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Chapter 7

Audit Research and Practice: A Dialogue on ‘Relevance’

Philomena Leung, Lee White and Barry Cooper

There are a variety of international academic journals that publish accounting and audit research. However, only a handful of these specialise in audit research. McKee (2010) reviewed three specialised audit journals and measured their relative ‘impact’ for the six-year period 2001 – 2006 using a citation count method. McKee (2010) found that the top 10 articles in *Audit: A Journal of Practice & Theory* averaged 73 citations compared to an average of 40 citations for *Managerial Auditing Journal* and 27 citations for *International Journal of Auditing*. He also commented that the order of these three specialist audit journals in terms of number of citations parallels their order in terms of age of journal. The three journals also vary significantly in terms of number of articles published per year, but this did not appear to affect their citation frequency.

Citations provide information about the impact that a journal or article has on research (O’Leary, 2009) and impact is important in assessing the contributions of that journal or article and its relative importance within its field (McKee, 2010). Academics are interested in how often their work is cited. The ability to publish an article in leading journals is generally taken as a significant achievement demonstrating high quality research, which is often construed as recognition of the impact of the piece of research by an author’s peers. As Hopwood (2008) pointed out, making a decision to research issues, or use research methods that do not appear to be of interest to such journals, is often perceived by emerging and established scholars as potentially highly damaging to their career prospects. This system is also considered by some to deter wider dissemination and knowledge transfer activity to non-academic users of research (Unnerman and O’Dwyer, 2010).

On the other hand, as reported by Parker et al. (2010), accounting research has become too far removed from the interests of the profession and practitioners and its impact is not so easily discernable (Tilt, 2010). Even in 1993, Bindenga (1993) presented a highly critical view of audit research. He believed that extant audit research lacks practical relevance and that a number of important audit issues have not been adequately addressed by research. While Biggs et al. (1994) disputed Bindenga’s views, arguing that audit research not only meets the high standards of scientific inquiry, but also makes several significant contributions to the practice of audit, the question of the relevance and impact of audit research to audit practice remains a highly debated matter.

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8. Thomas E McKee (2010, pp. 724 – 733) used a Google Scholar citation analysis to examine the ‘impact’ of three leading international auditing journals: *Audit: A Journal of Practice & Theory*, *Managerial Auditing Journal* and *International Journal of Auditing*, for the period 2001 – 2006. The top 10 citations from each of these journals were used to analyse relative journal citation frequency, publication topics and leading authors.
This chapter offers an overview of the perceived relevance and impact of audit research on audit practice. It provides some evidence regarding the perceptions of usefulness of some of the audit research from the accounting profession's viewpoint and attempts to address the question of what are the likely issues that lead to such perceptions.

A review of audit research

This first section provides a scan of the extant audit research literature and identifies common areas that are contemporary and which are captured in both audit research and practice.

The editors of *Managerial Auditing Journal* (MAJ), a non-North American journal, celebrated 25 years of the journal's publication in 2010. In an analysis of the trend of published articles over 25 years using key words, eight areas of audit research were identified: audit and assurance issues; ethics; financial reporting; controls; organisational matters; governance; management reporting; and risk management. While research in areas of audit and assurance issues remained strong over the period 1986 – 2009, financial reporting and governance appear to be the areas most audit researchers have focused on in recent years. This trend may reflect the global development of the International Financial Reporting Standards (IFRS) and the growing awareness of corporate governance in the market, and suggests that academics have responded to the contemporary business agenda.

