A QUALITATIVE EXAMINATION OF AUDITORS' DIFFERING ETHICAL CHARACTERIZATIONS ACROSS THE PHASES OF THE AUDIT☆

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ABSTRACT

Over the last decade, many published papers lament auditors' shift from professionalism to commercialism and call for increasing auditors' commitment to the public interest (see, e.g., Bailey, 2008; Fogarty & Rigsby, 2010; Lampe & Garcia, 2013; Wyatt, 2004; Zeff, 2003a, 2003b). At the same time, suggesting effective methodologies for improving auditors' commitment to the public interest is particularly challenging because issues arising in the audit context are complex, and often involve tradeoffs between multiple stakeholders (e.g., Gaa, 1992; Massey & Thorne, 2006). An understanding of auditors ethical characterizations across separate phases of the audit process is needed so that methodologies

☆ *Data availability*: Because of the need to preserve respondents' anonymity, data requests will be considered on a case-by-case basis.

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can be devised to improve auditors' commitment to the public interest. Thus, in this paper we interviewed 24 auditors and asked them to describe critical ethical incidents that they have encountered throughout the various phases of the audit process. Our results not only document the tension underlying the shift between professionalism and commercialism in auditing suggested by others, but also show that ethical conflicts are found in each phase of the audit and there are cross-phase differences in the auditors' ethical characterizations. Limitations of the findings are also discussed as are suggestions for future research.

Keywords: Auditor professionalism; commercialization of the audit; commitment to the public interest; in-depth interviews; qualitative methodology; semi-structured interviews

INTRODUCTION

Since Enron's demise, a substantial body of work has decried the fall of the auditing profession due to commercialization of the audit and called for changes to increase auditors' commitment to the public interest (see, e.g., Bailey, 2008; Fogarty & Rigsby, 2010; Lampe & Garcia, 2013; Wyatt, 2004; Zeff, 2003a, 2003b). Providing the profession with a roadmap for positive change, however, is particularly challenging for a number of reasons. First, issues arising in the audit context often involve tradeoffs between multiple stakeholders (e.g., Gaa, 1992; Massey & Thorne, 2006). Second, an audit is complex and comprised of distinct phases (Caster, Massey, & Wright, 2000). To date, prior research's failure to investigate the complexity of issues across the various phases of the audit has hampered efforts to devise effective methodologies for improving auditors' commitment to various stakeholders and, ultimately, the public interest. Accordingly, the purpose of our paper is to provide insight into auditors' ethical characterizations across the four phases of the audit.

To accomplish our purpose, we heed calls to enrich the ethics literature by using qualitative methodologies (e.g., Cohen & Holder-Webb, 2006; Gaa, 1994; Jones, Massey, & Thorne, 2003), interviewing 24 auditors and asking them to describe critical ethical incidents that they have encountered throughout the various phases of the audit process. Our results document the tension underlying the shift between auditor professionalism and commercialism that others have suggested. Moreover, our analysis shows that auditors encounter ethical conflict in each phase of the audit and that their ethical characterizations differ across the phases of the audit. As a result, our results not only underscore the importance of devising approaches to improve auditors' commitment to the public interest but also suggest that in the design of such approaches, differences across audit phases should be taken into consideration.

The remainder of the paper is comprised of four additional sections. The first provides a review of the literature and includes development of our research question. The second outlines the research approach while the third presents our results and analysis. The last section contains our discussion and conclusions.

LITERATURE REVIEW

Although elusive to define (e.g., Kirk, 1984; Swinney & Elder, 2012), a review of the literature suggests the term "professionalism," as applied to the auditing profession, has a public interest purpose (cf, Lampe & Garcia, 2013), and is characterized by several cornerstone auditing concepts, including: due care, independence, objectivity, professional skepticism, and integrity (cf, Bailey, 2008; Kirk, 1984; Wyatt, 2004; Zeff, 2003a, 2003b). On the other hand, "commercialism," as applied to the auditing profession, has a self-interest interest purpose; it refers to auditors' focus on the business of auditing (e.g., Willmott & Sikka, 1997; Windsor & Warming-Rasmussen, 2009; Zeff, 2003a, 2003b), where the "client and the market occupy the center of the professional universe" (Fogarty & Rigsby, 2010, p. 319).

Wyatt (2004) and Zeff (2003a, 2003b) have been forefront in describing the shift from professionalism to commercialism in the audit profession in the late 20th and early 21st centuries. Zeff (2003a, 2003b), for example, chronicles changes in the auditing profession – dating back from the last quarter of the 19th century to the turn of the 21st centuries – and reports that since the mid-1960s, public accounting firms have transformed "from organizations strongly imbued with professional values to ones that strongly pursue goals associated with commercial and business success" (2003a, p. 190). Among the "defining events" leading to the change in the profession, Zeff (2003b, p. 280) points to the following:

- The actions taken by the Federal Trade Commission and the Department of Justice to force the profession to repeal its bans against competitive bidding and direct, uninvited solicitation of clients.

- The increasing degree of sharp competitiveness for audit clients by the big firms, accompanied by the burgeoning growth in tax and consulting services to compensate for declining profits in a saturated audit market.
- The gradual withdrawal of the big firms from active participation in the dialogue over accounting principles, partly stimulated by their exclusion from the standard-setting process when the FASB replaced the APB in 1973.
- The transformation of professional firms that happened to be businesses into businesses that happened to render professional services. The audit mentality at the top management of the firms was replaced by a consulting mentality, including a headlong drive for growth, profitability and global reach – business, not professional values.
- The consequent weakening of audit partners' will to take a stand against clients' questionable accounting practices, as their risk of doing so would fall squarely on their shoulders, and not be diversified throughout the firm, as in earlier decades.

Wyatt (2004) likewise chronicles the audit profession's history – but this time, starting in the 1940s. He, too, reports a shift from professionalism to commercialism, concluding that by the late 1990s, ''Primarily commercial interests had undermined the core values of the professional firm'' (Wyatt, 2004, p. 50). Among the factors that Wyatt highlights as having contributed to the shift are: the rise of consulting/nonaudit services, a move to hire nonaccounting graduates who lacked training in/knowledge of accounting and the profession's cornerstone concepts, and a push to generate revenues driven by a rise in the culture of greed. Wyatt (2004, p. 50) summed up the shift as follows:

> In essence, the culture of the leading firms in the profession had changed. New personnel who lacked a background that placed prominence on accounting professionalism gradually gained increasing influence in accounting firms. The consulting arms were rapidly growing and were gaining higher compensation levels than the audit and tax partners. The leaders of the audit and tax practices felt increasing pressure to grow revenues rapidly and, more importantly, to grow profit margins in their service areas. Those with a facility to sell new work advanced more rapidly. Cross-selling a range of consulting services to audit clients became one of the important criteria in the evaluation of audit partners. Those with the technical skills previously considered so vital to internal firm advancement found themselves with relatively less important roles. Staff personnel within the firms were easily able to observe the attributes of those who were the rapidly rising stars and undertook efforts to emulate these attributes. The focus on delivering quality professional service did not disappear, of course. No one rang a bell in a firm and announced, ''Quality professionalism is out!'' On the other hand, keeping the client happy and doing what was necessary to retain the client achieved a prominence that did not exist prior to the advent of the consulting arms.

More recently, because of renewed efforts in the profession to expand the acceptable range of services beyond traditional auditing, Bailey (2008), too, describes a shift from professionalism to commercialism in the late 20th century. Bailey (2008, p. C29) states:

> In recent years, there has been an effort by many in the practicing profession and some in academe to expand the breadth and depth of services that they wish to have identified as part of the core profession beyond the audits of financial statements. Justifying arguments include: (1) the basis of the assurance nature of the service gives the profession a comparative advantage; (2) the service, while not strictly or solely related to the audit of financial statements, enhances the ability of the auditor to complete a high-quality audit of the financial statements; and, (3) unless the professional firms can grow and expand their total revenue base, the public audit will be threatened by an inability to attract quality professionals. Although each of these positions has merit, in recent years these arguments have been driven beyond reasonable limits, seemingly taking the position that if it is profitable for the accounting firms, it is good for the profession and good for the public.

In a similar vein, Fogarty and Rigsby (2010) report a shift from professionalism to commercialism in concert with development of the Business Risk Audit approach in the 1990s. They state (at p. 315):

> In the new audit of the 1990s, major changes in the core values of the audit profession and in audit methodology supported blurring the differences between auditing and consulting (Robson, Humphrey, Khalifa, & Jones, 2007) as the commercial orientation of the audit profession was extended to its logical conclusion.

Given this shift to commercialism, it is not surprising the researchers call for changes to increase auditors' commitment to the public interest. For example, Bailey (2008, pp. C35–C36) calls upon the profession's leaders to "adopt in a deep and abiding way, the idea that we are not a business first, but rather that we are a profession first with the need to operate a viable business to support the profession's goals … ." Likewise, Lampe and Garcia (2013) recommend that audit professionals *act* like professionals. However, as Wyatt (2004, p. 53) notes, regulation is not a sufficient answer:

> The survival of the accounting profession as an important facet of our society cannot rely on the effectiveness of the Sarbanes-Oxley legislation. The leaders of the profession need to understand why they have failed to serve the public well in recent years. These leaders need to embrace policies now that will enable their professional staffs to once again meet the public's expectations.

