

# Auditor Perceptions of Statements on Auditing Standards 53 and 54: A Study of Demographics and Perceptions of Efficacy

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## Abstract

*This study examines the relationship between auditor demographics and auditor perceptions of Statements of Auditing Standards 53 and 54, and the extent to which these statements may be contributing to a previously unrecognized "expectations gap" between the Auditing Standards Board and practicing CPAs. Responses from a randomly drawn sample of AICPA auditors were subjected to a canonical correlation analysis in order to identify and define any underlying perceptual constructs. These constructs were subsequently compared with the stated objectives of the Statements.*

## Introduction

The differences in perceptions among auditors regarding certain generally accepted auditing standards have been the subject of only limited inquiry (Mutchler, 1984) and, although certain aspects of demographics have been reviewed in connection with specific auditor practices or procedures (White, Wyer and Janson, 1988), the relationship of auditor demographics and auditor perceptions of auditing standards has not been studied.

Although it remains to be seen whether implementation of Statements 53 and 54 will serve to reduce the Expectation Gap, that apparent breach between public expectations and auditors' perceptions of their responsibilities (Liggio, 1974; Collins, 1989; USGAO, 1989; Price Waterhouse, 1985; Treadway Commission, 1987), the perceptions of those who must implement the Statements will almost certainly influence the outcome. In fact, research clearly indicates that individuals often behave in ways that insure that their expectations will be fulfilled (Jones, 1977). If "beliefs have consequences whether they are true or false" (Jones, 1977), accountants' perceptions of the efficacy of the Statements may have the quality of a self-fulfilling prophecy. Both achievement and motivation have been linked to perceptions, with the perception of a high probability of success seeming to enhance performance, and the perception of a low probability of success seeming to result in decreased motivation and effort toward goal attainment. Furthermore, an individual's subjective assessment of the probability of success may be significantly impacted by culture and experience (Feather, 1982).

The perceptions of the Statements by accounting professionals, therefore, are of great importance in light of the significant lending and investing decisions that are made by bankers, financial analysts, and members of the general public on the basis of audited financial statements. Although studies of the expectation gap have focused on the perceptions of financial statement users, the economic and social significance of the perceptions of those who must actually implement the Statements should not be underestimated, for accounting professionals have been viewed as an essential element in providing access to capital markets, "since the sale of securities cannot take place without their involvement" (Burton, 1975).

If the Expectation Gap Auditing Standards are an appropriate response to public concerns (as stated by the AICPA in its transmittal letter to members), their implementation would be expected to benefit the auditing profession by improving audit planning and performance (AICPA, No. 53, 1988; AICPA, No. 54, 1988; Guy and Sullivan, 1988). Any enhancement in the perceived reliability of information provided to financial statement users due to improved audit planning and performance would, in turn, be expected to relieve the crisis of Congressional and public confidence in the profession, reduce the likelihood of federal regulation, and reduce the number of lawsuits against auditors, all of which have been described as manifestations of the expectation gap (Amhowitz, 1987).

This study examines auditor perceptions of the Statements with respect to their stated and overall objectives, and demographically-related differences in those auditor perceptions.

## Research Methodology

A mail survey was used to elicit the responses of auditors randomly chosen from a national list. Subjects were asked to respond to: (1) certain demographic questions which constituted the predictor (independent) variables and, (2) certain perceptual assertions related to the objectives of the Statements which constituted the criterion (dependent) variables. Following the data gathering process, the responses were subjected to a canonical correlation analysis.

The subjects for this study were randomly chosen by the AICPA from its national list of members identifying themselves as auditors in order to study the perceptions of those CPAs in public practice who were most likely to be in a position to implement the provisions of the Statements. In addition, it was anticipated that subjects chosen from that pool would have received the AICPA mailing that included the statements. Subjects would thereby have had an opportunity to familiarize themselves with the thrust of the comments.

The survey instrument consisted of two sections. The first section elicited demographic information regarding the auditor's experience and practice. The demographic questions were discussed with practitioners who participated in a test of the survey instrument. At the suggestion of those practitioners, a question was added regarding participation in the peer review process. The data collection stage of this study was concluded shortly after the AICPA adopted its current requirement for member participation in "quality reviews," but prior to its implementation date (White, Wyer and Janson, 1988). A summary of the demographic information is presented in Table 1.

The second part of the survey instrument consisted of twenty-one assertions, ten relating to Statement 53 and eleven relating to Statement 54. A five-point Likert scale, with potential responses ranging from "1" meaning "Strongly Disagree" to "5" meaning "Strongly Agree" was utilized to indicate a subject's opinion or perception of each assertion.