Table 1: *Managerial Auditing Journal* (Emerald Group Publishing Limited)
A summary of areas by key words

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<td>No.</td>
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<tr>
<td>Audit and assurance issues</td>
<td>282</td>
<td>60</td>
<td>346</td>
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<tr>
<td>Ethics*</td>
<td>78</td>
<td>17</td>
<td>107</td>
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<tr>
<td>Financial reporting and</td>
<td>14</td>
<td>3</td>
<td>48</td>
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<tr>
<td>other reporting topics**</td>
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<tr>
<td>Controls</td>
<td>28</td>
<td>6</td>
<td>51</td>
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<td>Organisational matters</td>
<td>32</td>
<td>7</td>
<td>44</td>
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<tr>
<td>Governance**</td>
<td>12</td>
<td>3</td>
<td>38</td>
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<tr>
<td>Management reporting</td>
<td>10</td>
<td>1</td>
<td>44</td>
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<tr>
<td>Risk management</td>
<td>16</td>
<td>3</td>
<td>27</td>
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<td>Total</td>
<td>472</td>
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* Ethics areas fluctuate suggest an impact of regulatory change.
** Significant increases in the research topics of financial reporting and governance.
A further analysis of the 758 auditing and assurance articles that were published in MAJ over the 25 years shows a broad spectrum of topics researched. They include internal audit, audit fees, the profession, audit conflicts, audit quality, independence and autonomy, auditing standards and guidelines, audit failures, and technical matters such as judgement sampling, value-for-money audit and online reporting. However, the majority of the audit papers concentrated on ‘audit practice’.

Solomon and Trotman (2003) found that 670 auditing papers had been published between 1976 and 2000 in five accounting journals10. Using the Solomon and Trotman (2003) database, together with a review of the articles published in Auditing: A Journal of Practice and Theory, Behavioural Research in Accounting and the Journal of Accounting and Public Policy, Humphrey (2008) divided the audit research discipline into two broad groups. The first group addressed specific auditing issues such as: audit quality; audit structure; audit fees; auditor independence; non-audit services; auditing expectations; risk assessment; audit history; regulation and liability; and auditor reputation. The second group explored the research approaches applied in the field of audit research, ranging from experimental judgement and decision research to contextual, historical and critical audit research. Although much audit research has discussed audit practice, Humphrey (2008) challenged the extent of academics’ knowledge of ‘audit practice’, highlighting a variety of concerns with dominant research approaches, and pinpointing a range of research questions which offer potentially rewarding insights into the audit practice arena. He argued that audit research can be of value when the focus is directly on understanding the practice of audit and the work of associated regulatory associations. Humphrey (2008) also observed that Francis (2004) and Defond and Francis (2005) encouraged further questioning of the nature of audit practice by asking questions as to what is an optimal level of ‘audit quality’ (that is, how much auditing and auditing regulation is enough?).

Also, there is the perspective that audit research has been hindered by the desired attachment to the so-called ‘scientific rigour’ and academics’ reluctance to undertake a more ‘qualitative’ or ‘critical’ approach. Humphrey (2008) and Diamond (2005) also acknowledged this. The North American educational approaches have also played a dominant role in the research agenda, but there are grounds for suggesting that there has also been a shift of gravity in terms of the global status of the International Accounting Standards Committee (IASC)/International Accounting Standards Board (IASB) and the European Union (EU) since 2005. Humphrey’s (2008) review highlighted the complex nature of the divide between audit research and practice and the emerging status of the European ideas with the increasing impact of globalisation. Also, following the recent spate of corporate collapses in the early 2000s, regulatory changes such as the Sarbanes-Oxley Act in 2001, and the Global Financial Crisis (GFC), it appears that high-level debates are now being fostered in Europe.

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The changing landscape in the audit environment

Using a dialogue between two academics (Leung and Cooper) and an experienced representative of the profession (White), the next three sections explore the perceived relevance and impact of some examples of audit research within the common areas identified in the literature review. This dialogue is followed by a discussion of the factors that contribute to the perceived relevance and impact of audit research on practice.

