How audit quality is determined in practice

Master’s thesis

Abstract:

This thesis investigates how audit quality is determined in practice. This thesis contributes by providing new insights in audit quality, that might be overlooked in existing literature, and which might be useful for improving audit firm quality. This is done by performing a case study at a Big 4 audit firm. Results indicate that practice and theory have similarities in the importance of inquiring knowledge of a client, auditor independence and time constraints. Client familiarity did play a role for independence, while there seemed no indication of client size and quasi rents playing a role. The most decisive factor for auditor capabilities was found to be experience. Additional factors found that might influence audit quality include the effect of client characteristics and working systematically and structured.

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1. Introduction

Audit quality is, by definition, an important factor for the validity of an audit, and the audit profession as a whole. There are a lot of factors that may come into play into deciding what audit quality entails. These factors are likely something that changes as a result of the relation between the auditor and the client, and might have an interplay over time. The effect of audit tenure, defined as the length of the relationship between an auditor and client firm, on audit quality is something that might work in multiple directions.

There are two primary schools of thought regarding the relation between audit tenure and audit quality. One school of thought argues that lengthy audit tenures may increase knowledge of the audited company and industry, which results in a higher audit quality over time. The other school believes that after a longer tenure the likelihood of familiarity forming between the audit staff members and the client staff members increases, which results in a lower likelihood that the auditor will make decisions that are unfavourable to the client, which in turn results a lower audit quality (Corbella et al., 2015).

A key determinant of audit quality is auditor independence (DeAngelo, 1981). Two main views regarding how audit tenure influences auditor independence exist. These are the regulatory view and the economic view. The regulatory view assumes that long audit tenure may lead to less auditor independence (Geiger & Raghunandan, 2002). The reason for this is that complacency, a lack of innovation, less rigorous audit procedures and a learned confidence in the client might occur after a long tenure at the client (Shockley, 1981). In contrast, the economic view says that auditor independence is lower in the initial years of an audit, which indicates that low audit tenure leads to lower auditor independence. This is because start-up costs at a new client are high, and significant transaction costs are incurred by the client when switching auditor. This makes auditors involved in the practice of low-balling. Low-balling means that the audit firm prices the initial audit fee below the avoidable costs of the audit in order to obtain the client. They do this to earn the rights on future audit fees from that client. This means that the audit firm will incur a loss in the first year, because of higher start-up costs, but makes up for it in the following years, when costs are lower. Because auditors want to keep their client long enough to make up for the losses incurred in initial years, independence might be lower in the initial years of an audit (Geiger & Raghunandan, 2002).

There is much empirical, mainly quantitative, literature on the relationship between audit quality and audit tenure. The results of these studies vary, and are contradictory to each other.

Corbella et al. (2015) find that audit quality improved as a result of mandatory audit rotation in Italy for non-Big 4 audit firms, while they find no significant indication for Big 4 audit firms. Mgbame et al. (2012) find a negative relation, which is not significant, between audit tenure and audit quality in Nigeria. Al-Thuneibat et al. (2011) find a negative relation between the length of the audit-firm client engagement and audit quality in Jordan. Johnson et al. (2002) find no proof for declining quality in longer audits, while they do find evidence of lower audit quality in the first three years of an audit. Geiger & Raghunandan (2002) find that audit reporting failures were more likely to occur in the initial years of an audit engagement, and find no evidence of long tenures to be associated with reporting failures.

This thesis performs a case study at a Big 4 accounting firm to look at how this relation holds in practice, and which factors might define and affect audit quality. This allows for breaking down audit quality into several factors, that together determine this quality. How these factors play out in practice can subsequently be observed independently. Furthermore, the open view towards audit quality allows for looking at other factors not yet discussed that might influence audit quality.