Despite these calls for change, little guidance is provided as to the particular changes needed to improve the profession's public interest focus. The lack of specificity is not surprising, however, for several reasons. First, issues arising in the audit context are complex, often involving tradeoffs between multiple stakeholders (e.g., Gaa, 1992; Massey & Thorne, 2006). As Apostolou and Crumbley (2008, p. 34) state, ''Because auditors cannot evaluate every transaction of a company [during the course of their audits], they have to make judgments and decisions dictated by a risk assessment and cost-benefit analysis.'' Further, contextual and individual factors bear upon auditors' assessment of risks and analysis of costs versus benefits (cf, Jones et al., 2003; Wolfe & Hermanson, 2004).

Second, not only are the issues arising in audit complex, but also, the audit itself (e.g., Apostolou & Crumbley, 2008). Caster et al. (2000) identify four distinct phases to the audit process – namely, risk assessment, program planning, execution and reporting (Caster et al., 2000) – each of which differentially impacts upon auditors' judgments and decisions. For example, in the risk assessment phase of the audit, auditors typically brainstorm ''about the susceptibility of the financial statements to material misstatement due to fraud, and the role of management in perpetrating and concealing fraudulent financial reporting. [In doing so,] auditors should be aware of the management's incentives to commit fraud as well as the opportunity for fraud to be perpetrated'' (Apostolou & Crumbley, 2008, p. 33). However, in their program planning, auditors' ''overall response to risk assessment involves procedures that are not predictable, such as modifying the assignment of personnel, the degree of supervision, and selecting auditing procedures'' (Apostolou & Crumbley, 2008, p. 34).

In light of the foregoing, any program to increase the degree to which auditors promote the public interest must necessarily recognize the complexity of issues auditors encounter across all the phases of the audit. To date, however, prior research has failed to consider the full range of issues auditors encounter in the various phases of the audit. Given the need for suggestions to increase auditors' consideration of the public interest and the importance of understanding the factors that influence auditors' judgments across all phases of the audit, this paper revisits the professionalism/commercialism shift. The objective is to ascertain differences in auditors' ethical characterizations across each of the four phases of the audit, which is particularly important as more judgment is being introduced into auditors' decision-making processes as the United States adopts more principles-based accounting standards (including IFRS). To do so, we investigate the following research question:

RQ. Do auditors' ethical characterizations differ across the four phases of the audit?

RESEARCH APPROACH

Our research attempts to highlight differences in auditors' ethical characterizations across the four phases of an audit. We utilize a qualitative methodology, analyzing auditors' verbal protocols about critical ethical incidents to capture their cognitions about ethical conflicts that occur throughout the audit process. Accounting researchers recognize that using narrations of critical audit incidents can be useful as a means for developing a deeper understanding into the auditors' thought processes (e.g., Kwok & Sharp, 2005; Sweeney & Pierce, 2004; see also Bédard & Gendron, 2004; Horton, Macve, & Struyven, 2004). Accordingly, we conducted in-depth interviews to obtain the rich data needed to gain insight into auditors' ethical cognitions.

As a research technique, Kerlinger (1986, p. 440) states that:

> The interview is probably man's oldest and most often used device for obtaining information. It has important qualities that objective tests and scales and behavioral observations do not possess. When used with a well-conceived [structure], an interview can obtain a great deal of information, is flexible and adaptable to individual situations, and can often be used when no other method is possible or adequate … . Most important, perhaps, the interview permits probing into the context and reasons for answers to questions.

The main drawback of the technique is that it is labor intensive.

Our interviews were conducted in a semi-structured format, which initially involved asking the auditors to relate critical ethical incidents they encountered during key phases of the audit. Semi-structured (or focused) interviews use a standardized set of questions, but allow the interviewer to follow up on unexpected findings and thus enhance the opportunities for new theoretical developments (Frankfort-Nachmias & Nachmias, 1992; Horton et al., 2004; Merchant, Chow, & Wu, 1995). Narrations about critical incidents permit the respondents to tell "stories" about their experiences and allow for rich responses (Martin, Feldman, Hatch, & Sitkin, 1983).

Hence, our interviews were guided by the following questions:[1]

1. Please tell me about the most important ethical incident that you have faced in your career that arose during the (each) phase of the audit.[2]
2. Why do you consider it an ethical incident?
3. Why do you consider it the most important ethical incident?
4. When did it occur? How long ago was that? At what level were you when it happened?

5. How was it resolved? Did your firm/supervisor/peer/colleagues support you?
6. How often would you say you face this incident?

Because it was important for our interviewees to consider all phases of the audit process, we asked them to describe the key ethical issues that they encountered during each of the four phases of an audit – risk assessment, planning, execution, and reporting (Caster et al., 2000). To ensure a similar understanding among our interviewees, we provided the auditors with the following definitions of each phase of the audit process (Caster et al., 2000):

1. *Risk assessment*: Please think about the audit process. One of the first steps in that process is to assess risks associated with performing the audit. For example, during this phase of the audit, auditors assess such factors as materiality, audit risk, inherent and control risks as well as business risk (that is, risks to the firm such as litigation or loss of reputation that may result from a particular client relationship).
2. *Program planning*: Please think about the program-planning phase of the audit. During the program-planning phase of the audit, the nature, extent, timing and staffing of audit tests are determined – based upon the risk assessment performed earlier.
3. *Execution*: Please think about the execution stage of the audit. Execution refers to the act of conducting the audit tests set forth in the audit program and evaluating the resultant test evidence.
4. *Reporting*: The last step in the audit process is to report or communicate the findings of the audit to the shareholders, audit committee, etc.

The interviewees are auditors at all hierarchical levels from large, multinational and small, local audit firms. Our sample selection was based on three factors. First, because evidence suggests that the interpretation of ethical issues may vary across audit firms (Sweeney & Roberts, 1997), we interviewed auditors from both Big 4 (B4) and local (small) firms. Second, since all levels of staff participate in the audit, we decided that a multi-participant view of the various ethical issues would give us a richer understanding of the audit process. In addition, some empirical evidence suggests that as audit experience increases, sensitivity to ethical issues declines (Ponemon, 1992; Sweeney & Roberts, 1997), therefore, we wanted to unearth whether ethical issues are viewed differently according to level of experience. Finally, because gender-specific findings for auditors' interpretations of ethical issues are conflicting (see, e.g., Jones et al., 2003 for a review of the literature), we also wanted to ensure that we interviewed both male and

Table 1. Characteristics of Interviewees.

Panel A: Large, multinational firms

Interviewee	Firm #1	Firm #2	Both Large Firms
	Number of interviewees by firm		
Partners	1	0	1
Managers	1	2	3
Seniors	2	2	4
Staff	2	2	4
Total	6	6	12
	Number of interviewees by gender		
	Male	Female	Total
Partners	1	0	1
Managers	1	2	3
Seniors	2	2	4
Staff	2	2	4
Total	6	6	12

Panel B: Small, local firms

Interviewee	Firm #1	Firm #2	Both Small Firms
	Number of interviewees by firm		
Partners	1	0	1
Managers	1	2	3
Seniors	2	2	4
Staff	2	2	4
Total	6	6	12
	Number of interviewees by gender		
	Male	Female	Total
Partners	1	0	1
Managers	3	0	3
Seniors	3	1	4
Staff	3	1	4
Total	10	2	12

female auditors to assess gender differences, if any. In total, 24 individuals were interviewed. Table 1 provides a summary description of the respondents.

In order to gain access to the auditors, we personally approached a partner at each firm included in our sample and asked permission to interview audit personnel for purposes of conducting a study of auditors' experiences and perceptions about the ethical incidents that arise in audits. Because of our selection criteria, we chose to approach only large, multinational and small, local firms. We asked each firm to permit us to meet with a gender-balanced mix of auditors drawn from each of the hierarchical levels.[3]

Because of the sensitive nature of the interviews, the firms agreed that the content of our interviews would be confidential from them. However, we did agree to provide the firms with a summary of our overall results – aggregated across all interviewees. This process yielded the agreement of 2 large, multinational firms and 2 small, local firms.[4]

Ultimately, the interviews were scheduled at a mutually convenient time (during the slower summer months). In some cases, the designated interviewee was unavailable the day of the scheduled interview because of client needs; in those cases, the firm provided a "substitute" interviewee. All of the interviews took place on site at the audit firm offices. Each interview, which lasted between 30 and 90 minutes, was taped and transcribed. In order to put interviewees at ease, at the beginning of the interviews, the researcher told the auditors that their participation was completely anonymous and that all identification would be removed from the tapes and transcripts of the recordings. The auditors were also informed that no findings would be tied to specific individuals or firms and that only aggregate information (for all interviews combined) would be provided to the firm.

RESULTS AND ANALYSIS

Overview

We analyzed the data to determine emergent patterns from which we could identify:

1. The underlying sources of ethical conflict for auditors during the audit;
2. Auditors' ethical characterizations during each phase of the audit; and
3. Differences across the phases of the audit.

(Van Maanen, 1979; see also Bédard & Gendron, 2004; Phillips & Phillips, 2007).

Correspondingly, our primary analysis involved three steps:

1. Performing content analysis to identify sources of ethical conflict for the auditors during the audit;
2. Analyzing the data to consider significant patterns in auditors' ethical characterizations of the four phases of the audit; and
3. Analyzing the data by audit phase to identify cross-phase differences.

Supplementing our primary analysis, we offer our observations about the degree to which we perceived differences in our results due to firm size, hierarchical level and gender.

