



THE AUDITOR'S REPORT

Volume 21, No. 3, Summer 1998

AUDITING SECTION/AMERICAN ACCOUNTING ASSOCIATION

REPORT OF THE PRESIDENT

Over the past 21 months I have had the privilege of serving the Auditing Section as Vice President-Academics and President. During this time I have learned a lot about the Auditing Section, how it works, and the services that it offers to its members. I have discovered that the Auditing Section offers many different services that should be useful to members with a variety of interests. Some members (like me, two years ago) may not be aware of all of these services, so I will use this message to highlight many of the services provided by the Auditing Section.

For members interested in auditing education, the Auditing Section offers a variety of paper sessions and CPE sessions on educational topics at its Midyear, Annual and Regional meetings. It offers publications such as the recent monograph, *Curriculum Innovation: Excellence in Audit Education*. The Section's Education Committee is constantly working on projects that usually produce informative reports that are distributed in some fashion, such as on the Section's web page. In addition, the web page provides links to a wide variety of educational resources.

For members interested in auditing research, the Auditing Section publishes *Auditing: A Journal of Practice & Theory*. Research-oriented monographs such as *Research Opportunities in Auditing: The Second Decade* are also published on occasion. The Section offers numerous research paper sessions at its Midyear, Annual and Regional meetings. It occasionally co-sponsors auditing research conferences and sometimes publishes their proceedings in supplemental issues of *Auditing: A Journal of Practice & Theory*. Through these activities, the Section provides valuable opportunities for peer review of its members' research. The Section also offers a useful research review service in the "Have You Seen?" column that appears in *The Auditor's Report*.

For members interested in auditing practice and standard setting, the Section has a Practice Advisory Council that reports to members on emerging issues in practice and attempts to team practitioners and academics on projects to improve the delivery of services in both areas. Watch for a major presentation by the



Barry E. Cushing

PAC at this year's Annual Meeting. The Section also has an Auditing Standards Committee that monitors auditing standard setting activities and reports to members on these activities and their research implications. Members are also regularly updated on Auditing Standards Board activities through the "ASB Update" column in *The Auditor's Report*. In addition, the Section has recently initiated a column in *The Auditor's Report*, beginning in this issue, on the practice implications of auditing research findings. A current project of the Auditing Section, sponsored by the Institute of Internal Auditors and headed by Jane Mutchler, involves an analysis of standards of independence and objectivity around the world, and will result in the publication of a monograph summarizing the findings.

The Auditing Section frequently engages in projects that have joint implications for

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FALL ISSUE DEADLINE

The deadline for material to be included in the Fall 1998 issue of *The Auditor's Report* is September 15, 1998. Please send all material to the editor at the address below by that date to ensure timely publication of the issue:

Gary P. Braun
University of Texas at El Paso
College of Business Administration, 260
Department of Accounting
El Paso, TX 79968-0542
Phone: (915) 747-7742
Fax: (915) 747-8618
Email: gbraun@utep.edu

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

<http://www.indiana.edu/~audsec/>
or access through the Rutgers University Accounting Web:
<http://www.aaa-edu.org>

MESSAGE FROM THE EDITOR

This is my final issue as editor of *The Auditor's Report*. As of Fall, 1998, Gary Braun of the University of Texas at El Paso will take over as Editor. I want to take this opportunity to thank everyone who worked with me on the newsletter over the past three years, including authors, Auditing Section officers, and American Accounting Association personnel. I especially thank Greg Trompeter and Tim Pearson for doing a wonderful job with the "Have You Seen?" column, Kurt Pany for his insightful reporting on the Auditing Standards Board, and Jim De La at AAA for his help and patience.

Report of the President (Continued from page 1)

education, research and practice. One example is the recent monograph *Auditing Practice, Research and Education: A Productive Collaboration*. Another example is the recent special task force report on "Future Audit, Attest, and Assurance Services."

For members interested in Continuing Professional Education, the Auditing Section offers various CPE sessions at its midyear, annual and regional meetings. For members interested in networking with other people with similar interests, the Section's meetings, web page and newsletter provide ample opportunities. Finally, for members interested in serving their fellow members and taking a leadership role in the field of auditing, the Auditing Section has numerous ongoing activities, committees, and so forth, most of which will be looking for volunteers in the near future. If you would like to volunteer, contact me or another member of the Executive Committee at the annual meeting and let us know where your interests lie.

All this for annual dues of \$15! And no, we're not planning to ask you for a dues increase in the foreseeable future. The Auditing Section is quite a bargain, don't you agree?

CALL FOR NOMINATIONS

Nominees for Election as Section Officers

At the annual Business Meeting of the Auditing Section in January 1999, members will elect two officers: Vice President—Academic (President-elect) and Treasurer. Those elected will begin serving their terms in August 1999. Please submit the names of individuals you would like to nominate for these positions no later than August 10, 1998. The Nominations Committee will then select the slate for election from these nominations.

Submit nominations to:

Barry Cushing, Chairperson, 1998-99 Nominations Committee
School of Accounting
David Eccles School of Business
University of Utah
Salt Lake City, UT 84112
Fax: (801) 581-7214
Email: actbec@business.utah.edu

CALL FOR NOMINATIONS

Editor: *Auditing: A Journal of Practice & Theory*

Please submit the names of persons who you would like to nominate as Editor of *Auditing: A Journal of Practice & Theory* to any member of the Editor Nominations Committee no later than August 15, 1998.

The members of the Editor Nominations Committee are:

Barry Cushing (Chair)
University of Utah
Mark Beasley
North Carolina State University
Ron King
Washington University, St. Louis
Joe Schultz
Arizona State University
Rick Tubbs
University of Iowa

The Editor Nominations Committee will transmit a list of nominees to the Auditing Section Executive Committee. The Executive Committee will then select the new editor. The Executive Committee plans to announce the name of the person they have selected during the 1999 Midyear Meeting of the Auditing Section.

ASB Update as of May 15, 1998

Kurt Pany, Arizona State University
Academic Member of the Auditing Standards Board

In this update, I discuss a number of the current ASB projects that I believe may be of interest. As always, feel free to contact me with any questions, comments and suggestions.

Restricted Use

The exposure period for this proposed SAS ended on May 6 and discussion of the document is scheduled for the June ASB meeting. The professional standards have been inconsistent in using terms such as "restricted use," "limited distribution" and "restricted distribution" when reports are not meant for general use. Because these terms may imply unintended differences of meaning, this proposed SAS attempts to eliminate the inconsistencies. The proposed SAS states that the primary reasons for restriction include the following: (1) The measurement criteria are not generally understood (e.g., information prepared following regulatory basis of accounting); (2) users take responsibility for the procedures performed (e.g., agreed-upon procedure engagements); (3) reporting is a by-product of an audit (e.g., a report on reportable conditions issued to the audit committee as a result of an audit). Also, for the first time in the professional standards, it includes a statement that a CPA may restrict the use of any report that is ordinarily "general use." For example, an audit report might be considered "restricted use" if so contracted with a client when no laws or regulations prohibit such a restriction.

Auditing Investments

In 1996 the Auditing Standards Board (ASB) issued Statement on Auditing Standards (SAS) 81 to provide auditing guidance consistent with recently issued accounting standards, including FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*, and No. 124, *Accounting for Certain Investments Held by Not-for-Profit Organizations*. The Board continues to work on a number of issues including:

- When is a confirmation from a broker sufficient evidence as to the existence of securities? May such a confirmation generally be considered as equivalent to a confirmation of accounts receivable? Under what circumstances must an auditor consider the internal control of the broker?
- When should an auditor use a specialist in auditing the values of financial instruments?
- How should a situation be handled in which the most qualified specialist relating to a financial instrument has a business relationship with the client and/or has developed the instrument?