In the United Kingdom, the Select Committee on Economic Affairs of the House of Lords commented in July 2010 on the domination of the Big Four auditing firms (the Big 4) in the audit market, resulting in the narrow field of choice that has raised concerns about competition, concentration, and audit quality, with possible conflicts of interest between audit and consulting in large firms. Questions were also raised regarding whether auditors could have mitigated the banking crisis of 2008 by alerting investors to the riskiness of the assets held by banks. The House of Lords released its request for submissions for an inquiry on ‘Auditors: Market concentration and their role’ (Select Committee on Economic Affairs, House of Lords (2010)).

In October 2010, the European Commission (EC) also published a Green Paper on audit policy and set the scene for wide-ranging debates on a number of controversial matters relating to the audit environment globally (Linklaters, 2010). They include:

- Making the appointment and remuneration of auditors the responsibility of a third party, such as a regulator (rather than the company being audited)
- Mandatory rotation of the audit firm (a concept considered but rejected by regulators following the fall of Enron, Parmalat and Ahold in 2002 – 2003)
- Prohibiting the provision of non-audit services by audit firms. Currently they may provide such services subject to safeguards to preserve audit independence
- Mandatory formation of an audit firm consortium to include smaller audit firms for the audit of larger companies. This is intended to reduce the domination of larger audits by the Big 4
- Considering the introduction of contingency plans, such as ‘living wills’, to address the threats posed by the risk of a systemically important audit firm failing
- The possible reversal of the consolidation of large audit firms over the past two decades. The EU seeks comments on whether this is desirable and how this could be achieved
- The potential for a real internal market for audit, possibly involving a single European passport for auditors and audit firms and implying the creation of a European-wide registration system with common professional qualification requirements and common governance, ownership and independence rules across the EU.

11 This chapter is based on research and a presentation by the three authors. Professor Philomena Leung and Professor Barry J. Cooper are presently joint editors of Managerial Auditing Journal. Mr Lou White is the Executive General Manager of the Institute. Mr White represents over 25 years of accounting and audit practice experience, and is involved in the global development of the audit profession. The chapter reports the viewpoints of auditing researchers (Leung and Cooper) and the profession (White)
The key issues raised by the EC are the concentration and competition in the audit market and the role and quality of audit. The EU posed a number of questions surrounding these areas to which practitioners and professional bodies were invited to respond.

As audit research develops, it is worth considering the development of the current changing audit scene and how it may be reflected in academic research. With respect to the changing audit scene, White indicated that there will be significant changes in the global audit landscape that will affect academics in the field as well as practitioners and the profession:

Right at the moment globally, in the audit space, it is a very special time, so these two reviews happening in Europe coming out of the GFC, it means that the status quo will not remain the same. That's the message.

So with that comes challenges for bodies, practitioners, academics, all of us who have a focus in this space, but equally comes a great time of opportunity if we can get it right. But the sense is— that audit is becoming more and more irrelevant in what it’s delivering. So if we could leave this view for reflection and then come back to the question, then that should really drive what we talk about as to how we make sure we get the relevance from audit research.

White’s concern regarding the relevance of audit research is examined through the following questions: What does audit research mean to the profession and the market? How does the profession react to audit research? What research methodology is easier to understand? and finally, Will audit research become more relevant to the profession?

What does audit research mean to the profession and the market?

While the profession is very much concerned about research underpinning policies and standards, it is not clear how the profession and the audit market view audit research. This section examines what audit research means to these stakeholders.

From a research standpoint, there is much on concentration and competition in the audit market, which are matters about market structure, or the economics of audit. This area of research includes audit pricing, audit fees, non-audit services, professional standards and professional practice. It also covers mergers, specialisation, audit affiliations, the effect on share prices, specialist competition and audit choice. Research on audit quality considers areas such as independence, earnings management, internal audit and audit committees, all of which are covered in the EU paper. It can be argued that accounting academics view audit research from the perspectives of audit quality and practice but on the other hand the audit environment has emphasised the market importance of the economics of auditing, leading to research into areas such as audit structures, fees, pricing, concentration and autonomy.

