

The Influence of the Affiliated Banking Expert (Representative of Lenders) on The Board of Directors Regarding Accounting Conservatism in Non-Financial Companies.

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Received Date: 12-11-2023; Accepted Date: 15-12-2023; Publication Date: 21-01-2024

Abstract

This study aims to investigate whether the presence of a subsidiary banking representative on a borrowing company's directors' board affects the level of accounting conservatism in its financial statements. This study also explores the effectiveness of the lender control mechanism in reducing the imbalance of information between the borrowing company and long-term creditors (lenders). Consequently, lenders will decrease their desire for control offered by conservatism. Meanwhile, the model proposed by [Basu \(1997\)](#) was used to measure conservatism by examining the asymmetric timing of profits. Three measures devised by critics of accounting were employed to assess the level of control exerted by bankers on the board of directors (variable control). First: [LaFond and Watts \(2008\)](#) "measures of the characteristics of the company associated with the conservatism ratio of market value to book, leverage, litigation risk, and size of the company". Second: [Ahmed and Duellman \(2007\)](#) "measures of corporate governance characteristics associated with conservatism, including board independence, board size, separation of CEO and chairman roles, average external directors, internal director ownership, external director ownership, and institutional ownership." Third, [Kroszner and Strahan \(2001\)](#) and [Gilson \(1990\)](#) "factors associated with the likelihood of having commercial

How to cite (APA):

AL Anssari, M. A., Nimr, H. S., Al-Tamimi, S. A. (2024). The Influence of the Affiliated Banking Expert (Representative of Lenders) on The Board of Directors Regarding Accounting Conservatism in Non-Financial Companies. *International Journal of Instructional Cases*, 8(1), 73-95.



**International Journal
of Instructional Cases**

bankers on corporate boards, such as stock return volatility, equity return volatility box, tangible assets, trade credit ratings, capital structure, bankruptcy risk, and industry membership." The findings demonstrate that the lender control mechanism effectively addresses the issue of information asymmetry, thereby mitigating the debt agency problem. Consequently, a conservative approach significantly reduces lenders' need for monitoring. Furthermore, the analysis revealed that companies that have a member from the banking industry on their board of directors exhibit a lower level of accounting conservatism compared to companies without any banking representation on their board. Academic research suggests that lending relationships can have a similar impact on conservatism. This means that when lenders have more control, conservatism tends to decline.

Introduction

Having a banker with financial and banking experience, like executives on the board of directors (BoFD) of companies, is a common way to ensure effective lender monitoring. [Fama and Jensen \(1983\)](#) provided a summary of the roles of the Board of Directors (BoFD) in managing and overseeing decision-making processes. Thus, when a banking representative assumes a position on the Board of Directors of the borrowing corporation, they will possess the authority and influence to actively engage in and shape the decision-making process. There are two different forms of banking representation (BoFD). First, the affiliated banker on board (AFB). Specifically, the banker serves as the representative of the lending bank to the company, maintaining a simultaneous relationship with the company. Additionally, the banker who is not associated with any specific bank and does not have a credit relationship with the company. The lending bank may request the appointment of a subsidiary representative to the board of directors in light of a potential financial crisis for the borrowing company. This is because having a subsidiary representative on the board provides valuable insight into the industrial developments of the borrowing company. Their proximity to events allows them to anticipate and address any negative news or crises that the company may encounter.

One possible method of appointing a subsidiary representative is when the borrowing company specifically requests it. In certain cases, companies with significant debts may choose to bring in experienced individuals and appoint them as board members ([Sisli-Ciamarra, 2012](#)). An illustrative example is the utilisation of banking experience, which encompasses extensive years of work in various banks, particularly in executive roles held by individuals throughout their tenure. Companies value the presence of these bankers on their boards not only for their financial and banking expertise, but also for their extensive network of relationships in the banking sector. This network can be beneficial in managing debts and securing new loans. In terms of the advantages gained by the lender, having the subsidiary representative present ensures that the information obtained by the lending bank accurately reflects the current

financial state of the company. It also provides a reliable outlook on the company's future, including the timing and amount of expected cash flows. This information is far superior to what the bank can gather from the borrowing company's periodic financial statements. As a result, they are more dependable (Stearns & Mizruchi, 1993).

A major concern regarding debt agencies is the asymmetry of information between the borrower and the lender. This is because borrowers have more knowledge than lenders (Gârleanu & Zwiebel, 2008). Therefore, it can be assumed that once the information imbalance is resolved, lenders will be able to enter into debt agreements with borrowers, having a comprehensive understanding of the credit score of the borrowing company. This study aims to address and mitigate the issue of information asymmetry by examining the most suitable methods observed in area studies. One such method is the submission of financial statements with a conservative approach to secure debt contracts, as the beginning of the 3rd millennium witnessed the emergence of "the four justifications for conservatism, contracting, litigation, regulation and taxation" (Watts, 2003b). "Accounting conservatism is one of the mechanisms for contracting major debts" (Basu, 1997; Mora & Walker, 2015; Ruch & Taylor, 2015; Watts, 2003b).

