How do Auditors Move from Skeptical Judgment to Skeptical Action? A Field Study

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What runs through an auditor’s mind when after gathering, evaluating and considering audit evidence, things don’t add up?

How do auditors transition from the “things do not add up” phase, to action (e.g., questioning, challenging and possibly expanding audit inquiry and procedure)?

Skeptical judgment $\rightarrow$ Skeptical action
Study Motivation

– PCAOB “continue[s] to observe instances in which the circumstances suggest that auditors did not appropriately apply professional skepticism in their audits.”

– Enforcement activities of the PCAOB and the SEC have focused on auditor actions

– A response to calls for exploratory, inductive approaches in audit research (Power and Gendron, 2015)
Study Motivation

- Brown, Cohen, and Trompeter (2013) noted, “…there is limited research that examines the relationship between skeptical judgments and skeptical actions”

- A complement to existing skeptical action research from experimental and survey design
Literature Review
Literature Review

Pressures, Conflicts and Incentives

– Auditors accommodating clients who could be future employers – Nelson (2009)

– Auditor client identification from long tenure – Bamber and Iyer (2007)

– Independence threat associated with auditor concern over risk of client loss – Blay (2005)
**Literature Review**

**Influence of Affect on Skeptical Action**

- Deliberate mindset condition increased skeptical action – Griffith et al. (2015)

- Negative mood condition increased skeptical action – Cianci and Bierstaker (2009)

- Positive mood condition decreased skeptical action – Chung et al. (2008)
Other Influences on Skeptical Action

- Audit management tone and work paper review emphasis – Carpenter and Reimers (2013), Turner (2001)
- Firm and professional audit standards – Griffith et al. (2012), Nelson et al. (2002), Ng and Tan (2003), Rasso (2015)
- Audit evidence attributes – Feng and Li (2014)
Literature Review

Other Influences on Skeptical Action

– Overall audit context (e.g., strength of the audit committee, past client relationship tone, going concern status) – Brown-Liburd and Wright (2011), Tucker, Matsumura, and Subramanyam (2003)
Theory
Theory

*Behavioral Theory of Motivation*

- Self-efficacy, within Social Cognitive Theory (Bandura, 1977, 1986), situated in the audit context

- Focuses on perceptions of personal capability that precedes action in challenging circumstances
Theoretical Framework
Theoretical Framework

Bandura’s (1977) model

Figure 1. Diagrammatic representation of the difference between efficacy expectations and outcome expectations.
Theoretical Framework

“An outcome expectancy is defined as a person’s estimate that a given behavior will lead to certain outcomes…”

Bandura’s (1977) model

Figure 1. Diagrammatic representation of the difference between efficacy expectations and outcome expectations.
Theoretical Framework

...An efficacy expectation is the conviction that one can successfully execute the behavior required to produce the outcomes” (Bandura, 1977, p. 193).

Bandura’s (1977) model

Figure 1. Diagrammatic representation of the difference between efficacy expectations and outcome expectations.
Theoretical Framework

“...individuals can believe that a particular course of action will produce certain outcomes...”

Bandura’s (1977) model

Figure 1. Diagrammatic representation of the difference between efficacy expectations and outcome expectations.
Theoretical Framework

“...but if they entertain serious doubts about whether they can perform the necessary activities, such information does not influence their behavior” (Bandura, 1977, p. 193).

Bandura's (1977) model

![Diagram of Bandura's model]

*Figure 1. Diagrammatic representation of the difference between efficacy expectations and outcome expectations.*
Theoretical Framework

For this reason, we explored what influences auditor efficacy expectations and how it occurs.

Bandura's (1977) model

![Diagram](image)

*Figure 1. Diagrammatic representation of the difference between efficacy expectations and outcome expectations.*
Theoretical Framework

Nelson’s (2009) model

– IVs (e.g., incentives, traits and knowledge) modeled to affect DVs of skeptical judgment and skeptical action.

– The audit context (other than incentives) and a behavioral theory were not included in this model
Proposed Self-Efficacy Model for Auditing
Proposed Self-Efficacy Model for Auditing

No color = the audit context and the auditor (literature and Nelson, 2009)

Blue = Bandura’s (1977) self-efficacy construct
Method
Method

Prior to entering the field:
- Gatekeeper approval; pre-interview meeting; pilot interview; purposeful selection of participants

In the field:
- Two rounds of interviews
- Two types of interview protocols
Analysis
Analysis

**Individual and Blended:**

1. Two rounds of coding

2. In-depth analytic memo and theoretical framework prepared for each participant

3. Individual analyses were combined into a blended presentation of themes in the adapted model
Study
Execution
Study Execution

Semi-structured Interviews:

- 12 of 16 were audio recorded and transcribed (others captured as typed notes during interviews)

- Held in private office spaces, primarily at firm offices
Study Execution

Member Checking (Reliability):

– First and second round transcripts

– Individual analytic memo / participant theoretical frameworks

  • Affirmed by all participants
Summary
Findings
Support/Collectivism

To enhance levels of self-efficacy, the participants sought the support of others. This provided the ability to more comfortably pursue skeptical actions. Otherwise, participants spoke of being ‘on an island’ and ‘operating in a silo’.
Summary Findings

Preparation/Homework

– ‘Homework’ and advanced preparation increased efficacy expectations associated with the contemplated skeptical action.

• The support of others on the team, and the collective thinking of the team, were prominent inputs in preparation for skeptical action with increased efficacy.
Summary Findings

The Relationship with the Client

– A quality (‘good’) relationship provided the ‘rebar’ necessary to support skeptical action with increased efficacy.

