



THE
AUDITOR'S
REPORT

Volume 25, No.3, Summer 2002

AUDITING SECTION/AMERICAN ACCOUNTING ASSOCIATION

REPORT OF THE PRESIDENT

This is my third and final report as President of the Auditing Section. I wrote my second report immediately after the Midyear Conference in Orlando. While I indicated that we had another very successful conference (which was not news to those of you who attended), I was holding my breath regarding the cost, which I am happy to report was a pleasant surprise. Thanks go to chair Jeff Cohen and the members of the 2002 Midyear Conference Program Committee for the Conference's success. Bob Ramsay will chair the 2003 Midyear Conference Program. The Spring issue of *The Auditor's Report* includes information about the 2003 Conference. The deadline for submitting papers is September 1, 2002. I am sure Bob would still like to hear from you if you are interested in volunteering for the Conference. I am also sure that Bill Heninger, chair of the CPE Committee, and Mark DeFond, chair of the Doctoral Consortium Committee, would be interested in your suggestions.

By the time you receive this issue of *The Auditor's Report*, you should have already made your plans for the AAA Annual Meeting in San Antonio. The Auditing Section is well represented on the program. Chair of the 2002 Annual Meeting Committee, Randy Elder, received 77 submissions, up from 72 submissions the prior year (while the total AAA submissions declined from 676 to 626). Forty-five papers were accepted (30 for auditing sessions, 6 for interdisciplinary sessions, and 9 for the forum). Randy and I want to thank the reviewers for their timely and substantive feedback on the 77 papers sent out for review. Special thanks also to Randy for managing this year's new electronic submission process, and making sure it worked smoothly for Section members. Bryan Church will chair the 2003 Annual Meeting Committee.

The Section had several milestones this year. The first was the online election of Section officers. The Executive Committee deemed this election format a success and this fall's election for 2003-2004 officeholders will also be online. It is still not too late to nominate yourself or a colleague! I especially want to remind you of the Section's new award this year: the Innovation in Auditing and Assurance Education Award. The announcements



E. Michael Bamber

for officeholder and award nominations are reprinted in this issue of the newsletter. All have a deadline of July 1, 2002.

The second milestone was the 25th anniversary issue of *The Auditor's Report*. Our newsletter has become an important source of information about auditing-related issues as well as Section news. For example, in addition to the regular columns, "Have you seen...?" compiled by Brad Reed and John Reisch, and the "ASB Update" by Ray Whittington, the Spring issue contained an update on developments in international auditing standards by Roger Simnett and Kay Tatum, an outline of the COSO's enterprise-wide risk management project by Mark Beasley, Doug Prawitt, and Larry Rittenberg,

and the press release of the GAO changes to auditor independence requirements. When one adds to the issues covered in the 25th anniversary issue the ASB's release of a new fraud exposure

(continued on page 2)

FALL 2002 ISSUE DEADLINE

The deadline for material to be included in the Fall 2002 issue of *The Auditor's Report* is September 15, 2002. The preferred, but not mandatory, format is Word files attached to email messages. Please send all material to the Editor at the address below by September 15, 2002 to ensure timely publication of the issue:

Mark H. Taylor

John P. Begley Endowed Chair in Accounting

Department of Accounting

College of Business Administration

Creighton University

Omaha, NE 68178

Phone: (402) 280-2602

Fax: (402) 280-5565

mhtaylor@creighton.edu

The address of the Auditing Section's Home Page on the World Wide Web is:

<http://raw.rutgers.edu/raw/aaa/audit/>

CALL FOR NOMINATIONS

Nominees for Election as Section Officers

The Auditing Section members will elect two officers in Fall 2002 for **Vice President–Academic (President-Elect)** and **Secretary**. Those elected will begin serving their terms in August 2003. Please submit names of individuals you would like to nominate for these positions no later than **July 1, 2002**. The Nominations Committee will then select the slate for election from these nominations. In addition, the Bylaws require the Nominations Committee to automatically place on the ballot any person whose nomination is accompanied by a signed petition of no fewer than one hundred (100) members in good standing of the Section and a signed statement by the nominee of willingness to serve if elected. This petition should also be received by July 1, 2002. Please submit nominations and/or petitions to E. Michael Bamber, Chairperson, Nominations Committee, by mail, fax, or email at the following address:

Professor E. Michael Bamber
J.M. Tull School of Accounting
Terry College of Business
University of Georgia
Athens, GA 30602

Phone: (706) 542-3601 • Fax: (706) 542-3630 • Email: mbamber@terry.uga.edu

President's Report

(continued from page 1)

draft to supersede SAS No. 82 and the almost daily press on Enron and Andersen, the importance and opportunities for auditing research and education have never been greater.

The third and related milestone is transforming the newsletter from a hard copy to electronic distribution. Newsletter editor Mark Taylor has done a great job not only managing this change, but also taking advantage of this opportunity to enhance the newsletter in terms of substance and layout. In case you missed the 25th anniversary issue, it is available along with earlier issues of the newsletter on the Section's web site.