Mora and Walker (2015) contend that: "Accounting conservatism also leads to lower book values compared to the economic values of net assets due to lower verification requirements to recognize losses compared to profits". Considering this, the conservative approach in accounting can potentially facilitate the violation of debt charters. These charters heavily rely on accounting data, enabling debt holders to proactively protect their interests through measures like debt renegotiation or restructuring (Ahmed et al., 2002; Nikolaev, 2010; Watts, 2003b). Given that providing conservative financial statements to lending banks is an early indicator of the solvency of borrowing companies, it becomes crucial for debt holders to emphasise the need for accounting conservatism. This ensures that credit decisions are made with precautionary measures in place to protect their interests. Given that the accounting system's outputs are critical for obtaining debt contracts, the concept of conservatism has evolved to give lenders a conservative approach to credit assessment. This is achieved through the concept of (temporary), which involves recognising revenues as soon as they are realised and accounting for expected losses (Watts, 2003b). According to Zhang (2008) and Ahmed et al. (2002), there is a strong correlation between conservatism and reduced debt costs. Additionally, Beatty et al. (2008) and Nikolaev (2010) suggest that debt contraction can also impact conservatism. This study highlights a topic currently under debate in the academic field. Some argue that conservatism enhances the effectiveness of debt contracts, while others argue that it diminishes it. Specifically, this debate focusses on the inclusion of control rights for lenders in debt contracts during crises and financial defaults. This approach is considered a potential solution to address information asymmetry.

Problem Statement

This study aims to assess the effectiveness of the lender monitoring mechanism through the banker's participation in the Board of Directors (BofD), in relation to the importance of accounting conservatism. Previous studies in this field have not reached a clear agreement on the impact of having a lender's representative on the board of directors. Several studies have shown varying levels of conservatism in the financial statements of borrowing companies when a banker serves on the board of directors. One study found a low level of conservatism (Erkens et al., 2014), while another study found a high level of conservatism (Bhaskar et al., 2017; Hu & Jiang, 2019; Jain et al., 2020).

Significance of the Study

Based on multiple studies (Ball et al., 2000; Ball et al., 2008; Ball et al., 2003; Barth et al., 2001; Watts, 2003a; Watts, 2003b), it has been determined that conservatism is a significant indicator of accounting quality. It is "an effective contracting tool, as it requires more stringent verification criteria for recognizing profits than in the criteria for recognizing losses" (Watts, 2003a). Therefore, companies are making efforts to present cautious financial statements in order to enhance their eligibility for debt contracts. Nonetheless, Ball and Shivakumar (2005) argue "conservatism provides biased and unfair results, when it defers the recognition of current revenues to the next period, whilst the recognition of expenditures for the next period is accelerated and recognized in the present period." Ball and Shivakumar's perspective highlight that conservatism distorts information, as evidenced by the literature's mechanism (Anssari & Al-Tamimi, 2023). Given the presence of information asymmetry between lenders and borrowers, the agency's debt problem leads to a conservative approach in financial statements. This raises the question of whether a lender control mechanism can effectively address the information asymmetry and potentially reduce the need for conservatism in financial statements driven by debt contracting. This study will provide definitive answers, particularly that being cautious in financial statements is not the sole solution to the issue of information imbalance between borrowers and lenders. This is because monitoring lenders could potentially be an alternative approach with greater efficacy.

Objectives of the Study

This study seeks to contribute to the existing literature by examining the influence of banking experts on the conservatism level in the financial statements of borrowing companies. Specifically, it focusses on the impact of the presence of a banking expert on the board of directors (BofD) in an environment where the lender control mechanism is active. This study addresses a gap in the current research, as this particular impact has not been extensively explored in this field before. This study also seeks to evaluate and critically discuss the patterns identified in previous studies

conducted in the last decade. These studies have produced conflicting or inconclusive results regarding the impact of the lender control mechanism through the subsidiary representative on accounting conservatism. Some notable examples include the works of [Jain et al. \(2020\)](#), [Hu and Jiang \(2019\)](#), [Bhaskar et al. \(2017\)](#), [Bonetti et al. \(2017\)](#), and [Erkens et al. \(2014\)](#). By examining these studies, we hope to gain a deeper understanding of the ongoing debate and the various perspectives presented.

Research Contribution

This study holds significant value for the field of accounting conservatism as it confirms the effectiveness of the lender control mechanism. This mechanism, represented by a representative from a subordinate bank on the board of directors (BofD), helps reduce the information imbalance between the lending bank, the borrowing company, and the need for conservative debt contracts. Furthermore, this study delves into the discussion and research surrounding the value of conservatism in debt contracting. The motivation for this debate stems from the perspective put forth by [Erkens et al. \(2014\)](#), stating that "few U.S. companies choose alternative mechanisms to monitor lenders because alternative mechanisms are expensive and contracting debt under accounting conservatism is a cost-effective solution to reduce the debt agency problem for the vast majority of companies."

Hypothesis Development

In order to actively contribute to the management of the borrowing company, lending banks often appoint a banker affiliated with them to serve on the board of directors. This arrangement can be negotiated or activated in times of crisis as specified in the debt contract. This study is conducted with the hypothesis that when a representative from the lending bank participates in the company management and holds a seat on its Board of Directors, it will significantly enhance and strengthen the relationship between the borrowing company and the lending bank. This is because being in close proximity to the main source of information and having an effective supervisory role can greatly reduce information asymmetry and save the bank from the costs and efforts of gathering information about the borrowing company. The monitoring of lenders will be highly effective for the borrowing company, as it will greatly benefit by securing debt contracts that are tailored to its specific circumstances. Considering the argument provided above, the research hypothesis is that companies that have an affiliate banker have less conservative accounting than companies that do not have an affiliate banker. This study presents findings based on a dataset collected from non-financial companies in UAE financial markets. It examines the influence of having a representative banker from a bank that has a lending relationship with the borrowing company.