Quantitative literature on audit quality often uses the same (Al-Thuneibat et al., 2011; Deis & Giroux, 1992; Garcia-Blandon & Argiles-Bosch, 2018; Mgbame et al., 2012) or a similar (Francis, 2004; Johnson et al., 2002) definition for audit quality as is introduced by DeAngelo (1981): *"The quality of audit services is defined to be the market-assessed joint probability that a given auditor will both (a) discover a breach in the client's accounting system, and (b) report the breach. The probability that a given auditor will discover a breach depends on the auditor's technological capabilities, the audit procedures employed on a given audit, the extent of sampling, etc. The conditional probability of reporting a discovered breach is a measure of an auditor's independence from a given client."*

This definition seems to be mainly focused on quantitative research. As an example, the probability aspect in the definition is something that fits right in with quantitative research. This viewpoint might not be shared in practice, a research subject of this thesis will therefore be how 'audit quality' is defined in practice by auditors themselves. This is to see if the definition used by DeAngelo (1981) is something that is agreed upon in practice. The case study method helps with this, in that it allows for a more open view of what audit quality actually consists of.

Studies regarding audit quality seem to be mainly quantitative. The named quantitative studies focus mainly on the statistical relation between audit tenure and audit quality. It focuses on "if" audit quality is influenced by another factor. What these studies do however not focus on is “how” audit quality is formed. There seems to be a lack of recent literature on how the relation between audit tenure and audit quality is shaped.

Another constraint of the quantitative research on this topic is that the measures on audit quality are controversial, and all used proxies have some limitations (Garcia-Blandon & Argiles-Bosch, 2017). By seeing how audit quality is defined in practice, this thesis may provide some insight on why the used proxies are limited, and what could be potential other factors to look at when trying to define audit quality. This may contribute by providing insight into how useful the used measures actually are, and provide new measures to use in further research.

Furthermore, since empirical, quantitative research provides contradictory results, this qualitative thesis might provide new insights on the matter, and give additional insights for future research directions. Which in turn might help in explaining why results are inconsistent. These new insight may also have practical relevance in that it may provide insight for audit firms in what an audit of high quality consists of, and what conditions have to be met to reach this high quality.

During the study, the case firm was involved in a program that was meant to increase audit quality. This provides some practical relevance to the study, as findings may be used to see what should be focussed on and what should not be focussed on to increase audit quality, and if the viewpoint of the program is shared in practice by auditors.

Furthermore, findings of the thesis may be used in the regulatory discussion on mandatory audit firm rotation. As much of the factors that can determine audit quality are influenced by audit tenure, this thesis provides insights in this discussion.

Out of this, the following research questions is formed: “*How is audit quality determined in practice?*”

Based on this, three sub-questions are formed:

RQ1: “*What is audit quality*?”

RQ2: “*How do the factors in the literature relate to audit quality in practice?*”

RQ3: “*By what other factors can audit quality be influenced?*”

The remainder of the thesis is structured as follows. Chapter 2 provides a literature review, which looks at existing literature on the determinants of audit quality and provides some sub questions. Chapter 3 describes the methodology of the paper. It states how the interviews and observations are conducted, and what attention is paid to. Chapter 4 describes the viewpoints that come out of the interviews and observations, and applies them to the sub questions. Chapter 5 gives a conclusion and a discussion.

2. Literature Review

This chapter gives an overview of possible factors that might influence the quality of an audit. Factors that are named in the literature include knowledge of a client (Geiger & Raghunandan, 2002; Johnson et al., 2002; Solomon et al., 1999; Francis, 2004), auditor independence (Flint, 1988; Dogui et al., 2014; DeAngelo, 1981; Geiger & Raghunandan, 2002; Corbella et al., 2014), auditor capabilities (DeAngelo, 1981; Corbella et al., 2015; Garcia-Blandon & Argiles-Bosch, 2017), and time constraints (Deis & Giroux, 1992). Subsequently, auditor independence is determined by familiarity to a client (Corbella et al., 2015; Shockley, 1981), the size of the client in relation to the size of the audit firm (Gavious, 2006), the financial condition of the client (Knapp, 1985; Windsor & Warming-Rasmussen, 2009) and quasi rents (DeAngelo, 1981). How all these factors influence audit quality is discussed in the following chapter. Each factor is discussed individually.