Sources of Auditors' Ethical Conflict during the (Overall) Audit

The first step in our analysis involved the systematic content analysis of the interview transcripts to identify sources of ethical conflict (Huberman & Miles, 1994). We had two researchers both with audit experience code the transcripts based upon the sources of conflict identified. The ''code book'' that identifies the sources of conflict identified in the transcripts and that we used for our analysis appears in Table 2.[5]

For the second step in our analysis, we considered the total number of items coded in our analysis (450 items), as shown in Table 3. From the authors' scrutiny of the transcripts and a review of the data in Table 3, two key sources of conflict in the auditors' resolution of ethical incidents (cf, Gaudine & Thorne, 2001) during the audit emerged[6]: ''performing the audit'' and the ''auditor–client relationship.'' The first broad theme of ''performing the audit'' focuses on the task of auditing. The second broad theme of the ''auditor–client relationship'' focuses on the interaction between auditors and their clients.

Sources of Auditors' Ethical Conflict during the Four Audit Phases

Of the (450) total items coded in our analysis (as shown in Table 3), approximately one-quarter related to each the risk assessment and execution phases of the audit. About one-third related to the planning stage of the audit and approximately 16% related to in the reporting stage of the audit. Thus, overall, ethical issues were most prevalent in the planning stage of the audit and least prevalent in the reporting stage of the audit.

Table 2. Code Book.

Panel A: Risk Assessment Stage

10000 Ethical issues during the risk assessment stage

- 11000 Client integrity
    - 11001 CEO's ethics
- 12000 Relationship with client
    - 12001 Length of time
    - 12002 Previous experiences
    - 12003 Personal relationship/liking
    - 12004 Satisfy the client
    - 12005 Size of fees
- 13000 Level of transparency/quality of controls
    - 13001 Control/reporting system
    - 13002 Financial performance
- 14000 Considerations inherent in risk assessment
    - 14001 Risk to CPA firm
    - 14002 Harm to third parties (shareholders, etc.)
    - 14003 Personal responsibility
    - 14004 Comfort level
    - 14005 Duties of the CPA
    - 14006 Ethical character of management
    - 14007 Economic environment/industry
    - 14008 New client
    - 14009 Going public/public company
    - 14010 Additional financing
- 15000 Examples
    - 15001 Withhold information from the auditors
    - 15002 Falsify reports
    - 15003 Related party transactions
    - 15004 IPO – stock promotion
    - 15005 Fraud – no specifics
    - 15006 Rapid growth
- 16000 Resolution
    - 16001 Do not accept/drop client
    - 16002 Discussion with partners
    - 16003 Force client to disclose controversial issue
    - 16004 Discussion with Board
    - 16005 Negotiate agreement with client
- 17000 Not my job
    - 17001 No responsibility
    - 17002 Refer to partner

Table 2. (*Continued*)

Panel B: Planning Stage

20000 Ethical issues at the planning stage
- 21000 Procedures/issues in making ourselves comfortable
  - 21001 Appropriate test
  - 21002 Level of risk
  - 21003 Appropriate number
  - 21004 Timing of test
  - 21005 Adequate staffing
  - 21006 Presence of controls
  - 21007 Understanding the client's business
  - 21008 Personal comfort level
  - 21009 Involvement of other auditors
  - 21010 Quality of audit staff
- 22000 Client relationship considerations
  - 22001 Cost overruns
  - 22002 Past experience
  - 22003 Relative size of fees
  - 22004 Relative size of client
- 23000 Client-specific concerns in carrying out procedures
  - 23001 Quality of client staff
  - 23002 Adequacy of fees
  - 23003 Adequacy of time on premises
- 24000 Examples
  - 24001
- 25000 Resolution
  - 25001 Engagement team discussion
- 26000 Not my job
  - 26001 No experience

Panel C: Execution Stage

30000 Ethical issues at the execution stage
- 31000 Considerations in making adjustments in the field
  - 31001 Theory versus practice
  - 31002 Finishing the audit after the report is released
  - 31003 Time pressures
  - 31004 Judgmental issues
  - 31005 Quality of staff
- 32000 Degree of trust in client
  - 32001 Balance between evidence and trust
  - 32002 Lack of cooperation
  - 32003 Timing of information

Table 2. (*Continued*)

Panel C: Execution Stage
33000 Other relationships with client
33001 Bookkeeping services
34000 Independence issues
34001 Other relationships
35000 Resolution
35001 Engagement team discussion
35002 Discussion with client
Panel D: Reporting Stage
40000 Ethical issues at the reporting stage
41000 Considerations in identifying reportable matters
41001 Defining materiality
41002 CPAs' responsibilities
41003 Differences in judgment
42000 Client relationship
42001 Standards versus client's needs
42002 Impact on relationship
42003 Responsibility to other parties
43000 Questioning the rules
43001 Common sense versus following the rules
44000 Resolution
44001 Discussion with audit committee
44002 Discussion with shareholders
44003 Discussion with client
45000 Examples
45001 Subsequent events
45002 Related parties
45003 Contingencies

Differences in Auditors' Ethical Conflict during the Four Audit Phases

For the third step in our analysis, we sorted the data according to each of the phases of the audit in order to identify the extent to which each of the two sources of ethical conflict (i.e., ''performing the audit'' and the ''auditor–client relationship'') existed in each phase of the audit. As show in Tables 4 and 5, respectively, both sources of ethical conflict, ''performing the audit'' and the ''auditor–client relationship,'' are found in each phase of the audit.

Table 3. Overall Code Book Category Counts/Percentages.

#	Code Book Description	Count	Percentage
10000	*Ethical issues during the risk assessment stage*		
11000	Client integrity	9	2.0
12000	Relationship with client	23	5.1
13000	Level of transparency/quality of controls	11	2.4
14000	Considerations inherent in risk assessment	39	8.7
15000	Examples	4	0.9
16000	Resolution	15	3.3
17000	Not my job	15	3.3
Subtotal		*116*	*25.8*
20000	*Ethical issues at the planning stage*		
21000	Procedures/issues in making ourselves comfortable	124	27.6
22000	Client relationship considerations	19	4.2
23000	Client-specific concerns in carrying out procedures	2	0.4
24000	Examples	0	0.0
25000	Resolution	1	0.2
26000	Not my job	3	0.7
Subtotal		*149*	*33.1*
30000	*Ethical issues at the execution stage*		
31000	Considerations in making adjustments in the field	67	14.9
32000	Degree of trust in client	44	9.8
33000	Other relationships with client	0	0.0
34000	Independence issues	0	0.0
35000	Resolution	0	0.0
Subtotal		*111*	*24.7*
40000	E*thical issues at the reporting stage*		
41000	Considerations in identifying reportable matters	21	4.7
42000	Client relationship	43	9.6
43000	Questioning the rules	6	1.3
44000	Resolution	4	0.9
45000	Examples	0	0.0
Subtotal		*74*	*16.4*
Total		*450*	*100.0*

A review of Table 4 in conjunction with Table 3 reveals that of 450 items in our analysis, approximately 68% (i.e., 308) relate to "performing the audit." Of the (308) items associated with "performing the audit," 80 items (26%) relate to the risk assessment phase of the audit; 130 items (42%) relate to the planning phase of the audit; 67 items (22%) relate to the execution phase of the audit; and 31 items (10%) relate to the reporting phase of the audit.

A review of Table 5 in conjunction with Table 3 reveals that of 450 items in our analysis, approximately 31% (i.e., 138) relate to the "auditor–client relationship." Of the (138) items associated with the "auditor–client relationship," 32 items (23%) relate to the risk assessment phase of the audit; 19 items (14%) relate to the planning phase of the audit; 44 items (32%) relate to the execution phase of the audit; and 43 items (31%) relate

Table 4. Execution of the Audit Task – Code Book Category Counts/Percentages.

#	Code Book Description	Count	Percentage[a]
10000	*Ethical issues during the risk assessment stage*		
13000	Level of transparency/quality of controls		
13001	Control/reporting system	9	2.9
13002	Financial performance	2	0.6
14000	Considerations inherent in risk assessment		
14001	Risk to CPA firm	6	1.9
14002	Harm to third parties (shareholders, etc.)	7	2.3
14003	Personal responsibility	5	1.6
14004	Comfort level	5	1.6
14005	Duties of the CPA	3	1.0
14006	Ethical character of management	4	1.3
14007	Economic environment/industry	2	0.6
14008	New client	1	0.3
14009	Going public/public company	5	1.6
14010	Additional financing	1	0.3
16000	Resolution		
16001	Do not accept/drop client	1	0.3
16002	Discuss with partners	6	1.9
16003	Force client to disclose controversial issue	3	1.0
16004	Discuss with Board	2	0.6
16005	Negotiate agreement with client	3	1.0
17000	Not my job		
17001	No responsibility	13	4.2
17002	Refer to partner	2	0.6
Subtotal		*80*	*26.0*
Total items coded "performing the audit"		*308*	*100.0*

Table 4. (*Continued*)

#	Code Book Description	Count	Percentage[b]
20000	*Ethical issues at the planning stage*		
21000	Procedures/issues in making ourselves comfortable		
21001	Appropriate test	14	4.5
21002	Level of risk	10	3.2
21003	Appropriate number	17	5.5
21004	Timing of test	4	1.3
21005	Adequate staffing	26	8.4
21006	Client controls	13	4.2
21007	Understanding the client's business	8	2.6
21008	Personal comfort level	8	2.6
21009	Involvement of other auditors	0	0.0
21010	Quality of audit staff	24	7.8
23000	Client-specific concerns in carrying out procedures		
23001	Quality of client staff	1	0.3
23002	Adequacy of fees	1	0.3
23003	Adequacy of time on premises	0	0.0
25000	Resolution		
25001	Engagement team discussion	1	0.3
26000	Not my job		
26001	No experience	3	1.0
Subtotal		*130*	*42.2*
Total items coded "performing the audit"		*308*	*100.0*