In part, the change to an electronic newsletter is a reflection of the times, but it was also one of several actions the Executive Committee took to put the section's finances back on a sound footing. Based on the analyses and projections provided by treasurer Rick Tubbs, I think that we have succeeded. The one uncertainty is that the AAA is also experiencing financial difficulties, and their actions can impact the sections.

Regarding issues still in process, I would like to mention two. First, I want to thank all who responded to my request to email the editors of the *Journal of Accountancy* expressing your support of the *Journal* to continue publishing the Practice Summaries from *Auditing: A Journal of Practice & Theory*. At the time of writing this report, I have no news to give you, other than we have not given up. Arnie Wright is not leaving any door unopened! However, if our efforts fail to persuade the editors of the *Journal of Accountancy* to change their policy, the Executive Committee in conjunction with Arnie Wright (outgoing editor) and Bill Messier (incoming editor) will pursue other publication outlets that provide an outreach to practitioners.

The second issue concerns whether it is time for the Section to change its name to recognize the expansion of assurance services with their teaching-related and research-related issues. I asked the Communications Committee to examine this question. As you will recall, the committee chair, Roger Debreceeny, asked you in an email to respond to a web-based survey. Both Roger

and I want to thank all of you who responded to the survey. Roger received 418 responses, many with detailed comments. The responses to the survey will provide the basis of a report by the Communications Committee that will be discussed at the next Executive Committee meeting. The primary finding is that there is no overwhelming desire for a change in the name of the Section with 237 responding "no," 92 responding "yes," and 89 being "neutral" to the question "Should we change the name of the Auditing Section?" When finalized, the Committee's report will be made available on the Section's web site.

Another item on the Executive Committee's agenda for its meeting in San Antonio is the Section's web site. If you have any suggestions for the web site, please forward them to webmaster Glen Gray or me.

As Vice President, I was especially struck by the large amount of work that goes on in the Section, much of it behind the scenes so that those involved do not always get the credit they deserve. This year has been no exception. Accordingly, I want to recognize the chairs of the Section's standing committees: Kay Tatum, Auditing Standards Committee; Roger Debreceeny, Communications Committee; Bill Dilla, Education Committee; Bill Wright, Research Committee; and Bob Tucker, Membership and Regional Coordinators Committee. The success of the Section is largely due to the unselfish efforts of these individuals and the members of their committees, together with similar efforts and the hard work of the members of the Section's various program committees and awards committees.

Finally, I want to recognize and thank the members of this year's executive committee (not that their work is over yet!): Stan Biggs (Past President), Rick Tubbs (Treasurer), Audrey Gramling (Secretary), Abe Akresh (Vice President–Practice), Joe Carcello (Vice President–Academic) and Andy Bailey (Historian). The highlight of my term has been interacting with these dedicated, hardworking individuals. The Section owes Stan, Audrey, and Abe special thanks as their terms on the Executive Committee end in San Antonio. We will specifically recognize their efforts at the Auditing Section Luncheon in San Antonio. I hope to see you all there.

CALL FOR PAPERS

NINTH ANNUAL MIDYEAR AUDITING SECTION CONFERENCE

The Ninth Annual Midyear Auditing Section Conference will be held in **Huntington Beach, California on January 16–18, 2003**. CPE sessions will be held on the afternoon of January 16. The remainder of the conference will consist of keynote, plenary, and concurrent sessions dealing with a wide variety of contemporary topics related to audit, attestation, and assurance practices, education, and research. You are encouraged to contribute to the program through submissions of auditing/attestation/assurance research and education papers, and special session proposals.

The conference will be held at the **Hilton Waterfront Beach Resort** in Huntington Beach, California. Located in Orange County between Los Angeles and San Diego, this hotel is a Four Diamond Resort with 290 ocean-view rooms. There are many nearby attractions such as Disneyland, Knott's Berry Farm, the Aquarium of the Pacific, and the Queen Mary, along with the local shopping areas of Fashion Island and South Coast Plaza.

SUBMISSION GUIDELINES

Research papers should follow the style guidelines of *Auditing: A Journal of Practice & Theory*. Submissions are not eligible for consideration if they: (1) have been published or accepted for publication, (2) were presented at the 2002 AAA Annual Meeting, or (3) were presented at more than one AAA regional meeting or other academic conference. Papers presented at the Research Forum of the AAA Annual Meeting are eligible for consideration. It should be noted that papers accepted for presentation at the 2003 Midyear Auditing Section Conference may also be submitted for presentation at the AAA Annual Meeting scheduled for August 2003.

SUBMISSION DEADLINE

Submission should be made by email (see *AJPT* guidelines) to **rjrams2@uky.edu** or by mailing a diskette to:

Robert J. Ramsay
Von Allmen School of Accountancy
355 Gatton College of Business and Economics
University of Kentucky
Lexington, KY 40506-0034
Phone: (859) 257-3702 • Fax: (859) 257-3654

Submissions must be received by **September 1, 2002**, to be considered for the program. Early submission is highly encouraged. Any questions should be addressed to Robert J. Ramsay via email.

