

Exploring Trust and the Auditor-Client Relationship

Morina D. Rennie
University of Regina

Lori S. Kopp
University of Lethbridge

W. Morley Lemon
University of Waterloo

November, 2006

The authors gratefully acknowledge the financial support of the Canadian Institute of Chartered Accountants/Canadian Academic Accounting Association Research Grant Program and the helpful advice of Mike Gibbins, Steve Salterio, Bill Kinney, Jack Ito, Celeste Brotheridge, Jean-Marie Nkongolo-Bakenda, Glenys Sylvestre, Ron Camp, participants at workshops at the University of Regina, the University of Waterloo, the University of Texas at Austin, the University of Auckland, and Victoria University of Wellington and anonymous reviewers.

Exploring Trust and the Auditor-Client Relationship

Abstract

This research examines financial statement auditors' trust of members of client management in the context of a disagreement with a member of audit client management. While auditor-client trust is essential to the efficient, effective conduct of an audit, the auditor must also act with professional scepticism. In this study we explore factors that can affect auditor trust of client management. In particular we look at attributes of the auditor that may influence the giving of trust, of the client representative that may attract trust, and of the auditor-client relationship. We find that trust-attracting behaviours on the part of a client representative during a disagreement appear to influence the trust that an auditor has for that client representative. Moreover, we find that these behaviours influence the impact that a disagreement has on the auditor's trust of the client representative. We also find a positive association between length of association between the auditor and client and the trust of the client representative. We observe a negative association between frequency of prior disagreements and trust of the client representative and between the auditor's predisposition to trust and the auditor's trust of a client representative. We find that auditors have a variety of strategies for trying to ensure that trust of client management does not impede professional scepticism.

Key Words: Trust, Auditor-Client Relationship, Auditor-Client Disagreements, Professional scepticism

Exploring Trust and the Auditor-Client Relationship

1. Introduction

While professional scepticism is essential to the financial statement audit, it is also the case that an audit could not be conducted in the absence of auditor-client trust. The auditor needs information provided by management and the cooperation of management to carry out the audit. Members of client management have a great deal more specific knowledge about the enterprise upon which the audit is being conducted than does the auditor. The auditor has no option but to bestow some degree of trust upon members of client management.

The peril inherent in conferring trust upon members of client management is that interpersonal trust can grow beyond an acceptable level. Beyond that acceptable level of trust, an emotional attachment may be created that has the potential to compromise judgment through undermining professional scepticism. Auditors currently have no guidance to help them understand what factors influence trust of client management or to assess what level of trust is safe and what level may lead to a situation of compromised judgment. To date there has been little research addressing issues around auditor-client trust that could help standard setters develop such guidance.

In this paper, we take a small step toward gaining an understanding of this important aspect of the auditor-client relationship. In this exploration, we seek simply to learn about factors that may affect an auditor's trust of a member of client management.

This study looks at trust in the context of a disagreement between an auditor and a client representative. Individuals tend not to be aware of the parameters of their trust of

another individual until they are in a circumstance that tests it (Stickel & Gamroth, 2006, 47). An auditor-client disagreement is such a circumstance.

We find that a client representative's display of openness of communication and demonstration of concern affect both the impact of a disagreement on the auditor's trust of the client representative and the overall trust that the auditor has for this individual.

We find that the degree of satisfaction that the auditor has with the outcome of the disagreement positively affects the auditor's trust of the client representative as does the length of association between auditor and client. Both the frequency of prior disagreements with the client representative and the auditor's predisposition to trust have a negative impact on the auditor's trust of the client representative. We also find that auditors have a variety of strategies for trying to ensure that trust of client management does not impede professional scepticism.

This research contributes to the audit judgment literature, particularly that relating to affective aspects of auditor judgment and to literature addressing auditor-client disagreements and negotiations. It also contributes to the broader literature on trust. The remainder of this paper is organized as follows: Background, Hypotheses, Method, Results and Discussion, Limitations, and Conclusion.

2. Background

Trust

Nooteboom (2002, 1-2) describes trust as a "complex and slippery notion" that researchers have had much difficulty with. As a result, the concept does not have a universally accepted definition (Rousseau, Sitkin, Burt, and Camerer, 1998, 394) and no one definition captures this concept in a fully satisfying way. Nonetheless, we offer the

Rousseau et al. definition as a succinct description that covers much of what trust entails:

Trust is a psychological state comprising the intention to accept vulnerability based upon positive expectations of the intentions or behavior of another (Rousseau et al., 1998, 395).

It has been argued that some level of trust is psychologically necessary in order for individuals to cope with complexity—in particular, to deal with the myriad of future possible behaviours (of others) that one must process during the course of decision-making. “It is not possible to acquire information on the future behavior of others except in an incomplete and unreliable fashion” (Luhmann, 1979, 37). Trust allows one to rule out certain negative and unlikely potential behaviours on the part of others, essentially overdrawing on the information that one currently possesses (Luhmann, 32), thus allowing individuals to function in situations that are uncertain, ambiguous and/or risky (Fairholm, 1994, 97). Lewis and Weigert (1985, 970) describe trust as making a “cognitive ‘leap’ beyond the expectations that reason and experience alone would warrant...” This “leap” allows one to act toward other individuals with some assurance even when one does not have all the information about those individuals that one would prefer to have. The trustor acts on faith, choosing to suspend doubts (Möllering, 2005, 30).

Trust between individuals accumulates through repeated encounters between these individuals (Dasgupta, 1988; Lines et al, 2005). Six (2005, 4) observes that “interpersonal trust-building is an interactive process involving (at least) two individuals learning about each other’s trustworthiness.” Cooperation and trust are mutually reinforcing – that is, greater trust leads to more cooperation and more cooperation leads to greater trust (Gambetta, 1988). Sztompka (1999) notes that when trust is confirmed,

returned, or reciprocated, it develops a self-enhancing capacity. “Trust breeds trust” (p. 110). Moreover, in a study of employee trust in managers, Bijlsma-Frankema, Rosendaal, and van de Bunt (2005) find that trust may also “breed heed” in some cases, in the sense that trust may create a desire to obey the trusted individual.¹

It could be argued that the auditing process is an ideal environment for trust development. During the course of the audit, members of client management have many opportunities to demonstrate good faith, thereby accumulating evidence of trustworthiness. The auditor’s predisposition to trust, together with consistent cooperation by client management, can be mutually reinforcing, potentially causing a gradual increase in trust between the auditor and client management.

As more trust accumulates, the cognitive base upon which the trust began is gradually displaced by an emotion-based trust. (For a demonstration of the impact of both cognition and affect on trust in a management context, see Morrow, Hansen, and Pearson, 2004). At higher levels of trust, the affective (emotional) component may be more salient than the cognitive component of trust (McAllister, 1997). If a financial statement auditor’s trust of client management reaches such a stage, professional scepticism may be at risk.

Trust, Professional Scepticism, and Suspicion:

Auditor-client trust is essential for the effective and efficient conducting of a financial statement audit. However, the auditor must not only maintain a sufficient level of trust to conduct the audit, but must also concurrently exercise professional scepticism.

Section 5090 of the *CICA Handbook (Audit of Financial Statements)* states:

The auditor should plan and perform an audit with an attitude of professional scepticism, recognizing that circumstances may exist that cause the financial statements to be materially misstated. (5090.05)

The standard goes on to address the issues of honesty and integrity but does not explicitly address trust:

Honesty and integrity on the part of management and of those charged with governance are critical for the effective operation of the financial reporting process. In planning and performing an audit, the auditor neither assumes that management is dishonest nor assumes unquestioned honesty. This means that it is not the auditor's objective to prove management's honesty and integrity, but to approach the audit with an attitude of professional scepticism that includes being alert for indications of dishonesty. It also means that, notwithstanding prior experience indicating that management is honest, the auditor nevertheless generally obtains corroborating evidence for management representations, including responses to enquiries resulting from the performance of analytical procedures. (CICA, 2006, 5090.07)

An attitude of professional scepticism can be looked upon as a form of suspicion. Hilton, Fein and Miller (1993, 502) describe suspicion in the following way: "To be suspicious is to question the motives that underlie a person's behavior or to question the genuineness of that behavior." However, as professional standards do not ask the auditor to question the motives but merely to be alert for the need to do so, professional scepticism, as practiced by financial statement auditors, can be viewed as a mild form of suspicion.