#	Code Book Description	Count	Percentage[c]
30000	*Ethical issues at the execution stage*		
31000	Considerations in making adjustments in the field		
31001	Theory v. practice	12	3.9
31002	Finishing the audit after the report is released	5	1.6
31003	Time pressures	23	7.5
31004	Judgmental issues	22	7.1
31005	Quality of staff	5	1.6
35000	Resolution		
35001	Engagement team discussion	0	0.0
35002	Discussion with client	0	0.0
Subtotal		*67*	*21.8*
Total items coded "performing the audit"		*308*	*100.0*

Table 4. (*Continued*)

#	Code Book Description	Count	Percentage[d]
40000	*Ethical issues at the reporting stage*		
41000	Considerations in identifying reportable matters		
41001	Defining materiality	4	1.3
41002	CPA's responsibilities	10	3.2
41003	Differences in judgment	7	2.3
43000	Questioning the rules		
43001	Common sense versus following the rules	6	1.9
44000	Resolution		
44001	Discussion with audit committee	1	0.3
44002	Discussion with shareholders	1	0.3
44003	Discussion with client	2	0.6
Subtotal		*31*	*10.1*
Total items coded "performing the audit"		*308*	*100.0*

[a]Percentage is based on a ratio of the count of the individual codebook category to the total count for all codebook categories related to "execution of the audit task." Due to rounding, sub-level percentages sum to 25.6% rather than the 26.0% reported for the subtotal.
[b]Percentage is based on a ratio of the count of the individual codebook category to the total count for all codebook categories related to "execution of the audit task." Due to rounding, sub-level percentages sum to 42.0% rather than the 42.2% reported for the subtotal.
[c]Percentage is based on a ratio of the count of the individual codebook category to the total count for all codebook categories related to "execution of the audit task." Due to rounding, sub-level percentages sum to 21.7% rather than the 21.8% reported for the subtotal.
[d]Percentage is based on a ratio of the count of the individual codebook category to the total count for all codebook categories related to "execution of the audit task." Due to rounding, sub-level percentages sum to 9.9% rather than the 10.1% reported for the subtotal.

to the reporting phase of the audit. Auditors' ethical characterizations of the audit – overall and by phase – are depicted in Fig. 1.

In sum, overall, issues related to "performing the audit" (at 68%) are more prevalent than are those related to the "auditor–client relationship" (at 31%).[7] In the risk assessment phase of the audit, issues related to "performing the audit" (26%) are approximately equally prevalent to those related to the "auditor–client relationship" (23%). The overall relationship, showing a higher proportion of issues related to "performing the audit" than the "auditor–client relationship," holds in the planning phase of the audit (i.e., 42% for "performing the audit"; 14% for the "auditor–client relationship"), but reverses in the execution and reporting phases of the audit. That is, only 22% and 10% of issues related to "performing the

Table 5. The Auditor–Client Relationship – Code Book Category Counts/Percentages.

#	Code Book Description	Count	Percentage[a]
10000	*Ethical issues during the risk assessment stage*		
11000	Client integrity		
11001	CEO's ethics	9	6.5
12000	Relationship with client		
12001	Length of time	5	3.6
12002	Previous experiences	15	10.9
12003	Personal relationship/liking	3	2.2
Subtotal		*32*	*23.2*
20000	*Ethical issues at the planning stage*		
22000	Client relationship considerations		
22001	Cost overruns	12	8.7
22002	Past experience	2	1.4
22003	Relative size of fees	3	2.2
22004	Relative size of client	2	1.4
Subtotal		*19*	*13.8*
30000	*Ethical issues at the execution stage*		
32000	Degree of trust in the client		
32001	Balance between evidence and trust	34	24.6
32002	Lack of cooperation	10	7.2
32003	Timing of information	0	0.0
33000	Other relationships with client		
33001	Bookkeeping services	0	0.0
34000	Independence issues		
34001	Other relationships	0	0.0
Subtotal		*44*	*31.9*
40000	*Ethical issues at the reporting stage*		
42000	Client relationship		
42001	Standards versus client's needs	11	8.0
42002	Impact on relationship	19	13.8
42003	Responsibility to other parties	13	9.4
Subtotal		*43*	*31.1*
Total items coded "the auditor–client relationship"		*138*	*100.0*

[a]Percentage is based on a ratio of the count of the individual codebook category to the total count for all codebook categories related to the "auditor–client relationship." Due to rounding, sub-level percentages do not always sum to the percentage reported for the corresponding subtotal.

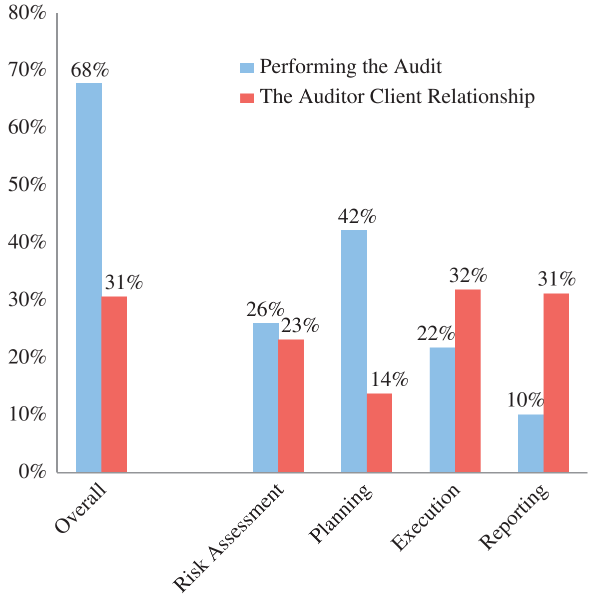

Fig. 1. Sources of Auditors' Ethical Conflict (Overall and Across the Phases of the Audit).

audit'' in the execution and reporting phases of the audit, respectively, whereas 32% and 31% of the issues related to the ''auditor–client relationship'' in the execution and reporting phases, respectively.

Auditors' Ethical Conflict in the Risk Assessment Phase

Risk Assessment involves determining the dangers associated with auditing a particular client. The purpose of risk assessment is to evaluate whether to accept and/or retain a client. As noted above, in the risk assessment phase of the audit, auditors are equally likely to encounter ethical conflict arising from ''performing the audit'' and the ''auditor–client relationship.'' As a result, both sources of conflict bear upon auditors' ethical characterizations of the risk assessment phase of the audit.

In making client acceptance/retention decisions, ''performing the audit'' involves assessing the audit context. In doing so, auditors consider engagement-specific features, such as whether the client is public and the client's industry, as explained below:

> … it's a risk I think we are willing to take just because we've been on the client for a long time client for a long time and we know they have a profitable line, we know they have

> a ton of cash, they've always been great to us, they're non-public, um their only shareholders are their parent who's the only one using the financials … . (B4 Firm #1, Senior #2, Male)

> … we often sit back and talk about industry specific items and where can there be problems, where can there be errors in their calculations, what other types of things that can come up … . (B4 Firm #1, Partner, Male)

And, although auditors profess professionalism in ''performing the audit,'' it is interesting to note that audit fees also affect their client acceptance/retention decisions, as explained below:

> It's again part of your engagement acceptance. I mean is this a job that you can perform with adequate profitability and um, sleep at night; that you and your partners aren't going to be sued and you're going to be able to justify your opinion? (Small Firm #1, Partner, Male)

> Part of [the decision about whether] to the ''dump'' the client was the fee because we weren't getting a lot of fee for the audit. So now we're talking about taking on a big risk and not getting adequately paid for it. (B4 Firm #2, Manager #1, Female)

The ''auditor–client relationship'' also affects auditors' risk assessments through trust. Trust in the client can aid auditors in their evaluation of risk in making client acceptance/retention decisions. As the quotes below highlight, the longevity of the client relationship as well as previous experiences affect the degree to which auditors trust their clients and, in turn, assess their clients' riskiness.

> Again, if a client has had a very good history, the same personnel, then you're probably not as skeptical. (Small Firm #1, Partner, Male)

> … the reason that we … had a lot of concern going in this year about their inventory was we went out there the year before and counted empty boxes … . That is an issue that we had to deal with the whole time because we had such little confidence in their inventory controls. (Small Firm #2, Senior #2, Female)

As is evident from the preceding quotes, positive experiences tend to inspire the auditors' trust whereas negative experiences (e.g., when the client has failed to divulge information to the auditor or, worse yet, has actively sought to deceive the auditor) tend to curtail the auditors' trust. Further, auditors' risk assessments involve balancing trust in their clients against carrying out their professional responsibilities with due care, as highlighted below:

> … the biggest thing during the risk assessment phase is you need to balance how deep you want to look into a client with maintaining a good reputation and a good relationship with them as well as covering yourself to make sure that you're not exposing the firm to any additional risk that you know that would not be compensated for. (B4 Firm #2, Senior #1, Male)

> I'm looking at it from the standpoint of how much am I willing to trust. Or what has my experience shown me as to how much I'm going to trust the people giving me the numbers. What has their history been in terms of representations they've made to me in the past? What have my audits disclosed in the past where I've come across or not come across things that I would deem to be an issue and are they things that I've found as a result of digging into something or was it presented to me at the outset of the audit? (Small Firm #2, Manager #2, Male).