The first ten assertions were designed to test opinions regarding the effect of implementation of Statement 53, with particular emphasis upon achievement of the specific and overall objectives of that statement. The number of assertions used was a function of the process of content development. The assertions were derived from the stated objectives contained in the first paragraph of Statement 53, as well as from the overall objectives expressed in the articles, briefings, and AICPA transmittal correspondence discussed above, and were refined in dialogue with practitioners who participated in a test of the survey instrument.

The remaining eleven assertions related to the

perceived effect of implementation of Statement 54, with emphasis on auditor perceptions of the assertions regarding the specific and overall objectives of that particular Statement. Once again, the number of assertions was not of significance in itself but an outcome of the development process outlined above. The assertions for each statement are presented in Tables 2 and 3.

## Analytical Methodology

Of interest was the extent to which an auditor's background, described in terms of a set of demographic variables, might influence perceptions of Statements 53 and 54 and the nature of underlying relationships that might result. Canonical correlation analysis is a statistical technique which can predict a set of multiple dependent variables, in this instance auditor perceptions, from a set of multiple independent variables. In reality, it is nothing more than an extension of regression analysis where a set of criterion variables, rather than a single criterion variable, is made a function of a set of predictor or independent variables. The essence of a canonical analysis is captured in four statistics. Canonical correlations measure the strength of the overall relationship between the set of independent variables and the set of dependent variables and it is interpreted just like  $R$  in regression analysis. Canonical roots measure the amount of shared variance between the independent and dependent sets. Eigenvalues are a measure of the total variance explained by each function and the number of functions computed is determined by the amount of total variance to be explained. Finally, the redundancy index is a measure of the amount of variance in the set of dependent variables explained by the set of predictor variables, taken one function at a time.

Tables 4 and 5 present the results of the canonical analysis.

As the results from the analysis of Statement 53 clearly suggest, the set of independent variables (i.e., years of experience, size of the firm, extent of audit work responsibility, proportion of publicly held clients, response to exposure drafts of the statements, availability of in-house training, incidence of audit related lawsuits, early implementation of the statements, and participation in peer review) explained an insignificant percentage of the variance in respondent perceptions. For example, the redundancy index for the first function (.1083) indicates that only 10.83 percent of the variance in auditor perceptions is explained by the set of demographic variables. And as one looks down the array of functions, the drop-off in statistical significance of the subsequent redundancy measures is pronounced. Clearly, auditor perceptions, as reflected in these responses to the Statement 53 assertions, were not influenced in any meaningful way by the set of demographic variables.

By contrast, the first function produced from the canonical analysis of Statement 54 was quite significant, as the accompanying level of significance (.0039) clearly suggests. As a consequence, the underlying relationships embodied in function one were subjected to closer scrutiny. This was accomplished by computing and interpreting the coefficients for both the demographic and perceptual variables making up the predictor and criterion sets. Table 6 presents the results of this process.

Only those variables with coefficients of .50000 and above were considered significant and the meaning of each coefficient was determined by referring to the mean responses on each of the original questions. What one hopes to see at this stage of a canonical analysis is a subset of independent factors that logically account for a significant amount of variance in a subset of the dependent variables.

In this case, those who responded to the exposure draft of Statement 54 and who are affiliated with firms that employ some form of peer review were more inclined to believe: (1) that Statement 54 will provide guidance with respect to the auditor's consideration of the possibility of illegal acts and, (2) that it is an appropriate response to public concern regarding audit responsibilities related to the detection of illegal acts of clients, whether it is an audit of a publicly held or non-publicly held company.

Correspondingly, respondents were disinclined to believe that Statement 54 will help provide more reliable information upon which to base lending and investment decisions, nor did they believe that Statement 54 will contribute in any significant way to enhanced government and public confidence in the auditing profession. Extrapolating from these results one might reason that the behavioral climate of the firm, a factor over which management exercises some control, is a potentially significant intervening variable affecting perceptions and implementation of audit related statements.

### Summary

The purpose of this study was to explore the nature of auditor perceptions of Statements 53 and 54 and to measure the extent to which these perceptions might be influenced by a set of independent, employment related variables. The findings may be summarized as follows:

(1) A significant gap would appear to exist between what Statements 53 and 54 were intended to accomplish and auditor perceptions of what the statements will accomplish.

(2) In general, employment related factors such as years of experience, size of the accounting firm, percent of audit related business, etc. had a far less significant impact on auditor perceptions of both statements than originally hypothesized.