AUDITING SECTION ANNOUNCES NEW AWARD

Innovation in Auditing and Assurance Education Award

The Executive Committee is seeking nominations from the Section's membership for the first Innovation in Auditing and Assurance Education Award to be given at the Auditing Section Midyear Conference in January 2003. The purpose of the award is to encourage innovation and improvement in auditing and assurance education. The award will recognize a significant activity, concept, or materials. The criteria used to judge the submissions include, but are not necessarily limited to:

- a. Innovation
- b. Educational benefits
- c. Adaptability by other educational institutions or to other situations

Nominations may include, for instance, a set of teaching materials, a creative instructional strategy, or an insightful teaching approach. The innovation should have been implemented so that evidence of its success can be evaluated. Award winners must be willing to share instructional materials with other members of the Section. A completed application should include the following:

- a. A description of the innovation, including sample materials
- b. Evidence that the innovation has been tested and shown to have educational benefits
- c. The name of a contact person, including the person's phone, email address, and office mailing address
- d. A copy of any published articles or working papers regarding the innovation by the nominee(s)

Individual faculty members or groups of faculty teaching or preparing materials to be used for auditing and/or assurance education are eligible to apply. Persons may also nominate another faculty member or group of faculty. At least one nominee must be a member of the Auditing Section. Nominations should be sent by July 1, 2002 to:

Professor E. Michael Bamber
J.M. Tull School of Accounting, Terry College of Business
University of Georgia
Athens, GA 30602-6252
Phone: (706) 542-3601 • Fax: (706) 542-3630 • Email: mbamber@terry.uga.edu

NINTH ANNUAL MIDYEAR AUDITING SECTION CONFERENCE

January 16–18, 2003
Huntington Beach, California

Your help in planning and conducting the Section's 2003 Midyear Conference is needed. If you are willing to volunteer your assistance in one or more of the following areas, please complete this form and hand it to a Steering Committee member or mail/fax it to the address/number below.

Name _____

Address _____

City _____ State _____ Zip _____

Phone _____ Fax _____ Email _____

Reviewer: If you are willing to assist by reviewing one to three manuscripts, please indicate your areas of competence/interest.

Research Areas _____

Research Methods _____

Session Chair or Discussant: Please indicate if you are willing to assist in either of these capacities.

Session Chair _____ Discussant _____

Special Sessions: Please provide any ideas that you have for special CPE topics, panels, workshops, etc. If you know any particular individual(s) who may be interested in the areas you recommend, please list their names. Use the back of this page for additional comments.

The Steering Committee very much appreciates your input. Mail or fax this form to:

Robert J. Ramsay • Phone: (859) 257-3702 • Fax: (859) 257-3654 • Email: rjrams2@uky.edu

CALL FOR NOMINATIONS

Notable Contributions to the Auditing Literature Award

The Auditing Section seeks submissions for the Notable Contributions to the Auditing Literature Award. The award will recognize a published work of exceptional merit that has made, or has the potential to make, a direct contribution to auditing or assurance research, education, and practice. To be eligible for submission, a work must have been published during the ten-year period ended December 31, 2001, and at least one of the authors of the published article, chapter, book, or monograph must be a current member of the Auditing Section. Selection of the award winner will be made by the Auditing Section's Notable Contributions to the Auditing Literature Award Committee. The award is presented at the 2003 Midyear Meeting of the Auditing Section. A work may be submitted either by the author or another individual with an interest in auditing research, education, or practice. Submissions must include five copies of (1) a nomination letter stating why the work is deserving of special recognition, and (2) the submitted work. Submissions should be sent by July 1, 2002 to:

Professor Joseph V. Carcello

University of Tennessee

601 SMC

Knoxville, TN 37996-0560

Phone: (865) 974-1757 • Fax: (865) 974-4631 • Email: jcarcell@utk.edu

CALL FOR NOMINATIONS

Distinguished Service in Auditing Award

The Distinguished Service in Auditing Award Selection Committee is seeking nominations from the Section's membership for the award to be given at the Auditing Section Midyear Conference in January 2003. This award recognizes outstanding and sustained service to the profession or the Auditing Section. The distinguished careers of past recipients of the award (Bob Roussey, Dave Landsittel, Jerry Sullivan, Don Leslie, Ken Stringer, Robert Mautz, Robert Elliott, W. W. Cooper, Jim Loebbecke, John Willingham, Jay Smith, William Kinney, Fred Neumann, Bob Sack, Dan Guy), and members of the first Practice Advisory Council (Tom Powell, Chair) represent the type of contribution to the profession that exemplifies this recognition. Nominations should be sent by July 1, 2002 to:

George Krull

Grant Thornton

Phone: (312) 602-8109 • Email: gkrull@gt.com

CALL FOR NOMINATIONS

Outstanding Auditing Educator Award

The Outstanding Auditing Educator Award Selection Committee is seeking nominations from the Section's membership for the award to be given at the Auditing Section Midyear Conference in January 2003. This award is given annually and recognizes outstanding contributions to the field of auditing education. Prior recipients of this award include Andy Bailey, Ira Solomon, William Kinney, Jack Krogstad, Glen Berryman, Fred Neumann, Howard Stettler, William Felix, Al Arens, Jim Loebbecke, Nick Dopuch, and Ken Trotman. Nominations should be sent by July 1, 2002 to:

Professor E. Michael Bamber

J.M. Tull School of Accounting

Terry College of Business

University of Georgia

Athens, GA 30602-6252

Phone: (706) 542-3601 • Fax: (706) 542-3630 • Email: mbamber@terry.uga.edu

CALL FOR NOMINATIONS

Outstanding Auditing Dissertation Award

The Auditing Section seeks nominations for its annual Outstanding Auditing Dissertation Award. The author of the dissertation judged to make the most outstanding contribution to auditing knowledge, among those dissertations nominated for consideration, will receive the award. The assessment of what constitutes an outstanding contribution will be based upon, but not limited to, the following criteria:

- The timeliness and importance of the problem(s) addressed.
- The creativity of the research.
- The development of an appropriate theoretical framework.
- The appropriateness of the research method and analysis.
- The potential for publication in a scholarly journal.
- The potential for the results to have an impact on the practice of auditing.

Selection of the award winner will be made by the Section's Outstanding Dissertation in Auditing Committee. A dissertation can be nominated either by the author or one or more members of the dissertation committee. Nominations will be considered complete when the following materials have been submitted:

- A letter from the dissertation chairperson stating that the dissertation has been completed and accepted by the degree-granting institution between January 1, 2000 and December 31, 2001 (dissertations can be nominated more than once).
- Five copies of a nomination letter stating why the dissertation is deserving of special recognition.
- An electronic copy of a paper from the dissertation that meets the criteria for papers submitted to *Auditing: A Journal of Practice & Theory* (refer to the latest issue for requirements related to length and other matters, e.g., submission of experimental instruments).
- An electronic copy of the entire dissertation.

Please submit all materials by July 1, 2002 to:

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University of Tennessee

601 SMC

Knoxville, TN 37996-0560

Phone: (865) 974-1757 • Fax: (865) 974-4631 • Email: jcarcell@utk.edu

Auditing Concurrent Sessions Preliminary Schedule
American Accounting Association
2002 Annual Meeting
San Antonio, Texas

Section Luncheon: 12:00 noon–1:45 p.m.

Speaker: Sherron Watkins, Vice President for Corporate Development, Enron Corp.

Session time: 2:00–3:30 p.m. Session date: Thursday, August 15, 2002

Session title: Auditor Size and Audit Quality

Moderator: Robert Rouse
College of Charleston

Paper 1. *Differences in Financial Statement and Compliance Audit Assessments between Brand Name and Nonbrand Name Auditors.* Stefanie Tate, University of New Hampshire

Paper 2. *Audit Quality and the Pricing of Discretionary Accruals.* Gopal Krishnan, City University of Hong Kong.

Paper 3. *Reporting Incentive Conflicts and Audit Effectiveness Differentiation between Big 6 and non-Big 6 Auditors.* Jeong-Bon Kim, Richard Chung, and Michael Firth, all at Hong Kong Polytechnic University

Discussant: Debra Jeter
Vanderbilt University

Session time: 4:00–5:30 p.m. Session date: Thursday, August 15, 2002

Session title: Perceived Audit Quality

Moderator: Nancy Uddin
Monmouth University

Paper 1. *The Effects of Internal Audit Structure on Financial Statement Users' Confidence in Their Protection from Financial Statement Fraud.* Kevin James, Middle Tennessee State University

Paper 2. *Determinants of the Perceived Quality of Audit Teams' Judgments.* Mark Peecher, University of Illinois at Urbana–Champaign; Jay Rich, University of Connecticut; and Richard Tubbs, The University of Iowa

Paper 3. *The Effect of Auditor Disclosure vs. Auditor Restrictions on Investors' Perceptions of Auditor Independence.* Lisa Milici Gaynor, Georgetown University

Discussant: Arnold Schneider
Georgia Tech University

Session time: 4:00–5:30 p.m. Session date: Thursday, August 15, 2002

Session title: Audit Judgment

Moderator: Richard Hwang
California State University, San Marcos and Chinese University of Hong Kong

Paper 1. *Determinants of the Timing of Interim and Majority of Audit Work.* Bilal Makkawi, Morgan State University; and Mohammad Abdolmohammadi, Bentley College

Paper 2. *The Mitigating Effect of Internal Control Effectiveness on the Relationship between Source Objectivity, Evidence Set Size, and Evidence Persuasiveness.* Diane Janvrin, Iowa State University

Paper 3. *The Impact of Risk Checklists and a Standard Audit Program on the Planning of Fraud Detection*

(continued on page 7)

Auditing Concurrent Sessions Preliminary Schedule

(continued from page 6)

Procedures. Stephen Asare, University of Florida; and Arnie Wright, Boston College