Attestation Re-Codification

The ASB has undertaken a series of projects to improve the usefulness of the Attestation Standards. The Attestation Stan-

dards were first issued approximately 12 years ago. During the past few years, there has been a proliferation of engagements performed pursuant to these standards. For example, the recently developed WebTrust attestation service provides guidance about policies and controls of entities offering services or products for sale over the Internet. Additionally, regulators are increasingly seeking to obtain assurance from the public accounting profession as to the reliability of an entity's assertions about internal control, compliance with laws and regulations, and a variety of other matters.

The first project is currently outstanding as an exposure draft that focuses primarily on improving the understandability of the conclusion communicated by the practitioner in an attest engagement. The proposed SSAE would:

- Enable the CPA to report directly on a specified subject matter, such as internal control or on management's assertion about internal control. For example, the CPA could now express a conclusion about internal control in part as:

In our opinion, Brody Company maintained effective internal control over financial reporting as of December 31, 19XX, based upon criteria established in [identify criteria].

Alternatively, the CPA could continue to report on management's assertion about internal control in part as:

In our opinion, management's assertion that Brody Company maintained effective internal control over financial reporting as of December 31, 19XX is fairly stated, in all material respects, based upon criteria established in [identify criteria].

- Eliminate the requirement for a separate presentation of management's assertion in certain cases where the assertion is included in the introductory paragraph of the CPA's report.
- Align attestation reporting language to that included in SAS No. 58, *Reports on Audited Financial Statements*.
- Provide guidance on the relationship between the *Attestation Standards* and the *Quality Control Standards*.

Electronic Dissemination of Financial Information

This task force is surveying CPAs on their experiences and beliefs relating to appropriate auditor responsibility when a client's financial statements are disseminated electronically, particularly on a web site. For example, should an auditor have a responsibility to determine that audited financial statements are properly included on a client's web site? If so, how far does this responsibility go? Should each number and word within the financial statements be compared to the "hard copy" financial statements"? Should changes to the website that might affect the financial statements be monitored? Should an auditor determine

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STANLEY F. BIGGS TO RECEIVE OUTSTANDING DISSERTATION CHAIR AWARD

Stanley F. Biggs will be presented with the Auditing Section's Outstanding Dissertation Chair award during the Section's luncheon at the AAA Annual Meeting in New Orleans. Professor Biggs is KPMG Peat Marwick Professor of Accounting at the University of Connecticut. His Ph.D. is from the University of Minnesota in 1978. He has been at the University of Connecticut since 1984 and has also taught at the University of Minnesota, the University of Wisconsin-Madison and the University of Southern California. He has also served as a visiting professor at the University of Maastricht in The Netherlands, the Norwegian School of Management, Sandvika, Norway, and the University of New South



Stanley F. Biggs

Wales. At the University of Connecticut he teaches auditing, financial accounting and a doctoral seminar in judgment and decision-making. He has served on the editorial boards of *The Accounting Review*, *Auditing: A Journal of Practice & Theory*, *Behaviorial Research in Accounting*, *Accounting Horizons*, and *Advances in Accounting*. His research has investigated decision behavior of auditors, financial analysts and bankers involved in complex tasks and has been published in *The Accounting Review*; *Journal of Accounting Research*; *Management Science*; *Accounting, Organizations and Society*; *Auditing: A Journal of Practice & Theory*; *Artificial Intelligence Magazine*; *International Journal of Intelligent Systems*, *Expert Systems Review*; and *Management Information Systems Quarterly*. His current research interests involve developing theories and descriptive evidence of auditor expertise.

ASB Update

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that any "links" to financial statements are properly identified as "unaudited"? This project is at an early stage of development and I particularly encourage any academics with insights into such issues to contact me.

Interpretations

• **Year 2000 Issue.** A continuing series of interpretations addressing this computer processing problem is in progress. Responsibilities include:

Overall—The auditor's responsibility relates to the detection of material misstatements of the financial statements being audited, whether caused by the Year 2000 Issue or by some other cause. An auditor does not have a responsibility to detect current or future effects of the Year 2000 Issue on operational matters that do not affect a client's ability to prepare financial statements.

Planning—The results of an auditor's consideration of the methods used to process accounting information pursuant to AU 311 may affect the auditor's assessed level of control risk, testing of internal control, and substantive procedures.

Internal Control Deficiencies—An internal control deficiency, including one relating to the Year 2000 Issue, becomes a reportable condition only when, in the auditor's judgment, it could adversely affect the organization's ability to record, process summarize, and report financial data consistent with the assertions of management in the financial statements being audited. For example, during the audit of financial statements for the year ended December 31, 1997, an auditor may become aware of computer programs that are correctly processing current data,

but would not function correctly if used to process data in the year 2000. This is not considered a reportable condition (although best practice would suggest that the auditor might wish to communicate it to management). Beginning with the January 1998 *Codification of Statements on Auditing Standards*, this and the preceding two areas follow AU 311.

Going Concern—This recently issued interpretation provides illustrations on how the Year 2000 Issue relates to SAS 59. It suggests that the auditor does not have a responsibility to plan and perform procedures solely to identify conditions and events relating to the Year 2000 Issue. However, the auditor does have a responsibility to consider whether the results of procedures performed in planning, gathering evidential matters relative to the various audit objectives, and completing the audit identify such conditions and events. In brief, conditions and events relating to the Year 2000 Issue must be considered in conjunction with other conditions and events in the consideration of a client's going concern status.

Management Discussion and Analysis—This interpretation is still in progress; it will provide guidance similar to that outlined above for MD&A engagements.

Segmental Disclosures—This interpretation, still in progress, will update the guidance in SAS 21 (AU 435) pursuant to the new accounting requirements of SFAS 131.

Finally, as always, if you have areas that you believe that ASB should consider I would appreciate your input; it need not be more than a paragraph or two summarizing the area. Also, I am interested in any research in which you may be involved that may provide insights into any of the above issues.

CONCURRENT SESSIONS SCHEDULE
AMERICAN ACCOUNTING ASSOCIATION 1998 ANNUAL MEETING
NEW ORLEANS, LOUISIANA

MONDAY, AUGUST 17 (10:30 AM – NOON)

Session Title: Audit Section's Practice Advisory Council Presents:
Electronic Commerce—Accountability Issues

Moderator: Tom Powell
Chairperson, Practice Advisory Council

Panelists: Mady Jalinous
President, Global Business Alliance

Graham Joscelyne
Auditor General, The World Bank

Gaylen Larson
Member, Financial Accounting Standards Board

MONDAY, AUGUST 17 (1:45 PM – 3:15 PM)

Session Title: Experimental Markets and Modeling

Moderator: Roger Martin
Michigan State University

Externalties and International Minimum Quality Standards When Demand is Rigid: Some Lessons from the Market for Audit Services. Marco Trombetta, The London School of Economics and Political Science.

The Audit Review Process: A Game-Theoretic Analysis. Scott Boylan and Ella Mae Matsumura, both at the University of Wisconsin—Madison and Robert Tucker, Northern Illinois University.

Auditor Reputation Building. Brian W. Mayhew, Georgia State University.

Discussant: Ron King
University of Washington—St. Louis

AUGUST 17 (3:45 PM – 5:15 PM)

Session Title: Internal Audit and Internal Control

Moderator: K. Raghunandan
University of Massachusetts Dartmouth

Agency Relationships and Internal Auditors' Consideration of Fraud. Bryan Church and Arnie Schneider, both of Georgia Tech and Jeffrey McMillan, Clemson University.

An Analysis of the Demand for Reporting on Internal Control. Heather M. Hermanson, Kennesaw State University.

The Effects of Internal Audit Outsourcing on External Auditor Independence. Jordan Lowe, Virginia Polytechnic Institute & State University, Marshall Geiger, University of Rhode Island, and Kurt Pany, Arizona State University.