It should theoretically be possible both to trust client management and to exercise professional scepticism toward that same client management so long as the auditor is able to hold only the minimum required level of trust of management. However, because the audit process provides a strong environment for the development of trust through reciprocal cooperation between auditors and client representatives, it is worth considering whether trust in this relationship can compromise professional scepticism—

that is, create such a faith in the client representative's intentions that violations of the auditor's trust by client management are overlooked.

The trust literature suggests that denial or overlooking of trust violations is exactly what can happen in the presence of a robust trust (McAllister, 1997). In an auditing context, for example, if a client representative were involved in perpetrating fraud and misleading the auditor about it (a trust violation), an excessive auditor-client trust would cause the auditor to overlook red flags associated with the fraud. The level of auditor-client trust may also lead to increased risk of self-deception on the part of the auditor. Mele (2001) describes self-deception as believing something is true because we want it to be true. The auditor must be alert to the possibility that self-deception may increase the likelihood that a trust violation would be overlooked. The consequence of an auditor's inappropriate response to trust violations in an audit could be a failure to detect fraudulent financial reporting.

The Panel on Audit Effectiveness (2000, p. 85), based on an extensive study of the quality of the financial statement audit, concluded that, "the premise of professional scepticism being based on an assumption of neither management's honesty nor dishonesty should be continued, but audit standards need to provide better guidance on how to implement that concept." We agree and we believe that standard setters could do much more in this area by: providing guidance around factors that influence auditor-client trust, identifying symptoms of excessive trust, and proposing methods to mitigate the risk of the auditor's mindset tipping toward unquestioning or uncritical belief in management's honesty.

Prior Research Relating to Trust in the Accounting Literature

There exists a small body of research looking at issues related to auditor trust, suspicion or professional scepticism. Using hypothetical scenarios, Shaub (1996) studied how situational and dispositional factors and past experiences influence the suspicion of auditors toward the client in the scenario. Shaub found that the situational factors of incentive for misstatement and accuracy of board minutes and the experience measure, historical client accuracy, influenced auditors' suspicion of the client.²

Using a series of hypothetical scenarios, Shaub and Lawrence (1996) used structural equation modelling to examine the influence of ethical disposition, experience and situational factors on auditors' professional scepticism. Professional scepticism was measured utilizing the Shaub (1996) suspicion measure. Shaub and Lawrence (1999) looked at levels of professional scepticism at different auditing career stages (based on hypothetical scenarios presented to auditors). They found that staff auditors showed higher levels of scepticism than seniors, managers and partners.

King (2002), in an experiment involving students playing auditor-like and manager-like roles, found that the "auditors" chose less rigorous "audits" in cases when the "managers" previously exhibited cooperative behaviour. This trusting behaviour was neutralized in conditions where the "auditors" were subject to group pressure to conform to group norms.

Hurt, Eining and Plumlee (2005) examined the relationship between auditors' professional scepticism and expanded information search, increased contradiction detection, and increased scrutiny of interpersonal information based on information provided in a hypothetical scenario. They found that the level of professional scepticism did affect these behaviours.

We advance this stream of research by examining trust actually experienced by auditors in situations experienced by those auditors. While assessments based on hypothetical scenarios can provide some understanding of psychological phenomena such as trust and suspicion, they can take us only so far.

Trust research in auditing is difficult to conduct adequately in an experimental setting because it is not possible to capture the multi-year aspect of most auditor-client relationships. To get an understanding of trust that is not purely hypothetical, individuals need a context based on their own experience. In the current study, auditors have provided information about their own trust of an audit client representative in an experience shared by these two individuals—a disagreement between them. The results provide insights into auditor trust of client management that could not be revealed using an experimental approach.

Auditor-Client Disagreements

In fulfilling his/her role in society to add reliability and credibility to management's financial statements, the auditor sometimes encounters situations where he/she has a concern that the unaudited financial statements may be materially misstated. When the auditor challenges client management about this issue, a disagreement incident occurs. Disagreements can also arise from issues around the audit process, audit scope, audit fees, or other matters.

Disagreements are significant events within the auditor-client relationship and events of this type help define the relationship between auditor and client in the future.

Disagreements underline the fact that conflict arises from the differing roles of auditors and client management with respect to the financial statements.

Although there has not been a previous research study looking at auditor-client disagreements *per se*, there has been a body of research looking at the related area of auditor-client negotiation. A disagreement is a necessary pre-condition for a negotiation event (Gibbins, McCracken & Salterio, in press).

Gibbins, Salterio, and Webb (2001) developed a model of auditor-client negotiation based on a survey in which experienced auditors were asked to describe an example of a negotiation incident and answer a series of questions around that incident. The purpose of this research was to learn, in a descriptive sense, about the process of negotiation itself. Gibbins, McCracken, and Salterio (2005, 2006 and in press) have built on this research by incorporating the perspectives of management.

The Gibbins et al. (2001) study has also spawned other research addressing auditor-client negotiation. Trotman, Wright, and Wright (2005), recognizing the importance of auditor-client negotiations, examined three intervention methods for enhancing auditor negotiation skill. Beattie, Fearnley, and Brandt (2004) used a grounded theory approach to develop a model of the negotiation process and the factors that influence the nature of the outcomes of the interactions. Ng and Tam (2003) and Bame-Aldred and Kida (2004) took an experimental approach, looking at judgment in an auditor-client negotiation context.

Our current study contributes to the literature on auditor-client disagreements through its use of an auditor-client disagreement as a context through which to understand trust

issues. We ask the auditor participants in this study to describe an incident involving a disagreement with a client that had occurred during the course of a financial statement audit. We then ask for assessments about trust of the client, client behaviours, and other circumstances surrounding that disagreement and that auditor-client relationship. Understanding trust under disagreement conditions helps us understand one of the important consequences of auditor-client disagreements.

3. Hypotheses

This study uses the auditor-client disagreement context as a platform to help us learn about factors influencing the trust that an auditor has for a member of client management. The factors that can be expected to influence trust are of three general types: (i) characteristics of the auditor that may influence the giving of trust, (ii) characteristics of the client representative that may attract trust and (iii) characteristics of the auditor-client relationship that may affect trust. The trust that an auditor has for members of audit client management could, if too great, pose a threat to professional scepticism.

Insert Figure 1 about here

Characteristics of the auditor that may influence the giving of trust

We propose that the development of auditor-client trust is influenced by the auditor's predisposition to trust. The starting point for the development of specific interpersonal trust is the predisposition to trust held by the individuals involved (Creed & Miles, 1996; McKnight, Cummings & Chervany, 1998; Rotter, 1980) and is a function of one's life experience to that point. For an auditor, this predisposition would be developed not only

through his/her own personal experience and education, but also through his/her professional experience with audit clients.

Prior research has provided some evidence that an individual's predisposition to trust is associated with the degree to which that individual trusts another specific individual in a specific situation (for example, see Johnson-George and Swap, 1982 and Korsgaard, Brodt, and Whitener, 2002). However, in an auditing context, Shaub (1996) found that his measure of general propensity to trust was not associated with auditor suspicion of a client (in hypothetical scenarios provided to subjects) but that propensity to trust audit clients was so associated.

