore, the 34 cases we identify represent a lower bound on the total number of pre-planned re-audits.

A second alternative scenario is that the incoming auditor initiates the decision to re-audit the company's past financial statements after being appointed as the company's new auditor. The incoming auditor would likely need to obtain the company's consent before performing the re-audit. Nevertheless, under this alternative scenario, the re-audit decision is primarily initiated by the incoming auditor rather than the company. Three pieces of evidence lend stronger support to re-audits being initiated by incoming auditors rather than companies.

¹¹ Appendix B provides two examples of pre-planned re-audits being disclosed in 8-K filings.

First, if companies were asking incoming auditors to re-do their past audits, we would expect incoming auditors to negotiate higher audit fees in return for the requested service. To the contrary, however, we find that incoming auditors are not able to charge higher fees in return for performing re-audits (Table 5). Second, if re-audits are requested by corporate officers or audit committees, we would expect more requests when the company has new officers or new audit committee members. The reason for this is that new officers and new audit committee members face less of a threat to their personal reputations if incoming auditors discover material misstatements in the company's past financial statements. However, as shown in Table 2, the associations between re-audits and new officers (new audit committee members) are not statistically significant at the 5% level. This finding suggests that re-audits are not generally initiated by corporate officers or audit committees. Third, if re-audits are requested by companies rather than being initiated by incoming auditors, we would not expect to find that re-audits are more likely when the incoming auditor can expect to win more clients from the predecessor auditor (H3). Our results in Table 2 strongly support H3. This finding suggests that re-audits are beneficial to incoming auditors in terms of improving their ability to win clients from the predecessor auditor.

Overall, the above findings suggest that, in the majority of cases, incoming auditors decide to perform re-audits after they are appointed as new auditors. However, this conclusion is somewhat tentative given that there is no regulatory requirement for companies to publicly disclose why their financial statements are being re-audited, who made the decision, and when the decision was made.¹²

¹² Our understanding is that incoming auditors perform re-audits with the consent of client companies. If companies were not consenting and they disagreed with the decision to perform a re-audit, we would expect incoming auditors to be dismissed after performing re-audits. We therefore examine whether there

5.2. Hypothesis 3 (*ClientWin*)

We hypothesize that an incoming auditor is more likely to re-do the audit if the incoming auditor can expect to win more clients from the predecessor auditor (H3). This hypothesis is based on two key assumptions: (1) re-audits lead to more restatements (as shown in Table 3), and (2) restatements cause predecessor auditors to lose clients to other audit firms (as shown in Hennes et al. (2014) and Swanquist and Whited (2015)).

We test H3 using a variable (*ClientWin*) that captures the historical tendency for clients to switch between the incoming and predecessor auditors. The *ClientWin* variable is intended to capture the closeness of fit between the clients of the incoming and predecessor auditors. Thus, we construct *ClientWin* as an *ex ante* measure of expected future client gains. To check that *ClientWin* is a reliable proxy for future client gains, we test its correlation with an *ex post* measure of client gains. The *ex post* measure (*ExpostClientWin*) is the number of clients that switch from the predecessor auditor to the incoming auditor in the 3-year period subsequent to the focal auditor switch, divided by the total number of clients that switch from the predecessor auditor to any other auditor during the same 3-year period.¹³ We find a highly significant positive correlation between the *ex ante* (*ClientWin*) and *ex post* (*ExpostClientWin*) variables (z-stat. = 11.381), suggesting that the *ex ante* variable reliably captures expected client gains that will materialize in the future.

is a positive association between re-audits and subsequent auditor dismissals. We find in an untabulated analysis that re-audits are negatively and insignificantly associated with future auditor dismissals. Therefore, we find no evidence that client companies punish incoming auditors who perform re-audits.

¹³ We use a 3-year window rather than a 5-year window to reduce the number of years that have to be dropped from the end of our sample period. Thus, we examine the period from 2005 to 2019 for this test, which includes 4,715 auditor changes.

Next, we test whether incoming auditors gain more clients from predecessor auditors after they re-audit the work of the predecessor auditors. To test this, we estimate *ex post* regressions in which *ExpostClientWin* is the dependent variable and *Reaudit* is the independent variable of interest. As shown in Table 6, we find highly significant positive coefficients on the *Reaudit* variable in these regressions (t-stats. = 6.277, 4.732). Consistent with H3, this finding implies that incoming auditors win more clients from predecessor auditors during the 3-year period after they re-audit the work of the predecessor auditors.

[INSERT TABLE 6 HERE]

5.3. Big 4 predecessors

Table 2 finds significant negative coefficients on the *PredecessorBig4* variable (z-stats. = -3.356, -5.052), implying that an incoming auditor is less likely to re-do the audit if the predecessor auditor is a Big 4 firm. In this section, we examine whether the strength of this result is different between Big 4 versus non-Big 4 incoming auditors.