Discussant: Aretha Hill
Florida A&M University

Session time: 10:15–1:45 a.m. **Session date:** Friday, August 16, 2002

Session title: Audit Pricing

Moderator: Charles Cullinan
Bryant College

- Paper 1. *Industry Specialization and Audit Fees: The Effect of Industry Type and Market Definition.* Ken Chen, National Cheng Kung University; and Randal Elder, Syracuse University
- Paper 2. *Market Leadership and Audit Pricing in City-Level Markets.* Andrew Ferguson, University of Technology, Sydney; Jere Francis, University of Missouri–Columbia; and Donald Stokes, University of Technology, Sydney
- Paper 3. *The Effect of Audit Committee Characteristics and Nonaudit Fees on Audit Fees.* Larry Abbott, The University of Memphis; Susan Parker, Santa Clara University; Gary Peters, University of Georgia; and Kannan Raghunandan, Texas A&M International University

Discussant: Audrey Gramling
Georgia State University

Session time: 2:00–3:30 p.m. **Session date:** Friday, August 16, 2002

Session title: Auditor Regulation–Analytical

Moderator: Susan Watts
Purdue University

- Paper 1. *The Economic Consequences of Limiting the Joint Provision of Audit and Nonaudit Services.* Derek Chan, University of Hong Kong
- Paper 2. *The Impact of Mandatory Auditor Rotation and Retention on the Market Shares of the Big 5 Accounting Firms.* Christie Comunale, Long Island University, C.W. Post Campus; and Thomas Sexton, SUNY at Stony Brook
- Paper 3. *Mandatory Rotation and Auditor Independence—An Analysis of Auditor's Reputation Effect.* Wu-Chun Chi and Hung-Chao Yu, both at National Chengchi University; and Shih-Tsung Chiu, National Taipei University

Discussant: Martin Wu
University of Illinois at Urbana–Champaign

Session time: 4:00–5:30 p.m. **Session date:** Friday, August 16, 2002

Session title: Audit Performance

Moderator: Gene Chewning
University of South Carolina

- Paper 1. *An Empirical Study of the Impact of Information Technology Externalities on the Costs and Prices of Statutory Audits of Public Corporations.* Rajiv Banker, Hsihui Chang, and Yi-ching Kao, all at The University of Texas at Dallas
- Paper 2. *Determinants of the Mix of Audit Procedures: Key Factors That Cause Auditors to Change What They Do.* J. Hans Blokdiijk and Fred Driehuisen, both at Limperg Instituut; Dan Simunic, University of British Columbia; and Michael Stein, University of Oregon
- Paper 3. *The Openness of Knowledge Sharing in Audits: An Exploratory Study.* Joanna Ho, University of

(continued on page 8)

Auditing Concurrent Sessions Preliminary Schedule

(continued from page 7)

California, Irvine; Sandra Vera-Muñoz, University of Notre Dame; and Chee Chow, San Diego State University

Discussant: Steve Wheeler
University of the Pacific

Session time: 10:15–11:45 a.m. **Session date:** Saturday, August 17, 2002

Session title: Nonaudit Services and Empirical Auditing Research

Moderator: Stanley Jenne
University of Montana

- Paper 1. *Auditor Provided Nonaudit Services: Modeling Fees and Willingness to Buy*. Keith Houghton, University of Melbourne; and Chris Ikin, University of Tasmania
- Paper 2. *The Influence of Nonaudit Service Revenues and Client Pressure on External Auditors' Decisions to Rely on Internal Audit*. William Felix, Jr., The University of Arizona; Audrey Gramling, Georgia State University; and Mario Maletta, Northeastern University
- Paper 3. *The Consequences and Information Content of the Types of FRR No. 31 Reportable Events*. Scott Whisenant, University of Houston; Srinivasan Sankaraguruswamy, Georgetown University; and Kannan Raghunandan, Texas A&M International University

Discussant: Hema Rao
SUNY at Oswego

Session time: 2:00–3:30 p.m. **Session date:** Saturday, August 17, 2002

Session title: Nonaudit Services and Auditor Independence

Moderator: Alan Reinstein
Wayne State University

- Paper 1. *Do Nonaudit Services Compromise Auditor Independence?* Hollis Ashbaugh, Ryan LaFond, and Brian Mayhew, all at University of Wisconsin–Madison
- Paper 2. *Nonaudit Services and Shareholder Ratification of Auditors*. K. Raghunandan, Texas A&M International University
- Paper 3. *Nonaudit Services and Auditor Reporting on Stressed Companies*. Marshall Geiger, University of Richmond; and Dasaratha Rama, Texas A&M International University

Discussant: Srinivasan Sankaraguruswamy
Georgetown University

Session time: 4:00–5:30 p.m. **Session date:** Saturday, August 17, 2002

Session title: Auditor Quality and Legal Liability—Analytical

Moderator: Noel Addy
Mississippi State University

- Paper 1. *Managing Auditor Litigation Risk by Screening Clients and Forming a Strategy as a Litigator*. Ella Mae Matsumura, University of Wisconsin–Madison; Seung-Weon Yoo, Hong Kong University of Science and Technology; and Robert Tucker, Fordham University
- Paper 2. *An Equilibrium Analysis of Auditor Quality and Legal Liability Rules*. Chiawen Liu, Yuan Ze University;

(continued on page 9)