H1: In the context of a disagreement between an auditor and a member of audit client management, the auditor's predisposition to trust is positively related to the auditor's trust of that individual.

Characteristics of the client representative that may attract trust

Second, we propose that the development of auditor-client trust is influenced by characteristics of client representatives that attract trust. Whitener, Brodt, Korsgaard, and Werner (1998), in a manager-employee context, suggest that the following categories of behaviour influence perceptions of trustworthiness (and therefore potentially increase trust given): behavioural consistency (i.e., reliability or predictability); behavioural integrity (consistency between words and deeds); sharing and delegation of control; communication (giving accurate information, providing explanations for decisions, openness); and demonstration of concern. Some of these behaviours could well be relevant in the auditor-client context. Client representatives who are skilled in exhibiting trust-attracting behaviours may have many opportunities to demonstrate them to an auditor during the course of an audit, thereby potentially increasing the level of

trust. In this study, we look at two trust-attracting behaviours that may be relevant in the auditor-client context—openness of communication and demonstration of concern.³

There has been no research in the auditor-client context to date that looks at the impact on trust of openness of communication. However, in studies of employee trust in supervisors, it has been found that trust is enhanced when the supervisor initiates the free exchange of ideas with employees. For example, Gabarro (1978, p. 291) found that both superiors and subordinates believed that free communication about task problems or other issues was very important for the development of trust. Also in an employer-employee context, Korsgaard et al. (2002) found that trustworthy behaviour in the form of openness of communication by a manager was negatively associated with employee attribution of a negative event to the manager. (See Whitener et al. 1998, for other related research). It is of interest to learn whether a similar outcome would be observed between an auditor and client—a very different type of relationship.

H2a: In the context of a disagreement between an auditor and a member of audit client management, the client representative's degree of openness of communication is positively related to the auditor's trust of that individual.

H2b: In the context of a disagreement between an auditor and a member of audit client management, the client representative's degree of openness of communication is positively related to the effect that the disagreement has on the auditor's trust of that individual.

The second trust-attracting behaviour that we are looking at in this study is demonstration of concern. McAllister (1995, p. 29) observes that behaviours such as demonstrating interpersonal care and concern (as opposed to self-interest) can be important for developing affect-based trust. Once trust has grown to this level, the idea that the trusted individual genuinely cares is hard to dispel, even when behaviour becomes inconsistent with this belief (p. 30). Prior research in employee trust in superiors suggests that superiors' demonstration of concern enhances employee trust

(For example, see Whitener, et al, 1998, Korsgaard et al., 2002). This idea has not previously been tested in an auditing context. Again, it is important to learn whether such an impact would also be observed in an auditor-client relationship which does not normally exhibit the power disparity found in the employee-employer context.

H3a: In the context of a disagreement between an auditor and a member of audit client management, the client representative's degree of demonstration of concern is positively related to the auditor's trust of that individual.

H3b: In the context of a disagreement between an auditor and a member of audit client management, the client representative's degree of demonstration of concern is positively related to the effect that the disagreement has on the auditor's trust of that individual.

Characteristics of the auditor-client relationship that may affect trust

Third, we propose that the development of auditor-client trust is influenced by characteristics of the auditor-client relationship. In this study we look at two aspects of the auditor-client relationship. The first is the length of the relationship. McAllister, referring to relationship partners in general, observes that:

As trust matures...cognition-based trust becomes overlaid with affect-based trust and emphasis shifts from beliefs about partner predictability and dependability to beliefs about the stable personal qualities of relationship partners and their orientation to the relationship. This increase in affect-based trust brings needed reassurance to interdependent relationship partners. The process is marked by a gradual decoupling of trustworthiness assessments from the experiential foundations on which trust is initially based (McAllister, 1997, 97)

The tenure of the auditor has long been suggested to be a factor that may cause undue closeness between auditors and their clients. For example, it has often been suggested to be a factor that can compromise independence which is related to professional scepticism (for example see, Kleinman, Palmon and Anandarajan, 1998 for a review). Research in other fields demonstrates a positive relationship between length of association and trust. For example, Coulter and Coulter (2002) found that length of the relationship is a moderating variable in assessments of trust in a service provider. In an

auditing context, Shaub (1996) did not observe a significant relationship between length of association and the auditor's suspicion/trust of the client in hypothetical scenarios. However, effects of long-term association are difficult to capture in hypothetical situations that have not actually been experienced by a study's participants, so we do not necessarily expect that Shaub's result would be observed in the context of actual auditor-client relationships.

H4: In the context of a disagreement between an auditor and a member of audit client management, the length of the auditor-client relationship is positively related to the auditor's trust of the audit client representative.

The second aspect of the auditor-client relationship that we look at is the nature of the relationship with the client—the past experience in this relationship. For this study, we look at the impact of the frequency of prior disagreements with the client on trust. An auditor-client history that includes many disagreements may be indicative of a client representative that tends to push the limits of GAAP or influence the audit process. Repetition of this type of behaviour could well have an impact on an auditor's trust, as the intentions of the client representative may come into question. We expect to see a negative relationship between frequency of prior disagreements and auditor trust in the client representative. Shaub (1996) found an influence of past experience with the client on auditors' trust or suspicion of the client (although not specifically in the area of prior disagreements).

H5: In the context of a disagreement between an auditor and a member of audit client management, the frequency of prior disagreements with the client representative is negatively related to the auditor's trust of that individual.

4. Method

Participants

The participants in the study were 71 partners, senior managers and managers from across Canada. Senior individuals from six national/international accounting firms were asked to distribute our cover letter and instrument to individuals at manager level and above in their firms. The completed materials were then returned to the researchers. See Table 1 for demographic information about the participants and the incidents.

.....

Insert Table 1 about here

.....

Procedure

The instrument first asked the participants to do the following:

Think of a time, since you were at least at the manager rank, when you had a disagreement with a member of client management during the course of a financial statement audit. The disagreement could be either serious or minor. Briefly describe this disagreement (including the issue causing the disagreement).

Our approach is similar to the experiential questionnaire approach (see Gibbins and Qu, 2005) that was employed in the Gibbins et al. (2001) and Gibbins et al. (2005, 2006 and in press) auditor-client negotiation studies, and by Nelson, Elliott, and Tarpley (2002) in an earnings management context, in that it is based on situations that respondents have themselves experienced. The respondents themselves chose the cases on which their responses were based. Our study differs from the above negotiation studies in that it uses disagreements and responses around those disagreements as a means to test hypotheses about factors that may influence auditor-client trust; that is, the nature of the disagreement itself is of interest in this current study only to the extent that it helps us get at auditor's trust of the client representative in the disagreement.

Korsgaard et al. (2002) used a similar approach in a management-employee trust context as did Lind, Tyler, and Huo (1997) in a procedural justice context. We focus on a

significant actual event in an auditor-client relationship. Because this event was a disagreement, the behaviour of the participants would have an important influence on auditor-client trust.

Participants who had never had such a disagreement were asked to skip the questions relating to the auditor-client disagreement. Four participants did so. One participant described disagreements in general rather than a specific disagreement and another participant provided a disagreement from a time before he/she was at the manager level so these responses were not included in analyses relating to specific disagreements. This left 65 responses relating to specific disagreements for analysis. Participants who were able to recall a specific disagreement went on to answer questions about their level of satisfaction with the outcome, the effect of the disagreement on trust, the extent of prior disagreements, behaviours of the client representative during the disagreement, trust of the client representative, tenure with the client, and other information about the disagreement, the client, the firm and the respondent.

Finally, participants answered questions about the importance of trust in the audit and strategies they use to make sure trust for the client does not impede professional scepticism. They also answered some questions about their general trust in people and in clients.

Instrument and Measures

The instrument was carefully developed so as to elicit meaningful and considered responses from our participants. The instrument was developed to allow us to collect both qualitative and quantitative data.