Big 4 incoming auditors are likely to perceive that their own quality is as high (or perhaps higher) than predecessor Big 4 firms. In contrast, non-Big 4 incoming auditors may perceive that their own quality is inferior to predecessor Big 4 firms. We therefore expect that the coefficients on *PredecessorBig4* are less (more) negative when the incoming auditor is a Big 4 (non-Big 4) firm. We test this by adding a *PredecessorBig4* × *IncomingBig4* interaction variable to Table 2, where *IncomingBig4* equals one if the incoming auditor is a Big 4 firm (zero otherwise).¹⁴ As expected, an untabulated regression reveals a significant positive coefficient on the *PredecessorBig4* × *IncomingBig4* variable (z-stat. = 2.124). Therefore, the negative association between re-audits and

¹⁴ The main effect of the *IncomingBig4* variable is already captured in Table 2 with the inclusion of incoming auditor fixed effects.

PredecessorBig4 is significantly weaker (stronger) when the incoming auditor is a Big 4 (non-Big 4) firm. This finding suggests that the decision to re-do the audit reflects the incoming auditor's perception of their own quality relative to that of the predecessor auditor.

5.4. *Going-concern opinions*

Table 2 finds significant positive coefficients on *GoingConcern* (z-stats. = 1.834, 2.496), implying that an incoming auditor is more likely to re-do the audit if the predecessor auditor issued a going-concern modification in the company's past audit report. In this section, we examine whether companies demand re-audits in this situation because the company wants the incoming auditor to issue a clean opinion instead of a going-concern modification.

We find that incoming auditors issue going-concern modifications in 6.27% of re-audits (*Reaudit* = 1) and in 4.59% of observations without a re-audit (*Reaudit* = 0). In an untabulated model of going-concern reporting, we find no significant association between the incoming auditor's issuance of a going-concern opinion and re-audits. Therefore, we find no evidence that re-audits are motivated by a company's desire to receive a clean audit opinion from the incoming auditor. This finding is consistent with our inference from Section 5.1 that, in most cases, the decision to perform a re-audit is initiated by the incoming auditor rather than the company.

6. Summary and conclusion

Our study provides the first evidence on the decision to re-audit previous financial statements that were originally signed off by the company's predecessor auditor as being fairly stated. We find that the past financial statements are re-audited by incoming auditors in 14.1% of auditor changes. The re-audit decision is driven by a number of economic factors. First, incoming auditors

perform re-audits when there are concerns relating to the quality of the original audit by the company's predecessor auditor. Surprisingly, the re-audit decision is not strongly affected by indicators of potential problems with the client's financial reporting quality. Second, we find strong evidence that re-audits occur when the incoming auditor can expect to win more clients from the predecessor auditor by finding material misstatements that the predecessor auditor overlooked.

Consistent with re-audits uncovering material misstatements that were missed by the predecessor auditor, we find significantly more future restatements when the incoming auditor re-audits the company's past financial statements. Therefore, re-audits are helpful for providing assurance as to the fair presentation of past financial statements. However, a downside to re-audits is that there are longer delays to the issuance of the company's current year audited financial statements. Surprisingly, we also find that incoming auditors do not receive higher audit fees from their clients when they re-audit the past financial statements. Therefore, the main incentives for incoming auditors to perform re-audits is to reduce their risks of taking on new clients and to improve their chances of winning clients from predecessor auditors.

Overall, our findings indicate that re-audits have important benefits and costs to financial statement users, incoming auditors, and predecessor auditors. Financial statement users benefit from greater audit assurance on the company's past financial figures. However, re-audits are costly to financial statement users because re-audits delay the issuance of the audited financial statements. Incoming auditors benefit from re-audits by reducing the risks associated with taking on new clients. Incoming auditors also have incentives to perform re-audits in order to win clients from predecessor auditors. While incoming auditors can benefit from re-audits, they also bear the additional costs as they are apparently unable to charge clients higher audit fees.

Our study's main contribution is being the first to examine the re-audit phenomenon. As a first exploration of the topic, our study paves the way for future research on the determinants and consequences of re-audits. Our study also contributes to the prior literatures on accounting restatements and audit delays by showing that re-audits are useful for detecting past misstatements and that re-audits lead to delays in the release of audited financial reports.

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APPENDIX A
Variable Definitions

Dependent Variables

<i>Reaudit</i>	= 1 if the incoming auditor issues an audit opinion on the financial statements that were previously audited by the predecessor auditor; = 0 otherwise.
<i>FutureRestate</i>	= 1 if the company restates the financial statements of the final fiscal year audited by the predecessor auditor; = 0 otherwise. We require the restatement to be announced after the incoming auditor is appointed to ensure that this variable captures future restatements that are plausibly affected by the incoming auditor's decision to re-audit the final financial statements of the departing auditor.
<i>Delay</i>	= the natural logarithm of the number of days between the fiscal year end date and the signature date of the incoming auditor. We require the fiscal year end to be the first one after the incoming auditor is appointed.
<i>Ln(AF)</i>	= the natural logarithm of the audit fee paid to the incoming auditor in the first year of the engagement.
<i>Ex post Client Win</i>	= the number of clients switching from the predecessor auditor to the incoming auditor in the 3-year period subsequent to the focal auditor switch, divided by the total number of clients switching from the predecessor auditor to any other auditor in the 3-year period subsequent to the focal auditor switch.