As the above quotes highlight, auditors' professional values concerning "performing the audit" can be at odds with the auditors' concern for profitability. When placing trust in the client, professional and commercial considerations create tension for auditors. On the one hand, the auditors want to uphold their responsibility to perform the audit with due care. On the other hand, they seek profitability and are therefore inclined to trust the client in order to achieve profitability. The quotes below epitomize auditors' tension in the risk assessment phase of the audit:

> I did the risk assessment for the coming year … if there was an ethical dilemma, to me personally, all signs point to … there's no way this client should be accepted. But … I don't know what decisions are being made, I can only speculate. My speculation is, you know, this client pays their bill, they have huge audit fees, we have huge overruns which they pay … how many clients do that … we budget 2,700 hours and come up 3,500 and they pay the difference … you know, at a good rate so, its hard for a partner who has that client and is booking business to wave good-bye to $400,000 of fees … in general we definitely assess all of those risks prior to the engagement or prior to acceptance of the client or to the continuance of the client from year to year … . Even in the case where this client, to me, is considered very high risk. That doesn't mean that we just go ahead and do a shoddy audit. I mean, we address the risks; we try to get comfortable with those risks and work around it somehow to get comfortable. (B4 Firm #2, Manager #2, Male)

> … from a business risk standpoint … there was clearly control and inherent risk associated with that client … it was a really tough situation. I mean one week we were talking about resigning, the next week we said, well, let's see how we can work through this. And … this was kind of a tell-tale year, if it didn't go well … we would have definitely pulled out … . So part of the argument was … if we could get comfortable over here that we're willing to take them, then we also have to get the fee to go with it. But … the fee didn't come first. It was the business decision … do we want to be there. (B4 Firm #2, Manager #1, Female)

Auditors' Ethical Conflict in the Program Planning Phase

Program planning includes determining the nature, extent, timing and staffing of the audit tests. As noted previously, in this phase of the audit, auditors are more likely to encounter ethical conflict arising from "performing the audit" than they are from the "auditor–client relationship." Thus, while both sources of conflict bear upon auditors' ethical characterizations of the program planning phase of the audit, "performing the audit" plays a greater role.

In prioritizing their program planning work to "perform the audit," auditors recognize the need to adhere to their professional standards, expanding the nature and/or extent of testing in those areas that are more risky or prone to error.

> That is an issue that we had to deal with the whole time because we had such little confidence in their inventory controls. A lot more time was spent and so that was something that when we were planning the audit we had to decide how much we were going to test, what we were going to test, and what we were going to do to assure ourselves that that sort of problem wasn't going to happen again. (Small Firm #2, Senior #2, Female)

> For example, if they said accrued liabilities must be tested [if they are] greater than say between 10 and 25% [of the balance], I tried to go down to 10% [in my planned testing] just to be more conservative. (a) Because this was actually a brand new client for us so obviously you want to get comfortable your first year; and (b) to be honest I didn't think that going that low would require that much work. (B4 Firm #1, Senior #2, Male)

Correspondingly, in their program planning, auditors recognize that they can reduce the nature and/or extent of testing in those areas that are less risky or prone to error and still adhere to their professional standards:

> I always have to step back and look at the big picture and say where is our risk here? You know our risk may not be in fixed assets, that is not a revenue [account], let's really beat that one [the revenue account] to death but fixed assets, okay we can flex that this year. It is a lot of judgment … . (B4 Firm #1, Manager, Female)

> … we will look at last year's test and if there are a lot of discrepancies … then we might cut it down maybe 10 more from 60 to 50. (Small Firm #1, Staff #2, Male)

In planning their work to "perform the audit," auditors are also concerned about utilizing staff that have an appropriate level of understanding to perform audit tasks.

> Maybe you know that you have risks in your area so you want a more experienced staff and those are the types of things that you look at [in making staffing decisions]. (B4 Firm #2, Staff #1, Male)

> I don't want to give the staff two [second year staff] the work because I know they can handle more, but I don't know that I have a staff one [first year staff] to actually handle it. (B4 Firm #1, Senior #1, Female)

Nevertheless, in their program planning, auditors recognize the tension created by professional and commercial considerations. On the one hand, they have a responsibility to plan the audit by prioritizing necessary work.

On the other hand, they need to maintain profitability. The following shows the ethical conflict that arises with regard to program planning and the ''audit task'':

> … it's a fine line, because we need to make money at it and at the same time we need to deal with the expectation that the public has of us to make sure that we design our tests appropriately … . I have some very technically complex clients that do some very innovative deals and as a result of that we have a lot of executive involvement. The profitability suffers a little bit, but the firm understands that … that's the type of situation in audit management risk that we need to deal with … . And we talk about it all the time … should we put this person on it, should we put that person on it and at the end of the day … it's better to have the more senior person. And the person with the requisite experience does it and the profitability is going to suffer but that's just part of the business. (B4 Firm #1, Partner, Male)

> I think in planning it [the audit], obviously one of our concerns is who's going to do it … when we do internal control work, usually it's the staff, the lowest level of staff doing it … . So you're planning it and you're saying … ''you know, I'm going to have this person do it, but if there's a problem at this client, are they really going to be the ones who find it?'' Chances are they aren't going to know … they just started and they need that guidance, they need training [so] you're going to need [experienced] staff to or the senior to … really go through their [the new staff person's] work and review it timely and try to identify the issues that I'm not sure that they would be able to identify. The problem then becomes, when we do the budget … because we all have the budget constraints, does anyone else have enough time and do I have enough time to devote to them to say … ''you know let's go find this.'' … Here's what our total hours are going to be and based on our profitability do you think that it [adding staff to the plan] could work? (B4 Firm #1, Senior #1, Female)

Albeit with lesser overall frequency, the ''auditor–client relationship'' also affects auditors' program planning. As the quotes below highlight, past experiences with the client and the client's sensitivity to the audit fee affect the degree to which auditors prioritize their audit procedures.

> [We address it] every time we go through and do the planning for the individual client. One of the things we look at is … the audit program and kind of ripping apart the audit program and saying okay can we reduce anything cause I mean we live by budgets and you know you kind of want to keep a realistic budget for each client … I mean if we have a client that historically we've had good relations and never had any problems, it seems ridiculous that we are doing all this overkill in testing an area where there is no risk really. (Small Firm #2, Senior #2, Female)

> Expand the budgets; but, if you expand the budgets, you probably have to expand the fees and that is just real touchy. (B4 Firm #2, Staff #1, Male)

Further, auditors are keenly aware of the financial ramifications associated with the level of trust they place in their clients. Distrust of the client can result in expanded audit work and, thus, reduced audit profits. Accordingly, as borne out by the following quote, commercialism considerations create conflict for auditors in balancing their responsibility to prioritize planning necessary audit work against trust in their clients:

> It's kind of a "Catch 22" because on the one hand we want to be able to provide value to our clients and in order to do that we really want to know what keeps them up at night so we can focus our attention appropriately. Uh, but on the other hand you sit back and say … isn't the whole purpose of an audit is not to necessarily just look where they want us to look, so it's a real balancing act … . And at the end of the day you just say … well it's got to be an audit … you know, and the relationships you have with your clients, they understand that. (Small Firm #1, Partner, Male)

As the above quote suggests, auditors' professional values would dictate that, in their program planning, they focus on those areas that are risky or prone to error. At the same time, auditors recognize the importance of keeping the client happy and the corresponding financial benefit from the client. As such, when performing program planning, auditors' professional values can be at odds with commercial considerations. The quote below epitomizes auditors' tension in the program planning phase of the audit:

> All right there's these three jobs that need the things by such and such a date. How can we allocate the staff and the quality of the staff equally to these jobs? I will say there is a certain amount of risk assessment that's done. Like how important is this client to us and will they be offended if we are two weeks late. Or are we only getting 30% of our rates on this job. What's our downside – who do you want to keep happy? (Small Firm #2, Manager, Male)

Auditors' Ethical Conflict in the Execution Phase

Execution of the audit involves actually conducting the audit tests and evaluating the resultant audit evidence. In conducting their audits, auditors are concerned about both the quantity of audit tests and the quality of the personnel performing the tests. As highlighted earlier, in the execution phase of the audit, auditors are somewhat less likely to encounter ethical conflict arising from "performing the audit" than they are from the "auditor–client relationship." Thus, while both sources of conflict bear upon auditors' ethical characterizations of the program planning phase of the audit, the "auditor–client relationship" plays a somewhat greater role.

Not surprisingly, as the following quotes suggest, in "performing the audit," auditors are concerned about the sufficiency of their testing in light of circumstances such as complexity or risk (e.g., weak internal controls):

> I hate to say this but I've used these words in the past … . 'He's a partner, he's got to sign it, if he wants me to do [sample] 30 and I think we can do 20, I'll do 30.' … At the

end of the day, I figure he's the person who's putting his liability on the line and if that makes him comfortable … . I think I get more concerned when it's on the opposite side … if someone said you only need to do five [and] that doesn't make me feel really comfortable; you know it's not that much more work to do at least another 5, if not another 10 … . [And, for one client, we] did site visits. Do you know how difficult it is to go out to the environmental clean up site and try [to stay on] budget? We did it. We met with these program mangers … we spent the time. We had all their specialists come in and walk us through their models so we would really understand … their processes and going through budget estimates because it was all contract accounting. So I think we made a lot of investments to ensure we fully understood the picture … . (B4 Firm #1, Manager, Female)

… when we get out there [to the audit], if the controls aren't there and we can't see what we need to see, then we're going to do X [more substantive testing]. (B4 Firm #1, Senior #1, Female)

Likewise, auditors expand their testing when, during the course of performing audit tests, anomalies arise.

