

FOUNDATION FOR AUDITING RESEARCH

ONLINE INTERNATIONAL CONFERENCE PROGRAM

Auditing - the Human Factor

21 JUNE 2021

WWW.FOUNDATIONFORAUDITINGRESEARCH.ORG

FOUNDATION FOR
AUDITING
RESEARCH



**“WE COMBINE OUR
KNOWLEDGE &**

Strengthen the audit
profession’s learning curve.”

DEAR PARTICIPANT,

We welcome you to the 6th International Conference of the Foundation for Auditing Research. The theme of this year's conference is Auditing - the Human Factor.

Throughout the past year we have found our way in digital communication. We have learned to appreciate the value of our social networks and through meetings using digital means. During these interactions we as individuals wield control over these systems and it is clear from the interactions how important the human factor is in making the communication work: the systems work for us and we are in control of the information.

In auditing we increasingly deploy machines to conduct analyses. These machines can produce any information we want them to produce, but does the information make sense? Auditors are experts in assessing the validity and the reliability of the information these machines produce. Can the machine be trusted on providing appropriate reports? How does the auditor assure that that is the case, and how does the human factor come in play?

On the 21st of June, we will further explore the importance of the human factor in the audit process. We will discuss the human context of financial misstatements, the impact of team compositions on learning and how to respond to potential CEO integrity issues.

During this year's online conference, we would like to invite you to participate. Please share your knowledge, thoughts and opinions on how academia and practice can work together to achieve our joint objective: moving the audit profession forward.

On behalf of Henriette Prast, chair of the FAR board and Olof Bik, academic board member and managing director, we wish you an inspiring conference.

Kind Regards,

Jan Bouwens

Academic board member and managing director of the Foundation for Auditing Research

MONDAY 21 June 2021

Auditing – The Human Factor

12:30 – 12:40 **Welcome and opening speech**

Jan Bouwens, FAR Managing Director

12:40 – 13:10 **Plenary 1 – The auditor’s evaluation of misstatements –
Exploration, drivers, and consequences**

*Ann Vanstraelen, Maastricht University &
Ulrike Thürheimer, UNSW Sydney*

13:10 – 13:20 **Discussant**

Fabian Klar, BDO

13:20 – 13:40 **Q&A Online Audience**

13:50 – 14:20 **Plenary 2 – Why some auditors thrive while others struggle
– The effects of multiple team membership on audit quality**

Reggy Hooghiemstra, University of Groningen

14:20 – 14:30 **Discussant**

Esmée Hofland, Mazars

14:30 – 14:50 **Q&A Online Audience**

14:50 – 15:05 **Break – Podcast with Tjibbe Bosman on “Robotic Process
Automation for the Extraction of Audit Information”**

15:10 – 15:40 **Plenary 3 – Imitation behavior of junior auditors:
Does it enhance or hamper audit quality?**

*Eddy Cardinaels, KU Leuven &
Evelien Reusen, RSM*

15:40 – 15:50 **Discussant**

Sytse Jousma, EY

15:50 – 16:10 **Q&A Online Audience**

16:20 – 16:50 **Plenary 4 – CEO behavioral integrity,
auditor responses, and firm outcomes**

*Shane Dikolli, Darden School of Business,
University of Virginia*

16:50 – 17:00 **Discussant**

Rick Dekker & Marnix Pouw, Deloitte

17:00 – 17:20 **Q&A Online Audience**

17:20 – 17:30 **Closing reflections**

*Jan Bouwens, FAR Managing
Director*

The auditor's evaluation of misstatements: exploration, drivers, and consequences

Team: Prof. dr. Ann Vanstraelen
Prof. Roger Simnett
Prof. Gopal Krishnan
Prof. Teri Yohn
Dr. Ulrike Thürheimer

Startdate: January 2017

A key responsibility of the auditor is to ensure that financial statements are free from material misstatements. Auditors may detect misstatements during the audit process for which the auditor, through a negotiation process with management, either requires or waives an adjustment. This decision will influence the financial statement information set available to users of financial statements and is thus of high importance for audit quality. The decision to waive an adjustment is inherently subjective and difficult and requires judgment from auditors and managers. The overall aim of the research project is to gain a better understanding about this critical part of the audit, which determines audit quality.