Discussant: Susan Ayers
University of Tennessee

MONDAY, AUGUST 17 (3:45 PM – 5:15 PM)

Session Title: Audit Planning

Moderator: David Satava
University of Houston—Victoria

Comprehension of Nonroutine Transactions During Audit Planning: Evidence from Free Recalls and Inferences. Jerry Strawser, University of Houston, William Shafer, California State University—Los Angeles, and Roselyn Morris, Southwest Texas State University.

The Interaction Between Internal Control Assessment and Substantive Testing in Audits for Fraud. Reed Smith, Sam Tiras, and Stan Vichitkarn, all of the University of Oregon.

The Effects of Decision Aid Orientation and Client Financial Health on Risk Identification, Documentation, and Assessment for Actual Audit Clients. Jean Bedard, Northeastern University and Lynford E. Graham, Rutgers University—Newark.

Discussant: Mark Nelson
Cornell University

TUESDAY, AUGUST 18 (10:30 AM – 11:45 AM)

Session Title: Webtrust and Other Electronic Commerce Assurance Services

Moderator: Glen L. Gray
California State University, Northridge

Panelists: Roger Debrecey
Nanyang Technological University

Ted Mock
University of Southern California

Walter Primoff
*Deputy Executive Director,
New York State Society of CPAs
Member, AICPA Electronic Commerce
Assurance Services Task Force*

Gary Riske
*Information Risk Management Partner,
KPMG Peat Marwick
Member, AICPA Electronic Commerce
Assurance Services Task Force*

Raj Srivastava
University of Kansas

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Concurrent Sessions... (Continued from page 5)

TUESDAY, AUGUST 18 (10:30 AM – NOON)

Session Title: Independence–Experimental Markets and Modeling

Moderator: Richard Brody
University of Nevada, Las Vegas

Negotiations as the Auditor's Response to the Client's Wishes About Financial Accounting and Disclosure Choices. Steve Salterio and Mike Gibbins, both at the University of Alberta.

Low Balling, Legal Liability, and Auditor Independence. Zhaoyang Gu and Chi-wen Jevons Lee, both at Tulane University.

Incentives in Outsourcing Internal Audit. Nan Zhou and Murugappa Krishnan, both at the University of Minnesota.

Discussant: Galen Sevcik
Georgia State University

TUESDAY, AUGUST 18 (1:45 PM – 3:15 PM)

Session Title: Audit Markets

Moderator: Philip Wallage
University of Amsterdam

Did the 1991 Amendment to Section 86 of the Ontario Municipal Act Improve Competition in the Municipal Audit Market in Ontario? Sati P. Bandyopadhyay, University of Waterloo and Jennifer L. Kao, University of Alberta.

The Effect of Auditor Choice on Regulatory Attention in the Credit Union Environment. D. Lee Warren, Belmont University, Greg Trompeter, Boston College, and Tim Pearson, West Virginia University.

Board Governance and Audit Firm Type. Mark S. Beasley, North Carolina State University and Kathy R. Petroni, Michigan State University.

Discussant: Dan Simunic
University of British Columbia

TUESDAY, AUGUST 18 (1:45 PM – 3:15 PM)

Session Title: Auditor Performance and Review

Moderator: Jay C. Thibodeau
Bentley College

Accountability Effects on Auditors' Performance: Influence of Knowledge, Problem-Solving Ability and Task Complexity. Hun-Tong Tan and Alison Kao, both of Nanyang Technological University.

The Role of Outcome Information in the Evaluation of Auditor Performance in Trial Settings. John Wermert, Drake University.

The Effects of Specialization in Audit Workpaper Review on Review Efficiency and Reviewers' Confidence. E. Michael

Bamber, University of Georgia and Robert J. Ramsay, University of Kentucky.

Discussant: Jay Rich
University of Connecticut

TUESDAY, AUGUST 18 (3:45 PM – 5:15 PM)

Session Title: Audit Markets and Auditor Reporting

Moderator: Allen Craswell
University of Sydney

Auditor Changes and Discretionary Accruals. K. R. Subramanyam and Mark L. DeFond, both of the University of Southern California.

Risk Based Client Screening by the Big 6 Accounting Firms. Jere Francis and John K. Reynolds, both of the University of Missouri–Columbia.

A Comparative Investigation of the Reporting of the External Auditor in the U.K., Germany, and Denmark. Lars Kiertzner, The AARHUS School of Business.

Discussant: Ken Gaver
University of Georgia

TUESDAY, AUGUST 18 (3:45 PM – 5:15 PM)

Session Title: Audit Errors

Moderator: Jack Kiger
University of Tennessee

Reasons Generation: A Comparison Between Audit Groups and Individual Auditors. Janne Chung and Gary S. Monroe, both of Edith Cowan University.

Audit Investment in Response to Litigation Potential, Misstatement Direction, and Fee Structure. Jamie Pratt, Indiana University, Orié Barron, Penn State University, and James D. Stice, Brigham Young University.

Assessments of Relative Frequency and Relative Importance of Errors by Audit Partners in the Banking and Healthcare Industries. Catherine Usoff and Vincent Owhoso, both of Bentley College, and William F. Messier, Jr., Georgia State University.

Discussant: Mark Peecher
University of Washington

WEDNESDAY, AUGUST 19 (10:30 AM – NOON)

Session Title: Client Acceptance and Quality Control

Moderator: Mary Callahan Hill
Kennesaw State University

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Concurrent Sessions... (Continued from page 6)

General Technologies Group Ltd.: An Audit Case. Michael C. Knapp, University of Oklahoma and Carol A. Knapp, University of Central Oklahoma.

Risk, Strategy, and the Client Acceptance Decision. Karla M. Johnstone, University of Wisconsin–Madison.

The Role of Client Integrity in Client Acceptance Decisions. Philip Beaulieu, University of Calgary.

Discussant: Kathryn Kadous
Rutgers University

WEDNESDAY, AUGUST 19 (10:30 AM – NOON)

Session Title: Audit Evidence: Search and Evaluation

Moderator: Brian Ballou
Auburn University

The Interdependence of Hypothesis Generation and Information Search in Diagnostic Reasoning. Stephen Asare and Arnold Wright, both of Boston College.

Developing Analytical Procedures Expertise: Is Error Specific Experience Equivalent to General Audit Experience? Ed O'Donnell, Mississippi State University.

Analytical Modeling of Multiple Hypotheses Evaluation in Auditing. Arnold Wright, Boston College, Raj Srivastava, University of Kansas, and Ted Mock, University of Southern California.

Discussant: Stan Biggs
University of Connecticut

WEDNESDAY, AUGUST 19 (1:45 PM – 3:15 PM)

Session Title: Practice Development–Firm Image and New Service Lines

Moderator: Morley Lemon
University of Waterloo

Voluntary Attestation in the Asset Management Industry: Its Influence on Users' Perceptions and Decisions. Audrey A. Gramling, University of Illinois and Neil Fargher, University of Oregon.

An Examination of Factors Affecting Audit Practice Development. Jeffrey Cohen and Greg Trompeter, both of Boston College.

The Corporate Images of the 1996 Big 6 and the 1987 Big 8. Peter Moizer, Leeds University.

Discussant: Karen Pincus
University of Arkansas

Auditing Section Forum Papers

Big 6 Market Share Differentiation in City-Level Audit Markets. Donald J. Stokes, University of Technology, Sydney, Jere R. Francis, University of Missouri–Columbia, and Don Anderson, University of Queensland.

The Influence of Audit Committees as Boundary Spanners in the Selection or Retention of External Auditors. Alan Reinstein and Barbara Price, both of Wayne State University, Thomas R. Weirich, Central Michigan University.

The 150-Hour Rule: An Analysis of Education Requirements in the Audit Market. Chiawen Liu, Yuan Ze University, Chi-wen Jevons Lee, Tulane University, and Taychang Wang, National Taiwan University.

Calibration: A Comparison between Audit Groups and Individual Auditors. Gary S. Monroe and Janne Chung, both at Edith Cowan University.