I know there was an issue that when … all the confirm responses … said that credits have been issued subsequent to year end. Then the team itself kind of started getting a little nervous … . So we had to go back and revamp our testing a little bit because we now wanted to make sure that we relied a lot more on our subsequent credit invoices, credit memos that were issued after year end. So in that particular instance, the discomfort that we had ended up causing us to do a lot more testing to try and finally make us comfortable enough to think that they weren't boosting up their sales and their receivables and then issuing credits subsequent to year end. (Small Firm #2, Senior #2, Female)

We really didn't show them [the client] the memo [we received during audit testing about their bill and hold scheme]. So we tried to get an understanding of it and kept going through it and going through it. We expanded our cut off testing a lot to make sure there was no other situation, no other shipments like that. We wanted to make sure that at the end of every month things were okay and then pretty much it went up through the manager and the partner and eventually we got comfortable with the fact that it was a proper transaction and they were okay. (B4 Firm #2, Senior #1, Male)

Auditors also want to ensure that audit staff have an appropriate level of understanding to perform the audit tasks. As the following quotes suggest, the auditors recognize that certain staff are more qualified for some tasks than others and that additional supervision is often necessary to ensure the sufficiency of testing performed by lower level staff:

We are doing … a December 31st year end [audit]. And they [the client] want to go to press on January 15th with their yearly numbers. That gives us fifteen days to do the audit … . We have to do whatever it takes to make the 15th deadline but I always think, "Are we really doing enough work or are we taking short cuts?" … On some of the bigger issues, the partner … likes to be involved in those kinds of decisions … . if it is a real high risk area he wants to know who is doing it and he wants to see me there all day everyday to make sure that I am just watching everybody … . (B4 Firm #1, Manager, Female)

I answered the [staff person's] question and it was a relatively simple question [and] she said, "OK." So then a few hours later, she asked me another question and it was the same question, it was just for a different check. So then I finally said to her, "are you not comfortable with what it was that I asked you?" I mean because she basically asked me every single item that was on her list and she re-asked me whether or not she handled it correctly. So I got a little nervous … and I pretty much went and redid the whole test with her … . (Small Firm #2, Senior #2, Female)

Nevertheless, in their execution of the audit, auditors tend to concentrate on commercial considerations (e.g., maintaining profitability) despite the potential conflict with their professional responsibilities – both in the sufficiency of their work and in the quality of the staff performing the work. As highlighted by the following quotes, in "performing the audit," auditors struggle with balancing doing sufficient audit work with reducing audit work in order to maintain profitability:

… you always have to walk that line … with the fees [but] you know you have to test enough to cover yourself. And at the same time you don't want to go crazy and … perform more if it is not necessary or [if] it really isn't [that risky]. In other words, [if] there really is no risk in a certain area … you don't really want to go crazy in it … . But you still need to get the work done because if you do skirt around the side and then something comes back later … it bites you and it could lead to a lot of problems. You have to know where you can cut corners and where you can't. [Sometimes] I will cut a little corner here and there, but I always try and make sure that … I'm not exposing the boss or myself … to any additional risks by that. (B4 Firm #2, Senior #1, Male)

… when we do the audit, we're going to pretty much beat things up that we deem to be risk areas … sometimes probably to the degree of overkill. [But] so I'm probably coming at it from the standpoint of: Okay what's it going to hurt us as a firm? Where is the risk lying in terms of somebody coming after us? Where are we going to blow this audit if we do and what would be the ramifications to us? Where is there the most leeway for the client and his recording of transactions? Where are the soft numbers, you know, the obsolescence of inventory, the collectibility of receivables, those sorts of things? … and again I think ethically because ultimately this client is paying our bills and there is always that … . (Small Firm #2, Manager #2, Male)

Likewise, as highlighted in the quotes below, although more experienced staff are better qualified to perform certain audit tasks, auditors recognize that, at times, the use of less experienced staff may be a cost saving measure:

I mean you're under a lot of pressure to come in under the budget … Someone decides … that you can do the audit in 1000 hours. And when you get out there and you find that you've already gone through 1000 hours in the first couple weeks, and you still

> haven't even gotten close to the report … how do you get there … how do you get done? You can't really cut corners, you have to do all the steps, you have to do everything, and there's pressure there … you answer to the partner and if they want to know why it took Johnny twelve hours to audit payables when it took Sarah one hour last year, then you know, and … that's kind of how you get reviewed upon that type of stuff. Your performance. (B4 Firm #2, Manager #2, Male)

> We find it difficult sometimes to staff jobs appropriately. You might have a younger person doing things that they don't necessarily have all the requisite experience to do and the senior managers and partners need to spend more time with them. But, sometimes that's done from an efficiency perspective or a cost perspective because that might be the only person you have available. On the other hand, you might say you want to give this person an opportunity to really step up. You then get a benefit financially because they're at a lower billing rate. So, you need to balance that … with making sure you've got the appropriate level of supervision … . (B4 Firm #1, Partner, Male).

Indeed, time budgets create tension for auditors – particularly those at the staff level. On the one hand, they want to do a thorough job in carrying out audit tests. On the other hand, however, time budget pressures discourage them from doing so.

> … one of the issues that might arise is whether you [are] cutting on your work to make the budget. And, if this is ethical or not or if you should spend more time but do a more quality and effective job than pleasing your supervisor that it took you exactly whatever the budget is saying … . Once you have a really good understanding of what you're asking [the client] for, you can perform the task more efficiently. But sometimes it's not really that easy because sometimes you are new to the engagement and you don't really know the client that well as a first year staff … . And of course we are talking also about the budgets and stuff so everything put together sometimes can be very stressful. (Small Firm #2, Staff #2, Female)

> It is kind of hard, being at my level, to watch a budget and try to learn at the same time, and knowing that it is going to take me a lot longer than maybe it took the person last year because I'm still new in the game. I'm thinking about what people above me are going to think if I am charging all these hours to a code … . It kind of discourages you from doing a complete not a complete job but the best job you can possibly do. (B4 Firm #2, Staff #2, Female)

In conducting their audit tests and evaluating audit evidence, the ''auditor–client relationship'' affects auditors' evaluation of the audit evidence they obtain as well as the degree to which they obtain cooperation from the client. There appears to be a relationship between the degree to which auditors trust their clients and the weight auditors place on evidence obtained when carrying out the audit tests. For example, when clients attempt to enter the auditors' professional territory by dictating audit procedures, auditors' skepticism can increase. In turn, as the following quotes suggest, the level of trust the auditors place in their clients decreases, causing the auditors to discount audit evidence and/or reconsider their audit procedures.

> … the client also was a CPA … and in situations where he would try to guide me on how I was going to conduct my test and you know, I think we were always kind of butting heads on "well you know I have to do the procedure, you tell me I don't need to do the procedure" type of thing based on his experience … as a firm or as a auditor I had an issue of whether or not is this client a good client or is this guy trying to tell me how to conduct my audit to evade an audit in a specific area. (Small Firm #1, Senior #2, Male)

> Some clients … like to get more involved in actually seeing how you're auditing, in giving you suggestions … obviously it's up to us to determine that these suggestions make sense, but that's something I have come across – at a couple clients, the client will give you suggestions as far as "no I think you should do it this way," but obviously that's a red flag. (B4 Firm #1, Senior #2, Male)

Indeed, when a client has violated the auditors' trust, the auditors increase their skepticism and expand audit testing, as noted by the quote below.

> … now that they [management] didn't tell me [about one issue], what else did they not tell me. So I had to expand areas in that case because once you find someone you don't trust anymore, it's completely gone! You look at everything they say with a different spin on it. (Small Firm #2, Manager #1, Male)

At the same time, when clients trust the auditor, they are more cooperative during the execution phase of the audit. As highlighted in the quotes below, auditors recognize both the importance of maintaining a good relationship with their clients and that a lack of cooperation from the client can hamper audit testing:

> [In] the execution phase, [when the client has] represented to me that this is what this is … how far do you push it and how much evidence is enough evidence, because you don't necessarily want … your client to feel that you don't trust them … . And again it's this balancing act between making sure you have enough competent evidential matter … without making your client feel that you think they're dishonest and that you don't trust them. (B4 Firm #1, Partner, Male)

> If the client doesn't like you, they are not going to tell you stuff. If they don't tell you stuff, it makes the audit a lot harder … . (B4 Firm #2, Staff #1, Male)

In terms of the "auditor–client relationship," auditors emphasize clients' needs, and, in so doing, recognize the tension created between carrying out the audit with due care and maintaining a good relationship with the client.

> … although the audit is a compliance function, there needs to be value created out of that function as well. And we can provide a lot of value by understanding our client's businesses and what's important to that business. But that doesn't mean that we are

going to overlook cash because they don't think that it's important. There are certain things obviously that we have to do and will continue to do. (B4 Firm #1, Partner, Male)

I don't think that I would cut back on certain testing [just to reduce the audit fee]; I think, as discussed with the partner, we would do less in certain areas next year that are lower risk, just to keep the client happier but then focus more on other [riskier] areas (Small Firm #1, Senior #2, Male).

As the above quotes highlight, when handling client differences, professional and commercial considerations create tension for auditors. On the one hand, the auditors want to uphold their responsibility to perform the audit with due care. On the other hand, because commercialism affects auditors' audit testing, it is clear that the *business* of auditing has an impact on the professionalism of auditors' work.

Trying to balance the business that we're in versus making sure that we do enough from an audit perspective. It is sometimes difficult, because we try to find ways to make the audit more efficient so we can make more money, obviously because it's a business, and at the same time you need to make sure that you do enough and … appropriately identify items as errors and therefore run your statistical samples appropriately, or you find ways to justify that it's not an error or an isolated incident. (B4 Firm #1, Partner, Male)

Auditors' Ethical Conflict in the Reporting Phase

Reporting is the final phase of the audit. It involves the auditors' communication of the audit findings with those internal and external to the client. As discussed previously, in the reporting phase of the audit, auditors are much less likely to encounter ethical conflict arising from "performing the audit" than they are from the "auditor–client relationship." Thus, while both sources of conflict bear upon auditors' ethical characterizations of the reporting phase of the audit, the "auditor–client relationship" plays a much greater role.