The key objectives of the project are to understand, in the Dutch context, the type, nature, magnitude and direction of detected misstatements and subsequent adjustments; to understand the drivers of misstatement detection and adjustments, including audit input and process factors at the firm, office, partner and engagement level; to understand the consequences of misstatement detection and adjustment for financial statement users; and finally to understand how changing external conditions, including inspections and the new auditor reporting model, influence auditor behavior with regard to their adjustment decisions.



Ann Vanstraelen and Ulrike Thürheimer

2016B04 - The auditor's evaluation of misstatements: exploration, drivers, and consequences

How did you get into auditing research?

Ann: “I have been following the financial news from an early age. When I was starting my PhD, I read an article about bankruptcies in Belgium. The headline was that auditors were always too late with disclosing going-concern problems as many companies received a clean auditor's opinion in the year prior to bankruptcy. Intrigued by this, I decided to conduct an economic analysis of the auditor's going-concern opinion decision-making process as the subject of my PhD. So from the beginning, I was very interested in the topic of audit quality. Soon I found my way to Maastricht University, because they were the first to put academic auditing research on the map in Europe.“

Ulrike: “During my studies, I was always interested in research. I loved reading research papers. Ann, who was my professor in the auditing courses, was always a great role model, and I started my PhD with her as my supervisor. What fascinates me about auditing is the business model. Auditors provide an opinion, that is valuable, but consumers do

not have much or any insight into how the auditor formed this opinion. On top of that, auditors also face many conflicts of interests, for example being paid by the client while serving their shareholders. All of this makes researching auditing quite interesting.”

Why do you think auditing is so exciting?

Ann: “Many people are relying on the information provided by the auditor. The prosperity of society is highly dependent on the provision of reliable information that is necessary for good decision-making by various stakeholders. I consider it a prestigious profession. I always tell my students that in the past, like in ancient Egypt and China, auditing was considered one of the most prestigious occupations that served society. However, in the past 20 years, auditors have received bad publicity. I want to conduct research that is relevant for audit firms, standard-setters and regulators.”

Ulrike “One goal of the 2016B04 project is to research the value of auditing for society. The auditor, by detecting misstatements and through the process of adjusting and waiving misstatements, stands between pre and post-audited financial statements. This is how we can estimate the impact of the auditor. It’s important for our research to stay close to and to be informative for practice, but also standard-setters and regulators. Ultimately, we as researchers also want to have impact.”

What are, according to you, the most relevant issues in auditing?

Ann: “First, audit quality is one of the key challenges. Audit firms have already invested heavily in improvement in recent years. The next big step is digital transformation. The Big 4 audit firms invest a lot in digital platforms to have a more efficient and effective audit. Practice is ahead of standard-setters when it comes to technology, so this must be coordinated. Also, we will need a different type of auditor who understands these technologies. With robotic process automation, for example, some tasks currently done by junior auditors can be eliminated, but that will also make the job more interesting. This does not mean auditors will become irrelevant, technology is a facilitator. Second, the profession must address the needs of society. We see a shift in society’s expectations of society towards reporting fraud or climate risks. For example, EY recently portrayed climate risk as a Key Audit Matter. Auditors don’t have

the monopoly for other types of assurance, but they do have the reputations of providing independent high-quality opinions on information.”

What will your message be at the conference?

Ann: “We want to give insight into the value of the audit by providing descriptive evidence on detected misstatements and how they are evaluated. We know that there is some variation in audit quality. Our research could help audit firms to explain these variations. Next, we want to investigate what happens to detected misstatements and the impact of, for example, misstatements that are waived on the financial statements that are released to the public.”

Ulrike “The human factor in our study is about the process of evaluating detected misstatements, during which both auditors and clients are involved. This is often characterized as a negotiation process. As Ann mentioned, with this project, we can also show the value of the audit, and this should be of interest to the profession and other stakeholders. It provides insights into the value that auditors create.”

What does your ideal study look like?