Literature Review

The addition of a banking expert to the Board of Directors brings significant

advantages to companies. On one hand, the non-affiliated banker contributes valuable banking and financial expertise. On the other hand, the affiliated banker not only brings their expertise in these areas but also provides exceptional support during the borrowing process, thanks to their familiarity with all the necessary creditworthiness information. However, there are those who view conservatism as a means of incurring debts (Basu, 1997; Mora & Walker, 2015; Ruch & Taylor, 2015; Watts, 2003b). The accounting literature also indicates that the presence of a banker affiliated with the board of directors of the borrowing company can impact the desire for accounting conservatism. One particular study conducted in Australia is Erkens et al. (2014), which found that "affiliated bankers, or executives of lending banks working on the boards of directors of borrowing companies, can stand as a private channel for providing lending banks with the creditworthiness of borrowing companies, leading to low conservatism accounting." To minimise the costs related to accounting conservatism, affiliate bankers assist the borrowing firms (Bhaskar et al., 2017; Chava & Roberts, 2008; Gao et al., 2017; Kravet, 2014; Nini et al., 2009).

A study conducted in Europe by Bonetti et al. (2017) found a positive correlation between the presence of a non-affiliated banker (or representative of non-lending banks) and accounting conservatism. According to Bonetti and other scholars, having a banker affiliated with the board of directors can greatly impact the push for accounting conservatism. This is because it allows for easier communication and information sharing between the lending bank and the borrowing company. Prior studies (Chemmanur et al., 2019; Chou & Feng, 2019; Huang et al., 2014) have shown that managers' practical experience is associated with favourable organisational outcomes and, as a result, reduced profit management (Faleye et al., 2018; Wang et al., 2015). The actions and perspectives of banking professionals who frequently serve on boards have a significant impact on the enhancement of the board's oversight role, leading to an increase in accounting conservatism (Madhi et al., 2023). The findings of this study provide evidence in favour of the hypothesis that boards with greater strength tend to generate more conservative profits (Ahmed & Duellman, 2007; Lara et al., 2009). The previous discussion brought us face-to-face with the intricate nature of debt agency, where the clash of interests between shareholders and long-term creditors becomes evident. Debt contracting has evolved to address the issue of debt agency, serving as a crucial tool in distributing control rights between borrowers and lenders. Specifically, the procedure of transferring control rights by means of agreement violations to the lenders themselves, enabling these lenders to assertively safeguard their own interests (Black & Cox, 1976; Jensen & Meckling, 2019).

A study conducted by Nguyen et al. (2020) challenges the findings of studies conducted by Erkens et al. (2014) and Bonetti et al. (2017). Regarding this matter, the present study suggests that the two studies did not provide a definitive explanation regarding the company's use of a subsidiary banker or a non-affiliated banker. Furthermore, the two studies did not address the historical practical experience of the

affiliated banker and their potential expertise in debt and financial markets. This expertise could provide valuable insights into the necessary level of accounting conservatism needed to effectively monitor debt.

Nguyen and other critics (2020) analysed the role of banking expertise for the (BoFD) within the framework of accounting conservatism. The study presented a novel way to assess the banking experience at the (BoFD) by utilising the extensive practical knowledge of individual managers, which is considered crucial for corporate success. Nguyen and other critics (2020) argue that having a banker on the Board of Directors is unnecessary. However, they still believe that it is crucial for the banking experience to be overseen by someone with expertise in the field. Thus, the study conducted by Nguyen and other critics (2020) focused on various aspects of the banking experience. They also offer several reasons for why they anticipate that the banking experience in the (BoFD) would have a significant impact on accounting conservatism. Specifically, experienced managers in the banking sector can provide the (BoFD) with valuable insights regarding the demand for accounting conservatism. This information is crucial in the market for borrowing companies to start reducing accounting conservatism and, consequently, avoid the costs associated with conservatism. Most notably, the study discovered a strong link between conservative accounting practices and the inclusion of individuals with banking experience on the board of directors. Some experts argue that conservatism can help address the debt agency problem, but it comes with a high cost. When agreements are violated, it can have a significant negative impact on the borrowing companies (Beneish & Eric, 1993; Nini et al., 2009; Roberts & Sufi, 2009). In addition, a conservative approach could potentially lead to a scenario where contract breaches occur without justification, resulting in unwarranted warning signs and unnecessary expenses for all parties involved (Gigler et al., 2009).

Several empirical studies have found that a significant number of American companies have bankers serving on their boards. In a study conducted by Kroszner and Strahan (2001), it was discovered that 32% of larger organisations had a certain percentage. Similarly, Santos and Rumble (2006) found that 25% of non-financial companies in their S&P 500 sample had individuals with a banking background serving on their boards. As per the research conducted by Kroszner and Strahan (2001), it was found that certain bankers are associated with banks that have a lending relationship with the company, such as subsidiaries. However, the majority of these bankers represent banks that may not necessarily provide loans to the company (i.e., non-subidiaries). These independent bankers primarily provide financial expertise, while affiliated bankers also enhance the lending relationship. One advantage of this enhanced lending relationship is that borrowers may enjoy greater access to credit and potentially lower interest rates on loans. Bankers in this field can also be advantageous to borrowers as they often offer loans to other businesses within the same industry. Meanwhile, borrowers incur significant costs when dealing with a representative from an affiliated bank for two reasons. First, companies in the academic sector may

experience a decrease in operational flexibility due to increased monitoring. Additionally, banks with a representative role can leverage their access to information to potentially gain advantages from borrowers (Rajan, 1992).

As the financial and banking literature conducted by Sisli-Ciamarra (2012) points out,

Once a banker joins the board of directors, the bank begins to lend to the company on better terms, with a lower cost of monitoring, a decrease in information asymmetry leads to a reduction in the use of collateral and undertakings, and a decrease in the cost of monitoring translates into lower loan rates. Conversely, if a bank gets representation on the board of directors after it has already provided loans to a company.