The Control Environment and Financial Reporting Decisions. Jill D'Aquila, Iona College.

The Provision of Assurance Services: An Experimental Investigation of the Peer Review Process. Jeff L. Payne, University of Mississippi.

The Effect of the Reform Act and Central Bank on Naming Auditor Defendants in Securities Class Actions. Ross D. Fuerman, Suffolk University.

Client Acceptance and Retention: A Case. Stanley E. Jenne, University of Montana.

Toward a Model of Risk Management in Auditing. Denise M. Patterson, California State University–Fresno, H. Fenwick Huss and Fred A. Jacobs, both of Georgia State University, and Manyong Park.

Outsourcing of Internal Audit Function: Implications for Auditor Objectivity. Sunita S. Ahlawat, Rutgers University.

The Premium for Specialization: Does it Exist for Non-Big 6 Audit Firms? Christine Jubb, Keith A. Houghton, and Russell Mathews, all of the University of Melbourne.

The Relevance of Audit Committees for Colleges and Universities: Insights from Administrators. Robert C. Elmore, Tennessee Tech University, Zabihollah Rezaee, Middle Tennessee State University, and Joseph Z. Szendi, Reutlingen University–Germany.

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Forum Papers... (Continued from page 7)

Agency Costs and Audit Pricing: Evidence on Discretionary Accruals. Judy Tsui, Ferdinand A. Gul, and Charles J. P. Chen, all of the City University of Hong Kong.

The Role of Audit Industry Expertise and Auditee Profitability in Pricing New Engagements. Paul L. Walker, University of Virginia and Jeffrey R. Casterella, University of Auckland.

An Attentional Model of Serially Received Information in Accounting Judgment. Bairj Donabedian, Pace University.

On the Usage of Analytical Procedures: Direct Evidence From Auditors. Chak-Tong Chau and Stephanie Higby, both of the University of Texas at San Antonio.

State Accountant Privity Laws: Narrowing the Scope of Accountant Liability to Third Parties. Carl Pacini, Georgia Southern University and David Sinason, Northern Illinois University.

Auditors' Assertion-Level Inherent Risk Assessments: A Descriptive Analysis. Gary P. Braun, University of Texas at El Paso.

A Comprehensive Structure to Help Analyze, Detect and Prevent Fraud. Mohamed Bayou, University of Michigan–Dearborn and Alan Reinstein, Wayne State University.

On the Aggregation and Disaggregation of Audit Evidence. Anthony Steele, University of Warwick and Paul C. van Batenburg, Deloitte & Touche–Amsterdam.

The Shareholder Wealth Effects of Shifts in Auditor Liability Laws. Carl Pacini, Georgia Southern University and Patrick F. Maroney, Florida State University.

Accounting Practitioners' Views on the AICPA's New Assurance Services. William E. Shafer, California State University–Los Angeles and Roselyn E. Morris, Southwest Texas State University.

The Impact of Non-Financial Performance Indicators on Auditors' Analytical Review Judgments. Gary L. Holstrum, Sandra L. Schneider, Tanya L. Benford, Christie L. Comunale, and Monica D. Barnes, all of the University of South Florida.

Internalizing the External Audit: A Transaction Cost Approach. Cameron Morrill and Janet Morrill, both of the University of Manitoba.

An Experimental Study of Hong Kong and Chinese Auditors' Perceptions of Auditor Independence. Ramesh Narasimhan, Montclair State University and Stephanie S.H. Ng, Herman Ng & Co.–Hong Kong.

Market Reaction to LLP Formation: A Test of the Insurance Hypothesis. Shifei Chung, Rowan University, Ramesh Narasimhan, Montclair State University, and Pai-Hwang Wei, University of New Orleans.

Audit Size and the Quality of Financial Statements. B. Brian Lee, Concordia University and Hay Y. Chung, Kyunghee University.

Bounded Rationality of Audits: Perspectives from Detection of Earnings Misrepresentations. Amal El-Sabbagh, Concordia University.

Control Risk Assessment: Does the Metric Matter? Ronald E. Marden, Appalachian State University and Somnath Bhattacharya, University of Texas at El Paso.

KARLA JOHNSTONE WINS OUTSTANDING DISSERTATION AWARD

Karla Johnstone will receive the Auditing Section's Outstanding Dissertation Award during the Section's luncheon at the AAA meeting in New Orleans. Karla received her Ph.D. from the University of Connecticut in 1997 and is currently an assistant professor at the University of Wisconsin–Madison. Her research interests relate to judgment and decision making in accounting. Karla's research has investigated the auditor's client acceptance



Karla Johnstone

decision for clients of varying risk levels, the impact of client risk on the judgment processes underlying concurring partner reviews in auditing, client-auditor negotiation and accounting curriculum effectiveness. Karla's teaching interests include auditing and financial accounting. She has received various awards including the Coopers & Lybrand Doctoral Fellowship (1994–1996), the Educational Foundation for Women in Accounting Laurels Fund Scholarship (1996), the University of Connecticut Doctoral Fellowship (1995–1996), and the Connecticut Society of CPA's Ph.D. Scholarship (1995).

CALL FOR PAPERS AI/ET Section Workshop 1998

The Seventh Annual Research Workshop on AI/ET in Accounting, Auditing and Tax will be held Saturday, August 15, 1998, in New Orleans. The workshop is sponsored by the Artificial Intelligence/Emerging Technologies Section in conjunction with the Annual Meeting of the American Accounting Association. The AAA meeting is scheduled from August 16–19, 1998, also in New Orleans.

Topics

Papers should be related to education, application or research and both a financial topic and an artificial intelligence/emerging technology topic.

- **Financial areas:** accounting, auditing, tax and other financial domains.

- **Artificial intelligence areas:** expert systems, neural networks, case-based reasoning, machine learning, natural language processing, intelligent databases, intelligent agents, intelligent devices (smart phone, intelligent TV) and other artificial intelligence areas.

- **Emerging technology areas:** security (system uptime, authenticity), image processing, communications technologies, internet and public on-line services, world wide web, training and technology competency, Year 2000, electronic commerce, workflow technology, private networks (local, wide, municipal, intranets), EDI, data mining, group technologies, assurance services, voice recognition, wireless connectivity, Java and other emerging technologies.

- **Research Issues:** literature reviews, organizing research issues; task selection; feasibility analysis; knowledge acquisition; explanation; knowledge representation (e.g., structure of

rule base, neural network, case base etc.); knowledge processing; uncertainty; integration; intelligent databases; validation and verification; changes in usage; innovative uses; impacts on organizations, management, education, practice; legal implications, deeper understanding of financial domains; cognitive modeling and other issues.

Manuscript Guidelines

Papers submitted elsewhere will be considered. Early stage papers are encouraged. There will be a special issue of the *International Journal of Intelligent Systems in Accounting Finance & Management*. If you want your paper considered for that special issue, please indicate that in your cover letter. Please include your email address.

Submission Deadline

Items submitted for consideration must be received (not just postmarked) by Tuesday, June 16, 1998. Emailed papers in rich text format are encouraged. Please DO NOT fax papers. We expect to inform individuals of accept/reject decisions for the workshop by July 8.

Notification will be made by email to those who have included their email address.

Send email to: brownc@bus.orst.edu

Send four copies of research paper to:

Carol E. Brown
Oregon State University
College of Business
200 Bexell Hall
Corvallis, OR 97331-2603

One Country, Two Professions: Challenges for The Auditing Profession in Hong Kong Special Administrative Region

Judy Tsui, Professor and Head of the
Department of Accountancy, City University of Hong Kong

INTRODUCTION

Professional accountants are regarded as professionals, equal in every respect to the more uniformly recognized professions of law and medicine. In recent years, as the subject matter with which associations are concerned has increased in complexity and volume, their services have become more critical and more in demand. Our industrialized and information technology world of today cannot survive without the services of professional accountants. Perhaps, nowhere in the world is this more evident than in Hong Kong *vis-a-vis* the Chinese Mainland.