2.1. Knowledge of a client

Over the years an auditor might develop knowledge about a client's internal business operations, processes and systems, which is important to be able to deliver an audit of high quality (Geiger & Raghunandan, 2002). This is, for example, in line with the research of Johnson et al. (2002) who find that reporting failures are more likely to occur in the first three years of an audit. Geiger & Raghunandan (2002) speak of a learning curve at a client, where an auditor has to learn about the client to perform a better audit. This learning curve is quite straightforward, if there is longer tenure the auditor gathers more knowledge of the client which allows for a better audit quality. The learning effect will however decrease over time, because in the initial years of an audit more knowledge is obtained than in later years.

Furthermore, Solomon et al. (1999) argue that quality may increase if an auditor becomes familiar with the client's industry, which allows for more accurate audit judgment. It seems that the learning curve that was mentioned before, might also be applicable to a certain industry. This indicates that if auditors become more familiar with an industry, they might be able to perform a better audit for every company in that industry.

An indication of the impact of industry expertise are accounting firms promoting their expertise in specific industries, and market shares within industries not being equally large among large accounting firms, as is argued by Francis (2004). Furthermore, he argues that audit fees are higher for audit firms that are the largest auditor in an industry, which implies higher audit quality. In addition to this, Ferguson et al. (2003) find that the market perception and pricing of audits in Australia is primarily based on office-level industry leadership in city-specific audit markets. This indicates that clients are willing to pay more for an audit firm that is the leader in an industry for their city, and thus that they perceive these auditors to be of higher quality.

2.2. Auditor independence

Auditor independence implies the absence of external pressures or personal relationships that may compromise the objectivity and integrity of auditors exercising their responsibilities (Flint, 1988). Auditor independence presupposes the existence of a personal and professional distance between the auditor and the client, as well as the ability to form a judgment that is unbiased and consists of no conflict of interest (Dogui et al., 2014).

Independence is seen as an important determinant of audit quality. If an auditor is independent from a client, audit quality is perceived to be higher. This happens because an independent auditor will be more likely to report on a discovered breach in a client's financial statements and will be less likely to give in to client demands (DeAngelo, 1981). So, in other words, auditors are independent if they are inclined to report found misstatements and irregularities. Auditors that are truly independent will have less ties with the client, and will therefore be able to provide the public with higher quality audits. Not being associated with the client allows the auditor to exercise unimpeded judgment when planning and conducting the audit (Geiger & Raghunandan, 2002).

Multiple factors that influence auditor independence can be named. Factors influencing auditor independence include familiarity to a client (Corbella et al., 2015; Shockley, 1981), the size of the client in relation to the size of the audit firm (Gavious, 2006), the financial condition of the client (Knapp, 1985; Windsor & Warming-Rasmussen, 2009) and quasi rents (DeAngelo, 1981). These factors are all discussed individually in section 2.2.1 until section 2.2.4.

2.2.1. Familiarity to a client

As is argued by Corbella et al. (2015), extended audit tenure may lead to familiarity forming between audit staff members and client staff members, stale audit tenures, and a decreased likelihood of the auditor taking decisions that are contrary to decisions taken in the year before. Shockley (1981) argues that as a result of long audit tenure, complacency, a lack of innovation, less rigorous audit procedures, and a developed confidence in the client may occur after a long association with the client. This indicates that too much familiarity to the client will lead to a less critical view by the auditor. The auditor is more likely to follow the same procedures as the previous years, and just assume that everything will be right at the client.

2.2.2. Audit firm size relative to client size

Gavious (2006) argues that the auditor being paid by the client may lead to a conflict of interest for the auditor. Auditors are driven to comply with the wishes of their clients in order to not lose future audit fees. This means that the auditor has an economic incentive to work in the interest of the client.

Gul (1991) argues that it is likely that an audit firm is more dependent on the client if the audit fee is a significant portion of its income. This decreases the auditor's ability to withstand management pressure and will make it more likely that the auditor gives in to the client. This means that auditor size also plays a role in this. A bigger audit firm will be less dependent on a single client, and will thus be less afraid to lose this client. What however should be noted, is that it might be more insightful to look at single offices of a firm than at the complete firm. The reason for this is that individual engagements are typically administered by an office-based engagement partner (Francis, 2004).