Variables of Interest

<i>AuditConcerns</i>	= 1 if the 8-K filing disclosing the auditor change indicates potential audit concerns related to the company's predecessor auditor; = 0 otherwise. We code the variable as one if any of the following audit concerns are indicated in the 8-K filing: (1) there was a limitation on the scope of the audit performed by the predecessor auditor; (2) the predecessor auditor had problems with its PCAOB registration (i.e., revocation or suspension of registration, deregistration, or no registration); (3) the predecessor auditor was barred by the SEC from conducting public company audits; (4) the predecessor auditor received an SEC inquiry about the quality of one or more audits; (5) there are questions concerning the independence of the predecessor auditor.
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APPENDIX A (cont.)
Variable Definitions

<i>ClientConcerns</i>	= 1 if the 8-K filing disclosing the auditor change indicates potential concerns related to the company's financial reporting; = 0 otherwise. We code the variable as one if any of the following conditions are indicated in the 8-K filing: (1) there was an accounting disagreement between the predecessor auditor and the client; (2) the predecessor auditor concluded that the company's management was not reliable; (3) the predecessor auditor resigned from the engagement; (4) the company committed an illegal act; or (5) the company received an SEC inquiry about its financial reporting.
<i>ClientWin</i>	= the likelihood of the incoming auditor being able to win clients from the predecessor auditor. We measure this variable as the number of client switches between the incoming auditor and the predecessor auditor, divided by the total number of client switches from and to the incoming auditor. The numerator and denominator are measured using a five-year window prior to the focal auditor switch event. Both the numerator and denominator are measured at the audit office level.
<i>ScopeLimitation</i>	= 1 if the 8-K filing disclosing the auditor change indicates that there was a limitation on the scope of the audit performed by the predecessor auditor; = 0 otherwise.
<i>PCAOBRegistration</i>	= 1 if the 8-K filing disclosing the auditor change indicates that the predecessor auditor had problems with its PCAOB registration (i.e., revocation or suspension of registration, deregistration, or no registration); = 0 otherwise.
<i>SECBan</i>	= 1 if the 8-K filing disclosing the auditor change indicates that the predecessor auditor was barred by the SEC from conducting public company audits; = 0 otherwise.
<i>SECInquiryAuditor</i>	= 1 if the 8-K filing disclosing the auditor change indicates that predecessor auditor received an SEC inquiry about the quality of one or more audits; = 0 otherwise.
<i>LackIndependence</i>	= 1 if the 8-K filing disclosing the auditor change indicates that there are questions concerning the independence of the predecessor auditor; = 0 otherwise.
<i>Disagreement</i>	= 1 if the 8-K filing disclosing the auditor change indicates that there was an accounting disagreement between the predecessor auditor and the client; = 0 otherwise.
<i>PredecessorResign</i>	= 1 if the 8-K filing disclosing the auditor change indicates that the predecessor auditor resigned from the engagement; = 0 otherwise.
<i>MgtNotReliable</i>	= 1 if the 8-K filing disclosing the auditor change indicates that the predecessor auditor concluded that the client company's management was not reliable; = 0 otherwise.

APPENDIX A (cont.)
Variable Definitions

Control Variables

<i>IllegalActs</i>	= 1 if the 8-K filing disclosing the auditor change indicates that the client company committed an illegal act; = 0 otherwise.
<i>SECInquiryClient</i>	= 1 if the 8-K filing disclosing the auditor change indicates that the client company received an SEC inquiry about its financial reporting; = 0 otherwise.
<i>PredecessorBig4</i>	= 1 if the predecessor auditor is a Big 4 firm; = 0 otherwise.
<i>PriorRestate</i>	= 1 if the company announces a restatement within a one-year period prior to the appointment of the incoming auditor; = 0 otherwise.
<i>GoingConcern</i>	= 1 if the 8-K filing disclosing the auditor change indicates that that predecessor auditor issued a going concern modification to the company in a recent audit report; = 0 otherwise.
<i>OfficerChange</i>	= 1 if the company changed its CEO or CFO prior to the appointment of the incoming auditor; = 0 otherwise. The event window for the officer change is from the signature date of the final financial statements audited by the predecessor auditor up to the signature date of the first financial statements audited by the incoming auditor.
<i>AC_Change</i>	= 1 if the company changed any of its audit committee members prior to the appointment of the incoming auditor; = 0 otherwise. The event window for the audit committee change is from the signature date of the final financial statements audited by the predecessor auditor up to the signature date of the first financial statements audited by the incoming auditor.
<i>AuditPeriod</i>	= the number of days between the incoming auditor's appointment and first audit report, divided by the number of days between the beginning of the fiscal year and the incoming auditor's first audit report.
<i>PriorDelay</i>	= the natural logarithm of the number of days between the fiscal year end date and the signature date of the incoming auditor. We require the fiscal year end to be the most recent one before the incoming auditor is appointed.
<i>PriorLn(AF)</i>	= the natural logarithm of the audit fee paid to the predecessor auditor in the last year of the engagement.
<i>Ln(TA)</i>	= the natural logarithm of the company's total assets in the most recent year before the auditor change.
<i>ROA</i>	= the company's return on assets (net income divided by total assets) in the most recent year before the auditor change.
<i>Loss</i>	= 1 if the company's net income is negative in the most recent year before the auditor change; = 0 otherwise.