STRUCTURE OF THE PROFESSION IN HONG KONG

The profession in Hong Kong acquired legal and professional status under the Hong Kong Professional Accountants Ordinance (1995) on January 1, 1973. This ordinance empowers the Hong Kong Society of Accountants (HKSA) to regulate the practice of the accountancy profession, to conduct examinations to qualify its members and to issue practising certificates. As of January 1998, the Hong Kong Society of Accountants has 13,696 members, 918 accounting firms and 21,084 registered students. Student members need to pass all of the 14 professional examinations and acquire relevant accounting experience before qualifying as professional accountants under the Professional Accountants Ordinance. Currently, the HKSA conducts a Joint Examination Scheme with the Association of Chartered Certified Accountants (ACCA) for the 14 professional subjects. Graduates from recognized degree programs can obtain exemptions from up to ten papers. This Joint Examination Scheme is an implicit acceptance of the U.K. model by the HKSA. Similarly, the Statements of Standard Accounting Practice issued up to 1993 are practically identical to those issued in the U.K. This is perhaps what is known as the colonial legacy, since Hong Kong had been a British Colony for over a hundred years. With the change in sovereignty on July 1, 1997, it is expected that there will be new developments and directions in the auditing profession in Hong Kong.

Since the return of sovereignty to the People's Republic of China, no discernible change in the profession has occurred. Pursuant to the Sino-British Joint Declaration in December 1984 and the Basic Law adopted by the National People's Congress of the PRC in April 1990, it is expected that there should be little or no material change for 50 years. It follows that there should not be significant changes in the profession in Hong Kong SAR.

New Directions

To prepare the auditing profession in Hong Kong to face up to the unprecedented challenges ahead in the 21st century, the

HKSA believes that a new strategic direction in the training and accreditation of professional accountants is called for. This change, in fact, occurred as early as 1990. The Hong Kong Society of Accountants (HKSA) in its Third Long Range Plan (1993) has decided to upgrade its already highly respected qualification to an internationally recognized one. Professional accountants in Hong Kong must possess knowledge and skills which are not only internationally transferable, but also uniquely relevant to Hong Kong's special environment. It is opportune for HKSA to draw up its own list of competency standards and requirements. The HKSA should also develop its own independent professional examinations. This well-established framework of professional accreditation will enable the auditing profession in Hong Kong to secure a foothold into the 21st century for its further advancement. It is expected that by raising the admission requirement to graduate entry and implementing its own professional examination system, the HKSA, under the framework of international trade organizations, will establish mutual recognition with internationally reputable professional accountancy bodies. To this end, a Steering Committee on Professional Accreditation was set up to draw up proposals for a new professional accreditation system. The Society carried out three phases of consultation. The first Consultation Paper "Into the 21st Century-Accreditation of Professional Accountants in Hong Kong" was published in 1995. This paper proposed to establish the Society's own independent professional examination with graduate entry.¹ This is based on the belief that graduate entry will have a positive effect on the quality of intake to the profession and strengthen the basis for further development. This graduate entry admission requirement will bring HKSA in line with many top tiered professional accountancy bodies around the world. With some 30 written responses and informal feedback obtained from numerous forums, the HKSA drew up a Position Paper with the help of a consultant in 1996. The details of the Position Paper included the proposals of a Conversion Program and a Foundation Program designed for nonaccountancy graduates and sub-degree diplomates respectively. There was widespread support for the Society to upgrade to graduate entry and to implement its own Professional examinations. In June 1997, the Society published the Position Paper "Accreditation of Professional Accountants in Hong Kong: Into the 21st Century: New Professional Accreditation System." This paper sets out the objectives of the framework for membership

(Continued on page 11)

¹ Currently, the HKSA runs a Joint Examination Scheme with ACCA which does not require graduate entry.

One Country, Two Professions: ...

(Continued from page 10)

requirements, identifying important elements and the detailed framework for membership requirements.

The primary objective for this new professional accreditation system is to ensure that professional accountants in Hong Kong SAR possess the requisite competencies to meet the challenges in Hong Kong, mainland China and the Asia Pacific region. This development recognises the unique position of Hong Kong as an international financial centre and a major player in the Asia Pacific region. In particular, the development of mainland China has resulted in a significant impact on the Asia-Pacific economies with new challenges confronting professional accountants in Hong Kong SAR. The present Joint Examination scheme that HKSA has with ACCA does not explicitly address these unique challenges for professional accountants in Hong Kong. Associated with this unique development, there is a worldwide trend to require graduate entry in order to further upgrade the quality of future professional accountants.

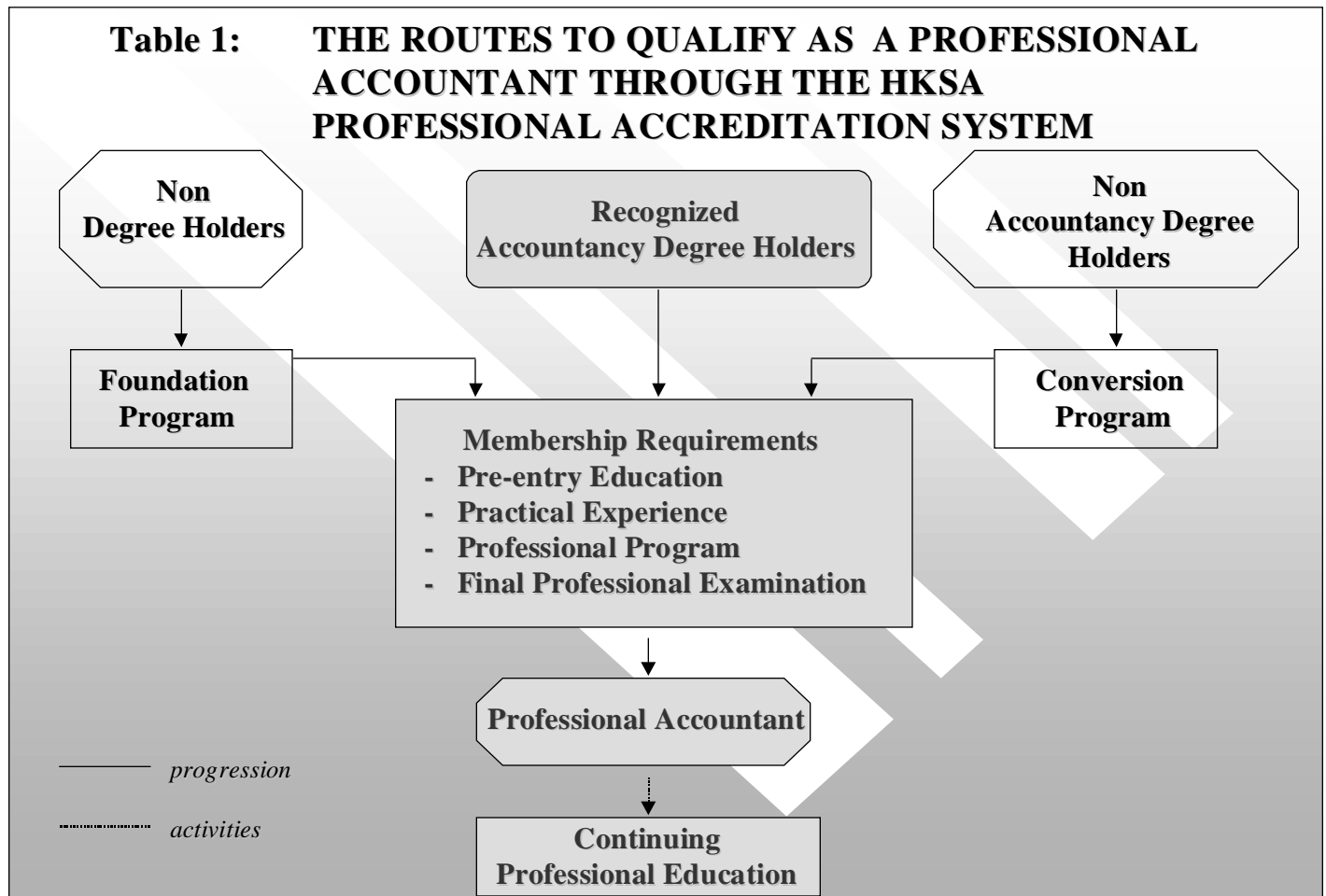
The Society recognizes that many of the generic skills included in graduate level competencies are becoming increasingly important to the accountancy profession. The focus of the Society is to identify competencies required of competent practitioners. The fields of competency include: Auditing, Financial Ac-

counting and External Reporting, Financial Management, Information Management and Technology, Legal Environment of Business, Management Accounting, Professional Ethics and Taxation, and Tax Planning. The incorporation of communications, ethics, information technology and international accounting, and business will be integrated into each of the above fields of competency.