There are however other ways in which auditor size plays a role. Since Big 4 firms work with office-based engagements, their knowledge is both office- and client-specific (Ferguson et al., 2003). A big office will still have more human capital in house. A large office with more engagement hours available provides more opportunities for auditors to acquire expertise. This effect is amplified by the notion that in a big office, an auditor will have more peers who can be consulted, as is argued by Francis & Yu (2009).

2.2.3. Financial condition of the client

Users of financial statements perceive that management is more likely to obtain its preferred resolution in a conflict with the auditor when the client is in good financial shape. This may be because, in these situations, the auditor faces little risk of legal exposure. The reduced risk for legal exposure leads to the auditor being less motivated to resist management pressure, as is argued by Knapp (1985). Which indicates that auditors would exercise more caution when dealing with clients in poor financial condition (Windsor & Warming-Rasmussen, 2009).

2.2.4. Quasi rents

DeAngelo (1981) notes that quasi rents may also play a significant role in auditor independence. Audit technology is characterized by large client-specific start-up costs. This means that an auditor that is already working at a client has a cost advantage over competitors. The audit firm can produce an audit for fewer costs, since it has already dealt with the higher start-up costs. This allows incumbent auditors to set future fees above the avoidable costs. The extra money generated from the higher audit fees are called quasi rents. Transaction costs of switching auditor for the client will further increase the incentive for the client to not switch auditor. If the relationship between the auditor and the client ends, this poses higher costs on both parties. DeAngelo (1981) states that the anticipation on these quasi rents has two main effects: First, auditors bidding for the initial audit engagement will low-ball, they set the costs of the audit below the costs of the initial audit. They do this to obtain the initial job. Second, this creates an incentive for the auditor to make choices in favour of the client. This incentive occurs because it is costly for the auditor to switch client, if this happens the auditor loses its quasi-rents. This means that the auditor will not be entirely independent.

Furthermore, DeAngelo (1981) finds that this effect is smaller for large audit firms, which might be due to large firms being less dependent on a single client. However, this is when looking at the complete audit firm size. When scaling down to office size, as Francis (2004) recommends, this difference might become much less. A single client will have much more impact on a single office, than on the firm as a whole. So, low-balling at a single Big 4 office might still lead to less independence, in the same sense as it does at a non-Big 4 office.

2.3. Auditor capabilities

The capabilities of an auditor will influence the likelihood that the auditor will detect a breach in a client's financial statements (DeAngelo, 1981). Education, training and knowledge of professional standards are of influence on the capabilities of an auditor, as well as their independence and objectivity, their knowledge of a client's operations and industry, and an auditors working relationship with the management of the client firm, as is argued by Corbella et al. (2015). Further factors that can influence personal capabilities are an auditor's personality traits. Windsor & Warming-Rasmussen (2009) find that differing auditors personalities leads to auditors having various ethical predispositions in response to conflict. This indicates that an auditor's character determines to a certain extent how they will deal with a situation, which in turn influences audit quality.

Garcia-Blandon & Argiles-Bosch (2017) argue that the learning curve for a client is something that can be largely intrinsic to audit partners. If that is the case, it seems that the aforementioned capabilities of the auditor will also be of influence on this learning-curve effect.

Lead auditors are expected to play a significant role in the outcome of the audit process. Since single audit partners will differ from each other in personal attributes (Gul et al., 2013), they should also differ in audit quality (Garcia-Blandon & Argiles-Bosch, 2017). To a certain extent however, the decisions of a single auditor are somewhat restrained by a firm's quality control procedures, such as internal reviews, second partner signoffs, and technical consultations, as is argued by Knechel et al. (2015).

The role that personal capabilities play in audit quality indicate that how tenure and quality might relate to each other could work out differently from person to person. For example, how steep the learning curve at a certain client is might differ from auditor to auditor. Furthermore, it might be the case that certain auditors prefer certain industries. These notions imply that, for different auditors, the relation between audit tenure and audit quality might work out in different ways.

2.4. Time constraints

Deis & Giroux (1992) argue that audit hours, the total amount of hours put in the audit, is a suitable surrogate to use for audit quality. Intuitively, this means that if an audit firm has less time for a client, this will lead to lower quality. As a result of this, audit quality may be lower in periods that are busy for audit firms, whereas quality might be higher in periods that are less busy for the audit firm.