Table 1
Descriptive statistics, correlation matrix, and univariate tests
Panel A: Descriptive statistics

Variable	Obs	Mean	S.D.	P25	P50	P75	Min	Max
<i>Reaudit</i>	5,299	0.141	0.348	0	0	0	0	1
<i>FutureRestate</i>	5,299	0.071	0.256	0	0	0	0	1
<i>Delay</i>	5,173	4.540	0.485	4.290	4.489	4.663	3.135	6.339
<i>Ln(AF)</i>	5,079	11.645	2.191	10.419	11.715	13.162	0	15.558
<i>AuditConcerns</i>	5,299	0.035	0.185	0	0	0	0	1
<i>ClientConcerns</i>	5,299	0.224	0.417	0	0	0	0	1
<i>ClientWin</i>	5,299	0.090	0.216	0	0	0.063	0	1
<i>ScopeLimitation</i>	5,299	0.002	0.046	0	0	0	0	1
<i>PCAOBRegistration</i>	5,299	0.022	0.146	0	0	0	0	1
<i>SECBan</i>	5,299	0.003	0.051	0	0	0	0	1
<i>SECInquiryAuditor</i>	5,299	0.000	0.019	0	0	0	0	1
<i>LackIndependence</i>	5,299	0.009	0.096	0	0	0	0	1
<i>Disagreement</i>	5,299	0.013	0.115	0	0	0	0	1
<i>PredecessorResign</i>	5,299	0.213	0.410	0	0	0	0	1
<i>MgtNotReliable</i>	5,299	0.004	0.060	0	0	0	0	1
<i>IllegalActs</i>	5,299	0.001	0.031	0	0	0	0	1
<i>SECInquiryClient</i>	5,299	0.002	0.039	0	0	0	0	1
<i>PredecessorBig4</i>	5,299	0.314	0.464	0	0	1	0	1
<i>PriorRestate</i>	5,299	0.173	0.378	0	0	0	0	1
<i>GoingConcern</i>	5,299	0.401	0.490	0	0	1	0	1
<i>OfficerChange</i>	5,299	0.297	0.457	0	0	1	0	1
<i>AC_Change</i>	5,299	0.122	0.327	0	0	0	0	1
<i>AuditPeriod</i>	5,079	0.514	0.250	0.311	0.543	0.727	0.048	1
<i>PriorDelay</i>	5,126	4.484	0.440	4.277	4.477	4.644	3.045	6.122
<i>PriorLn(AF)</i>	5,021	11.524	2.404	10.275	11.634	13.173	0	15.573
<i>Ln(TA)</i>	5,299	16.107	3.768	13.728	16.594	18.918	6.230	23.135
<i>ROA</i>	5,299	-9.459	42.376	-1.722	-0.224	0.014	-319.438	0.770
<i>Loss</i>	5,299	0.709	0.454	0	1	1	0	1

Notes: See Appendix A for variable definitions. We winsorize the continuous variables at the 1st and 99th percentiles to mitigate the influence of outliers.

Table 1 (cont.)