The objective of the new Professional Program is to enhance candidates' skills in advanced technical know-how in accounting and its related disciplines, and to develop a strong sense of professionalism and ethics. The program includes four professional core modules namely, External Accountability, Financial Aspects of Business Strategy and Management, Systematic Overview and Attestation of Information Processes, and Taxation and Tax Planning. Each module requires 120 hours of self-study with attendance and participation required in four workshops and satisfactory performance in a two-hour open book examination. There is a final professional examination requirement which comprises a six-hour examination held in two sessions. It is designed as an integrated case study type examination which tests the integration of all competencies required of a practitioner. Details of the routes to qualify as a professional accountant are given in table 1.

(Continued on page 12)

Table 1: THE ROUTES TO QUALIFY AS A PROFESSIONAL ACCOUNTANT THROUGH THE HKSA PROFESSIONAL ACCREDITATION SYSTEM



One Country, Two Professions: ...

(Continued from page 11)

An international consortium, consisting of the Institute of Chartered Accountants in Australia, Institute of Chartered Accountants of New Zealand and Deloitte Touche Tohmatsu, was established in 1997 to develop course materials for this new program. It is expected that this team will be able to further the long term cross-border cooperation amongst professional accountancy bodies. The materials developed will have an international focus with a strong local orientation, particularly in mainland China.

Another contentious issue facing the profession after 1997 is the language issue. The new professional examinations will continue to be conducted in English since this is essential in maintaining Hong Kong as an international financial center. The use of English will further enhance the international recognition of the future HKSA qualification. There is a Chinese proverb that says "it takes a decade to grow a tree and a century to foster a man of virtue". Though mother tongue teaching is highly promoted in Hong Kong in recent years, it will take many more

years before professional accountants can communicate effectively in both languages. It will even take a much longer time before Chinese can take precedence over English. The need to continue to promote English as an international language cannot be overemphasized. On the other hand, the promotion of the Chinese language in the profession cannot be overlooked. In times to come, a parallel system may materialize.

CONCLUSION

The new professional accreditation system is introduced to ensure that Hong Kong's professional accounting standards reflect international standards. This will facilitate the recognition of the accounting profession in Hong Kong as one worthy of international repute. With the higher professional standard of professional accountants in Hong Kong, we can serve as a bridge in cooperating with mainland China to achieve its targets in the modernization process including upgrading its accounting profession to meet international standards. In time, the accounting profession in Hong Kong and the mainland will converge smoothly and no doubt be one profession in one country.

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CALL FOR PAPERS 1999 AAA Western Regional Conference April 29–May 1, 1999 Newport Beach, California

The AAA's 1999 Annual Western Regional Conference will be held at the Westin South Coast Plaza Hotel in Newport Beach, California, April 29–May 1, 1999. Now in its 34th year, the Western Regional Meeting brings together 250–300 scholars—faculty, administrators and doctoral students—for presentations of papers, panels and workshops on new developments in accounting. The theme of the conference will be Electronic Commerce.

The Westin is a well-located business hotel, nestled in the heart of Southern California's Orange County. Close to fine beaches and attractions like Disneyland, the hotel is a short, free shuttle ride from the John Wayne Orange County, California, International Airport. There also are a host of shuttles connecting the hotel with the Los Angeles International Airport and other airports serving Southern California. The American Accounting Association has negotiated special discount rates for the hotel and airfares.

Papers submitted for presentation will be blind refereed, and authors of accepted papers can choose to have either an abstract

or an up-to-eight-page version published in the *Proceedings*. Five copies of completed manuscripts conforming to *The Accounting Review* style guidelines are to be submitted; the submission deadline is November 1, 1998. Papers will be presented in 90-minute concurrent sessions on Friday, April 30 and Saturday, May 1.

For further information and updates, visit the Western Region's web page at <http://www.rutgers.edu/accounting/raw/aaa/western/western.htm>, or contact:

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HAVE YOU SEEN...?

Greg Trompeter, Boston College, and Tim Pearson, West Virginia University

Given that this is the last *Have You Seen* column that we will compile, we would like to take the opportunity to thank Peter DiCarlo and Jen Gregorski for their invaluable assistance over the past three years.

Greg Trompeter and Tim Pearson

“An Examination of Moral Development within Public Accounting by Gender, Staff Level, and Firm,” by R. A. Bernardi and D. F. Arnold, *Contemporary Accounting Research* (Vol. 14, Number 4, 1997): 653–668.

This study extends prior research on the average level of moral development in public accounting by examining five large accounting firms and multiple staff levels. The research highlights the need to include auditors from several firms in research designs, provides evidence of differences in moral development among public accounting firms, and profiles the profession’s average level of moral development for three levels. The data are from 494 managers and seniors from five Big 6 firms. Using the defining Issues Test (Rest 1979a) to measure moral development, several results were noted. First, the results indicate a difference in the average level of moral development among firms, suggesting that use of subjects from only one firm inhibits the generalizability of findings regarding moral development. Second, female managers are at a significantly higher average level of moral development than male managers. The data suggest that a greater percentage of high-moral-development males and low-moral-development females are leaving public accounting than their respective opposites. These results indicate that the profession has retained, through advancement, males who are potentially less sensitive to the ethical implications of various issues.

“A Bayesian Analysis of Cost-Effectiveness of Auditing for Small Businesses,” by A. V. Deshmukh, P. H. Siegel, and K. E. Karim, *Advances in Accounting* (Vol. 15, 1997): 265–277.

This paper investigates the effect of the responsibility of the auditor to detect management fraud and the reliability of the present audit technology on the cost-effectiveness of auditing and accessibility of audit services to small businesses. By applying the Bayesian framework, this paper demonstrates that due to the low base rates of management fraud, detection of management fraud requires extremely reliable audit technology. This condition provides a plausible explanation for the following phenomena: (1) the existence of audit failure in the presence of management fraud; (2) the increasing reluctance of firms to undertake “risky” audits, making it difficult for small businesses to obtain audit services; and (3) the increasing client concentration in auditing to spread the audit risk resulting in an increased cost of auditing small businesses.

“Determinants of the Justifiability of Performance in Ill-Structured Audit Tasks,” by J. Kennedy, D. N. Kleinmuntz, and M. E. Peecher, *Journal of Accounting Research* (Vol. 35, Supplement, 1997): 105–123.