Auditing Concurrent Sessions Preliminary Schedule

(continued from page 8)

and Taychang Wang, National Taiwan University

Paper 3. *A Model of Auditors' Preferences for Bright-Line Accounting Standards*. Dennis Caplan, Iowa State University; and Michael Kirschenheiter, Columbia University

Discussant: Ping Zhang
University of Toronto

Session time: 4:00–5:30 p.m. **Session date:** Saturday, August 17, 2002

Session title: Auditor Choice and Quality

Moderator: Raquel Galindo
Autonomous University of Madrid

Paper 1. *Former Audit Firm Personnel as CFOs: Frequency and Effect on Audit Quality*. Thomas Dowdell and Jagan Krishnan, both at Temple University

Paper 2. *Audit Firm Size, Industry Specialization, and Earnings Management by Initial Public Offering Firms*. Jian Zhou, SUNY at Binghamton; and Randal Elder, Syracuse University

Paper 3. *Entrepreneur Choice of Auditor and Retained Ownership in IPO Markets: Experimental Evidence*. Brian Mayhew, University of Wisconsin–Madison; Jeffrey Schatzberg, The University of Arizona; and Galen Sevcik, Georgia State University

Discussant: Stephen Taylor
University of Technology, Sydney

The six papers listed below were submitted to the Auditing Section but accepted for presentation in interdisciplinary sessions. Please check the Annual Meeting program for further information on these papers.

Do Nonaudit Services Compromise Auditor Independence? Jere Francis, University of Missouri–Columbia; and Bin Ke, Pennsylvania State University

Economic Model of Auditing of Audience Claims by Internet Web Sites. Birendra Mishra, Rajiv Banker, and Ashutosh Prasad, all at The University of Texas at Dallas

Insights into Selection–Socialization: An Examination of the Moral Reasoning of Public Accountants in the U.S. and Canada. Linda Thorne, York University; Dawn Massey, Fairfield University; and Michel Magnan, Concordia University

Client Importance, Nonaudit Services, and Abnormal Accruals. Hyeesoo Chung and Sanjay Kallapur, both at Purdue University

Differential Use of Information by Financial Analysts for New Economy vs. Traditional Economy Companies: Implications for Assurance. Jay Thibodeau and Mohammad Abdolmohammadi, both at Bentley College; Roger Simnett, The University of New South Wales; and Arnold Wright, Boston College

Do External Auditors Perform a Corporate Governance Role in Emerging Markets? T. J. Wong and Joseph Fan, both at Hong Kong University of Science and Technology

The papers listed below were accepted for presentation in the Auditing Section Research Forum. Please check the Annual Meeting program for further information on the research forum.

Health Management, Inc.: An Audit Case. Michael Knapp and Carol Knapp, both at University of Oklahoma

Client Acceptance Decision and Auditor's Engagement Risk: The Role of Accounting Firm Alumni. Ilias Basioudis, Aston University

Audit Sampling Methods and Juror Negligence Awards: An Expectation Gap? David Gilbertson, Western Washington University; and Terri Herron, The University of Montana–Missoula

An Exploratory Investigation of Factors Affecting Big 5 Audit Budget Accuracy. Steve Buchheit and William Pasewark, both at Texas Tech University; and Jerry Strawser, Texas A&M University

Auditor Conservatism and Audit Quality: Evidence from IPO Earnings Forecasts. Philip Lee, Sarah Taylor, and Stephen Taylor, all at University of Technology, Sydney

Adverse Audit Findings for Nonprofit Organizations under the Single Audit Act: Risk, Industry Sector, and Auditor Effects. Elizabeth Keating, Northwestern University; Teresa Gordon, University of Idaho; Mary Fischer, The University of Texas at Tyler; and Janet Greenlee, University of Dayton

Risk and Staff Considerations and Their Impact on Auditors' Assessments of Audit Fees and Hours. Susan Hughes, Butler University

The Association between Nonaudit Service Purchases and Managers' Compensation Structure. Charles Jieping

ASB Update as of May 15, 2002

*Ray Whittington, DePaul University
Academic Member of the Auditing Standards Board*

In this update I will focus on the ASB's efforts to update its strategic plan. As always, please contact me if you have any questions, comments, or suggestions.

Horizons II

In December 1997, the ASB issued a strategic plan, *Horizons for the Auditing Standards Board*, that set forth its operational plans for the next three to five years. Much has occurred in the auditing profession since the issuance of that document. At its March 20, 2002 meeting, the Audit Issues Task Force decided to form a task force to develop the ASB's strategic plan for the next five years. The project, which tentatively has been labeled Horizons II, should be completed over the next nine months.

In developing Horizons II, representatives of the task force will be interviewing various stakeholders to get input to determine the issues that should be addressed by the ASB over this intermediate term. I will be responsible for getting input from the academic community. In the remainder of this update I will focus on issues that the task force has initially identified as potential candidates.

Auditing Accounting Disclosures

Auditing standards do not currently distinguish between the extent of the evidence that should be obtained about amounts included in the basic financial statements vs. information and amounts included in financial-statement disclosures. The ASB may add to its agenda a project that would address whether there should be a difference and, if so, the basis for that difference.