Descriptive statistics, correlation matrix, and univariate tests

Panel B: Correlation matrix

Variable	1.	2.	3.	4.	5.	6.	7.	8.	9.	10.	11.	12.	13.	14.	15.	16.
1. <i>Reaudit</i>	1.00	0.11	0.23	-0.28	0.26	0.06	0.07	-0.22	0.00	0.23	0.01	-0.04	-0.16	-0.31	-0.24	0.13
2. <i>FutureRestate</i>	0.11	1.00	0.07	0.03	0.07	0.02	0.00	-0.04	0.04	-0.01	0.02	-0.01	0.05	0.03	0.01	-0.01
3. <i>Delay</i>	0.22	0.07	1.00	-0.47	0.10	0.19	-0.13	-0.49	0.05	0.40	0.10	-0.06	-0.40	-0.57	-0.44	0.32
4. <i>Ln(AF)</i>	-0.23	0.03	-0.27	1.00	-0.14	-0.18	0.08	0.59	0.10	-0.52	0.03	0.19	0.50	0.85	0.53	-0.35
5. <i>AuditConcerns</i>	0.26	0.07	0.09	-0.12	1.00	0.10	0.07	-0.08	0.00	0.05	-0.02	-0.03	-0.09	-0.12	-0.07	0.03
6. <i>ClientConcerns</i>	0.06	0.02	0.15	-0.14	0.10	1.00	0.01	-0.16	0.04	0.10	0.02	-0.01	-0.18	-0.19	-0.13	0.09
7. <i>ClientWin</i>	0.12	0.01	-0.05	-0.03	0.13	0.05	1.00	0.22	-0.02	-0.07	-0.07	-0.03	0.06	0.11	0.07	-0.07
8. <i>PredecessorBig4</i>	-0.22	-0.04	-0.35	0.45	-0.08	-0.16	0.08	1.00	0.02	-0.40	-0.01	0.10	0.37	0.65	0.40	-0.28
9. <i>PriorRestate</i>	0.00	0.04	0.05	0.07	0.00	0.04	-0.02	0.02	1.00	-0.02	0.04	0.02	-0.02	0.08	0.02	0.00
10. <i>GoingConcern</i>	0.23	-0.01	0.30	-0.39	0.05	0.10	-0.01	-0.40	-0.02	1.00	0.03	-0.08	-0.33	-0.62	-0.59	0.40
11. <i>OfficerChange</i>	0.01	0.02	0.11	0.02	-0.02	0.02	-0.07	-0.01	0.04	0.03	1.00	0.19	-0.06	0.00	-0.06	0.07
12. <i>AC_Change</i>	-0.04	-0.01	-0.03	0.14	-0.03	-0.01	-0.05	0.10	0.02	-0.08	0.19	1.00	0.05	0.17	0.09	-0.02
13. <i>AuditPeriod</i>	-0.16	0.05	-0.30	0.44	-0.09	-0.18	0.00	0.37	-0.02	-0.32	-0.06	0.05	1.00	0.48	0.34	-0.26
14. <i>Ln(TA)</i>	-0.32	0.03	-0.40	0.64	-0.13	-0.18	-0.02	0.60	0.09	-0.59	0.00	0.17	0.45	1.00	0.70	-0.45
15. <i>ROA</i>	-0.12	0.02	-0.18	0.19	-0.03	-0.07	0.00	0.15	0.03	-0.19	-0.01	0.07	0.13	0.44	1.00	-0.79
16. <i>Loss</i>	0.13	-0.01	0.22	-0.25	0.03	0.09	-0.03	-0.28	0.00	0.40	0.07	-0.02	-0.25	-0.42	-0.14	1.00

Notes: The Spearman (Pearson) correlations are reported in the upper (lower) diagonal. Statistically significant correlations are shown in **bold** (p-value < 0.05, two-tailed). See Appendix A for variable definitions.

Table 1 (cont.)

Descriptive statistics, correlation matrix, and univariate tests
Panel C: Univariate comparisons

Variable	<i>Reaudit = 0</i>		<i>Reaudit = 1</i>		Difference
	Obs	Mean	Obs	Mean	
<i>FutureRestate</i>	4,551	0.060	748	0.138	0.078***
<i>Delay</i>	4,446	4.496	727	4.808	0.312***
<i>Ln(AF)</i>	4,376	11.846	703	10.394	-1.451***
<i>AuditConcerns</i>	4,551	0.016	748	0.155	0.139***
<i>ClientConcerns</i>	4,551	0.213	748	0.289	0.075***
<i>ClientWin</i>	4,551	0.079	748	0.156	0.077***
<i>ScopeLimitation</i>	4,551	0.001	748	0.007	0.005***
<i>PCAOBRegistration</i>	4,551	0.005	748	0.123	0.118***
<i>SECBan</i>	4,551	0.000	748	0.016	0.016***
<i>SECInquiryAuditor</i>	4,551	0.000	748	0.001	0.001
<i>LackIndependence</i>	4,551	0.009	748	0.011	0.002
<i>Disagreement</i>	4,551	0.014	748	0.012	-0.002
<i>PredecessorResign</i>	4,551	0.203	748	0.277	0.074***
<i>MgtNotReliable</i>	4,551	0.002	748	0.013	0.011***
<i>IllegalActs</i>	4,551	0.001	748	0.003	0.002*
<i>SECInquiryClient</i>	4,551	0.001	748	0.004	0.003*
<i>PredecessorBig4</i>	4,551	0.354	748	0.066	-0.289***
<i>PriorRestate</i>	4,551	0.174	748	0.167	-0.007
<i>GoingConcern</i>	4,551	0.357	748	0.674	0.317***
<i>OfficerChange</i>	4,551	0.295	748	0.310	0.015
<i>AC_Change</i>	4,551	0.127	748	0.090	-0.037***
<i>AuditPeriod</i>	4,376	0.530	703	0.417	-0.113***
<i>PriorDelay</i>	4,413	4.477	713	4.531	0.054***
<i>PriorLn(AF)</i>	4,330	11.733	691	10.217	-1.516***
<i>Ln(TA)</i>	4,551	16.606	748	13.071	-3.534***
<i>ROA</i>	4,551	-7.434	748	-21.784	-14.350***
<i>Loss</i>	4,551	0.684	748	0.861	0.176***

Notes: See Appendix A for variable definitions.