According to the findings of the Ciamarra study, there was no improvement in the parameters of the loan contract and debt ratios. This finding aligns with Gilson's (1990) theory, suggesting that creditors actively participate in business boards during challenging financial periods.

Research Methodology and Data Collection Sources

This study employs a descriptive analytical approach to identify the appropriate research variables. The necessary data is then collected from the financial reports of the sampled companies. The research hypotheses are examined by calculating means and standard deviations, and statistically analyzing the data using the Statistical Program for the Social Sciences (SPSS).

The study analysed financial reports of various firms obtained from their websites. These reports served as the basis for creating tables to collect research data over a span of ten years, from 2012 to 2021. In addition, the closing prices and the quantity of shares traded were obtained from the yearly reports of the Capital Market Authority for Securities. Microsoft Excel is commonly utilised for gathering and condensing data, which is then inputted into SPSS V.22 to obtain the study's variables.

Population and Sample of Study

The businesses registered in the financial market between 2012 and 2021 in the UAE form the study population. The annual financial statements of the companies sampled in the study included historical data, which were readily available in their information sources. The research was conducted on a final sample of (57) companies, which were distributed across six different sectors. Specifically, the industrial sector, the real estate sector, the transportation sector, the services sector, the energy sector, and the communications sector. The financial sectors, including banking and insurance, were not included in the study due to their unique characteristics and intricate financial instruments. The focus of the study was specifically on lending operations between commercial banks and non-financial companies.

Study Variables

In this study, the focus is on the linked banking expert (loan representative) as the independent variable, while conditional accounting conservatism and the control serve as the dependent variables.

These factors are explained as follows:

Measuring The Monitoring of The Bankers in the Board of Directors (The Independent Variable)

AFB, a dummy variable that really equals one when a business has an associated banker on its board and zero otherwise, was used to quantify the monitoring of bankers on the (BoFD). In measuring the independent variable (representative of lenders), the researcher relied on three main groups, each group containing financial ratios and indicators, as follows:

1. Measures of firms' characteristics associated to conservatism, which are: the market's ratio value to book value, financial leverage (total debts to total assets), litigation risk (a company that has any judicial requirements of any kind takes the number 1 and otherwise zero), and the company size (the natural logarithm of the total assets).
2. Measures of corporate governance characteristics in a conservative context encompass board independence (a binary variable indicating whether the CEO also serves as chairman of the board), board size, the separation of the CEO and chairman roles, and the average number of outside directors. Other measures include institutional ownership (common stock held by investors that is attributable to the total number of outstanding common shares) and inside director ownership (common stock held by inside directors is proportional to total common stock outstanding)
3. Factors influencing the presence of commercial bankers on company boards include capital structure, bankruptcy risk (using the Altman model), industry membership (a binary variable indicating whether the firm belongs to the industry sector), asset tangibility (the ratio of fixed assets to total assets), and trade credit ratings (a dummy variable equal to one when the firm has a business credit rating, and zero otherwise That).

Conditional Accounting Conservatism (Dependent Variable)

The Basu model quantifies conditional conservatism, which relates to the timing asymmetry of profits in response to positive and negative news. [Basu \(1997\)](#) introduces a model for measuring conditional conservatism. Basu explains that conditional conservatism arises due to the need for accurate identification of anticipated economic

losses and gains, which is facilitated by asymmetric verification. This concept is reflected in the understanding of anticipated economic losses in the present timeframe, while foreseeable economic gains are acknowledged in future periods. This concept emphasised the economic role in determining gains and losses in companies and underscored the significance of timing in their recognition. This is referred to as conditional conservatism. Stock returns tend to respond more swiftly to negative news compared to positive market returns when the accounting system is cautious. A dummy variable was set to one if the firm experienced negative stock returns and zero in all other cases, which was used to examine conditional conservatism. Here is a [Table 1](#) displaying the indicators used to measure conditional accounting conservatism.

Table 1: Measuring Conditional Accounting Conservatism.

M	Variable	Measurement Method
1	Earnings	Earnings before extraordinary items are attributable to the market value of equity at the beginning of the year.
2	Rat	The 12-month buy-and-hold return during a fiscal year.
3	DR	Equals one when Ret is negative, zero otherwise

Study Hypotheses

This study aims to assess how the presence of a banking expert influences the level of accounting conservatism among company boards of directors. The following theories were developed to fulfil the purpose of the current investigation:

The First Hypothesis: There are no effect of company characteristics measures on conditional accounting conservatism in the Emirati companies in the study sample.

The Second Hypothesis: There is no effect of measures of corporate governance characteristics on conditional accounting conservatism in the Emirati companies in the study sample.

The Third Hypothesis: There is no effect of the factors associated with the possibility of the presence of commercial bankers on companies' boards of directors on conditional accounting conservatism in the Emirati companies in the study sample.

The Statistical Methods

To test the study hypotheses, the next statistical methods were used:

1. Descriptive statistics were employed to analyse a dataset, arranging, categorising, summarising, and presenting it in the form of tables. Additionally, various statistical measures were computed to elucidate one or more variables within a population.
2. The research sample consists of Emirati enterprises, and the focus is on the conditional accounting conservatism. Multiple regression analysis is employed to examine the influence of the independent variable, which is the expertise of the

banking professionals, on the dependent variable (representative of lenders).