Drafts of the instrument at various stages were presented at research seminars at several universities and sent to expert researchers in the field to obtain feedback. We also pilot tested the instrument with three experienced Chartered Accountants. The quality of the instrument was improved significantly as a result of this process.

Two measures served as dependent variables in this study. The first was the auditor's trust of the client representative with whom this disagreement occurred. The following question was posed. "Based on your past and present experience, how would you characterize the level of trust you have in the client representative with whom you had this disagreement?" This question was adapted from the scale used in the Anderson and Narus (1990) study of distributor firm and manufacturer firm working partnerships.⁴ Our participants' responses were made on an 11 point scale (0 = "Do not trust this individual"; 10 = "Trust this individual completely"). This dependent variable was used for tests of H1, H2a, H3a, H4, and H5.

The second dependent variable was measured as the response to the following question: "What effect did this disagreement have on your level of trust in this client representative?" Responses were made on an 11 point scale (0 = "Significantly weakened trust"; 5 = "No effect on trust"; 10 = "Significantly strengthened trust").⁵ This dependent variable was used for tests of H2b and H3b. The independent variables of interest in these hypotheses were specific client behaviours during the disagreement.

Six independent variables were used to test the hypotheses. The independent variable for H1 was the auditor's predisposition to trust. We used a two item scale to assess this.⁶ Participants indicated their level of agreement/disagreement with the following statements: "Trustworthy clients are the norm" and "Most people are honest in their

dealings with others.” Responses were given on an 11 point scale (0 = “Strongly disagree”; 10 = “Strongly agree”). The first item was chosen from the Shaub (1996) study of auditor suspicion/trust.⁷ The second item was chosen from the McKnight, Choudhury, and Kacmar (2002) trust scale. Cronbach’s alpha on our predisposition to trust scale was .859.

The independent variables of primary interest in this study are those relating to client trust-attracting behaviours. In this study we examine the client’s demonstration of openness of communication and of concern, from the Whitener et al. (1998) model described earlier, to test H2 and H3. We asked the participants to consider the following with respect to the disagreement they had described: “Following are possible behaviours that individuals in disagreements sometimes have. Please indicate on the appropriate scale, the extent to which the client representative displayed each of the following behaviours during this disagreement.” Two of the five behaviours listed were “The client representative demonstrated openness of communication” and “The client representative showed concern about being fair to me” (the other three were filler items).⁸ Each were responded to on 11-point scales (0 = “Not at all”; 10 = “A great deal”).

The two independent variables relating to the auditor-client relationship were tenure and frequency of prior disagreements. Tenure, used to test H4, was measured as the response to the question: “Over how many years had you personally worked on engagements with this audit client at the time of the disagreement?” A supplementary measure of tenure was also taken. It was the response to the question “How many years had your firm been associated with this audit client at the time of this disagreement?”

To measure frequency of prior disagreements (to test H5) we asked subjects to tell us: “To what extent had you had previous disagreements with the client representative with whom you had this disagreement?” The response was given on a 11-point scale (0 = “Never”; 5 = “Occasionally”; 10 = “Frequently”).

A control variable, satisfaction with outcome of the disagreement, was also measured. Following their description of the outcome of the disagreement, participants answered the question “Were you satisfied with the outcome?” Responses were given on an 11-point scale (0 = “Not at all satisfied”; 5 = “Satisfied”; 10 = “Very satisfied”).

The level of analysis of interest is the interpersonal relationship between the auditor and a specific client representative who had been involved in a disagreement with this auditor. Thus both dependent variables are measures at this level of analysis—the impact of the disagreement on the auditor’s trust of this client representative and accumulated level of this auditor’s trust of this client representative.

Some of the independent variables relate specifically to the disagreement itself and so the survey questions are described at that level—in particular, the trust attracting behaviours of the client representative (H2A and H2B). Also, the control variable, satisfaction with the outcome of the disagreement is of this type.

However, the level of trust of a client representative that has been accumulated over time can be expected to be influenced by factors other than this specific disagreement. Therefore, a second type of measure asked for responses at the level of the larger relationship, as two hypotheses predicted that aspects of the relationship would influence the auditor’s trust (length of time working with this audit client and previous

disagreements with the client representative). Moreover, the trust literature suggests that an individual's predisposition to trust can also influence the trust that one has conferred in a specific individual. Therefore, the third level of analysis relates to the auditor's experience beyond this particular disagreement. In particular, the questions relating to the auditor's predisposition to trust were of this type.

Additional analyses were performed to see if other control variables needed to be considered in our analyses. The possible effects of the demographic measures: gender, position in the firm, type of firm, and number of years as a Chartered Accountant on our dependent variables were examined. We found that none of these variables were significantly related to the dependent variables.

5. Results and Discussion

The disagreements, as described by the study's participants, were independently categorized by two of the authors (Cohen's Kappa = 0.948). The raters then consulted with and achieved consensus on the classification of the few items for which they had initially made differing classifications.

The disagreements were of the following types: revenue recognition (7.7%); capitalization of expenditures as long-term assets (10.8%); other recognition/derecognition issues (9.2%); impairment (15.4%); business combinations (9.2%); valuation/measurement issues other than those involving impairment or business combinations (20.0%); presentation/disclosure issues (13.8%); and other issues (4.6%); the remaining disagreements were not described in sufficient detail for a definitive categorization. The nature of the disagreements chosen by our participants are

similar to those identified in the Gibbins et al. (in press) study on auditor-client negotiation.

The descriptive statistics for the dependent, independent and control variables can be found in Table 2 and the correlation matrix for dependent and independent variables can be found in Table 3.

.....

Insert Tables 2 and 3 about here

.....

The hypotheses are predicated on the ideas: (1) that disagreements may influence trust of the other party to the disagreement and (2) that auditors have varying levels of trust in audit client representatives. The distribution of the dependent variables suggests that these presumptions are reasonable.

Participants reported a wide range of influence that the disagreement had on their trust of the client representative involved in the disagreement—with responses covering the entire range of “significantly weakened trust” to “significantly strengthened trust.” The mean of the distribution was 4.94 with a standard deviation of 2.29. Of a total of 65 respondents recalling a disagreement: 24 (36.9%), indicated that their trust of the client representative was weakened by the disagreement; 24 individuals (36.9%) did not change their level of trust as a result of the agreement; and 17 auditors (26.2%) believed that the disagreement strengthened their trust of the client representative.

Participants also reported a full range of accumulated trust of the client representative involved in the disagreement (the question was “Based on your past and present experience, how would you characterize the level of trust you have in the client

representative with whom you had this disagreement?") All points on the scale were represented in the responses—ranging from 0 (Do not trust this individual) to 10 (Trust this individual completely). The mean response (standard deviation) was 6.02 (2.37).

Hypothesis Tests

The hypotheses were tested using multiple regression.⁹ Because all hypotheses specify a direction, one-tailed tests were used. Regression 1 tested H1, H2a, H3a, H4, and H5. Independent variables were: auditor's predisposition to trust, client representative's openness of communication during disagreement, client representative's demonstration of concern during disagreement, tenure of auditor-client relationship, and previous disagreements with client representative (with the auditor's satisfaction with the outcome as a control variable). The dependent variable was the auditor's trust of the client representative.

.....
 Insert Table 4 about here

The results for regression 1 are summarized in Table 4 and provide support for H2A, H3A, H4 and H5 (at $p < .05$ one tailed). The Adjusted R^2 for Regression 1 was 0.45. There was a positive relationship between trust-attracting behaviours by the client representative during the disagreement (openness of communication ($p < .001$) and demonstration of concern ($p < .05$)) and the auditor's trust in the client representative (H2a and H3a). This result indicates that auditor trust of client representatives may be influenced by affect and not purely by cognitively based assessments. This is consistent with findings by Korsgaard et al. (2002) in a study on employees' trust of management.