Technology

The ASB continues to be concerned that auditing standards do not adequately address the risks and other implications of new technology. Thus, a project with the objective of providing more guidance on effects of technology on audits of financial statements is being considered. The guidance may not be SAS-level but, instead, might take the form of an audit guide or tool kit.

Outsourcing

SAS No. 70, *Service Organizations*, provides guidance on the factors an independent auditor should consider when auditing financial statements of an entity that uses a service organization to process certain transactions. There is no guidance in the auditing literature for situations in which the entity outsources other business processes. For example, a number of entities have outsourced their entire accounting function. This possible agenda item would involve developing guidance on the effect of such outsourcing arrangements on the audit of financial statements.

Harmonization of Auditing Standards

Most individuals in the profession agree that harmonization of U.S. and international auditing standards is desirable. However, there are a number of ways in which this objective might be achieved. Several examples are enumerated below:

- Develop SASs that do not depart significantly from those of the International Federation of Accountant's International Auditing Standards (ISAs)
- Adopt ISAs in total and supplement them with SASs for matters that are particular to the U.S.
- Adopt ISAs modified to include requirements that are in SASs that are not currently included in the ISAs

The issue of harmonization also brings into question the role of the ASB after harmonization is substantially achieved. The ASB is looking for insight into the appropriate way to move toward harmonization of auditing standards.

Education and Experience of Auditors

Currently, auditing standards view the auditor as proficient in accounting and auditing. Given advances in technology and the complexity of business models and accounting standards, the ASB is questioning whether auditing standards set the appropriate bar with respect to the auditor expertise. Therefore consideration is being given to the need to readdress the skills and competencies needed to audit financial statements.

Other Issues

The ASB has identified a number of other issues that might be included in the strategic plan. These include:

1. Auditing assets, liabilities, and exchange transactions valued at fair value;
2. Auditing measurements and disclosures that require assumptions about future events;
3. Continuous auditing, including the appropriate definition of the phrase;
4. Enhancing public confidence in the audit;
5. Analytical commentary by the auditor to assist users evaluate the financial statements;
6. Assurance about other information in the report on the audit of financial statements, such as management's discussion and analysis, internal control, or compliance with laws and regulations;

Please provide me with any input you might have regarding these matters or others that you believe should be considered in the ASB's strategic-planning process.

HAVE YOU SEEN...?

Brad Reed, Southern Illinois University Edwardsville, and John T. Reisch, East Carolina University

“Accounting Professionals and the Accounting Profession: Linking Conduct and Context”, by F. Anderson-Gough, C. Grey, and K. Robson, *Accounting and Business Research* 32 (No. 1, 2002): 41–56.

Recent research has investigated the daily conduct of accounting professionals in Big 5 firms. The authors of this study extend this prior research by incorporating into the study of daily conduct the institutional setting within which accountants work. The authors note that becoming a professional is a complex socialization process that involves induction into a wide array of formal and informal norms that have to be both taught and learned. This paper analyzes the U.K. accounting profession in terms of the fragmentation of its professional bodies and the diversification of its markets, and links this to empirical findings from a qualitative research project examining the professional socialization of trainees in the U.K. regional offices of two Big 5 firms. Using semistructured interviews with trainees, the authors discuss the socialization of the trainees in three areas: being professional, qualification as a professional, and professional training and everyday work.

“The Association between Auditor Choice, Ownership Retained, and Earnings Disclosure by Firms Making Initial Public Offerings”, by P. A. Copley and E. B. Douthett, Jr., *Contemporary Accounting Research* 19 (No. 1, 2002): 49–75.

The authors of this paper test the predictions of Datar, Feltham and Hughes (1991) and Hughes (1986) regarding three signals to investors associated with an initial public offering. The three signals examined are auditor choice, retained ownership, and earnings disclosure. Using a sample of IPOs between 1990 and 1997 the authors find that the demand for high-quality auditors increases with firm risk. Additional results show that auditor choice, earnings disclosure, and risk are determinants of retained ownership. Finally, the results suggest that the signals chosen (i.e., retained ownership, auditor choice, and disclosure) are related through their cost structures and are chosen jointly to minimize the overall cost to the entrepreneur.

“Brand Name Audit Pricing, Industry Specialization, and Leadership Premiums post-Big 8 and Big 6 Mergers”, by A. Ferguson and D. Stokes, *Contemporary Accounting Research* 19 (No. 1, 2002): 77–110.

This paper investigates Big 6 brand-name and industry leadership audit pricing in Australian national audit markets. Prior studies show that Big 8 auditors earn higher audit fees than non-Big 8 auditors due to quality differentiation in the audits. The authors examine samples of Australian-listed public companies in each of the postmerger years 1990, 1992, 1994, and 1998 and estimate national audit fee premiums for the Big 6/5 auditors and the industry specialists and leaders. The authors find limited support for the ability of the Big 6/5 to obtain fee premiums over

non-Big 6/5 for those industries not having specialist auditors. Nonspecialist Big 6/5 auditors are able to obtain fee premiums over nonspecialist non-Big 6/5 for those industries having specialist auditors. However, this result holds only for the smaller half of the sample. The authors do not find strong support for the presence of industry specialist premiums in the postmerger years, especially after 1990, using various definitions of industry specialist. Finally, the results indicate limited support for the presence of industry leadership premiums.