Statistical Hypothesis Tests: The Results

Descriptive Analysis of the Study Variables

The variables used in the hypothesis testing models are presented in [Table 2](#), along with the necessary descriptive statistics to analyse their attributes:

Table 2: Results of Descriptive Statistics for the Study Variables.

Variable	Mean	St. Div	Max	Min
Measures of company characteristics associated with accounting conservatism				
Market to book value ratio	2.381	5.756	6.104	0.087
Financial Leverage	0.816	3.761	1.983	0.417
Litigation Risk	0.506	0.500	1.00	0.000
Company size	7.447	1.135	9.753	4.543
Measures of corporate governance characteristics associated with accounting conservatism				
Independence of the Board of Directors	0.768	0.417	1.000	0.000
Board size	1.643	0.431	2.846	1.079
Ownership of the internal director	0.045	0.214	0.130	0.002
Ownership of the outside director	0.001	0.008	0.082	0.001
Institutional ownership	0.547	0.992	0.735	0.0331
Factors associated with the possibility of having commercial bankers on corporate boards				
Volatility of stock returns	0.261	0.364	1.257	0.046
The volatility of stock returns square	0.081	0.176	2.414	0.002
Tangible assets	0.115	0.674	0.548	0.065
Business credit ratings	0.113	0.352	1.000	0.000
Capital structure	0.016	0.178	0.432	0.011
Bankruptcy risks	0.061	0.053	4.343	0.003
Industry membership	0.140	0.347	1.000	0.000

[Table 2](#) presents the key descriptive statistics for the study variables. The table indicates that the average values of the company characteristics measures related to conservatism were higher than the other measures. The research sample's enterprises experienced a rise in stock prices, as shown by the average market value to book value of 2.381 and a standard deviation of 5.756. In addition, the significant debt levels of numerous companies in the sample played a role in the average financial leverage of 0.816. The table highlights the variation in company sizes, categorised as large, medium, and small. The average company size was 7.447, with a standard deviation of 1.135.

The board of directors' independence and size had mean values of 0.768 and 1.643, respectively, in the descriptive statistics for the corporate governance traits associated

with accounting conservatism. The standard deviations for each were 0.417 and 0.431. Additionally, it showed that the proportion of common shares held by internal managers increased at the expense of external managers. The institutional ownership mean is 0.547 with a standard deviation of 0.992. The results indicate that the study sample companies exhibit strong governance.

Table 2 presents the key descriptive statistics for the factors related to the presence of commercial bankers on corporate boards of directors. The average volatility of stock returns and the square of stock returns volatility were 0.261 and 0.081, respectively. Additionally, there was a decrease in the proportion of fixed assets compared to total assets. The average value of the asset's tangible component was 0.115, with a standard deviation of 0.674. It became evident that a select few companies in the study sample possess a strong credit rating. The researcher explains that the variation in the sectors of the study sample may be the reason for this finding. The mean for the commercial credit ratings variable was calculated to be 0.113, with a standard deviation. The mean bankruptcy risk of the sample companies is 0.061, with a standard deviation of 0.053. This indicates that the majority of the companies in the sample demonstrate high efficiency and are likely to have long-term continuity.

Results of Descriptive Statistics for Companies That Have a Loan Representative

The T-test was employed in this study to evaluate the significance of variations in conditional accounting conservatism metrics among businesses with and without associated banking experts (AFBs).

Table 3: Significance of Differences Between Companies in Measures of Accounting Conservatism.

Variables	companies that have AFB (N=35)			companies that don't have AFB (N=22)			F. Test	Sig
	Mean	Median	St. Div	Mean	Median	St. Div		
Earnings	0.048	0.041	0.039	0.035	0.022	0.062	1.446	0.229
Rat	0.269	0.173	0.017	0.238	0.126	0.019	1.366	0.243
DR	0.360	0.114	0.021	0.358	0.176	0.033	1.545	0.214

The findings from **Table 3** indicate that there are no significant variations observed between companies with an affiliated banking expert (AFB) and those without, in terms of scalpel accounting conservatism indicators. This includes the average ratio of profits before unexpected items to total. In companies with a loan representative, the book value was (0.048), whereas in companies without a loan representative, the percentage was (0.035). The F value reached 1.446 at a significance level of 0.229, suggesting that the observed differences were not statistically significant. Although companies with a banking expert affiliation had slightly higher conditional accounting conservatism indicators compared to those without, the difference was not statistically significant. This implies that variations in stock returns, particularly negative ones, are

unlikely to be the main factor behind any differences in conservatism.

The next three tables display the results of descriptive statistics for the indicators measuring the independent variable (representing AFB loans), as follows:

Table 4: Significance of Differences Between Companies in Company Characteristics Related to Conservatism.

Variables	companies that have AFB (N=35)			companies that don't have AFB (N=22)			F. Test	Sig
	Mean	Median	St. Div	Mean	Median	St. Div		
MTB	2.039	1.632	2.417	3.883	3.708	4.975	4.151	0.036
Financial Leverage	0.819	0.749	0.912	0.869	0.739	1.549	1.400	0.237
Litigation Risk	0.473	0.442	0.504	0.521	0.479	0.500	0.982	0.471
Company size	7.304	7.149	1.065	7.508	7.246	1.154	1.524	0.198

The data in [Table 4](#) indicates that businesses that do not have a loan representative tend to have lower net book values for equity compared to market values. This leads to a higher level of accounting conservatism. On the other hand, firms with a loan representative also practise accounting conservatism, but at a slightly lower rate than these companies. Regarding the remaining variables, the variations among companies are not substantial. According to the table, companies with a loan representative tend to have a lower debt ratio compared to companies without one. The mean financial leverage for companies with a loan representative is 0.819, while it is 0.869 for companies without a loan representative. It is evident that there is a higher risk of litigation for companies that do not have a loan representative, as their numbers increase compared to other companies.