Ulrike “With regard to the 2016B04 project, we have a lot of data and information on the audit side, which is great. However, if we had more detailed information about the client side, and the negotiation process about detected misstatements, we could perform a more comprehensive study. Furthermore, the current focus of the study is on the evaluation of detected misstatements, i.e. the decision to adjust or waive. If we knew whether the auditor detected all misstatements or not, we could also shed more light on the process of misstatement detection.”

Ann: “In general, as empirical researchers, we are very dependent on data. The data gathering process has shown us how much effort it takes for the firms to collect the data. We have learned a lot from our conversations with the firms and I think they have learned from this process too. The audit firms are now investing much more in information systems that help to retrieve data that is suitable for both the audit firm’s internal processes and academic research. I believe this is one of the main outcomes of the FAR research projects. And this will pave the way for many exciting research opportunities in the future.”

Why some auditors thrive while others struggle: The effects of multiple team membership on audit quality

Team: Prof. dr. Reggy Hooghiemstra
Prof. dr. Floor Rink
Dr. Dennis Veltrop
James Zhang PhD student

Startdate: January 2017

Within (large) auditing firms it is common practice that assistants, supervisors, managers, and audit partners are members of more than one engagement team at the same time and thus typically hold multiple team memberships (MTMs). This also implies that even in a single workday, auditors may be working on a number of different tasks and may be interacting with a multitude of members from different teams. MTMs can create opportunities (e.g., motivation to adopt more efficient practices and increased learning opportunities), but at the same time can be demanding (e.g., time-schedule conflicts, switching costs, and increased efforts to coordinate individual auditors' work). Evidently, MTMs are a double-edged sword. Interestingly, while MTMs are a central aspect of how auditing work is organized, to date, auditing scholars have not examined the factors that make auditors thrive or struggle within an MTM environment.

Therefore, this research project will focus on how and under what conditions working in an MTM-environment affects individual auditors' job performance as well as engagement team audit quality via both job-related outcomes (i.e., job satisfaction, job engagement, and intentions to leave) and auditor attitude (i.e., professional skepticism).



Reggy Hooghiemstra

2016B02 - Why some auditors thrive while others struggle – The effects of multiple team membership on audit quality

How did you get into academia?

“Initially I started working as an auditor, but when I saw a vacancy for a PhD position I knew that was it for me. My PhD was based on psychology, mainly how people explain outcomes in terms of factors they can or cannot influence themselves and how this is reflected in financial reports.”

How did you get interested in auditing?

“My education was in auditing, but I was always attracted to the combination of different topics. It enables me to develop different research skills, look at problems from different angles. For instance, especially when I started to work with Dennis Veltrop, who is also on the FAR team, I was more deeply drawn into psychological processes going on in teams, like supervisory boards. The step to other types of groups like audit teams was easily made.”

You worked in auditing for some time, what are the main challenges the profession faces?

“When I was trained, we tended to focus on

how to audit financial statements. In recent years, companies have started to put more emphasis on non-financial elements like CSR reports. It's becoming an important factor in the education of auditors at Universities and at the audit firms themselves. The competencies that auditors need to develop for new assurance services are comparable to core-audit skills, but also distinct. Another challenge is, more broadly, the disappearance of a traditional work/life balance. People face high workloads, it's a challenge to keep up. The current generation no longer wants to live to work, but work to have a nice life. This would require a new vision on planning systems and on how work is organized.”

How do you engage with practice?

“We do talk to practitioners, but during my teaching activities I'm also very much involved with the students of the executive program and the students which I supervise. They either work at an audit firm or do an internship. Through them, I hear what happens practice, what current challenges they face. The connection with students is very important for me to keep my research practice-oriented and relevant.”

How should your research influence the profession?

“We show that there are differences between ranks, managers seem to be dealing with more teams more easily than less experienced team members. For them, it's important to work on fewer engagement at the same time. It also seems to be important that they have some recovery time from their prior engagement. Giving more junior auditors more time to process the knowledge, provides more capital in the future to acquire knowledge more quickly.”

What will your message be at the conference?