This paper examines determinants of justifiability of performance in ill-structured audit tasks. Justifiability is the extent to which task performance can be defended. An ill-structured audit task is a nonroutine task that lacks definitive applicable authoritative guidance, has multiple courses of action, and requires the auditor to exercise significant judgment. In the experiment, auditors with varying experience levels assessed performance justifiability for scenarios in which an engagement partner evaluated an aggressive accounting treatment favored by a high business-risk client. The authors manipulated both the level of authoritative guidance presented and whether the engagement partner’s preliminary decision (prior to consultation) was to allow or disallow the aggressive accounting treatment. The authors found that when participants were provided with less authoritative guidance, justifiability depended primarily on the consultation process; in contrast, when participants were given more authoritative guidance, justifiability depended on both the decision and consultation. Regardless of the level of authoritative guidance, justifiability was greatest when the engagement partner and the consultant agreed, and was enhanced when the engagement partner followed the consultant’s advice (regardless of its nature). However, seeking advice but not following it was regarded as more justifiable than not seeking advice in the first place, suggesting consultation is the key to establishing justifiability.

“Accounting Consultation Units: An Organizational Memory Analysis,” by S. Salterio and R. Denham, *Contemporary Accounting Research* (Vol. 14, Number 4, 1997): 669–691.

In this paper, the authors report the results of research that examines the role of accounting consultation units in public accounting firms. They describe the five largest accounting consultation units in Canada. The accounting consultation units are then examined through the lens of organizational memory theory. The authors find differences among the accounting consultation units in their ability to act as a source of organizational memory for their firms. These differences include the following: the amount of resources devoted to the consultation function, the structure of the units, the mandate received by the unit from the firm, and the availability and amount of documentation about previous consultations. These differences suggest that firms’ accounting consultation units differ in their ability to provide technical accounting advice. This variability may affect the actual or perceived quality of such advice to both clients and external regulators. In addition, this paper introduces organizational memory theory to the accounting literature.

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The Audit Review Process—Are Two Heads Better Than One?

By Stephen Asare
Visiting Professor, Boston College

INTRODUCTION

The audit review process is an essential element of accounting firms' quality control programs and is mandated by authoritative standards. Both the practice and academic worlds, albeit for slightly different reasons, devote significant resources to this process. The old saying that "two heads are better than one" motivates the practice world focus. Specifically, public accounting firms acknowledge the fallibility of human judgments and devote resources to the review process with the expectation that the process can detect and correct judgment and decision errors. In this vein, the review process is a control mechanism geared to enhancing the overall quality of the audit.

On the other hand, and predictably so, a curious academic world focuses on examining the conditions under which the review process improves audit quality. That is, rather than accept the notion that "two heads are better than one," academics seek to "audit" that notion with the expectation of identifying the conditions under which the notion is true, false or only partially true. Notice that because academicians seek to "audit" the review process, they gain valuable insights that can enhance the review pro-

cess (in practice) even as a well-conducted audit of a client's financial statements can add value to the client's activities.

The purpose of this essay is to discuss some of the academic findings in a way that, I hope, will enhance additional dialogue between the practice and the academic worlds. As these worlds are interrelated, the importance of such an ongoing dialogue cannot be overemphasized. The following issues are discussed:

- Does the review process lead to an improvement in the overall quality of an audit (i.e., are two heads better than one)?
- How does familiarity with the preparer affect the review process?
- Does review effectiveness depend on whether the review is done in the presence or absence of the preparer?
- How does the rank of the reviewer affect the review process?

I stress that these issues represent a sampler of the academic literature on the audit review process. They are neither meant to be exhaustive or even representative of the many issues that have

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Have You Seen...?

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"The Effects of SAS No. 82 on Auditors' Attention to Fraud Risk Factors and Audit Planning Decisions," by M. F. Zimelman, *Journal of Accounting Research* (Vol. 35, Supplement, 1997): 75–97.

This study investigates whether the Auditing Standards Board's Statement on Auditing Standards No. 82 requiring auditors to separately assess the risk of fraud will lead auditors to spend more time reading fraud cues and design audit plans that are more sensitive to fraud risk. Auditors are currently required to assess misstatement risk without documenting whether an expected misstatement is intentional or unintentional (holistic risk assessments). The author predicts that separately assessing the risk of intentional and unintentional misstatements will lead auditors to spend more time attending to fraud cues. In turn, the information auditors gain by allocating more attention to fraud cues is expected to lead them to develop audit plans that are more likely to vary with fraud risk when compared to plans developed by auditors who make holistic risk assessments. The experiment involving 108 practicing auditors from two Big 6 firms required them to document risk assessments and audit planning judgments. The results provide evidence that separately assessing fraud risk (as required by SAS No. 82) will influence auditors' attention to fraud cues and audit planning decisions. Specifically, SAS No. 82 can be expected to direct auditors' attention to fraud cues and lead to overall increases in budgeted

hours. However, the results suggest that the nature of audit plans may not be affected.

Keeping the Legacy Alive: Articles and Papers, 1979–1997, by Robert Mednick, Andersen Worldwide SC (1998).

For most of the past 25 years Bob Mednick has been involved in professional policy making at Arthur Andersen. For the past 16 years he has been chairman of the policy group and currently holds the title of Managing Partner—Professional and Regulatory Matters. He will retire on August 31, 1998. Throughout his career, Mednick has been at the forefront of debate on financial accounting and reporting issues. In his role with Arthur Andersen and/or as a member or chair of several influential AICPA committees, he has given hundreds of speeches and, quoting from Emerson's Professional Services Review, is possibly the "most published practicing CPA in America."

This book contains reprints of 19 articles and papers that Mednick has written over the past 20 years. Throughout these papers, he regularly addresses the five following basic themes: (1) expansion of the traditional attest function into new attest and assurance services, (2) reform of accountant's legal liability, (3) development of a new approach to establishing standards of auditor independence, (4) updating the licensure and regulation of the profession for the 21st century, (5) transformation of today's CPA into the premier information professional of the 21st century. This book is a thoughtful read for students and professors alike as it contains the vision of one of the profession's leading thinkers of the past 20 years.

The Audit Review Process...

(Continued from page 14)

been (or are being) studied. The interested reader should see the articles written by Solomon (1987) and updated by Rich et al. (1997) for an excellent and comprehensive treatise.

Are Two Heads Better Than One?

Various academic studies have addressed this question. The typical study asks a reviewer to review simulated workpapers containing known or seeded errors. Review effectiveness is then evaluated with respect to whether the reviewers detect and correct these errors. The preponderance of the evidence from these studies suggest that reviewers detect a significant portion, but not all, of the errors. In a slight variation of these studies, reviewed judgments are compared to individual judgments. For instance, a manager may be asked to review a senior's workpapers and the manager-reviewed judgments are then compared to an individual senior or manager judgments. Here again, the results suggest that reviewed judgments are more accurate than individual judgments.

Not only do these results suggest that "two heads are indeed better than one," but also that "two heads are not perfect." A key practice implication of these dual findings is that there are opportunities for additional risk reduction at successive levels of review. In an attempt to reduce cost, there have been attempts to re-engineer the review process away from the traditional, multiple-layered structure. Such attempts should proceed with caution.

Does Familiarity With the Preparer Affect the Review Process?

The adage "two heads are better than one" is as old as another one, "familiarity breeds contempt." Accordingly, concerns have been raised as to whether effectiveness gains that, otherwise, will be derived from the review process can be negated when the reviewer is familiar with the preparer. This is a significant concern given that reviewers frequently, but not always, are familiar with the preparer. Notice that similar concerns have been raised in various recurring relationships, including the auditor client relationship, leading some to propose mandatory client rotation and concurring partner reviews. So does familiarity with the preparer impair review effectiveness?

In one study, reviewers were asked to review the workpapers of either a familiar or unfamiliar preparer (from another office) who had completed either a simple or a complex task. To further reflect practice, reviewers conducted their review under moderate time pressure. The workpapers were very comprehensive and contained the procedures performed, supporting evidence and the conclusions reached. Further, the workpapers contained known preparer errors which allowed review effectiveness to be evaluated.