In reporting the results of their audits, auditors often face tight reporting deadlines. In turn, tight reporting deadlines often result in issuance of the audit report when the audit work is not substantially complete. Since it is unusual for audit reports to be altered once issued, in "performing the audit," audit work completed after the issue date of the report is potentially not of the same quality as the work completed prior to the issue date as highlighted below:

… the budget and time is definitely a huge issue for people sometimes. I feel you have to be substantially complete with the audit in order to have your opinion on it [the financial statements]. Sometimes I feel like we are not substantially complete with the audit when we actually do it. There could be AR [accounts receivable] outstanding at that point. We

> might not have gotten 100% of the confirms back [but] they had to file, they are public so it was rushed. It's not like it was a private company. So it was the day it needed to be done that was it. And things hadn't been reviewed … . You know just my work [at a staff level]; we filed just according to my work, which is surprising. (B4 Firm #1, Staff #2, Female)

> It happens all the time. You could be doing fieldwork after you issue the report. Hopefully it's nothing important but it's like a step you missed. You do assess it and say, "Is this going to change the report? If not, let's just get in there and do more work." (B4 Firm #2, Manager #2, Male)

When reporting judgmental decisions, auditors use their professional judgment to decide what "number" should be included in the financial reports. When making judgmental reporting decisions, ethical conflict arises over the propriety of the selected "number." Two quotes characterize this issue:

> You are often faced with questions of whether or not an adjustment is material, or do you want to make them [clients] restate their prior year's financial statements because you found a footing error in a schedule. [We] talk about these things all the time and those are the judgment calls made all the time. (B4 Firm #1, Partner, Male)

> … we find sometimes it [an account] is definitely off $8,000. There is no doubt about it, so we post the $8,000. Sometimes … it is … a projection … . So sometimes we need to kind of go back and sort of, not second guess ourselves, but sort of go back and see if we can reduce some of the amounts a little bit because there are judgment calls. And who is to say that $10,000 is any more correct than $8,000 or $12,000. (Small Firm #2, Senior #2, Female)

Often, in reporting judgmental decisions, auditors compromise with their clients as borne out from the following:

> In terms of a concern with this number [reserve estimate] and how we're going to address it … there's certainly differences of opinion amongst the accounting professionals here [but, in the end,] we actually found a middle ground. A middle ground was sort of reached. It was probably closer to the client's middle than my middle, but there was an adjustment made. (Small Firm #2, Manager #2, Male)

> Stuff that was blatantly wrong they [clients] would have to fix, but when we're talking about reserves and stuff you know we have a number that we want and you know maybe meet them half way kind of thing. (B4 Firm #2, Senior #1, Male)

During the reporting phase of the audit, considerations related to the "auditor–client relationship" are more prevalent than those concerning "performing the audit." In reporting the results of their audits with due care, auditors consider clients' needs as well as the impact of their reporting on the "auditor–client relationship." As captured in the following, auditors are concerned not only with keeping clients happy and providing them with ''value,'' but also with keeping clients from getting into ''trouble'' (particularly with the audit committee):

> [In writing our management letter comments], most of the clients understand that we're not saying it to be vicious, we're trying to add value, which is how we like to term it, add value to the clients. (B4 Firm #2, Staff #1, Male)

> Well, I think the ethical issue that we face there [is] what types of things do you report to the audit committee and how do you report them, in a way that doesn't get your client in trouble. (B4 Firm #1, Partner, Male)

Indeed, in reporting the results of their audits, auditors are aware that the ''auditor–client relationship'' plays a role in the clients' decisions about whether to retain the audit firm. Accordingly, the auditors recognize that reporting disagreements can lead to severe economic consequences (i.e., loss of the client):

> Again a $50,000 client to us is a couple million dollar client, maybe a $10,000,000 client to a [large international firm]. We would certainly struggle with telling a $50,000 client to walk [over a reporting disagreement]. (Small Firm #2, Manager #2, Male)

> If they [clients] didn't like our [audit] opinions I don't think they would keep us there. They would find another firm. (B4 Firm #1, Staff #2, Female)

Nonetheless, despite any affinity the auditors may have for their clients, most recognize their responsibility to stand firm in upholding the interest of the public.

> I think what we've got to realize is that despite the fact that the client pays for our services, we are actually performing services for the third party. We should keep that in mind in all the work that we're doing that some people are actually relying on our opinions and we might lose a client … . So I think the most important thing is just to keep in mind that we are servicing third party. I know it sounds difficult because we are in business to pay our bills and to make money … . The bottom line is you've just got to look out for people who are going to rely on the statement. That is what we are there for. (Small Firm #2, Staff #1, Male)

> We had to assess going concern and we had said we need to issue a going concern opinion and it was a public client and we knew it wasn't going to be good … . The partner and I went into the CFO and we just sat with her and talked and said this is what it has to be and we can't get around it and she really fought us hard on it. And at that time I want to be an advocate for my client … . But, at the same time, I need to realize I have a certain code of conduct; as a CPA, I have got to do a certain job. (B4 Firm #1, Manager, Female)

As the above quotes suggest, defending differences of opinion and deciding how hard to push the client seem to involve a series of professional and commercial tensions that are the source of auditors' ethical conflict. In spite of their recognition of their duty to third parties, and perhaps most disconcerting, it is not clear that auditors are always able put the public interest at the forefront of their actions as evidenced by the following quotes:

> I understand that technically this is what, if you read the rules black and white, that's what the rules said. But there's got to be some common sense applications to some of these accounting principles from a professional perspective … my personal view was it [correction of an error] probably was immaterial, but the audit committee made the right decision [in forcing client management to correct the error] because they gave the reader the most accurate financial information. It's tough sometimes when you get put in those positions because you're not sure who you're going to agree with. Are you going to agree with the audit committee or with management? (B4 Firm #1, Partner, Male)

> … what are you going to do about [a client] rigging the books … . They [audit firm partners] did let it go. They gave an unqualified opinion. I wasn't in on the meeting with the client – I might have said something that would have gotten me into trouble … ethics are a great thing but you can really throw yourself on your sword … . If I had gone out on a big ethical crusade on this one particular thing … and hurt my career, what would I have gained out of it? This is a case in which having the auditors paid by the company doesn't work. You know when your purse strings are tied to the person you audit in a situation like that doesn't work. Because if we were hired by the bank [a third party], we never would have given an unqualified opinion on that audit. (Small Firm #1, Manager, Male)

Primary Analysis Summary

In this study, we find evidence of the professionalism/commercialism tension highlighted in prior papers. That is, we document the tradeoff auditors face in simultaneously maintaining a high degree of professionalism (e.g., performing the audit with a public interest focus) and the commercial aspect of the audit (e.g., performing the audit with a self-interest focus), which has been suggested in prior literature.

Additionally, we find that the professionalism/commercialism tension arises not only from "performing the audit" but also from the "auditor–client relationship." While auditors want to meet their professional obligations to ensure they can justify their opinion on the financial statements, at the same time, they face tension from "performing the audit" because they must maintain profitability while doing so. Thus, auditors tend to focus on performing minimal audit tests and adding only "value added" (i.e., billable) steps to the audit (cf, Lampe & Garcia, 2013). In addition, the auditors use lower-level (i.e., inexperienced) staff when possible to maximize their realization rate. The following quotes epitomize these relationships:

> You know you are always looking for an area that you can ''help'' the client and add value. (B4 Firm #2, Manager #2, Male)

> Theoretically, we give everybody equal service, but you don't give everyone equal service. You fulfill the standards but you don't give them all the same people … . Who is a client that we think can be a referral source for business? Who do we want to impress because they have a good standing in the community and the more people they are going to talk about in the business community about us in a favorable light the better it will be for us? (Small Firm #2, Manager, Male)

Meanwhile, auditors perceive the audit as a ''quest'' (by clients) for an unqualified opinion. Accordingly, auditors face tension from the ''auditor–client relationship'' because, in managing relationships with their clients, they must simultaneously maintain a high degree of professionalism (e.g., keeping their independence from the client in order to exercise an appropriate level of skepticism) and foster the commercial aspect of the audit (e.g., developing and maintaining a rapport with the client in order to retain the client). The following quotes epitomize these relationships:

> … as much as everyone has their standards and all that, I still think the main goal for all of us is to give an unqualified opinion. I mean, it's what we strive for because without that you don't keep the client and you try to find ways to give an unqualified opinion that are supported by any of the audit programs, the AICPA, all the standards that we're held up to. (Small Firm #1, Senior #1, Male)

> I can't tell the client to … well, I can, but it's certainly rare that I'm going to tell the client.... I'm resigning from this job … . I would say within the last busy season there have been a couple of issues that have arisen … and I thought the [deferred tax asset] numbers were a little aggressive, a little inflated. And I think one of the partners … probably didn't think they were as aggressive as I did. So again now you're dealing with that internal struggle of well, yeah you're my boss and yet I think … there are certain partners that are more willing to give the client the benefit of the doubt. I think that's probably true, at least … primarily to, satisfy a client. (Small Firm #2, Manager #2, Male)

Supplemental Observations

In addition to our results above, the following general observations emerged. First, we did not perceive any systematic differences in responses for auditors in large, multinational firms as compared to those of auditors in small, local firms. Likewise, we did not note any pattern of gender-specific differences in auditors' responses. We did, however, note differences according to hierarchical level. For example, staff reported encountering very few ethical incidents outside of the execution phase of the audit. This finding is not entirely unexpected given the general lack of experience that staff have with the other phases of the audit (i.e., risk assessment, program planning and reporting).