“We will probably be combining our insights on the multiple team memberships and on advice seeking. How do people approach their colleagues to learn and get advice? It definitely relates to the Human Factor: although digitalization is becoming a bigger part of the audit, it's still humans that are responsible. We study how people work in teams, the challenges they face, how they familiarize with other team members and how they make the best use of their teams for their personal learning curve.”

“The conference will give us a nice opportunity to get direct input on our project, see our problems in a different perspective than we do. You can have a nice research in academic terms but if it does not resonate with practice, it doesn’t make sense what you are studying.”

What would your ideal study look like?

“I don’t think there is one, frankly. During the process I always end up with new questions, ideas, alternative methods. Your result is an answer to the question you pose in the introduction, but bound by the decisions you make along the way. You can never rule out alternative explanations. But it’s a good thing, it triggers to start a new research, on the same topic or another direction.”

2018B01

Imitation behavior of junior auditors: Does it enhance or hamper audit quality?

Team: Prof. dr. Eddy Cardinaels
Prof. dr. Kristof Stouthuysen
Dr. Evelien Reusen
Viola Darmawan PhD student

Startdate: November 2018

After the financial crisis, international standard setters have focused substantial attention on the improvement of quality audits of financial statements, for which the responsibility, ultimately, rests with auditors. Accordingly, the judgment and decision-making literature in auditing is largely concentrated on individual auditor judgments. However, auditors do not work in isolation, but interact with each other in audit engagements and with other participants in the financial reporting process.

This project proposes three specific research objectives on this matter, corresponding to three separate yet related studies. The first study investigates junior auditors' tendency to imitate, even when those practices are not always ideal. Of direct relevance, this might lead auditors failing to exercise sufficient professional skepticism in the conduct of their audits. In the second study, the focus is still on imitation, but considering audit team engagements and auditors' herd behavior in fraud assessment tasks. The aim is to examine whether reputation concerns and task ambiguity may at times lead auditors to ignore private information and copy the opinions of others. The third objective is to study auditor decision-making in reporting critical audit matters. Specifically, the team wants to examine how auditor tenure and shareholder involvement in the selection of auditors influence auditors' decision to report more original information than management discloses in the financial report.



Eddy Cardinaels

2018B01 – How auditors’ internal and external interactive relationships impact their judgement and decision making

How did you get into academia?

“I’m a professor in management accounting. I am very much interested in how people make decisions in organizations. We know people do not always have all the necessary information to make optimal decisions. There are biases that affect decision making and human interaction can affect those biases. That sparked my research interest.”

How did you get acquainted with the auditing field?

“In auditing, a lot of decision making takes place under pressure. Auditors have a lot of responsibilities: they must think about many different aspects that affect their job. I realized our fields have a lot in common. Then, I met Kristof Stouthuysen, who was working on imitation biases in the area of buyer-supplier contracting. We decided to work together on this topic in the context of financial auditing.

“At first, I didn’t know much about auditing, so I started doing interviews with people in practice. We talked about current issues, and whether

our research was making sense to them. I find it important that my research has impact on practice, talking to people helps a great deal with this. I really value the insights; they lead to good research ideas.”

What does your research focus on?

“Most junior auditors learn on the job. We are focusing on imitation behavior as a means to learn. Sometimes, imitation behavior seems to be beneficial for your performance rating, especially when pressuring conditions are in place, like a ranking system. People then tend to behave in favor of the ranking system, while you would want to foster creative thinking. Our study shows that imitation does not help auditors to get better in their work, which is not a satisfying conclusion. Thus, imitation is not necessarily beneficial for the quality of the audit. Imitation does work well when people are somewhat familiar with the topic. It helps them to imitate the good practices. It might become problematic when you imitate without critical thinking. Investing in training to reach familiarity with the topic is an important factor here.”

What would you consider to be the biggest challenges in the audit profession?

“From a research perspective, I believe that cross-field examination can help, for example from management accounting. We could think about how auditor’s incentives relate to compensation and critical thinking. Another important topic would be workload management, on which we have started a second FAR-study. We see some variations in the number of clients that auditors serve. How can this be explained, and does it affect audit quality, for example? We tend to think about audit quality at office or team levels, but on the level of individual auditors, we can study what thrives or diminishes individual performance. What role do incentives play here? I think that studying audit quality on the individual auditor level is very beneficial in answering those questions.”