As discussed earlier, the involvement of affect in a trust relationship can influence one's response to trust violations—something that should be of concern to auditors.

The results also suggest that level of trust is affected by aspects of the relationship between auditor and client. The tenure of the relationship does appear to impact trust (H4), greater length of association being associated with greater levels of trust ($p < .05$). An alternative measure of tenure is the length of association between the audit firm and the client company. The regression was run using this alternative measure with very similar results. Finally, not surprisingly, the frequency of prior disagreements with the client representative had a negative impact on trust ($p < .05$). This finding provides support for H5.

Hypothesis 1 proposed that the auditor's predisposition to trust would be positively related to the auditor's trust in the client representative and was not supported. In fact, the relationship was significant in the opposite direction to that hypothesized. (Because of this, a two-tailed p-value is reported for this variable in Table 4 while the remaining p-values relating to hypothesis tests are reported on a one-tailed basis). A univariate regression with trust of this audit client representative as dependent variable and predisposition to trust as an independent variable was carried out to try to understand this result. The univariate test showed no significant relationship between the two variables ($p = .247$). Only when the client representative behaviour variables were included in the regression, did predisposition to trust become significantly negatively correlated with the level of trust in this audit client representative.

Researchers in other disciplines have observed that when individuals have high expectations of another's behaviour and are disappointed, their negative response is

more extreme than is seen for individuals with low expectations (for example, Brockner, Tyler, and Cooper-Schneider (1992) in a study of institutional commitment and perceived unfairness and Chrobot-Mason (2003) in the context of minority employees' trust of the organization). Although our results suggest only indirectly that something like this may be going on, they do point to an intriguing and somewhat counterintuitive possibility—that auditors with a high predisposition to trust may in fact react more negatively to untrustworthy behaviours on the part of client representatives than those with a lower predisposition. This is an issue that is worth exploring further.

The second regression (Table 5) was concerned with the relationship between client representative trust-attracting behaviours during the disagreement and the impact of this disagreement on the auditor's trust in the client representative (H2B and H3B). Both hypotheses are supported. Client representative's openness of communication ($p < .01$) and the client representative's demonstration of concern ($p < .05$) were associated with the impact of the disagreement on the auditor's trust for the client representative with the auditor's satisfaction with the outcome acting as a control variable. The adjusted R^2 for Regression 2 was 0.25. Again we observe evidence of the role of affect in the auditor-client trust relationship.

.....
 Insert Table 5 about here.

Auditors' views on the importance of trust to the audit

The 71 participants were asked the question "In your experience, how important is it for auditors to trust their clients?" The response scale ranged from 0 (Not at all important) to 10 (Very important). The midpoint of the scale was labelled, "Important."

The mean response to this question was 8.2 (standard deviation = 2.2) which suggests a relatively high level of importance attached to auditors' trust in the client. Participants were asked to explain their answers.

Respondents tended to approach this question from one (or more) of three different (but related) levels of analysis—the role of trust in the auditor-client relationship itself, that it is a part of the client-acceptance decision; the importance of trust to the performance of the audit; and the caution that professional scepticism is important (or that too much trust should not occur) during the process of conducting audit procedures. See Table 6 for a summary of responses.

.....

Insert Table 6 about here.

.....

For those addressing the impact of trust on the auditor-client relationship itself, a prominent theme was that trust is a minimal requirement for allowing a company to be an audit client—for example: if trust isn't present, the auditor should decline the engagement; that trust is a critical/fundamental aspect of the relationship; the relationship is based on trust (no trust—no relationship). Illustrative comments were:

“Trust implies integrity which is a basic requirement for client acceptance...”

“Complete trust in clients' is not acceptable. However, basic trust must be present. Otherwise the auditor must decline the engagement.”

Those that commented on the importance of trust to the performance of the audit described their views in terms of the impossibility (or inefficiency) of performing the audit without trust—for example: the audit would be prohibitively expensive/infeasible; the

auditor can't do a 100% test; an entity that is not trustworthy is not auditable. Some comments falling in this category were:

"It would not be feasible to audit a client where the trust was lacking."

"Where little or no trust exists, the cost of an effective audit is prohibitive."

Other comments in this category of responses related to the practical issue of information asymmetry and the resultant dependency of the auditor for information provided by client representatives. For example:

"An audit will not uncover all matters no matter how well planned and executed. Information and issues need to be raised by the client so that appropriate judgements can be made. As businesses increase in complexity, the auditor cannot be expected to understand all facts to the same extent as management."

"Ultimately, as auditors, we cannot expect to find everything that might be important to the f/s. If matters are hidden, we are at a huge disadvantage. Accordingly, the level of trust is important (to both parties)."

The third category of comments related to the conduct of audit procedures themselves. For example, it was not seen as appropriate to count on management's good faith or to rely on trust when performing audit procedures. The need for scepticism was raised frequently, even though the specific question was about the importance of trust. Some comments in this category were:

"Given the nature of work, while we must always maintain professional scepticism, if you do not have the basic trust that your client is doing all the right things, then we should resign from the account."

"I think [trust]... is extremely important, however, in our role as auditor we still need to ensure we have the appropriate amount of scepticism too – so there is more to it than just trust."

In summary, a basic level of trust is needed to enter into an auditor-client relationship and to be able to conduct an audit; but the auditor must also exercise professional

scepticism. Our concern is whether this trust can or does reach such a level as to compromise professional scepticism. One of our participants put it this way: “If there is no trust, auditor should not accept/re-accept client. Having said that, auditing requires external evidence to support management’s assessments therefore complete trust is dangerous/problematic to remaining continually skeptical.”

How auditors ensure that auditor-client trust does not impede professional scepticism

“The dance between auditors and clients is often very delicate, especially when corporate managers are under intense pressure to put out positive earnings numbers” (Callahan, 2004, 145). So how do auditors, who must hold some level of trust in their client representatives in order to conduct the audit, ensure that client trust does not impede the exercise of professional scepticism? Our participants had many comments to make in this regard. Most comments related to either strategies within the audit process or to the auditor’s attitude/mindset when conducting the audit (several respondents addressed both). See Table 7.

.....

Insert Table 7 about here.

.....

The more prominent theme was the audit process. Several respondents discussed the importance of following a rigorous audit process that follows professional standards and is carried out by well trained, skilful and experienced professional auditors. Careful attention to following accepted auditing procedures is viewed as a means of overcoming issues around the auditor-client relationship. For example:

“Ensure that we have an appropriately planned audit, that looks at all risk and significant areas.”

“Very rigorous/uncompromising internal standards for independence, training and audit file completion.”

Other respondents gave more specific process-related strategies that included: Ensuring that management representations are corroborated/verified/substantiated; having a good/open/frank communication process with client representatives; reviewing audit work at multiple levels (including quality control partner review); training of auditors, rotating of key engagement team members; consulting on critical/difficult issues; ensuring sound knowledge of business and industry; and requiring the client management to provide documentation on accounting policy choices. Some example comments are:

“Do necessary audit work and do not hesitate to push back.”

“Communicate the auditor responsibilities in conducting an audit.”

“I am up front with every issue that arises from the audit.”

“By having my decision reviewed on a regular basis”

“Independent quality assurance reviews and audit risk management”

The second theme of the participants’ comments related to attitude or mind set. Areas covered included: exercising of professional scepticism; maintaining objective/independent attitude; putting trust aside when conducting audit; understanding client motivation; developing a culture of quality in the firm; keeping the perspective of the shareholder in mind; and maintaining attitude of professionalism.

Some illustrative comments are:

“Do not become a ‘friend’.”

“Our first duty is to the shareholders to be their “eyes” and report faithfully and truthfully no matter how difficult that is.”