(3) Two underlying factors over which management has some control, reviewing and response to exposure drafts and the use of a peer review system to enhance audit quality, appear to have some influence on how employees perceive audit pronouncements.

Although the scope of this study clearly limits the extent to which one might generalize from its findings, issues do come to mind as a consequence of this research that, in the opinion of the authors, warrant further investigation and that represent a basis for future research.

First, the results of this study suggest the presence of a previously unrecognized "expectations gap," one between those responsible for formulating auditing directives such as Statements 53 and 54 and those responsible for implementing such directives, the auditing community. A better understanding of the cause(s) of this kind of discontinuity and, correspondingly, that might be done to remedy it, could be achieved through an expanded study. Second, by utilizing a broader set of demographic factors, going well beyond what the authors have attempted in this study, one might gain a broader understanding of those factors over which management exercises some control that most strongly influence auditor perceptions of professional directives of all kinds. Finally, the relationship between the "behavioral climate" of the firm and auditor perceptions of statements issued by the Auditing Standards Board would seem to be an inviting avenue for further research. Indeed, if there is a significant link between the culture of the firm and auditor perceptions, on one hand, and motivation and effectiveness in implementing directives of all kinds on the other, then understanding the dynamics of the process would seemingly lead to enhanced audit quality.

### \*\*\* References \*\*\*

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TABLE 1  
Demographic Information

Number of Respondents: 86

Years of Audit Experience

|                                     |       |
|-------------------------------------|-------|
| Less than 1 yr                      | 0%    |
| 1 yr or more, but less than 3 yrs   | 2.3%  |
| 3 yrs or more, but less than 6 yrs  | 0%    |
| 6 yrs or more, but less than 10 yrs | 1.2%  |
| 10 yrs or more                      | 96.5% |

Individual or Firm Responded to SAS Exposure Drafts

|            |       |
|------------|-------|
| Yes        | 25.6% |
| No         | 67.4% |
| Don't Know | 7.0%  |

Size of Firm

|                                       |       |
|---------------------------------------|-------|
| Big 8 and National                    | 20.9% |
| Regional and local > 25 professionals | 19.8% |
| Local < 25 professionals              | 41.9% |
| Sole Practitioner                     | 17.4% |

Firm Has Formal In-House Training Program for Professional Staff

|     |       |
|-----|-------|
| Yes | 53.5% |
| No  | 46.5% |

Audit Engagements as % of Firm's Chargeable Hours

|         |       |
|---------|-------|
| 0-20%   | 35.2% |
| 21-40%  | 35.3% |
| 41-60%  | 16.5% |
| 61-80%  | 10.6% |
| 81-100% | 2.4%  |

Lawsuit Has Been Filed Against Respondent or Respondent's Firm by a User of Audited Financials During the Past 5 Years

|            |       |
|------------|-------|
| Yes        | 20.9% |
| No         | 76.8% |
| Don't know | 2.3%  |

Audit Engagements as % of Respondent's Own Chargeable Hours

|         |       |
|---------|-------|
| 0-20%   | 37.3% |
| 21-40%  | 27.9% |
| 41-60%  | 12.9% |
| 61-80%  | 11.3% |
| 81-100% | 10.6% |

Firm Elected to Implement SAS 53 and SAS 54 Prior to Their Effective Date

|     |       |
|-----|-------|
| Yes | 40.7% |
| No  | 59.3% |

Proportion of Firm's Audit Clients That are Publicly Held Corporations

|         |       |
|---------|-------|
| 0-20%   | 84.7% |
| 21-40%  | 9.4%  |
| 41-60%  | 5.9%  |
| 61-80%  | 0%    |
| 81-100% | 0%    |

Firm Submits to Peer Review of Its Quality Control System

|     |       |
|-----|-------|
| Yes | 68.2% |
| No  | 31.8% |

TABLE 2  
Statement 53 Assertions / Descriptive Statistics

Variables

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Will provide guidance on the auditor's responsibility to detect and report errors and irregularities

Is an appropriate response to public concerns regarding the detection of errors and irregularities

Will help provide more reliable information upon which to base lending and investing decisions

Will not increase audit costs

Will reduce the number of lawsuits brought against auditors by users of financial statements

Will benefit the auditing profession by improving audit planning and performance

Will promote Congressional and public confidence in the auditing profession

Will reduce the likelihood of federal regulation of the auditing profession

Will improve the quality of communications with clients

Is equally appropriate for application to audits of publicly held and non-publicly held companies

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TABLE 3  
Statement 54 Assertions

Variables

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Will provide guidance with respect to the auditor's consideration of the possibility of illegal acts

Will provide guidance with respect to the auditor's responsibilities when a possible illegal act is detected.