During the conference, what will be your main message?

“We will mainly share our insights on imitation behavior, but foremost we like to emphasize the human factor in auditing. We know that people make mistakes, it’s part of human nature. If we can document the biases which affect the way we make decisions, then we can think of solutions. But first, we need to understand those biases. Working together with adjacent fields such as psychology and management accounting can lead to some very useful research ideas.”



Evelien Reusen

2018B01 – How auditors’ internal and external interactive relationships impact their judgement and decision making

How did you get into academia?

“I got the opportunity to do a PhD at KU Leuven, after which I was happy to join RSM, Erasmus University. My expertise is mainly in the area of Management Accounting and Control. This means that I am coming from a somewhat different background, but many of the principles also apply to the auditing field. Both disciplines have a behavioral orientation. It is much about judgment and decision-making but, for example, also about how to motivate people, often from a very behavioral perspective. This is exactly where the “human” factor comes in. I find it fascinating as a researcher to examine and understand what makes people behave and decide as they do, which may have consequences for managerial decision-making in general, but also – in an audit context – for audit quality in the end.”

How did you get acquainted with the auditing field?

“Management controls are an essential part of the structure and operations of any organization. The larger and more complex the organization and its activities, the more care must be given to

the design of the control systems. And this I would say especially also applies to audit firms. For example, I think incentive and promotion systems influence the way auditors do their work, how they make decisions, and how careful they make their judgements. In my research, I also have been studying imitation behavior – a common type of human behavior. In our daily lives we often imitate each other to guide our own choices; also in professional environments this can significantly affect individuals' judgment and decisions. Our FAR research project is set out to investigate this in the field of auditing, and particularly aims to explore the determinants and implications of imitative and herding behavior in relation to audit quality.”

What would you consider to be the biggest challenges in the audit profession?

“My general impression is that the quality of audit remains an important issue. Specifically, recurring factors identified as influencing audit quality are tone from the top and role model behavior, the quality of supervision and training, team interactions, and the extent to which the firm promotes an environment that favors speaking up about potential issues. With a good understanding of such factors we could reflect on the effectiveness of current firm practices and could come up with potential interventions, if needed.”

How do you interact with the profession?

“We try to have a dialogue. I think it's a two-way process: research is informed by practice and the other way around. We regularly have conversations about our research design with practice. Do they think it makes sense, do they recognize our frameworks? We are very much open to input from practice. I like the initiative to bring young professionals and academics together in seminars like the Brown Bags that FAR is organizing. I believe this is a great opportunity to facilitate connections and to keep our research projects focused on practically relevant matters.”

What will your main message be at the conference?

“My main message would be that, if we want to properly understand auditors' behavior, judgment and decision-making – and want to install certain interventions to enhance or preserve audit quality – the human factor cannot be overlooked and really must be “factored in””

“Specifically, at the conference, we would like to discuss the insights from our study on junior-senior imitation. Since the last masterclass, we have been finetuning and diving deeper into the results. It’s a good moment to present it again and receive feedback and see how practitioners can maybe relate to what we found. Also, raising awareness of the observed issues would allow for improvements in the quality of auditor judgments, so that’s something we’d like to bring up for discussion.”

What would you ideal study look like?

“With my ongoing research projects, I’ll continue to examine imitative and herding behavior and, particularly, its consequences for judgment and decision-making in accounting and auditing practice. For example, in our new study, we will examine herding behavior in relation to a fraud assessment task. Herding means conforming to the group’s consensus, although an individual might have other ideas or solutions. In studying this, it would be interesting to do a true field study or experiment where we could observe the dynamics that arise during an actual brainstorming session, or when auditors work in a team on a specific task. While there are limits to what we as researchers can do, I believe there is much more to be explored in this area; and I’m looking forward to uncovering further insights in close cooperation with the profession.”