Table 2
Determinants of re-audit

$$Reaudit = \beta_1 AuditConcerns + \beta_2 ClientConcerns + \beta_3 ClientWin + \beta_4 PredecessorBig4 + \beta_5 PriorRestate + \beta_6 GoingConcern + \beta_7 OfficerChange + \beta_8 AC_Change + \beta_9 Ln(TA) + \beta_{10} ROA + \beta_{11} Loss + Incoming Auditor FE + Year FE + Industry FE + u$$

	Expected sign	<i>Reaudit</i>			
		(1) Coeff.	(1) Z-stats	(2) Coeff.	(2) Z-stats
<i>AuditConcerns</i>	H1 +	2.063***	10.081		
<i>ClientConcerns</i>	H2 +	-0.074	-0.702		
<i>ClientWin</i>	H3 +	0.966***	3.734	0.901***	3.343
Audit Concerns:					
<i>ScopeLimitation</i>	+			1.514	1.436
<i>PCAOBRegistration</i>	+			2.513***	8.255
<i>SECBan</i>	+			3.535***	4.635
<i>SECInquiryAuditor</i>	+			1.550	1.344
<i>LackIndependence</i>	+			0.313	0.717
Client Concerns:					
<i>Disagreement</i>	+			-0.186	-0.302
<i>PredecessorResign</i>	+			-0.069	-0.644
<i>MgtNotReliable</i>	+			2.522***	2.609
<i>IllegalActs</i>	+			0.403	0.174
<i>SECInquiryClient</i>	+			1.384*	1.823
Control variables:					
<i>PredecessorBig4</i>	-	-0.696***	-3.356	-0.975***	-5.052
<i>PriorRestate</i>	?	0.189	1.622	0.148	1.248
<i>GoingConcern</i>	+	0.228*	1.834	0.315**	2.496
<i>OfficerChange</i>	+	0.193*	1.900	0.157	1.536
<i>AC_Change</i>	+	0.297*	1.813	0.304*	1.884
<i>Ln(TA)</i>	-	-0.157***	-7.489	-0.178***	-9.079
<i>ROA</i>	-	0.001	1.223	0.001	1.470
<i>Loss</i>	+	0.077	0.544	0.105	0.749
Incoming auditor fixed effects			Yes		Yes
Year fixed effects			Yes		Yes
Industry fixed effects			Yes		Yes
Observations			5,299		5,299
Pseudo-R ²			0.219		0.224

Notes: Standard errors are corrected for clustering on the incoming auditor. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively (two-tailed tests). See Appendix A for variable definitions.

Table 3

Future restatements and re-audit

$$\begin{aligned} \text{FutureRestate} = & \beta_1 \text{Reaudit} + \beta_2 \text{AuditConcerns} + \beta_3 \text{ClientConcerns} + \beta_4 \text{ClientWin} + \beta_5 \text{PredecessorBig4} \\ & + \beta_6 \text{PriorRestate} + \beta_7 \text{GoingConcern} + \beta_8 \text{OfficerChange} + \beta_9 \text{AC_Change} + \beta_{10} \text{Ln(TA)} + \beta_{11} \text{ROA} \\ & + \beta_{12} \text{Loss} + \text{Incoming AuditorFE} + \text{Year FE} + \text{Industry FE} + u \end{aligned}$$

	<i>FutureRestate</i>			
	(1)		(2)	
	Coeff.	Z-stats	Coeff.	Z-stats
<i>Reaudit</i>	1.161***	7.990	1.152***	7.912
<i>AuditConcerns</i>	0.621***	2.792	0.615***	2.738
<i>ClientConcerns</i>	0.130	0.958	0.113	0.829
<i>ClientWin</i>	-0.056	-0.221	-0.057	-0.226
<i>PredecessorBig4</i>	-0.761***	-4.842	-0.760***	-4.796
<i>PriorRestate</i>			0.319**	2.309
<i>GoingConcern</i>	0.103	0.660	0.093	0.594
<i>OfficerChange</i>	0.146	1.231	0.133	1.112
<i>AC_Change</i>	-0.273	-1.508	-0.276	-1.516
<i>Ln(TA)</i>	0.124***	4.297	0.116***	4.005
<i>ROA</i>	-0.000	-0.134	-0.000	-0.094
<i>Loss</i>	0.030	0.221	0.017	0.125
Incoming auditor fixed effects		Yes		Yes
Year fixed effects		Yes		Yes
Industry fixed effects		Yes		Yes
Observations		5,299		5,299
Pseudo-R ²		0.067		0.069

Notes: Standard errors are corrected for clustering on the client company. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively (two-tailed tests). See Appendix A for variable definitions.