Is an appropriate response to public concern regarding the auditor's responsibilities related to detection of illegal acts of clients

Will help provide more reliable information upon which to base lending and investing decisions

Will not increase audit costs

Will reduce the number of lawsuits brought against auditors by users of financial statements

Will benefit the auditing profession by improving audit planning and performance

Will promote Congressional and public confidence in the auditing profession

Will reduce the likelihood of federal regulation of the auditing profession

Will improve the quality of communications with clients

Is equally appropriate for application to audits of publicly held and non-publicly held companies

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TABLE 4  
Canonical Correlation Analysis  
Statement 53

| Functions | Canonical Correlations | Canonical Roots | Eigenvalues | Redundancy | Proportion of Total Redundancy | F-Ratio | Level of Significance |
|-----------|------------------------|-----------------|-------------|------------|--------------------------------|---------|-----------------------|
| 1         | .6790                  | .4610           | .8553       | .1083      | .1083                          | 1.1455  | .1833                 |
| 2         | .6226                  | .3876           | .6330       | .0406      | .1490                          | .9026   | .7077                 |
| 3         | .4858                  | .2360           | .3089       | .0277      | .1767                          | .6476   | .9819                 |
| 4         | .3780                  | .1429           | .1667       | .0171      | .1937                          | .5041   | .9977                 |
| 5         | .3137                  | .0984           | .1092       | .0032      | .1970                          | .4243   | .9986                 |
| 6         | .2945                  | .0867           | .0950       | .0014      | .1984                          | .3581   | .9983                 |
| 7         | .1836                  | .0337           | .0349       | .0042      | .2026                          | .2109   | .9996                 |
| 8         | .1169                  | .0137           | .0139       | .0004      | .2030                          | .1410   | .9984                 |
| 9         | .0810                  | .0066           | .0066       | .0013      | .2043                          | .1041   | .9809                 |
| 10        | .0043                  | .0000           | .0000       | .0000      | .2043                          | .0012   | .9727                 |

TABLE 5  
Canonical Correlation Analysis  
Statement 54

| Functions | Canonical Correlations | Canonical Roots | Eigenvalues | Redundancy | Proportion of Total Redundancy | F-Ratio | Level of Significance |
|-----------|------------------------|-----------------|-------------|------------|--------------------------------|---------|-----------------------|
| 1         | .8269                  | .6837           | 2.1615      | .0765      | .0765                          | 1.5218  | .0039                 |
| 2         | .6799                  | .4622           | .8595       | .0881      | .1647                          | .0812   | .3198                 |
| 3         | .6084                  | .3701           | .5876       | .0378      | .2025                          | .8727   | .7361                 |
| 4         | .5044                  | .2544           | .3412       | .0068      | .2093                          | .6741   | .9476                 |
| 5         | .3985                  | .1588           | .1888       | .0089      | .2181                          | .5266   | .9868                 |
| 6         | .3527                  | .1244           | .1420       | .0129      | .2311                          | .4318   | .9908                 |
| 7         | .2383                  | .0568           | .0602       | .0032      | .2343                          | .2769   | .9966                 |
| 8         | .1504                  | .0226           | .0231       | .0011      | .2353                          | .1781   | .9934                 |
| 9         | .0848                  | .0072           | .0072       | .0005      | .2359                          | .1158   | .9504                 |

TABLE 6  
 Canonical Coefficients for Function One  
 Statement 54

| Predictor Set              |              | Criterion Set              |              |
|----------------------------|--------------|----------------------------|--------------|
| Variables                  | Coefficients | Variables                  | Coefficients |
| Years of experience        | .0001        | Consideration/illegal acts | -.9343       |
| Firm size                  | .2044        | Guidance/illegal acts      | .3862        |
| Audit hours/firm           | -.0449       | Appropriate/illegal acts   | .9267        |
| Audit hours/individual     | .2877        | More reliability           | -.5247       |
| Client profile             | .4299        | Cost implications          | -.1608       |
| Response to exposure draft | .5286        | Legal implications         | .2501        |
| Training approach          | -.1688       | Improved planning          | .3077        |
| Litigation experience      | -.0421       | Improved confidence        | -.7045       |
| Timing of implementation   | .2935        | Less regulation            | .3653        |
| Use of peer review         | -.9417       | Improved communication     | -.3712       |
|                            |              | Broadly applies            | .5457        |