Shane Dikolli

Shane Dikolli is the Bank of America Associate Professor in Business Administration at the University of Virginia, Darden Business School. His research interests focus on the performance evaluation of CEOs and CEO integrity. In auditing, Shane has conducted research on auditor's perceptions of client performance measurements and how they affect client risk assessment. Shane currently holds editorial board member positions at various journals, including *Accounting, Organizations & Society* and *Journal of Management Accounting Research*. He also serves as an editor at *The Accounting Review*.

How did you get into academia?

"After some time working as an accounting trainee, I accepted a position in the Budgets office of a large University. At the time, the academic Accounting department in the business school was short of instructors, and I decided to accept a part-time role teaching management accounting to undergraduates. I found it very enjoyable. My interest in research questions grew, and I ended up doing a Ph.D. at the University of Waterloo in Canada. In my thesis, I mainly focused on performance measures that incentive contract designers should use when a CEO has a short horizon. My current occupation in Virginia is a good fit. The Darden School

of Business pays special attention to advancing practice. It's very encouraging when the school expects faculty to engage with a practitioner audience."

How did you get acquainted with the auditing field?

"First, I worked on a project about how auditors perceive performance measures that their client's managers use. These perceptions have an impact on how auditors assess client risk. We found that auditors perceived a client as riskier when the client's managers faced riskier incentive contracts. In a recent paper, we studied the behavioral integrity of CEOs. Understanding the management team is important for auditors when assessing audit risk. A low integrity CEO, for example, could mean a greater chance of misstatement in the financial reports. We find that auditors respond to low-integrity CEOs by performing more audit work. As a consequence, clients with low-integrity CEOs appear to have higher audit fees."

"We also see that access in practice to more detailed data is developing. Data access will trigger many new opportunities for the management accounting field, for example, in the interaction between internal management accounting information and the application of internal audit processes. We could also exchange a lot of data-processing skills with practice. We, as academics, might have opportunities to help practitioners assemble large datasets designed for testing hypotheses."

What would you consider to be the biggest challenges in the audit profession?

"I think the main thing is the continuing evolution of the profession in how it uses technology, without losing emphasis on the human factor. In some contexts, you might be able to do 100% population testing, but it's humans who do the programming. You must be able to trust that the inputs are reliable and truthful and represent the economic transactions. I could see a shift away from an emphasis on sufficient evidence to more of an emphasis on appropriate evidence. Technology is taking over more standard work, so an increasingly important role of auditors will be in their ability to apply critical judgment."

How would that reflect in the auditor's education?

“This is a challenging subject. I believe a vital role of a University education is to teach their students to think conceptually about business problems which helps them operationalize solutions that ultimately depend on the context. For example, auditors can use many types of software to analyze and communicate information in performing audits. A conceptual framework for thinking about the role of the software would be constructive. Students can use such a framework to understand what the information reports might look like and what inferences they might be able to extract from the reports.”

During the conference, what will be your main message?

“I’m very much interested in this idea of integrity, of honoring your word. Integrity has economic consequences. The paper that I will present shows this by examining large samples of shareholder letters. We measure integrity by looking at words that CEOs use in shareholder letters. When a CEO does too much explaining relative to other CEOs facing similar circumstances, we conjecture that the market does not view the CEO as credible. I will be discussing some quite interesting anecdotes.”

What would your ideal research look like?

“I’d love to do a field experiment. A company would let us come in and implement both a treatment and a control group. It could be a way to see if we can improve how organizations share information among business units. For example, I’m curious about how to design information to make effective decisions more efficiently. With increasingly abundant sources of information, there’s a danger of information overload in organizations. How might it be possible to avoid information overload and do more with less information? What is the best information to use? These are important questions in both the auditing and management accounting fields.”

FOUNDATION FOR AUDITING RESEARCH

Copyright © 2021 by Foundation for Auditing Research

The Foundation

The Foundation for Auditing Research offers the unique opportunity to bring about cooperation between researchers and audit firms for exchange in the search for the drivers of audit quality and the root causes of audit quality failures.

Contact

Foundation for Auditing Research
Straatweg 25
3621 BG Breukelen
The Netherlands

info@foundationforauditingresearch.org
www.foundationforauditingresearch.org

a unique collaboration between
science and practice in auditing