Table 4

Audit delay and re-audit

$$Delay = \beta_1 Reaudit + \beta_2 AuditConcerns + \beta_3 ClientConcerns + \beta_4 ClientWin + \beta_5 PredecessorBig4 + \beta_6 PriorRestate + \beta_7 GoingConcern + \beta_8 OfficerChange + \beta_9 AC_Change + \beta_{10} Ln(TA) + \beta_{11} ROA + \beta_{12} Loss + Incoming Auditor FE + Year FE + Industry FE + u$$

	<i>Delay</i>			
	(1)		(2)	
	Coeff.	T-stats	Coeff.	T-stats
<i>Reaudit</i>	0.139***	5.248	0.159***	6.211
<i>AuditConcerns</i>	0.102**	2.323	0.112***	2.602
<i>ClientConcerns</i>	0.077***	4.562	0.066***	4.001
<i>ClientWin</i>	-0.086***	-3.401	-0.064***	-2.634
<i>PredecessorBig4</i>	-0.124***	-8.073	-0.106***	-7.541
<i>PriorRestate</i>	0.081***	5.014	0.035**	2.262
<i>GoingConcern</i>	0.058***	3.507	0.041***	2.618
<i>PriorDelay</i>			0.316***	15.958
<i>OfficerChange</i>	0.092***	6.569	0.103***	7.733
<i>AC_Change</i>	0.007	0.389	0.029*	1.675
<i>Ln(TA)</i>	-0.020***	-5.563	-0.017***	-5.176
<i>ROA</i>	-0.000	-1.464	-0.000*	-1.849
<i>Loss</i>	0.031**	2.173	0.007	0.507
Incoming auditor fixed effects		Yes		Yes
Year fixed effects		Yes		Yes
Industry fixed effects		Yes		Yes
Observations		5,173		5,125
Adjusted R ²		0.233		0.308
Within R ²		0.223		0.299

Notes: Standard errors are corrected for clustering on the client company. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively (two-tailed tests). See Appendix A for variable definitions.

Table 5
Audit fees and re-audit

$$\begin{aligned} \ln(AF) = & \beta_1 Reaudit + \beta_2 AuditConcerns + \beta_3 ClientConcerns + \beta_4 ClientWin + \beta_5 PredecessorBig4 + \beta_6 \\ & PriorRestate + \beta_7 GoingConcern + \beta_8 OfficerChange + \beta_9 AC_Change + \beta_{10} PriorLn(AF) + \beta_{11} AuditPeriod \\ & + \beta_{12} Ln(TA) + \beta_{13} ROA + \beta_{14} Loss + Incoming Auditor FE + Year FE + Industry FE + u \end{aligned}$$

	<i>Ln(AF)</i>			
	(1)		(2)	
	Coeff.	T-stats	Coeff.	T-stats
<i>Reaudit</i>	-0.007	-0.100	0.011	0.153
<i>AuditConcerns</i>	-0.299*	-1.896	-0.296*	-1.915
<i>ClientConcerns</i>	0.086	1.484	0.079	1.359
<i>ClientWin</i>	-0.234**	-2.159	-0.233**	-2.139
<i>PredecessorBig4</i>	0.137*	1.891	0.080	1.080
<i>PriorRestate</i>	0.141**	2.134	0.132**	2.003
<i>GoingConcern</i>	0.067	1.453	0.057	1.238
<i>OfficerChange</i>	0.106**	2.051	0.094*	1.812
<i>AC_Change</i>	0.217***	2.967	0.221***	3.013
<i>PriorLn(AF)</i>			0.092***	4.896
<i>AuditPeriod</i>	1.394***	10.725	1.366***	10.510
<i>Ln(TA)</i>	0.275***	24.729	0.245***	18.947
<i>ROA</i>	-0.004***	-8.874	-0.004***	-7.722
<i>Loss</i>	0.212***	3.242	0.199***	3.041
Incoming auditor fixed effects		Yes		Yes
Year fixed effects		Yes		Yes
Industry fixed effects		Yes		Yes
Observations		5,079		5,021
Adjusted R ²		0.471		0.472
Within R ²		0.457		0.460

Notes: Standard errors are corrected for clustering on the client company. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively (two-tailed tests). See Appendix A for variable definitions.