A preliminary review of the research into the two broad audit areas mentioned above, namely, the economics of auditing and the role and quality of audit, shows an interesting result. For the period 2000 – 2011, 101 articles on audit quality and audit roles were listed in the Emerald database, of which 60 refer to audit pricing and matters concerning the economics of auditing. The Emerald database
represents Accounting, Auditing and Accountability Journal, Managerial Auditing Journal and Asian Review of Accounting.


The debate about the relevance of this audit research is not new. Hay et al. (2006) and Knechel and Willekens (2008) have argued that this whole field of research (about audit fees and pricing) has been characterised by a production-orientated approach and has ignored potential demand-side factors that may well drive audit fees.

Where is the impact coming from the actual research? White argued that audit research means quite a lot to the profession. However, he noted:

We at times might focus a lot on outputs and not a lot on the outcomes. So I try and think about some audit research that has actually had a significant influence, and I can think of some, but they’re probably more the exception than the norm. So those statistics that you quoted earlier – 2439 articles – that’s a lot, and I’m not sure I’m seeing a lot of influence or outcomes from this type of research.

**How does the profession react to audit research?**

This second question explores the types of reactions from the profession’s standpoint regarding some examples of audit research that directly deal with the contemporary topics of audit market and quality. In soliciting deeper insights, three examples of audit research are discussed: the economics of auditing; audit roles; and quality. Each of the following articles is briefly discussed. The responses to the cases are produced below.

**Case 1:** A study (Hamilton et al., 2008) on the economics of auditing which investigated whether audit markets remained competitive in the wake of Arthur Andersen’s demise and merger with Ernst & Young to create the Big 4. Macro-economic in nature, the study relates directly to the audit market and high profile events. The authors found evidence of a big firm brand name price premium when estimating the audit fee model across all clients, and when estimating it separately across large and small clients.

White observed that if he understood correctly, not a lot happened in the pricing after the demise of Arthur Andersen. He further observed that he could have made that comment without being referred to the case. White remarked:

> From the profession’s perspective, the ‘so what question’ arises.
Case 2: Using a large sample of United States (US) audit client firms over the period 2000–2005, this study investigated whether and how the size of a local practice office within an audit firm (i.e., the office size) is a significant, engagement-specific factor determining audit quality and audit fees over and beyond audit firm size at the national level. Jong-Hag et al. (2010) measured audit quality using unsigned abnormal accruals, and the office size was measured in two different ways: one based on the number of audit clients in each office and the other based on a total of audit fees earned by the office. The authors found that the office size has statistically significant positive relations with both audit quality and audit fees, after controlling for national-level audit firm size. The positive relations support the view that large local offices provide higher quality audits compared with small local offices, and that such quality differences are priced in the market for audit services.

In reflecting on the message coming from this case, White ‘believed’ that such research does not provide a significant influence on the profession except by confirming the obvious practice:

It’s moving to a different place but I’m not sure that’s still the right place. What I mean by that – I think that is quite interesting and it does attract thinking when we talk about what the drivers of audit quality are. So at the highest level, they would say the drivers are, or one of the key ones is, the skills and experience of people involved in the audit, undertaking the audit.

... good audits can be done in large and small offices and not-so-good audits can probably be done in large and small. So it’s interesting. It hasn’t really hit the mark.

Case 3: A working paper12 presented at the Accounting and Finance Association of Australia and New Zealand (AFAANZ) in 2010 which re-examined the long-standing debate of whether consulting fees earned by auditors affect their independence. The authors used a model that predicts a negative relation between auditor supplied non-audit fees and auditor independence. The test examined auditors’ propensity to issue a going concern opinion for a sample of US companies experiencing financial stress. The authors documented a reliable negative relation between non-audit fees and their proxy for auditor independence.

