A Call for Academic Inquiry: Challenges and Opportunities from the PCAOB Synthesis Projects

In 2011, the Public Company Accounting Oversight Board (PCAOB) approached the accounting academy about developing a number of research projects designed to amalgamate existing research on a number of topics into a series of knowledge bases for informing future regulatory action (i.e., the Synthesis Projects). The original reports from the project were delivered to the PCAOB late in 2011. This Supplement to Auditing: A Journal of Practice & Theory presents 11 papers derived from the original Synthesis Projects.

Each of the papers is based on a theoretical framework that facilitates the development of testable propositions. The use of an overarching framework allows researchers to identify gaps in the literature that might be addressed by other researchers in order to improve our conceptual understanding of important auditing issues, as well as audit practice and decision making. It is our hope that positioning each review within an appropriate theoretical framework will yield opportunities for the academy to advance audit research in a systematic and coherent manner. Consequently, one of the common themes across the papers is suggestions for future research on regulation and practice utilizing different methodological approaches. While most papers highlight opportunities for research using archival and experimental methods, several also address how interviews and other qualitative methods can be useful in developing insights into current audit practice. By providing these frameworks, and integrating multiple methodologies, we hope that the papers in this issue provide guidance for rigorous and relevant future research.

The papers included in this volume describe overarching themes related to the audit process and audit outcomes. In the next section, we summarize the seven papers dealing with the audit process. In the subsequent section, we consider the four papers addressing issues related to audit outcomes. We end with some broad conclusions about the state and future of audit research.

AUDIT PROCESS

The first of the seven papers related to the audit process that we mention is by Bratten, Gaynor, McDaniel, Montague, and Sierra (2013). This paper addresses a critical issue raised by the global financial crisis, namely, auditing fair value measures and evaluation of audit inspection findings related to fair value. This paper adapts the Bonner (2008) framework that evaluates auditor judgment through the lens of the environment, the task, and the person. The authors use this framework to identify gaps in the literature relevant to the improvement of current auditing judgments of fair market values. In addition to presenting a testable and useful theoretical framework, the authors highlight related PCAOB-identified deficiencies (e.g., professional skepticism and judgment problems). The authors present a number of different lines of inquiry that are united in the common theme of how estimates are audited, and how the judgments that
auditors make on fair value are evaluated. This paper sets the tone for this issue in highlighting the need for researchers to focus on improving the audit judgment process so that the quality of financial statements is ultimately improved.

One factor that affects these judgments is professional skepticism, which is examined in the paper by Hurtt, Brown-Liburd, Earley, and Krishnamoorthy (2013). This paper extends the framework presented by Nelson (2009) in categorizing research on skepticism into streams pertaining to auditor characteristics, evidence characteristics, client characteristics, and environmental characteristics. The authors find a significant research gap in the area of skeptical action. This gap yields an opportunity for other researchers to refine our definition of skepticism and to understand how it may best be imparted through training and socialization. The paper’s coverage of the ways to measure professional skepticism, both as an antecedent to judgment as well as the action itself, yield potential public policy implications.

As an initial step in the audit, the audit firm must make judgments on what items to sample and how to evaluate the results of the testing. Elder, Akresh, Glover, Higgs, and Liljegren (2013) provide a framework that relies on U.S. and international standards to inform our understanding of the sampling process. Among the issues raised in this article are those pertaining to the use of statistical and nonstatistical sampling, and the identification of items that should be subject to sampling. The authors also raise questions about the role of the regulatory environment or cultural differences in evaluating the effectiveness of different audit sampling techniques. The authors’ finding that the extant sampling research is dated and ignores these contextual factors suggests new routes for further research that may serve to yield improvements in the efficiency of the audit sampling process.

As a result of SOX (U.S. House of Representatives 2002), the audit of internal controls over financial reporting (ICOFR) has garnered much attention from auditors, regulators, and academics. Asare, Fitzgerald, Graham, Joe, Negangard, and Wolfe (2013) review the research on internal control and present a judgment and decision-making perspective organized around five performance factors: auditor attributes, client attributes, auditor-client interactions, task attributes, and the environmental context. The authors relate these factors to the planning, scoping, testing, evaluation, and reporting of ICOFR. They find a lack of research on the scoping and evaluation stages of ICOFR. The paper highlights how audit firms can improve the ICOFR audit process, and how researchers can test competing approaches to improve the effectiveness and efficiency of the ICOFR process.

One of the difficulties of conducting an audit relates to subsequent events. Chung, Cullinan, Frank, Long, Mueller-Phillips, and O’Reilly (2013) discuss this matter, and point out that a number of the PCAOB’s inspection reports have identified deficiencies in the audit of subsequent events. This paper is positioned within the behavioral accounting and the psychology literatures and identifies factors that can influence the audit of subsequent events. The authors present a cognitive-based model that highlights the environmental, individual, and task-specific factors that can influence the effectiveness of the audit of subsequent events. They find that complexity is introduced into the process through the need for auditors to remain vigilant for subsequent events. The authors identify both systematic approaches to evaluating subsequent events as well as heuristics that may lead to suboptimal audit results. This leads to a number of testable research questions on the degree to which accountability or client preferences affects the audit in this area. Ultimately, this paper may provide a roadmap on how to understand and improve the audit judgment processes and decisions that are made concerning subsequent events.

For better or worse, outsourcing is a reality that affects the accounting functions examined by audit firms. Bierstaker, Chen, Christ, Ege, and Mintchik (2013) explore the implications for auditors when transaction processing, asset valuation, information technology, and internal audit have been outsourced by the audit client. They discuss the implications of outsourcing on inherent and control risk, showing how inherent risk may be affected by the mere act of outsourcing and by the specific process outsourced, and how control risk may be affected by factors related to the client, the
outsource provider, and the auditor of the service organization. This area is fertile ground for researchers, and the authors present a framework that allows researchers to examine issues such as the objectivity, competence, and work performed by the user organization, service organization, and service auditor. The authors also tackle the issue of outsourcing the internal audit function. As the authors point out, this is an area that is seeing increasing outsourcing and raises the question of how external auditors differentially evaluate the internal audit function of a client.