The findings of the T-Test, which was used to gauge how significant the variations in corporate governance traits linked to accounting conservatism were across our organisations, are shown in [Table 5](#):

Table 5: The Significance of the Differences Between Companies in Corporate Governance Characteristics Related to Conservatism.

Variables	companies that have AFB (N=35)			companies that don't have AFB (N=22)			F. Test	Sig
	Mean	Median	St. Div	Mean	Median	St. Div		
Independence of the Board	0.871	0.712	1.017	0.514	0.469	0.924	3.478	0.023
Board size	2.468	1.378	2.987	2.244	1.178	2.632	1.014	0.247
Ownership of the internal director	0.039	0.027	0.119	0.053	0.040	0.145	2.987	0.044
Ownership of the outside director	0.011	0.009	0.078	0.007	0.005	0.066	4.442	0.000
Institutional ownership	0.433	0.341	0.309	0.529	0.417	0.880	0.987	0.286

According to [Table 5](#), companies with a loan representative on their boards of directors exhibit a higher level of board independence, with a mean score of (0.871) compared to (0.514) in other companies. Companies with an affiliated banker tend to have lower

internal manager ownership, higher external manager ownership, and lower institutional ownership compared to companies without an affiliated banker. The differences in the independence of the Board of Directors, the possession of internal directors, and the ownership of external directors between companies with affiliated banking experts and other companies have revealed their significance.

The T-Test results are presented in [Table 6](#) to measure the significance of the differences between firms regarding the criteria linked to the likelihood of having commercial bankers on company boards of directors:

Table 6: The Significance of the Differences Between Companies in the Factors Associated with the Presence of an Affiliated Banker.

Variables	companies that have AFB (N=35)			companies that don't have AFB (N=22)			F. Test	Sig
	Mean	Median	St. Div	Mean	Median	St. Div		
Volatility of stock returns	0.229	0.214	0.387	0.238	0.198	0.290	1.366	0.243
volatility of stock returns square	0.092	0.77	0.072	0.083	0.071	0.107	1.549	0.214
Tangible assets	0.121	0.113	0.241	0.100	0.092	0.464	0.267	0.605
Business credit ratings	0.748	0.662	0.411	0.547	0.513	0.499	5.214	0.000
Capital structure	0.026	0.017	0.33	0.021	0.007	0.027	1.897	0.261
Bankruptcy risks	0.053	0.46	0.071	0.070	0.059	0.087	3.643	0.006
Industry membership	0.129	0.117	0.336	0.163	0.151	0.371	1.114	0.336

According to [Table 6](#), companies with a banking expert on their boards of directors tend to have higher tangible assets and achieve a better commercial rating. These companies also experience lower fluctuations in stock returns compared to companies without a banking expert. The mean commercial credit for companies with a banking expert is 0.748 with a standard deviation of 0.546, while the mean volatility of stock returns is 0.229 with a standard deviation of 0.387. Companies with a loan representative had a lower risk of bankruptcy (mean of 0.053) compared to companies without a loan representative (mean of 0.070).

The T-Test results indicate significant differences in the risks of commercial credit and bankruptcy between businesses with a banking specialist and those without. In contrast, it was found that the variations in the other factors were less significant. In particular, the arrangement, physical nature of assets, square of stock return volatility, and stock return volatility Being a member of the capital and industry sectors was contingent upon having a moral worth that surpassed five percent.

The Results of Multiple Regression Analysis: Testing the Study Hypotheses Testing the First Hypothesis of the Study

The first sub-hypothesis of the study was evaluated using multiple regression analysis. This analysis focused on examining the influence of company characteristics variables

on conditional accounting conservatism in the sample businesses of the study. The analysis results are presented in the table below, based on the provided model:

$$\text{Earnings} = \beta_0 + \beta_1 \text{DR} + \beta_2 \text{MTB} + \beta_3 \text{Lev} + \beta_4 \text{Litigation} + \beta_5 \text{Size} + \varepsilon_{it}$$

Table 7: Measuring the Effect of Company Characteristics Measures on Conditional Accounting Conservatism.

Variables	B	Beta	T – Test	Sig	VIF
Constant	0.684		3.062	0.002	
DR	- 0.041	- 0.071	- 1.920	0.048	1.016
MTB	0.057	0.040	2.527	0.014	1.331
Financial Leverage	- 0.004	- 0.093	- 1.311	0.191	1.168
Litigation Risk	0.114	0.062	1.839	0.057	2.717
Company size	- 0.082	- 0.304	- 2.474	0.016	3.473
Companies with a loan representative (AFB=1)	Companies that do not have a loan representative (AFB=0)				
R = 0.312	R = 0.133				
R ² = 0.097	R ² = 0.015				
F – Test = 3.598	F – Test = 1.595				
Sig = 0.037	Sig = 0.160				
Durbin – Watson = 2.178	Durbin – Watson = 1.643				
Dependent variable: Abnormal earnings ratio (conditional conservatism).					

Table 7 displays the results indicating that company characteristics associated with conservatism account for (9.7%) of the variations in accounting conservatism. The multiple correlation coefficient achieved a value of 0.312, while the coefficient of determination R² for the model reached 0.097. Approximately 90.3% of the remaining percentage can be attributed to either the model's random error or the inability to incorporate additional independent variables that were necessary for the model. In addition, the chart clearly demonstrates the significant importance of the model. The F value of (3.598) was achieved at a significance level of (0.037), which is significantly lower than the acceptable threshold of (5%). It is evident that the presence of certain firm characteristics in loan representative-holding entities has an impact on conditional accounting conservatism.