Table 6

Ex post client gains and re-audit

$$Ex\ post\ Client\ Win = \beta_1 Reaudit + \beta_2 AuditConcerns + \beta_3 ClientConcerns + \beta_4 ClientWin + \beta_5 PredecessorBig4 + \beta_6 PriorRestate + \beta_7 GoingConcern + \beta_8 OfficerChange + \beta_9 AC_Change + \beta_{10} Ln(TA) + \beta_{11} ROA + \beta_{12} Loss + Incoming\ Auditor\ FE + Year\ FE + Industry\ FE + u$$

	<i>Ex post Client Win</i>			
	(1)		(2)	
	Coeff.	T-stats	Coeff.	T-stats
<i>Reaudit</i>	0.077***	6.277	0.050***	4.732
<i>AuditConcerns</i>	0.030	1.287	-0.012	-0.646
<i>ClientConcerns</i>	0.019**	2.209	0.004	0.513
<i>PredecessorBig4</i>	0.042***	4.693	0.010	1.201
<i>PriorRestate</i>	-0.002	-0.172	-0.000	-0.041
<i>GoingConcern</i>	-0.027***	-2.994	-0.024***	-3.052
<i>OfficerChange</i>	-0.032***	-4.447	-0.019***	-2.944
<i>AC_Change</i>	-0.012	-1.217	-0.008	-0.844
<i>ClientWin</i>			0.456***	19.020
<i>Ln(TA)</i>	-0.005***	-2.660	-0.002	-1.077
<i>ROA</i>	0.000	1.291	0.000	0.522
<i>Loss</i>	0.005	0.564	0.010	1.247
Incoming auditor fixed effects		Yes		Yes
Year fixed effects		Yes		Yes
Industry fixed effects		Yes		Yes
Observations		4,715		4,715
Adjusted R ²		0.057		0.218
Within R ²		0.048		0.211

Notes: Standard errors are corrected for clustering on the client company. ***, **, and * denote statistical significance at the 1%, 5%, and 10% levels, respectively (two-tailed tests). See Appendix A for variable definitions.

APPENDIX B

Two examples of re-audits disclosed in 8-K filings

1. Auditor change for GROW CAPITAL, INC. disclosed on March 14, 2017

Item 4.01 Change in Registrant's Certifying Accountant

On March 9, 2017, Grow Condos, Inc. (the "Company") engaged L J Soldinger Associates LLC ("Soldinger") as the Company's new independent registered public accounting firm. The engagement was approved by the Audit Committee. During the fiscal years ended June 30, 2016 and 2015 and through the date of this Current Report on Form 8-K, neither the Company nor anyone acting on its behalf consulted Soldinger with respect to (i) the application of accounting principles to a specified transaction, either completed or proposed, nor the type of audit opinion that might be rendered on the Company's financial statements, and neither a written report was provided to the Company nor oral advice provided that Soldinger concluded was an important factor considered by the Company in reaching a decision as to any accounting, auditing or financial reporting issue; or (ii) any matter that was the subject of a disagreement or a "reportable event" as described in Items 304(a)(1)(iv) and (v), respectively, of Regulation S-K.

On December 23, 2016, the Company filed an 8-K/A which stated that On December 22, 2016, the Company was advised by the staff of the Securities and Exchange Commission that on December 20, 2016 the Public Company Accounting Oversight Board issued Release No. 105-2016-054 wherein it barred Scrudato from acting as independent auditor for public companies. Because Mr. Scrudato had his registration revoked by his regulator, there will be no attachment to this Form 8-K reflecting his opinion on this matter. In addition, our June 30, 2016 year-end financial statements will be re-audited by Soldinger and presented together with the upcoming audit for the year ended June 30, 2017 when we file our next Form 10-K. Should Soldinger come to the conclusion that the results of that period require adjustment, we will also amend and update our previously issued Form 10-Q's subsequent to the year ended June 30, 2016. At this time, we do not believe that any re-statement will be likely to occur.

2. Auditor change for GREENWAY TECHNOLOGIES INC disclosed on September 30, 2015

Item 4.01 Changes in Registrant's Certifying Accountant.

On September 17, 2015, the Securities and Exchange Commission issued an order instituting a public administrative and cease-and-desist order against Terry L. Johnson, CPA, the previous auditor for the registrant who resigned as the registrant's auditor on May 6, 2015. On July 7, 2015, the PCAOB withdrew the registration of Terry L. Johnson, CPA. As a result of the Commission's order, Terry L. Johnson, CPA was denied the privilege of appearing or practicing before the Commission for failing to comply with PCAOB auditing standards. Terry L. Johnson, CPA was also cited for the issuance of audit reports that falsely stated that Terry L. Johnson, CPA conducted its audits in accordance with the standards of PCAOB.

On September 24, 2015, the registrant was made aware of the Commission's order dated September 17, 2015, against Terry L. Johnson, CPA. Due to the Commission's order, the

registrant can no longer include the audit reports of Terry L. Johnson, CPA in the registrant's filings with the Commission.

The registrant has made the decision to have its financial statements for the years 2012, 2013, and 2014, re-audited by its current auditor, Patrick D. Heyn, CPA, P.A. who was engaged by the registrant on June 3, 2015. If the registrant should conclude, after the re-audits of its financial statements for the years 2012, 2013, and 2014, that its financial statements for the years 2012, 2013, and 2014, should no longer be relied upon because of an error in such financial statements as addressed in FASB ASC Topic 250, Accounting Changes and Error Corrections, the registrant will make a prompt announcement on Form 8-K as required by the rules of the Commission.