“Cultural’ attitude of ‘highest quality work’, no client is individually critical to the firm.”

There appeared to be some disagreement on the preferred relationship between the auditor and client representative, however. While some indicated it was important to not let the relationship become close, there were comments that described the value of a close relationship in terms of assessing the client representative’s character.

The compensating strategies suggested by these highly experienced auditors suggest that they are quite aware of the potential problem with the need to trust the audit client representative and at the same time ensure that they conduct a proper audit. It is also apparent from these comments that these auditors are well intentioned in their desire to do the right thing.

It is, however, an unresolved question as to whether the psychological distance, necessary to ensure that a proper audit is done, can be achieved. For example, Bazerman, Morgan, and Loewenstein (1997) and Bazerman, Loewenstein, and Moore (2002), suggest that impartial judgment on the part of auditors is not possible because “bias typically enters unconsciously and unintentionally at the stage of making judgments....” (1997, page 91). Such bias comes into the picture because of unintentional “selective sifting and integrating of audit information” (93). Whether Bazerman (who is not a financial statement auditor) and colleagues, or highly experienced auditors who are involved in auditor-client relationships daily have this right is a question that deserves further exploration. This research does show that trust is influenced by trust-attracting behaviours and the length of the relationship, both of which have the potential to create bonds that affect an individual at levels that he or she is not aware of.

6. Limitations

A limitation of this study is that the subjects were not supervised in completing the survey instrument and so there is a risk that some participants may not have worked independently. However, because the survey responses were based on a specific experience of each individual respondent, the chance of collaboration by respondents is remote. A second limitation is that, to preserve anonymity, the subjects did not identify their firms and so we are unable to indicate the proportionate response by firm and state that each of the six firms participated. Nor did we require those distributing instruments to tabulate the number of instruments distributed compared to those returned. Because our subjects had control over their own data in the sense that they generated the context for the responses, the possibility of non-response bias is not the significant issue that it might be in other situations. A third limitation is that we rely on the recall of the auditors of these incidents and this brings with it the risk that the events were not recalled accurately. Moreover, the respondents recalled unique incidents and these incidents varied in recentness. A fourth limitation, as discussed earlier is the use of a single-item scale for measuring auditors' predisposition to trust. As such, it was not possible to do a Cronbach's alpha measurement. All of these limitations work against observing significant results.

7. Conclusion

Auditor-client trust is essential to the efficient, effective conduct of an audit. Yet the auditor must also act with professional scepticism. In this study we have explored factors that can affect auditor trust of client management. In particular we looked at attributes of a client representative that may attract trust, attributes of the auditor-client relationship

and the auditor's own predisposition to trust. We found that trust-attracting behaviours on the part of client representatives during a disagreement do appear to influence the level of trust that an auditor has for a client representative (and also influence the impact that the disagreement has on the auditor's trust for the client representative). We also found that the length of association between the auditor and client positively influenced trust that the auditors have for a client representative involved in a disagreement and that the frequency of prior disagreements is negatively associated with the auditor's trust. We found that the auditor's predisposition to trust was negatively associated with the trust of the client representative.

We believe this study, which is the first to use actual auditor-client situations to examine real auditor-client trust (rather than hypothetical situations and therefore hypothetical trust) has contributed to three literatures. First, it contributes to the audit judgment literature—especially the potential influence of affect on judgment. More specifically, it adds to the fledgling literature on auditor-client trust. This study also contributes to the auditor-client disagreement literature in that it addresses one potential outcome of an auditor-client disagreement—the auditor's trust of that client representative together with factors that may influence trust in this context. Finally, the study contributes to the larger literature on trust, and in particular, trust in conflict scenarios. Other work in this area (Korsgaard et al, 2002) explored trust of a manager by an employee in the context of a disagreement about the employee's job and in relationship with the fairness of human resources policies. Until the current study, trust influences associated with the behaviours of parties to a disagreement in a relationship other than an employer-employee relationship (and the power disparity implied by that relationship) had not been studied. We have shown that even in a relationship of equals, the behaviour of one party

in a disagreement can impact trust. Moreover, we have shown that aspects of the relationship itself can influence trust.

Our study suggests some fruitful areas for further research. For example, follow up work could be done on the relationship between an auditor's predisposition to trust and the level of trust bestowed on a specific client representative. Another interesting avenue of research would be to look at the relationship between auditors' trust of client representatives and the auditor's professional scepticism or perhaps the relationship between trust and independence. Researchers could also look into other client behaviours that may attract trust. A tangential stream of research would be to consider client trust of auditors in the context of an auditor-client disagreement. There is much more to be learned about auditor-client trust and its relationship with professional scepticism. We leave this to future research.

Endnotes

1. There is no evidence on whether a similar outcome could occur in an auditor-client context—that is, whether auditor trust of client management could create a desire to acquiesce to a client representative's wishes. This may be an important area for future research.
2. Shaub treats suspicion as being synonymous with professional scepticism (Shaub, 1996, 156) and treats trust as being the complement of suspicion (155).
3. Many trust-attracting behaviours could influence an auditor's trust of a client representative. "Openness of communication" and "demonstration of concern" were chosen for this first study examining trust-attracting client behaviours for two reasons: 1. These are behaviours that can be demonstrated during the course of a single disagreement and 2. There has been empirical evidence in another context to support hypotheses about these behaviours in the current study.
4. The adaptation of a question from a study about working partnerships should not be taken as an indication that we believe that an auditor/client relationship is a partnership as clearly it is not. Our choice was motivated by the observation that the Anderson and Narus wording was an excellent way to elicit the participants' level of accumulated trust in another individual in an ongoing relationship – whatever the nature of that relationship.
5. Although the two dependent variables turned out to be correlated, they are distinct concepts. One is a measure of accumulated trust at a point in time and the other is the change in trust due to a specific event (a disagreement).
6. To find a measure of our participants' predisposition to trust, we first examined existing trust scales (approximately 25–30 of them) to assess their appropriateness for our needs. Most are lengthy and many contain questions that are not oriented to experienced professionals. Use of such a scale would risk trying the patience of our (mostly audit partner) participants and take too much of their time. Face validity would also be compromised if the participants could not see the value answering numerous questions that appeared not to be related to the subject of the study. So we opted to use relatively few questions to assess predisposition to trust.
7. The three other items from the Shaub (1996) "General Client Trust Scale" were also included in our instrument to give us the option of using Shaub's measure of predisposition to trust as well. However, we found that Shaub's scale had poor reliability (Cronbach's alpha was .463).
8. The items of interest in this study were listed second and fourth of the five items. The filler items were used to reduce the probability that participants would guess the hypotheses. These filler items were listed first, third and fifth were as follows: "The client representative tried to persuade me that he/she was right by using convincing arguments"; "The client representative tried to use his/her power over me to get what he/she wanted"; and "The client representative seemed willing to compromise to find an outcome that both of us would feel was acceptable." These items were adapted from Lind et al (1997) in a study of procedural justice assessments. Some of these items were correlated with trust (Pearson Correlations (two-tailed) are .006 (n.s.), -.353 ($p < .001$) and .501 ($p < .001$), respectively). However, these items are not part of the

Whitener et al (1998) model and we did not make or test hypotheses about them. Therefore, the results are not reported here.

9. Univariate tests of these variables provided very similar results. Univariate tests showed significant results for all hypothesized relationships in the expected direction, except for hypothesis 1 regarding predisposition to trust, for which the p value (two tailed in this case) was 0.247.