In responding to this case, White reflected that research may not always come up with a solution to some problems. As the problems about audit independence and non-audit fees are not only topical, the profession is also interested in any insightful research on the matter:

In this instance, the research actually is confirming where there are different perceptions or views around the business community and with regulators. The one that keeps bubbling around is whether non-audit services of any level leads to somehow a compromising of audit quality and ultimately the audit opinion. So I actually think that’s a very valid piece [of research] because these perceptions do get bandied around, and that actually would be very helpful in contributing to not only the discussion but then potentially whatever public policy settings might come – and inevitably they will – in terms of non-audit services. So I actually find that really quite useful.

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Bridging the Gap between Academic Accounting Research and Professional Practice
Lee was asked if such research findings change a professional’s viewpoints. He replied:

The short answer is yes. Maybe you’re attracted at times to research that is aligning with your gut feel or your sentiments… But I think you’d be a fairly naïve leader if you only rely on your gut feel and not with people who are actually conducting some rigorous research. So I think when that research might come out to a different point to what you’re feeling, I think you should show some courage to want to then engage with it and not be dismissive of it. That’s where I’d be on that sort of view.

**The issues of research methodology**

In an assessment of the respectability of audit research, Biggs et al. (1994) referred to three criteria for evaluating research rigour (mainly from a North American perspective). First, research provides scientific answers to questions rather than opinion. That is, research addresses questions through the development of logical theory and the systematic analysis of empirical evidence. Second, scientific answers nearly always involve replication of results across multiple studies. Third, research-based answers to many complex practical questions often involve time-consuming development of scientific knowledge. Biggs et al. (1994) claimed that this type of audit research has already provided some results that have been highly relevant to audit practice, but not all issues of practical importance can be addressed. For instance, theoretical work that seems irrelevant one day may provide the basis for highly relevant research in the future.

The authors further pursued the issue of rigour and sought the views of the profession regarding the issue of relevance. Though the research methodology used is largely dependent upon the research problem, the use of research methodology is somewhat dictated by the users of the publications concerned. For example, professional journal users would be receptive to simpler data; an academic journal known for its quantitative approach would publish research articles with highly sophisticated quantitative and statistical analyses. In Humphrey’s (2008) analysis of ‘scientific rigour’, he questioned the tendency of researchers to fail to contemplate a qualitative mode of research and pursue a more quantitative-based approach, even though the research question is ideally suited to the former. Nearly all of the 2439 audit research articles in the Business Source Premier are statistical empirical analyses. However, White’s view is quite different. The following highlights the view of the profession regarding rigour and statistical research:

> From my perspective, you sort of get a quite mathematical style of approach in a quite systematic style of research. At other times you can get – not survey but a lot of engagement in conversation – qualitative conversations. I suppose both of them have some pluses … that always lead me a little bit to the rigour question. You know, how do you actually strike the right approach in determining research?

Research undertaken by the profession, though often without statistical analyses, is often regarded as acceptable in the business community as reliable and good quality research. On the other hand, some qualitative research is recognised and well accepted in the area of social sciences research. With respect to preference of research methodology, White will typically favour an approach that is easier to digest:
For me, when I - I’m just casting my mind back to when I’ve looked at different pieces of research, the ones which are a highly mechanical, statistical approach, I must admit, leave me generally pretty cold. And that’s even as a - previously as a practitioner who used to do all sorts of models in terms of altered evidence and all this sort of stuff. I find it a pretty hard read.

Will audit research become more relevant?

This section explores various means and considerations to enable more relevant audit research to be published and used by the audit profession. In making a piece of research relevant, it is important that the reader becomes ‘engaged’ with the research:

If that’s [the highly mechanical and statistical approach] used in the methodology, then you really need some very good commentary at the front ... to really engage the reader, to capture that sleepless night or whatever the real point is of it ... On the counter side, the qualitative, where there’s the engagement - if it’s a great case study, generally I’m quite interested in reading that and engaging. You can feel it obviously quite realistically. (White)