In addition, research has demonstrated that the market value to book value ratio significantly influences accounting conservatism. The reason for this is solely because T reached a value of (2.527) with a significance level of 0.014. Furthermore, a notable negative relationship was observed between company size and accounting conservatism, with a T value of (-2.474). At a statistically significant level (0.016), it was found that litigation risk had a direct impact and financial leverage had an inverse impact on conditional accounting conservatism in companies with a loan representative. However, this effect was not proven to be significant. The correlation between litigation risks and

conservatism suggests that a robust judicial system leads to a higher inclination from management to adopt accounting conservatism. This is due to management's concern about legal repercussions for misrepresenting changes in asset values.

The results in the previous table indicate that there is no observed impact of company characteristics on conditional accounting conservatism, particularly in companies without a loan representative. The F value at a significance level of 0.160 was found to be 1.595.

The prediction of conditional accounting conservatism in companies with a loan representative can be determined based on the company's characteristics and the following treatment:

$$\text{Earnings} = 0.684 - 0.041\text{DR} + 0.057\text{MTB} - 0.004\text{Lev} + 0.114\text{Litigation} - 0.082\text{Size} + \varepsilon_{it}$$

Based on the previous results, we have sufficient evidence to reject the initial null sub-hypothesis and support the alternative hypothesis, which is stated as follows: The study sample consists of Emirati companies with a loan representative, and it examines the impact of company characteristics measures on conditional accounting conservatism. Based on the previous results, it is reasonable to accept this hypothesis. The study sample examines the impact of company characteristics measures on conditional accounting conservatism in Emirati companies (companies with a loan representative).

Testing the Second Hypothesis of the Study

Table 8: Measuring the Effect of Corporate Governance Characteristics Measures on Conditional Accounting Conservatism.

Variables	B	Beta	T – Test	Sig	VIF
Constant	1.216		3.167	0.000	
DR	- 0.041	- 0.071	- 1.862	0.054	3.127
Independence of the Board	0.225	0.083	3.637	0.000	1.456
Board size	0.006	0.032	0.987	0.152	2.109
Ownership of the internal director	- 0.007	- 0.116	- 1.645	0.092	1.783
Ownership of the outside director	0.091	0.108	2.018	0.028	1.482
Institutional ownership	0.127	0.416	2.982	0.008	2.398
Companies with a loan representative (AFB=1)	Companies that do not have a loan representative (AFB=0)				
R = 0.424 R ² = 0.178 F – Test = 5.994 Sig = 0.000 Durbin – Watson = 2.415	R = 0.297 R ² = 0.088 F – Test = 1.963 Sig = 0.047 Durbin – Watson = 1.821				
Dependent variable: abnormal earnings ratio (conditional conservatism)					

The second sub-study hypothesis was tested using multiple regression analysis. This analysis aimed to explore the connection between corporate governance characteristics and conditional accounting conservatism in the companies included in the study. The findings indicate a strong link between corporate governance and accounting conservatism. It becomes more imperative to incorporate a significant level of accounting conservatism in the financial statements as the effectiveness of governance improves. The following table displays the results of this analysis, based on the following mode.

$$\text{Earnings}_i = \beta_0 + \beta_1 \text{DR} + \beta_2 \text{IND} + \beta_3 \text{BOD} + \beta_4 \text{OOD} + \beta_5 \text{OID} + \beta_6 \text{INS} + \varepsilon_{it}$$

Table 8 displays the findings, indicating that corporate governance characteristics linked to conservatism account for 17.8% of the variations in conservatism. The multiple correlation coefficient achieved a value of 0.424, while the coefficient of determination R^2 for the model reached 0.178. Approximately 82.2% of the remaining percentage can be attributed to either random error in the model or the omission of other independent variables that could have been included. The conditional accounting approach considers the remaining percentage. The model's F value of 5.94, with a significance level of (0.000), demonstrates its exceptional quality in the table. This value is below the threshold of significance (1%), reinforcing the model's academic rigour and conciseness. This indicates that corporate governance characteristics have an impact on conditional accounting conservatism in companies with a representative for loans.

The table clearly shows that the independence of the board of directors has the most significant influence on the level of accounting conservatism in corporate governance. Businesses that prioritise board independence often adopt conservative accounting practices. Research findings indicate that the degree of accounting conservatism does not have any correlation with the size of the board of directors or internal director ownership. In addition to the noted correlation between the proportion of external directors' shares and conditional accounting conservatism, it is worth mentioning the positive influence of institutional ownership on conditional accounting conservatism in companies with a banking expert in affiliation. Hence, the effective implementation of corporate governance mechanisms helps limit opportunistic behaviour among corporate boards of directors, through the utilisation of conservative accounting practices.

The prediction of conditional accounting conservatism in companies with a loan representative can be determined based on the company's characteristics and the following treatment:

$$\text{Earnings}_i = 1.216 - 0.041_i \text{DR} + 0.225 \text{IND} + 0.006 \text{BOD} - 0.007 \text{OOD} + 0.091 \text{OID} + 0.127 \text{INS} + \varepsilon_{it}$$

The coefficient of determination R^2 of 0.088 indicates that there is a significant impact

of corporate governance features on accounting conservatism in firms without a loan representative, although the influence rate is relatively lower. This is supported by the findings presented in Table 7. Corporate governance measures have a limited explanatory power of (8.8%) in accounting conservatism for companies without a loan representative.