In a related vein, Bame-Aldred, Brandon, Messier, Rittenberg, and Stefaniak (2013) explore how external auditors make decisions regarding the extent of reliance to be placed on internal audit work in complex environments. Reliance on internal auditing by external auditors has accelerated in recent years as clients are attempting to both garner cost savings as well as improve their compliance with SOX-related regulation. The authors present a framework for both understanding and improving this process. The framework incorporates environmental factors such as the client’s governance structure and client management characteristics, and moderating variables such as the legal environment. They find that even though extensive research exists related to external auditors’ evaluation of internal audit quality factors, there is limited research concerning the effects of auditor reliance on internal audit on subsequent audit quality. This paper then suggests ways for research to help provide public accounting firms with guidance on how to more effectively and efficiently rely on internal auditors.

**AUDITING OUTCOMES**

There are four papers on the outcomes from the audit process, generally considered in the broader context of audit quality. One aspect of audit quality is the ability to detect the presence of fraud. Statement on Auditing Standard No. 99 (AICPA 2002) requires auditors to actively search for fraud when conducting an audit. Trompeter, Carpenter, Desai, Jones, and Riley (2013) review the fraud literature and examine the completeness of the fraud triangle as a vehicle for understanding and detecting fraud. They present a model that expands the traditional fraud triangle to include a broad conceptualization of fraud detection techniques and demonstrate how researchers and auditors can benefit from this broader conceptualization. They also expand the accounting-based understanding of fraud by incorporating insights from criminology, sociology, ethics, and organizational behavior.

Ultimately, an audit firm must render an audit opinion within the audit report. Mock, Bédard, Coram, Davis, Espahbodi, and Warne (2013) examine what information users expect from the audit report and the factors that influence the usefulness of the report. Research still finds an expectations gap in the audit report, which the authors attribute to communication and content issues. The standard pass/fail nature of the audit opinion provides little insight to users. Users claim to want more information on the conduct of the audit, as well as information on materiality levels and risk evaluations. One of the interesting aspects of this paper is that it highlights the importance of understanding international users and regulators and how research in other countries can help inform the debate in the United States. As the format of the audit report is an ongoing public policy question, the paper is especially important as it presents many opportunities for future research. They specifically discuss the potential for enhanced disclosure to improve the report and how research can guide in developing a report that may attenuate the expectations gap.

In a further development of the expectations gap literature, Carson, Fargher, Geiger, Lennox, Raghunandan, and Willekens (2013) consider research conducted in different jurisdictions in order to identify the factors associated with the issuance of going concern opinions. They specifically consider client factors, characteristics of the auditor, relationships between auditor and clients, and other factors in the environment. They also provide recent descriptive information regarding the rate of going concern opinions in the United States over the last decade, and discuss the impact of the size of the client firm on the going concern process. An important contribution of this paper is the
documentation of the consequences of going concern audit opinions for a broad spectrum of stakeholders, including non-owners. The authors identify a need in future research for consideration of issues related to the accuracy of going concern opinions driven by regulator and public interest, and the responsibilities of management in the financial reporting framework.

Finally, the broader question of audit quality is addressed by Knechel, Krishnan, Pevzner, Shefchik, and Velury (2013). The authors extend Francis (2011) by providing a balanced scorecard approach to understanding audit quality. They highlight that audit quality is a multi-faceted concept and note that what is considered to be high audit quality may depend on the view adopted by any given stakeholder. The paper disaggregates the discussion of audit quality into four dimensions: inputs, processes, outcomes, and context. This model provides researchers with the ability to move the research field beyond studies of limited or isolated outcome measures and may assist in the development of a more comprehensive understanding of audit quality. The authors discuss multiple methods for examining audit quality and provide ideas on different aspects of the audit to advance this understanding.

CONCLUSION

We have learned a number of important lessons from these projects and reports. First, it is very obvious that the audit research field is vibrant, exciting, and growing. Second, a broad range of topics is being examined using a broad range of audit methods by a very diverse population of high-quality researchers around the world. Neither North America nor English-speaking countries have a monopoly on important audit research in today’s academic environment. Research performed across a broad spectrum of institutional settings and countries can answer questions that may not have even been raised in some environments. Regulatory developments such as the proposals on audit regulation in the European Union (European Commission 2010), the expansion of subject matter subject to assurance such as greenhouse gas emission reporting (Simnett et al. 2009a; Simnett et al. 2009b), and further development of current audit methodologies related to XBRL or continuous auditing (Rezaee et al. 2002; Plumlee and Plumlee 2008; Srivastava and Kogan 2010) promise to raise even more exciting opportunities for future auditing researchers.

It is our hope that this issue will stimulate research that exerts a positive effect on practice, theory, and regulation. We believe that the presentation of the Synthesis Projects, spanning such a wide range of audit research, and well grounded in solid theoretical frameworks, will enable researchers to attack these issues in a systematic and rigorous manner. This will manufacture a body of research that is coherent and generalizable and will help to overcome some of the limitations of existing research. In an ideal world, we will no longer entertain research that simply represents data in search of an explanation. Rather, we hope that some of the insights in these papers will encourage more and more researchers down the path of expectations-based and theoretically-driven research using multiple methods and searching out innovative and appropriate sources of data. Overall, we feel that the next decade of audit research will present continued opportunities and advancements to the audit research community.

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REFERENCES