References

- Anderson, J.C., & Narus, J.A. (1990). A model of distributor firm and manufacturer firm working partnerships. *Journal of Marketing* 54(1), 42-58
- Bame-Aldred, C., and Kida, T. (2004) A comparison of auditor and client negotiation decisions. Working paper Washington State University. Available at SSRN <http://ssrn.com/abstract=536903>
- Bazerman, M.H., Loewenstein, G., and Moore, D.A. (2002). Why good accountants do bad audits. *Harvard Business Review* 11, 96-
- Bazerman, M.H., Morgan, K.P, Loewenstein, G.F. (1997). The impossibility of auditor independence. *Sloan Management Review* 38(4), 89-94.
- Beattie, V., Fearnley, S., and Brandt, R., (2004) A grounded theory model of auditor-client negotiations. *International Journal of Auditing* 8(1): 1-19.
- Bijlsma-Frankema, K. Rosendaal, B. W., and van de Bunt, G. (2005). Does trust breed heed? Differential effects of trust on heed and performance in a network and a divisional form of organizing. In K. Bijlsma-Frankema and R. K. Woolthuis (Eds.) *Trust Under Pressure: Empirical Investigations of Trust and Trust Building in Uncertain Circumstances* (206–232). Cheltenham, UK: Edward Elgar.
- Brockner, J., Tyler, T. R., & Cooper-Schneider, R. (1992). The influence of prior commitment to an institution on reactions to perceived unfairness: The higher they are, the harder they fall. *Administrative Science Quarterly* 37(2), 241-261.
- Callahan, D. (2004). *The Cheating Culture: Why More Americans are Doing Wrong to Get Ahead*. New York: Harcourt.
- Chrobot-Mason, D. L. (2003). Keeping the promise: Psychological contract violations for minority employees. *Journal of Managerial Psychology* 18(1/2), 22-45.
- CICA (2006). *CICA Handbook*. Toronto: Canadian Institute of Chartered Accountants.
- Coulter, K. S., & Coulter, R.A. (2002). Determinants of trust in a service provider: The moderating role of length of relationship. *The Journal of Services Marketing* 16(1), 35-50.
- Creed, W. E. D., & Miles, R.E. (1996). Trust in organizations: A conceptual framework linking organizational forms, managerial philosophies, and the opportunity costs of controls. In R. M. Kramer, & T.R. Tyler (Eds), *Trust in Organizations: Frontiers of Theory and Research* (pp. 16-37). Thousand Oaks, CA: Sage Publications.
- Dasgupta, P. (1988). Trust as a commodity. In D. Gambetta (Ed.), *Trust: Making and Breaking Cooperative Relations* (pp. 49-72). Oxford: Blackwell.

- Fairholm, G. W. (1994). *Leadership and the Culture of Trust*. Westport, CT: Praeger.
- Gabarro, J. (1978). The development of trust, influence, and expectations. In A. Athos, J. Gabarro (Eds) *Interpersonal Behavior*. Englewood Cliffs: Prentice Hall.
- Gambetta, D. (1988). Can we trust trust? In D. Gambetta (Ed.) *Trust: Making and Breaking Cooperative Relations* (pp. 213-237). Oxford: Blackwell.
- Gibbins, M., McCracken, S. A., & Salterio, S. E. (2005). Negotiations over accounting issues: The congruency of audit partner and chief financial officer recalls. *Auditing: A Journal of Practice & Theory* 24(supplement), 171-193.
- Gibbins, M., McCracken, S. A., & Salterio, S.E. (2006). The auditor-client management relationship in financial reporting negotiation: Focusing on the dyad. Working paper, University of Alberta, University of Toronto and Queens University.
- Gibbins, M., McCracken, S.A., & Salterio, S.E. (in press). The Chief Financial Officer's Perspective on Auditor Client Negotiations. *Contemporary Accounting Research*.
- Gibbins, M., & Que, S Q. (2005). Eliciting experts' context knowledge with theory-based experiential questionnaires. *Behavioral Research in Accounting* 17, 71-88.
- Gibbins, M., Salterio, S., & Webb, A. (2001). Evidence about auditor-client management negotiation concerning client's financial reporting. *Journal of Accounting Research* 39(3), 535-563.
- Hilton, J. L., Fein, S. & Miller, D.T. (1993). Suspicion and dispositional inference. *Personality and Social Psychology Bulletin*, 19(5), 501-512.
- Hurt, K., Eining, M. and Plumlee, D. (2005). An experimental examination of professional skepticism. Working paper, Baylor University.
- Johnson-George, C., & Swap, W.C. (1982). Measurement of specific interpersonal trust: Construction and validation of a scale to assess trust in a specific other. *Journal of Personality and Social Psychology* 43(6), 1306-1317.
- King, R. R. (2002). An experimental investigation of self-serving biases in an auditing trust game: The effect of group affiliation. *The Accounting Review* 77(2), 265-284.
- Kleinman, G., Palmon, D., & Anandarajan, A. (1998). Auditor independence: A synthesis of theory and empirical research. *Research in Accounting Regulation*, 12, 3-42.
- Korsgaard, M.A., Brodt, S.E., & Whitener, E.M. (2002). Trust in the face of conflict: The role of Managerial trustworthy behavior and organizational context. *Journal of Applied Psychology* 87(2), 312-319.

- Lewis, J. D., & Weigert, A. (1985). Trust as a social reality. *Social Forces* 63(4), 967–985.
- Lind, E.A., Tyler, T.R., and Huo, Y.J. (1997). Procedural Context and Culture: Variation in the Antecedents of Procedural Justice Judgments. *Journal of Personality and Social Psychology* 73(4), 767-780.
- Lines, R., Selart, M., Espedal, B., & Johansen, S.T. (2005). The production of trust during organizational change. *Journal of Change Management* 5(2), 221-245.
- Luhmann, N. (1979). *Trust and Power*. Chichester: John Wiley & Sons.
- McAllister, D. (1995). Affect- and cognition-based trust as foundations for interpersonal cooperation in organizations. *Academy of Management Journal* 38(1), 24-59.
- McAllister, D. (1997). The second face of trust: Reflections on the dark side of interpersonal trust in organizations. *Research on Negotiation in Organization* 6, 87-111.
- McKnight, D.H., Choudhury, V., and Kacmar, C. (2002). Developing and validating trust measures for e-Commerce: An integrative typology. *Information Systems Research* 13(3), 334-359.
- McKnight, D. H., Cummings, L., and N. Chervany. (1998). Initial trust formation in new organizational relationships. *Academy of Management Review* 23(3), 473-490.
- Mele, A.R. (2001). *Self-Deception Unmasked*. Princeton, NJ: Princeton University Press.
- Möllering, G. (2005). Rational, institutional and active trust: just do it!? In K. Bijlsma-Frankema and R. K. Woolthuis (Eds.) *Trust Under Pressure: Empirical Investigations of Trust and Trust Building in Uncertain Circumstances* (pp. 17–36). Cheltenham, UK: Edward Elgar.
- Morrow, J.L., Hansen, M.H., & Pearson, A.W. (2004). The cognitive and affective antecedents of general trust within cooperative organizations. *Journal of Management Issues* 16(1), 48-64.
- Nelson, M. W., Elliott, J. A., & Tarpley, R. L. (2002). Evidence from auditors about managers' and auditors' earnings management decisions. *The Accounting Review* 77(Supplement), 175-202.
- Ng, T. B., & Tan, H. (2003). Effects of authoritative guidance availability and audit committee effectiveness on auditors' judgements in an auditor-client negotiation context. *The Accounting Review* 78(3), 801–818.
- Nooteboom, B. (2002). *Trust: Forms, Foundations, Functions, Failures and Figures*. Edward Elgar: Cheltenham, UK.
- Panel on Audit Effectiveness (2000). *The Panel on Audit Effectiveness Report and*

Recommendations, August 31, 2000. Stamford, CT: Panel on Audit Effectiveness (www.pobauditpanel.org).