“The Relation between Audit Pricing and Audit Contract Type: A Public Sector Analysis”, by J. Thorne, S. A. Holmes, A. S. McGowan, C. A. Strand, and R. H. Strawser, *Journal of Accounting and Public Policy* 20 (No. 3, 2001): 189–215.

This study examines the extent to which audit contract type is capable of explaining the variation in audit fees, after controlling for variables found to be significant correlates in prior audit economics studies. The authors note that two types of contracts define the economic relationship that exists between the independent auditor and client. Under fixed-fee contracts the total fee is negotiated prior to the evidence-gathering phase of the audit examination. In contrast, cost-reimbursement contracts specify rates by day or hour, to be charged for various categories of personnel, but the total audit fee cannot be determined until after the examination is completed and the actual hours worked are known. Using North Carolina local government data, the authors find evidence that audit fees are, on average, lower for fixed fee contracts than for cost-reimbursement contracts. Also, the probability of negotiating a fixed-fee contract increased for governmental units with higher financial risk when they engaged an independent auditor with more knowledge about the public sector.

“The Value of Management Letters to Unlisted Companies”, by S. Manson, S. McCartney, and M. Sherer, *British Accounting Review* 33 (No. 4, 2001): 549–568.

In this study the researchers investigate the issues raised in management letters and the perceived value of management letters to management and the auditor. The researchers also evaluate whether the size of the audit firm or the length of audit tenure had any effect on the contents of management letters or their value to unlisted companies. The authors find that the issues most frequently raised in management letters related to internal control and accounting systems but that other issues, such as taxation and general business advice, are often included. They find little difference in the contents of management letters issued by Big 5 audit firms and other firms. Clients generally considered that the advice given in management letters was valuable. Again, there was little difference between clients of Big 5 audit firms and other firms. Similarly, the length of audit tenure had no statistically significant effect. Finally, auditors considered the most important benefit of the management letter was its potential for enhancing clients' perceptions of the auditor.

(continued on page 12)

Have You Seen...?

(continued from page 11)

“Ethical Audit Decisions: A Structuration Perspective,” by J. F. Dillard and K. Yuthas, *Journal of Business Ethics* 36 (March 2002): 49–64.

This paper discusses and applies structuration theory as a means for understanding and improving ethical decision making within the audit domain. The paper expands on previous work that suggests that an auditor’s action is affected by responses to past decisions and the recognition of being held accountable for the consequences of the action. The authors argue that structuration theory provides a framework for considering ethical dilemmas by recognizing the centrality of human agency and social structures, as well as the dynamic interrelationship among the two. In an auditing context, this requires auditors to communicate with stakeholders so auditors can better understand how their actions affect stakeholders, and likewise, so stakeholders can become more informed and supportive of the auditor’s objectives.

“Litigation Risk and Audit Fees: Evidence from U.K. Firms Cross-listed on U.S. Markets,” by A. Seetharaman, F. A. Gul, and S. G. Lynn, *Journal of Accounting & Economics* 33 (February 2002): 91–115.

The authors conduct an empirical test on whether audit fees reflect risk differences across liability regimes. The authors find that auditors of U.K. firms charge fee premiums for their services when their clients access U.S. capital markets, but not when they access non-U.S. markets. Tests indicate that the results cannot be fully explained by increased disclosure requirements mandated by U.S. securities laws, and thus, suggest that the fee premiums (estimated to be roughly 20 percent) reflect the above-average litigation risk of the U.S. capital market.

“Audit Firm Industry Experience: A Review and Synthesis of the Archival Literature,” by A. A. Gramling and D. N. Stone, *Journal of Accounting Literature* 20 (2001): 1–29.

In this paper the authors review, synthesize, and evaluate archival research on audit firm industry expertise using a framework from structural economics that characterizes the market for audit services into three dimensions: (1) market structure (studies examining internal conditions of the market such as numbers, size, and market shares of buyers [companies] and sellers [auditors]); (2) market strategy (relationship between industry expertise and audit firm strategies, such as advertising and human resource policies); and, (3) market performance (factors affecting characteristics such as quality and pricing of audit services). The paper concludes with a section on directions for future research.

“Investor Dissatisfaction toward Auditors,” by B. J. Sainty, G. K. Taylor, and D. D. Williams, *Journal of Accounting, Auditing & Finance* 17 (Spring 2002): 111–136.

A metric to measure shareholder dissatisfaction with the auditor is developed in this study by analyzing the shareholder ratification vote of the external auditing firm. Using a sample of 1,265 companies with an auditor ratification vote in 1997, the authors find significant investor dissatisfaction with lower-quality auditors (non-Big 6) and the receipt of going-concern audit opinions (investors reacted strongly when a financially healthy firm received a going concern and when there was a change from a non-going-concern to a going-concern report). In addition, after controlling for known factors influencing auditor change, the results indicate that managers show sensitivity to shareholder dissatisfaction signals by subsequently changing auditors.

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