Interestingly, the study found that being familiar with the preparer led to more effective reviews of the complex task. Specifically, the results indicated that reviewers were more confident of the work done by the familiar preparer, in spite of iden-

tical workpapers. This confidence allowed reviewers of the familiar preparers to focus more of the review time evaluating the preparers' conclusions. In contrast, reviewers of unfamiliar preparers were less confident of the work done and spend too much of the review time reperforming the preparers' audit work. The combined effect of this was that reviewers' of the familiar preparers detected and corrected more of the conclusion errors. This is certainly good news for public accounting firms as audit team members, assigned to several engagements, become very familiar with each other. Perhaps the only bad news is that when the task was simple, overconfidence in the familiar preparer appeared to have slightly hurt review effectiveness.

Two clear practice implications can be drawn from these findings. Flexible time budgets are needed on occasions when a reviewer is asked to review the work of an unfamiliar preparer. Second, reviewers should guard against complacency when reviewing seemingly simple tasks completed by familiar preparers.

Reviewing in the Presence or Absence of the Preparer

A reviewer may review the workpapers in the presence or absence of the preparer. An interesting question that has attracted the attention of academics is the relative effectiveness of the two approaches. In one study, preparers were asked to generate plausible causes of an unexpected fluctuation in a client's financial ratios. The preparers' output was then reviewed by a reviewer in the preparer's absence or presence. The results indicated that reviewing in the presence of the preparer allowed the "two heads" to communicate more effectively and increased the number of plausible causes identified. A key implication of this finding is that the review process could be enhanced if the reviewer maintains regular contacts and discussions with the preparer as the audit work is being done. In effect, and subject to logistical feasibility, a "real-time" review may be more beneficial than a "batch" review.

Does the Rank of the Reviewer Affect the Review Process?

Current review technology is structured such that seniors perform detailed, mechanical reviews and managers perform general, conceptual reviews. Such a work design is justifiable to the extent that seniors are better at detecting mechanical errors and managers are better at detecting conceptual errors. Again, not taking the justification for this work design for granted, academics have studied whether this division of labor matters. In one study, managers and seniors were asked to review simulated workpapers containing known mechanical and conceptual errors. The results confirmed that seniors are better at detecting mechanical errors while managers are better at detecting conceptual errors. Again, this result suggests that the multiple-layered review structure adds value which must be taken into account when redesigning the review technology.

The foregoing discussion highlights four main findings from the academic world. First, the review process enhances audit quality but is not perfect. Second, familiarity with the preparer does not negate the benefits of the review process.

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1998 University of Waterloo Audit Symposium

“Assurance Services: Academic and Professional Perspectives”

Sponsored by:

The Centre for Assurance Services, School of Accountancy, University of Waterloo
and the Auditing Section of the American Accounting Association

Funded by:

The Ernst & Young Foundation

Chair:

W. Morley Lemon, PhD, FCA, CPA
Coopers & Lybrand Professor of Auditing

March 27–28, 1998

Four Points Hotel
Kitchener-Waterloo, Ontario

THURSDAY, MARCH 26

8:00 - 10:00 p.m. Reception—Trillium Suite

FRIDAY, MARCH 27

8:00 a.m. Continental Breakfast—Ballroom

8:45 a.m. **Welcome**— *W. Morley Lemon;*
Jim Kalbfleisch, Vice President Academic &
Provost, University of Waterloo

9:00 a.m. **Plenary Session**— *Robert Elliott*, KPMG,
Peat Marwick LLP

Chair— *J. Efrim Boritz*, University of
Waterloo

(Continued on page 17)

The School of Accountancy, University of Waterloo, held its fifth Auditing Symposium at the University on March 27–28, 1998. The focus of the Symposium was Assurance Services. The program included Bob Elliott, KPMG Peat Marwick LLP, as keynote speaker, a panel of senior partners from the Big 6 discussing Assurance Services from the perspective of their firms and four research papers that were each discussed by an academic and a practitioner.

The Symposium was attended by academics from Canada, the United States and Australia, and practitioners from Canada. The Symposium was co-sponsored by the Auditing Section which will publish the proceedings in a supplement to *Auditing: A Journal of Practice & Theory*. The Symposium was again funded by the Ernst & Young (Canada) Foundation.

The Audit Review Process...

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On the contrary, it enhances review effectiveness. Third, reviewing in the presence of the preparer may be more beneficial than reviewing in the absence of the preparer. Finally,

the multiple-layered review structure, wherein managers review senior-reviewed judgments, is not redundant. As noted, and reflecting my own bias, this is just a sampler of the issues addressed by the academic world. I hope that these findings and their implications will persuade the audit practice world that the academic world can help solve the puzzle on how to enhance audit efficiency and effectiveness.

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Waterloo Conference Program ...

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- 10:30 a.m. Coffee
- 11:00 a.m. **Evidence of Non-Big 6 Market Specialization and Pricing Power in a Niche Assurance Service Market**— *Charles Cullinan*, Bryant College
- Discussants—*Daryl Lindsay*, University of Saskatchewan; *Barry Brownlow*, Brownlow, Thompson & McKay
- Chair— *Ken Klassen*, University of Waterloo
- 12:30 p.m. Lunch—Viking Suite
- 1:45 p.m. **A Methodology for Developing Measurement Criteria for Assurance Services: An Application in Information Systems Assurance**— *Steve Sutton*, Texas Tech University; *Vicky Arnold*, University of Massachusetts Dartmouth; *Douglas Havelka*, Thomas Moore College
- Discussants—*Steve Salterio*, University of Alberta; *Janet Stockton*, BDO
- Chair: *Jennifer Kao*, University of Waterloo
- 3:15 p.m. Coffee
- 3:45 p.m. **Planning Assurance Services**— *Ron King*, *Rachel Schwartz*, Washington University
- Discussants— *Jeff Schatzberg*, University of

Arizona; *Doug Cameron*, Ernst & Young
Chair—*Sally Gunz*, University of Waterloo

- 5:15 p.m. Free time
- 6:30 p.m. Dinner—Viking Suite
Speaker— *Jim Sylph*, CICA
- SATURDAY, MARCH 28**
- 7:45 a.m. Continental Breakfast—Ballroom
- 8:30 a.m. **Timely industry information as an assurance service—Evidence on the information content of the Book-to-Bill Ratio**— *Neil Fargher*, University of Oregon; *Larry Gorman*, California Polytechnic State University; *Michael Wilkins*, Texas A&M University
- Discussants—*Audrey Gramling*, University of Illinois; *Frank Kelly*, Doane Raymond
- Chair—*Susan McCracken*, University of Waterloo
- 10:00 a.m. Coffee
- 10:15 a.m. **Panel Discussion** —*John Beech*, Deloitte & Touche; *Doug Isaac*, Coopers & Lybrand; *David Scott*, Price Waterhouse; *Dave Stephen*, Ernst & Young; *Axel Thesberg*, KPMG; *Ken Vallillee*, Arthur Andersen
- Chair— *Don Cockburn*, Retired Partner, Ernst & Young; Adjunct Professor University of Waterloo
- 12:00 p.m. Lunch—Viking Suite

PARTICIPANTS

Steve Aldersley
Ernst & Young

Vicky Arnold
University of Massachusetts
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Sati Bandyopadhyay
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University of Illinois

Sally Gunz
University of Waterloo

Charlotte Heywood
Wilfrid Laurier University

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Waterloo Conference Program ...
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Diana Hillier
Canadian Institute of Chartered
Accountants

Keith Houghton
University of Melbourne

Doug Isaac
Coopers & Lybrand

Kathryn Kadous
Rutgers University, Newark

Jim Kalbfleisch
University of Waterloo

Jennifer Kao
University of Waterloo

John Kearns
University of Waterloo

Frank Kelly
Doane Raymond

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Janet Stockton
BDO Dunwoody

Steve Sutton
Texas Tech University

Jim Sylph
Canadian Institute of Chartered
Accountants

Axel Thesberg
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Ken Vallillee
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Ping Zhang
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