- Rotter, J. B. (1980). Interpersonal trust, trustworthiness and gullibility. *American Psychologist* 35, 1-7.
- Rousseau, D., Sitkin, S. B., Burt, R. S., and Camerer, C. 1998. Not so different after all: A cross-discipline view of trust. *Academy of Management Review* 23(3), 393-404.
- Shaub, M.K. (1996). Trust and suspicion: The effects of situational and dispositional factors of auditors' trust of clients. *Behavioral Research in Accounting* 8, 155-174.
- Shaub, M.K., & Lawrence, J.E. (1996). Ethics, experience and professional skepticism: A situational analysis. *Behavioral Research in Accounting* 8(Supplement), 124-157.
- Shaub, M. K., & Lawrence, J. E. (1999). Differences in auditors' professional skepticism across career levels in the firm. *Advances in Accounting Behavioral Research*, 2, 61-83.
- Six, F. (2005). *The Trouble with Trust: The Dynamics of Interpersonal Trust Building*. Cheltenham, UK: Edward Elgar.
- Stickel, D. & Gamroth, C. (2006). Put your money in trust. *CA Magazine* 139(7), 47-55.
- Sztompka, P. (1999). *Trust : A Sociological Theory*. Cambridge, U.K. :Cambridge University Press
- Trotman, K. T., Wright, A. M., & Wright, S. (2005). Auditor negotiations: An examination of the efficacy of intervention methods. *The Accounting Review* 80(1), 349-367.
- Whitener, E. M., Brodt, S. E., Korsgaard, M. A., & Werner, J.M. (1998). *Academy of Management Review* 23(3), 513-530.

Figure 1: Factors Proposed to Influence an Auditor's Trust of a Client Representative

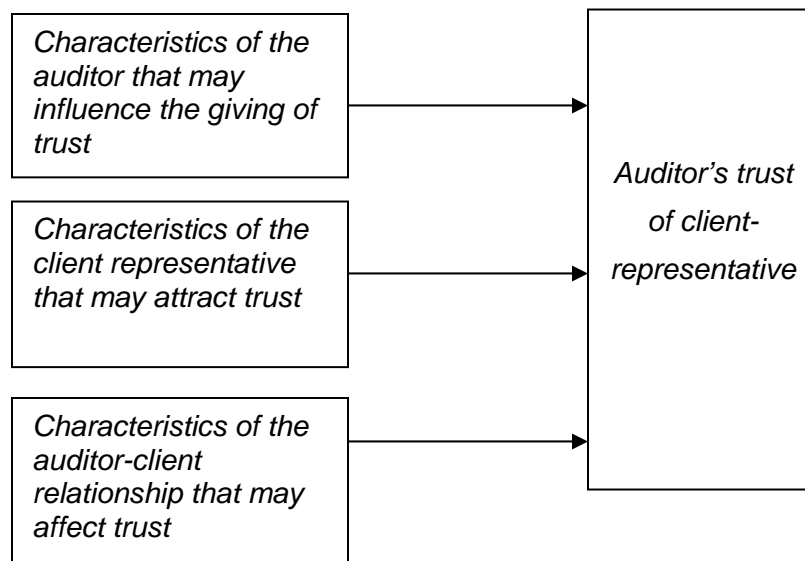


Table 1: Participants and Incidents

	Number	Percent	Mean (Standard Deviation)
Participants in study			
Partners (including two principals)	48	67.6%	
Senior managers	20	28.2%	
Managers	<u>3</u>	<u>4.2%</u>	
Total	<u>71</u>	<u>100%</u>	
Experience since becoming a Chartered Accountant (years)			17.5 (9.2)
Approximate percentage of time spent on financial statement audits			71.9 (22.5)
Males (females)	54 (17)	76.1% (23.9%)	
Participants working with Big 4 firms	41	57.7%	
Incidents			
Clients involved in incidents:			
Public companies	34	52.3%	
Non-traded subsidiaries of public companies	6	9.2%	
Private companies	16	24.6%	
Other types of organizations	<u>9</u>	<u>13.8%</u>	
Total	<u>65</u>	<u>100%</u>	
Importance of disagreement (0 = "only of minor importance" to 10 = "extremely important")			7.8 (2.0)
Age of disagreement (years)			2.4 (3.07)

**Table 2: Descriptive Statistics
Dependent, Independent and Control Variables (n=65)**

	Theoretical Range	Response Range	Mean	Standard deviation
<u>Dependent variables</u>				
Trust of the client	0–10	0–10	6.02	2.37
Impact of disagreement on trust of client	0–10	0–10	4.94	2.29
<u>Independent variables</u>				
Trust predisposition	0–20	4–20	14.22	2.96
Client's openness of communication	0–10	0–10	6.69	2.66
Client's demonstration of concern	0–10	0–10	4.66	2.71
Tenure for auditor (years)		.5–20	4.11	3.58
Tenure for firm (years)		1–25	6.87	6.34
Previous disagreements with client rep.	0–10	0–8	3.57	2.40
<u>Control variable</u>				
Satisfaction with outcome	0–10	3–10	7.95	1.95

Table 3: Correlation Matrix for dependent and independent variables (n=65).

	Impact of disagreement on trust	Trust pre-disposition	Communication	Concern	Tenure	Prior disagreements	Satisfaction with outcome
Trust of client	.621**	-.147	.576**	.458**	.225	-.312*	.150
Impact of disagreement on trust		.106	.422**	.422**	.124	-.204	.213
Trust pre-disposition			.060	.075	-.105	-.033	.105
Communication				.429**	.077	-.273*	-.066
Concern					.073	-.196	.201
Tenure						.052	-.236
Prior disagreements							.046

*Significant at the 0.05 level (2-tailed)

**Significant at the 0.01 level (2-tailed)

Table 4: Regression 1 – Tests of H1, H2A, H3A, H4 and H5
Dependent variable: Trust of client (n=65)

Variable	Hypothesized Direction	Standardized Coefficients	t	p-value*
Constant			1.664	
Trust predisposition	Positive	-.191	-2.041	.046
Openness of communication	Positive	.452	4.252	.000
Concern	Positive	.184	1.719	.046
Tenure	Positive	.217	2.237	.015
Previous disagreements	Negative	-.174	-1.795	.039
Satisfaction with outcome (control)		.222	2.228	.030

* p-values are one-tailed for hypothesized relationships (all of which specify a direction) and two-tailed for the control variable, satisfaction with outcome. The exception is the p-value for the Trust predisposition variable which has been reported on a two-tailed basis in this table because result was in the opposite direction to that hypothesized.

Table 5: Regression 2 – Tests of H2B H3B
Dependent variable: Impact of disagreement on trust of client (n=65)

Variable	Hypothesized Direction	Standardized Coefficients	t	p-value*
Constant			0.272	
Openness of communication	Positive	0.330	2.708	0.005
Concern	Positive	0.243	1.953	0.028
Satisfaction with outcome (control)		0.186	1.653	0.103

* p-values are one-tailed for hypothesized relationships (all of which specify a direction) and two-tailed for the control variable, satisfaction with outcome.

Table 6: On the importance of trusting clients (n=71)

	Number	Percent
Role of trust in the auditor-client relationship itself/pre-condition for client acceptance	31	33
Importance of trust to the performance of the audit	38	41
Professional scepticism is important (or too much trust should not occur) during the process of conducting audit procedures	18	19
Other	2	2
No response	<u>5</u>	<u>5</u>
Total (note that 23 respondents gave responses in two categories)	94	100%

Table 7: Ensuring that trust does not get in the way of professional scepticism (n=71)

	Number	Percent
Rigorous audit process/specific audit process strategies that help ensure that trust does not compromise professional scepticism	57	63
An independent/objective/sceptical attitude or mindset	28	31
Other	4	5
No response	<u>1</u>	<u>1</u>
Total (19 respondents made comments in two categories)	90	100%