Seniors, by contrast, reported encountering ethical incidents in each phase of the audit. Similar to the staff, however, the greatest concentration of issues the seniors encountered related to the audit phases on which they focus – namely, program planning and, to a somewhat lesser extent, execution. Managers and partners likewise reported encountering ethical incidents in all phases of the audit, with the majority of the issues they reported coinciding with the phases of the audit on which they focus (i.e., risk assessment and reporting). In addition, consistent with their more robust experiences, we noted that the partners and managers tended to provide longer/richer interviews than did the staff and seniors.

DISCUSSION AND CONCLUSION

Regulatory reforms are the typical response when ethical crises arise. For example, the SEC Acts of 1933 and 1934 followed the Stock Market Crash of 1929 and its ensuing Great Depression. More recently, the Sarbanes–Oxley Act (SOX) followed the scandals of the early 2000s (e.g., Enron, Worldcom, etc.). Such reforms, however, can be costly (Millar & Bowen, 2011; Roberts, 2004). Further, because regulatory provisions such SOX's creation of the PCAOB reduce self-regulation in accounting, they can lead to a deterioration of professionalism in the accounting profession (cf, Rice & Duncan, 2006; Wyatt, 2004).

To assist the audit profession in considering other types of reforms, this paper provides insights into auditors' ethical characterizations across the four phases of the audit. Our analysis supports prior work by documenting that auditors' ethical conflict can indeed be characterized as a tradeoff between professionalism (regard for audit quality – i.e., performing the audit with the utmost due care) and commercialism (regard for audit profitability – i.e., maintaining profitably) (see, e.g., Covaleski, Dirsmith, Heian, & Samuel, 1998; Gendron, 2001, 2002; McNair, 1990; Wyatt, 2004). Further, we find that the professionalism/commercialism tension that auditors face arises not only from ''performing the audit'' but also from the ''auditor–client relationship.'' Additionally, we identify phase-specific differences in auditors' ethical characterizations, which should be of interest to the audit profession for two reasons. First, highlighting the ethical incidents auditors may encounter in the various phases of the audit can heighten their sensitivity to them, which, in turn, may lead to improved ethical behavior (cf, Jones et al., 2003; Rest, 1984; Rest & Narváez, 1994). Second, knowledge of the ethical dilemmas that auditors may encounter in the various phases of the audit can be useful in education and training programs.

For instance, we find that audit staff encounter most of their ethical incidents during the execution phase of the audit, where ethical conflict arises more from the ''auditor–client relationship'' than from ''performing the audit.'' Accordingly, accounting faculty might focus in their audit classes on strategies to help students (i.e., aspiring audit staff) withstand the corresponding pressures they will face during the execution phase of the audit when they begin their professional careers. For example, enhancing the students' professional skepticism is one way to enable students to overcome the pressures arising from the ''auditor–client relationship'' during execution of the audit (cf, Apostolou & Crumbley, 2008). Accordingly, consistent with Plumlee, Rixom, and Rosman (2011), faculty can assist students in learning to exercise professional skepticism by training students in both divergent and convergent thinking.[8] However, future research is needed to assess the efficacy of such a pedagogical approach.

Likewise, we find that audit seniors encounter most of their ethical incidents during the planning phase of the audit, where the predominant source of ethical conflict is from ''performing the audit.'' Unfortunately, however, as Hammersley (2011, p. 119) reports, ''audit seniors respond to increased awareness of fraud risk by increasing planned sample sizes, but seniors do not plan effective modifications to a standard audit program … .'' Nonetheless, Hammersley (2011) notes that auditors can be aided in making effective audit program changes. Accordingly, the profession might consider developing decision aids that ''facilitate connection of fraud risks to required procedure changes'' (Hammersley, 2011, p. 119; see also Hoffman & Zimbelman, 2009) to assist seniors in effectively planning the nature, extent and timing of audit tests when facing risk factors, such as fraud risk factors. In the future, researchers might test whether such aids are, in fact, effective.

Finally, we find that managers and partners are more likely than staff and seniors to encounter ethical incidents during the reporting phase of the audit, where the ''auditor–client relationship'' is the predominant source of ethical conflict. In a similar vein, Brown and Popova (2012) report that auditors are more likely to waive audit adjustments when they are under pressure only from their clients than they are when they under pressure from two sources: (1) their clients, who are pressing them to waive proposed audit adjustments; and (2) an external source (e.g., the audit committee), who is exerting competing pressure on them to book the proposed audit adjustments. Thus, to assist managers and partners in effectively withstanding client pressures during the reporting phase, effective audit committees can, as a matter of course, exert competing pressure on auditors, to encourage the auditors to insist that the company's managers book all proposed audit adjustments. To assess the efficacy of this approach, future research is needed.

As with any study, there are limitations. For example, although the data suggest otherwise, it is possible the auditors were not entirely forthright in their responses to our queries. As a result, we may not have fully captured the ethical incidents the auditors have faced during the audit. Further, our interviews included only a small subset of auditors. Thus, our findings cannot purport to be generalizable to the population of auditors. Future research covering a broader spectrum of auditors is needed.

Despite the possibility that the auditors in our study were not candid in their responses to our queries, the auditors' responses appeared unconstrained – despite the sensitive nature of our interview topic (i.e., ethics). In short, the auditors freely shared information about the conflicts they experienced during all phases of the audit. Thus, methodological concerns typical to ethics research such as the impact of social desirability bias (e.g., Cohen, Pant, & Sharp, 1995; Jones et al., 2003), appear less a threat in this study than prior research, might suggest. Accordingly, the implication for researchers is that in-depth interviews may be particularly salient when studying auditors' ethical decision-making (cf, Liedtka, 1992). Moreover, the richness and candor of the data highlights the potential usefulness of qualitative methodologies – such as conducting in-depth interviews – in performing research in auditing (e.g., Humphrey, 2008; Power, 2003) and accounting ethics (e.g., Gaa, 1994; Jones et al., 2003).

NOTES

1. The appendix contains a copy of the semi-structured interview protocol.

2. As more fully discussed hereafter, we described what we meant by the terms so that all auditors could have a similar understanding of the terms we used (cf, Frankfort-Nachmias & Nachmias, 1992).

3. The firms (particularly the smaller firms) initially expressed concern about their ability to achieve gender balance across each of the hierarchical levels (e.g., in the firms participating in our study, there are fewer women than men at the partner level,

which makes it difficult to achieve gender balance at that hierarchical level). As a result, we modified our initial request by asking to meet with a mix of males and females drawn from the hierarchical levels of the firm.

4. One large, multinational firm that was approached declined to participate in our study because of concerns about the sensitivity of the interview topic (i.e., "ethics"). Although the disinclination of the firm to participate in our study could signal concerns about response bias, as discussed more fully hereafter, the candor of the interviewees' remarks tends to alleviate this concern.

5. We resolved any disagreements in categories on an intersubjective basis – by checking that the categories corresponded to the data, negotiation, and reformulation (Butterfield, Trevino, & Ball, 1996).

6. As before, we utilized an intersubjective process to resolve any differences, by rechecking that the sources corresponded to the data, negotiating, and reformulating (Butterfield et al., 1996).

7. Four items (i.e., 1%) related to examples the auditors gave about particular ethical incidents they encountered during the risk assessment stage of the audit. We did not categorize the examples as either relating to "performing the audit" or the "auditor–client relationship" as the examples did not lend themselves to such categorization.

8. Divergent thinking and convergent thinking are both part of professional skepticism; "divergent thinking requires auditors to mentally generate explanations for evidence or circumstances they identify as unusual and convergent thinking requires them to assess the plausibility of the explanations they generate" (Plumlee et al., 2011, p. 2).

9. For the various phases of the audit, the words in italic were replaced as follows:

Program Planning: *Please think about the program-planning phase of the audit. During the program-planning phase of the audit, the nature, extent, timing and staffing of audit tests are determined – based upon the risk assessment performed earlier.*

Execution: *Please think about the execution stage of the audit. Execution refers to the act of conducting the audit tests set forth in the audit program and evaluating the resultant test evidence.*

Reporting: *The last step in the audit process is to report or communicate the findings of the audit to the shareholders, audit committee, etc.*

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APPENDIX: INTERVIEW PROTOCOL

Prior to the start of the interview each interviewee was informed of the intent of the study (to determine auditors' experiences and perceptions about ethical incidents that arise in audits). Each interviewee was also reminded that their participation was completely anonymous; and all identification will be removed from the tapes and the transcripts of the recordings. Each interviewee was also informed that no findings would be tied to specific individuals or firms and that only aggregate information (for all interviews combined) would be provided to the firm.

Each interviewee was also asked questions about their background that encompassed the following topics:

- Education
- Experience in the audit industry
- Number of years as an auditor
- The different positions held
- Types of clients serviced (by industry and type of audit)
- Experience outside the audit industry

Then each interviewee was asked the following questions for each phase of the audit[9]:

Please think about the audit process. One of the first steps in that process is to assess risks associated with performing the audit. For example, during this phase of the audit, auditors assess such factors as materiality, audit risk, inherent and control risks as well as business risk (that is, risks to the firm such as litigation or loss of reputation that may result from a particular client relationship).

1. Please tell me about the most important ethical incident that you have faced in your career that arose during the risk assessment (program planning/execution/reporting) phase of the audit.
2. Why do you consider it an ethical incident?
3. Why do you consider it the most important incident?
4. When did it occur? How long ago was that? At what level were you when it happened?
5. How was it resolved? Did your firm/supervisor/peer/colleagues support you?
6. How often would you say you face this incident?