The study's alternative hypothesis, which suggests a connection between conditional accounting conservatism and corporate governance characteristics in Emirati companies, is supported by previous research and contradicts the second null sub-hypothesis (companies with a loan representative).

Testing the Third Hypothesis of the Study

The third sub-hypothesis of the current study was evaluated using multiple regression analysis. This analysis examined the impact of parameters related to the existence of an affiliated banker on conditional accounting conservatism in the selected enterprises. The analysis results are presented in the table below, based on the provided model:

$$\text{Earnings} = \beta_0 + \beta_1 \text{DR} + \beta_2 \text{VOL} + \beta_3 \text{SQ} + \beta_4 \text{ASS} + \beta_5 \text{COM} + \beta_6 \text{CAP} + \beta_7 \text{RISK} + \beta_8 \text{IND} + \varepsilon_{it}$$

Table 9: Measuring the Effect of Factors Associated with the Presence of Affiliated Banker on Conditional Accounting Conservatism.

Variables	B	Beta	T – Test	Sig	VIF
Constant	0.228		2.970	0.003	
DR	- 0.022	- 0.038	- 0.555	0.580	1.070
Volatility of stock returns	0.115	0.157	2.084	0.028	4.687
volatility of stock returns square	- 0.049	- 0.176	- 1.208	0.228	4.753
Tangible assets	0.085	0.138	1.821	0.043	1.860
Business credit ratings	- 0.107	- 0.264	- 2.351	0.017	1.013
Capital structure	0.021	0.038	0.724	0.472	1.865
Bankruptcy risks	0.074	0.117	1.728	0.049	2.328
Industry membership	0.017	0.063	0.964	0.387	1.547
Companies with a loan representative (AFB=1)			Companies that do not have a loan representative (AFB=0)		
R = 0.269			R = 0.124		
R2 = 0.072			R2 = 0.015		
F – Test = 3.268			F – Test = 0.745		
Sig = 0.014			Sig = 0.201		
Durbin – Watson = 1.624			Durbin – Watson = 1.196		
Dependent variable: abnormal earnings ratio (conditional conservatism).					

The results presented in Table 8 indicate that the model's coefficient of determination (R2) achieved a value of (0.072), while the multiple correlation coefficient reached

(0.269). These findings indicate that having an affiliated bank account accounts for 7.2% of the variation in conditional accounting conservatism. The remaining 92.8% can be attributed to random error in the model or the omission of other independent variables that could have influenced the results. In addition, the table indicates that the model was statistically significant with an F-value of 3.268 at a significance level of 0.014, which is below the accepted level of significance of 5%. This study examines the influence of a connected banker on conditional accounting conservatism in organisations that have loan representatives.

In addition, [Table 9](#) clearly indicates the variables that have the most significant influence on the level of accounting conservatism in the presence of an attached bank. These variables include commercial credit, stock return volatility, physical assets, and bankruptcy risk. The correlation between accounting conservatism and stock return volatility is evident. In practice, companies tend to adopt accounting conservatism to minimise information asymmetry, particularly in highly active and efficient financial markets where stock prices exhibit lower volatility.

Studies have shown a clear link between the level of tangibility of assets and accounting conservatism. When organisations expand their fixed and intangible assets, they tend to employ conservative accounting practices. There is a significant link between accounting conservatism and commercial credit. Therefore, businesses that undergo a commercial credit review tend to exhibit higher levels of accounting conservatism.

Companies with a loan representative may exhibit predictable conditional accounting conservatism based on factors related to the presence of an affiliated bank. This can be determined through the following treatment:

$$\text{Earnings} = 0.228 - 0.022\text{DR} + 0.115\text{VOL} - 0.049\text{SQ} - 0.085\text{ASS} + 0.107\text{COM} + 0.021\text{AP} + 0.074 + \text{ISK} + 0.017\text{IND} + \epsilon_{it}$$

The study confirms that the presence of an affiliated banker has an impact on conditional accounting conservatism in Emirati companies. This finding is based on the results obtained from the study sample, which consists of companies that have a loan representative. The rejection of the third null sub-hypothesis is indicated.

Conclusion

This study examined the level of accounting conservatism in the financial statements of the borrowing company and explored the impact of the lender control mechanism, which involves placing a subsidiary bank on the board of directors. A thorough investigation was conducted on the effectiveness of the lender control mechanism in reducing the information gap between the borrowing firm and the long-term creditors (lenders). This would reduce lenders' ongoing desire for the control that conservatism

provides. The findings of the current study, based on a review of the accounting literature, revealed several key trends. One approach to address the problem of debt agency is to enhance accounting conservatism in the financial statements, which can expedite the debt-contracting process. The borrower's debt management mechanism can be advantageous in reducing or mitigating the occurrence of information asymmetry. Furthermore, the core issue of the debt agency problem arises from the unequal distribution of information between the lender and the borrowing firm. Additionally, the lender greatly benefits from the banking expert's role on the board of directors of the borrowing firm, as they oversee and manage the decision-making process. Due to its efficiency, the system for monitoring lenders is highly effective, despite the associated costs. The findings from the three points suggest that the utilisation of debt contracting and accounting conservatism can be costly. However, companies with a banking expert on their board of directors can potentially avoid relying on debt contracting through conservatism as a means to reduce expenses. Ultimately, the lender control mechanism reduces the information asymmetry that underlies the debt agency problem, thereby reducing the lenders' reliance on conservative monitoring. This study also revealed that companies with a banking member on their board of directors exhibit a lower level of accounting conservatism compared to companies without a banking member on their board of directors. There is evidence to suggest that when lenders have control, conservatism tends to diminish.

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