• Participants ‘sought to understand’, to not be perceived as a threat, but rather as an interested party, desiring to learn.
Select Participant Quotes
Support/Collectivism

– Inventory obsolescence discussion

• “I was extremely confident in the decision...I had the support from, at the time, the partner and all the other partners, and specialists that we had involved.”
Select Participant Quotes

Preparation/Homework
– When discussing the benefits of rehearsal
  • “…then, when I speak to the client, the words aren’t coming out of my mouth for the first time…the more prepared I am, the more confident I am…I thought it out, I spoke it out. Just all of that helped me get more comfortable so that I wouldn’t have that pit.”
Select Participant Quotes

Relationship with the Client

– When asked what contributes to skeptical action when lacking confidence

• “It’s the relationship, if I really don’t understand it [the issue at hand], but I’m comfortable with the client…where I can ask them, ‘Can you just explain this to me?’ and I don’t have a fear. With a good relationship, that helps.”
Theoretical Framework Discussion
Theoretical Framework Discussion

How does Bandura’s theory apply in the audit context?

– Performance accomplishments and to a lesser extent, vicarious experience, emerged as factors that influenced perceived level of efficacy.

– Several other factors, not posited by Bandura, increased perceived efficacy within the audit context.
How does Bandura’s theory apply in the audit context?

– *Performance accomplishments* and to a lesser extent, vicarious experience, emerged as factors that influenced perceived level of efficacy.

– In effect, Bandura’s self-efficacy construct alone was not sufficient to explain how the participants persisted with skeptical action.
Theoretical Framework Discussion

Extension of self-efficacy theory in the audit context

1. Support/collectivism anchored in a strong desire to obtain backing and input from others before taking skeptical action
Theoretical Framework Discussion

Extension of self-efficacy theory in the audit context

– Skeptical action is primarily an individual exercise in practice and through the Bandura lens

– Yet, in the audit context, participants expressed a heightened sense of efficacy when skeptical action was preceded by support, consultation and collaboration with others
Theoretical Framework Discussion

Extension of self-efficacy theory in the audit context

2. Preparation/homework, to be ‘comfortable’ with skeptical action, was enhanced by the existence of support from others.
Extension of self-efficacy theory in the audit context

- When considering preparation / homework, the perceived amount topical or situational experience was not a factor.

- In difficult circumstances, advanced preparation / homework (e.g., rehearsal) was relied upon to increase efficacy, regardless of prior situational experience.
Theoretical Framework Discussion

Extension of self-efficacy theory in the audit context

3. The nature of the relationship with the client (‘good’ or ‘not good’) contributed to the level of efficacy
Theoretical Framework Discussion

Extension of self-efficacy theory in the audit context

- Participants sought to build ‘good’ relationships through communication strategies to enhance the relational pathway to skeptical action.

- When the client relationship was described as ‘good’, increased efficacy levels at the time of skeptical action were reported.
Adapted Self-efficacy Model
Adapted Self-efficacy Model

- No color = the audit context and the auditor (literature and Nelson, 2009)
- Blue = Bandura’s (1977) self-efficacy construct
- Dark orange = the primary extensions / themes of the Proposed Self-Efficacy Model
- Light orange boxes = secondary extensions / themes.
Strategic Communication
Pursuit of Comfort Support / Collectivism Relationship with the Client

Efficacy Expectations

Outcome Expectations

Knowledge Person (Auditor) Audit Evidence Auditor Skeptical Judgment

Pursuit of Credibility

Preparation / Homework

Support / Collectivism

Behavior (Auditor Skeptical Action)

Audit Context

Professional, PCAOB and Firm Audit Standards

Audit Management Tone

Traits

Experience & Training

Incentives

Affect

Outcome

Knowledge

Auditor Skeptical Judgment

Traits

Audit Context

Professional, PCAOB and Firm Audit Standards

Audit Management Tone

Traits

Knowledge

Experience & Training

Incentives

Affect

Outcome

Behavior (Auditor Skeptical Action)

Relationship with the Client

Strategic Communication

Outcome Expectations

Knowledge Person (Auditor) Audit Evidence Auditor Skeptical Judgment

Pursuit of Credibility

Preparation / Homework

Support / Collectivism

Behavior (Auditor Skeptical Action)
Support / Collectivism:

- Draws from a Pursuit of Comfort (Pentland, 1993) that permeates the audit experience as described by the participants, and
- Serves to strengthen the quality of Preparation/Homework
**Preparation / Homework:**

- Is strengthened by the level of support from others on the audit team, and
- Draws from the participants' Pursuit of Credibility, primarily in the eyes of the client, but also the audit team.
**Relationship with the Client:**

- Draws from the use of Strategic Communication,
- Influences the use of Strategic Communication, and is modeled to support the Pursuit of Credibility.
Possible Implications
Possible Implications

- Improved understanding of the distance between skeptical judgments and actions
- May lead to development of grounded theory of auditor efficacy
- Development of training and situational simulations for audit firms
- Auditing curriculum enhancement
Possible Future Research Directions
Possible Future Research Directions

Experiential Questionnaire (EQ)

- Development of a skeptical action EQ
  
  - To capture additional qualitative data among a broader population of auditors

- Development of additional skeptical action variables to test through experimental design

  - Refinement of the adapted model
Possible Future Research Directions

Development of Grounded Theory
– Case studies to move toward development of a grounded theory of auditor efficacy

International Replication
Possible Future Research Questions
Possible Future Research Questions

Absence of Support

– How are auditors impacted when considering skeptical action in the absence of a support network?

– How do they compensate when support is not present?
Possible Future Research Questions

Use of Communication Strategies

– What conditions allow auditors to most effectively use strategic communication strategies to affect skeptical action with increased efficacy?

– Are there certain attributes present in auditors who can more successfully apply these strategies? What context factors affect this ability?
Questions?
Thank You