Another issue in respect of a relevant audit research approach is its forward-looking aspect. For example, the Institute published a booklet in November 2009 titled The Benefit of Audit: A Guide to Audit Quality. The purpose of the guide is to enhance the communication between external auditors and audit committees. It describes five drivers of audit quality: firm culture; skills of audit partners and staff; audit process effectiveness; factors outside the control of the auditors; and the reliability and usefulness of audit reporting. The profession will find it useful if it provides some initial ideas for research, where researchers could conceptualise and further explore it. White also noted:

So at the highest level, doing some further work around that piece I think would be quite valuable. The second is, by picking up that piece of work that we'd already done and trying to explore it further I think is tremendous. The timing sounded great for me.

It was also noted that through engaging with the profession, the researcher will be able to:

broaden the research so that it’s actually got a wider impact and influence than perhaps just in one element that has already been identified by the profession ... if there was a type of deliverable or an outcome that we'd be really looking for research, it's got to be forward looking. And so when I talk with my team at the Institute in our policy area and looking at leadership and quality, we're continually trying to focus in on what are the two or three issues in 12 to 18 months' time that people are actually going to be talking about in this space, whatever the space might be - audit, accounting, sustainability, tax - because I think the relevance of the Institute can be that if we can get there quicker and identify the right issues - and that's really hard to do, you know, it's sort of like six out of 10, you've done really well - but if you can get there quicker than others, then your relevance is only going to be stronger. And I would have thought that's the same challenge for academic research, being forward looking and positioning yourself for the conversation already happening. (White)
Another matter highlighted in the dialogue is the timeliness of the research. White pointed to the value of earlier research work that is timely:

A piece I'll just add to this about taking too long is that when we did our submission to the House of Lords and were asked to then present oral evidence to the House, the reason some of that — the Institute's submission was recognized because some of the research that we'd been engaged in and had been provided to us actually added a lot to our composition. So it wasn't just hot air coming from us at a point in time. We'd actually done earlier some of the research work.

Conclusion

Although there is research published in respect of 'audit quality' and 'audit practice', one has to question whether such research is well understood and is used in the development of audit policy. Clearly the discussions on the implications of the EC's Green Paper and the UK's House of Lords' review demonstrate the lack of success.

Also, the discussion above has provided some understanding of types of audit research and how they are viewed by the profession. In order for the values of the accounting and auditing profession to remain aligned with the values of the profession, relevant accounting and auditing research is key. In auditing, audit policy is developed from audit research and audit practice — it is the nexus between the two. The relevance and impact of audit research can be seen from how it can influence practice and, to a larger extent, how it can shape audit policy.

We consider that published audit research, while wide-ranging, has only partly addressed the questions of audit practice, such as regarding 'audit quality'. In terms of audit policy, for example, the restrictions by the Sarbanes-Oxley Act 2002 regarding non-audit services and independence, means that audit research seems to have assumed a subordinate role. As Humphrey (2008, p. 181) pointed out, 'There has to be a questionable value to audit research if it is destined only to test the empirical validity of regulations, knowing full well that the demands and pressures on regulators can lead to changes in regulations on the grounds of political necessity and expediency, rather than being based on solid empirical evidence'.

For the audit profession, the challenge lies with the development and engagement in thought leadership. Post-implementation reviews of standards, for example, are important. Policy does not stand alone; it must be continuously revised and the role of research is crucial to enable feedback and engagement. A good starting point when thinking about research is how are researchers going to sense the impact of the research? Engagement between the audit profession, audit practitioners and the academic audit community, dissemination of research findings and ultimately participation in policy debates, are all part of the development.13

13. One example that was quoted was the commissioned research projects by the Association of Chartered Certified Accountants (ACCA) and the International Association for Accounting Education and Research (IAAER) for IFAC (International Federation of Accountants) Committees, namely the MAAS and the IAESR. Researchers are commissioned to conduct research on the agendas set by these Committees and deliverables are reported back twice a year to representatives of all the parties involved.
References