2.5. Summary

In summary, audit quality is associated with four main factors. Firstly, the knowledge of a client may help an auditor in forming an audit of higher quality. Understanding the processes at a client may lead to the auditor forming a better educated judgment. Secondly, auditor independence plays a role for auditor judgment. An independent auditor is less tempted to give in to pressure from the client, and can thus deliver a more objective judgment. Factors that may influence the ability to form independent judgment are an auditor's familiarity to a client, the size of the client firm relative to the size of the audit firm, the financial condition of the client, and the inclination to earn back incurred first-year audit losses. Thirdly, auditor capabilities are a decisive factor for audit quality. An auditor that is more capable is able to deliver better audit quality. Fourthly, time constraints play a role in determining audit quality. The more hours are put into an audit, the higher the quality of the audit will be.

3. Methodology

The study is conducted at a Big 4 accounting firm in the Netherlands. All interviews and observations are done within a single office. Participants were employees of the office. Interviews were conducted between employees with different amounts of working experience, ranging from one year to ten years of experience. This was done to obtain differing insights, as people with different amounts of experience might have a different perspective on the subject.

At the moment of the study, the case firm is involved in an internal project to increase audit quality. The reason for this is that the Dutch authority over financial markets (AFM) deemed it necessary to increase audit quality. This program resulted in many internal e-mails, meetings about quality and a week where an internal board did a check on quality, which allowed for a comparison of the tone at the top with the viewpoint in practice.

The choice of this firm was based on my connection to the firm, because I am active there as an intern. In line with this, access to the firm was obtained through the standard process of hiring interns by the firm. Consequently, this means that in all observations and interviews participants were informed of the role as intern I had during the research. This granted access to several client locations, allowed for obtaining insight in informal conversation, and helped in obtaining respondents for the interviews.

Data is collected through the use of three different methods: interviews, field observations, and analysis of internal e-mails. How the methods were used is discussed in the following paragraphs.

Observations were performed at multiple client locations, and in the main office itself. Team members were aware of me writing a thesis. Sometimes this led to conversation about the subject of the thesis, which led to some additional insights. At the client locations there was participation with the audit team in the role of an intern. This role allowed to get involved in auditor activities that were performed. This helped in gathering more insight into the profession and the processes that come with it. Subsequently, participation in an audit team gave insights on what factors are of importance for audit quality. Attention during observation was paid to how the audit process developed, and what were possible factors of influence for audit quality. Furthermore, the observations were seen as a chance to inquire about a perspective on the subject in informal conversation. This gave some additional insights which contributed to the research. Additionally, observations helped in gaining a basis of knowledge, which could be used for asking more in depth interview questions. So, the observation process was of support during the interview process.

Interviews made it possible to gain a more open view on what audit quality is, and what factors influence it. This left room for factors to be discussed that are not yet found in existing theory, and that might have been overlooked in the (quantitative) literature on the subject. For this reason the interviews are semi-structured. The questions in these types of interviews are open, so a respondent can formulate an answer in their own way. A benefit of a semi-structured interview is that a researcher can guide the conversation to certain subjects, while still giving the respondent the opportunity to talk about it in their own words (Bleijenbergh, 2015). This allowed for uncovering multiple perspectives on the matter, which were used in the analysis. The interviews are recorded and transcribed. Each transcription is analysed to uncover underlying themes. An overview of the conducted interviews is presented below:

Interview	Date	Function	Experience	Duration
1	16-05-2018	Staff	1,5 years at audit firm	20:11
2	17-05-2018	Staff	3 years at audit firm	24:09
3	23-05-2018	Contractor, active as senior	2 years at audit firm, 26 years active in accounting profession	30:42
4	23-05-2018	Senior staff	4 years at audit firm	25:43
5	28-05-2018	Staff	1 year at audit firm	30:27
6	05-06-2018	Senior manager	10,5 years at audit firm	23:20
7	05-06-2018	Senior staff	8 years at audit firm (including internships)	22:40

Figure 1: Interview characteristics

During the interviews attention was paid to the notion that views on audit quality in practice, can be different than what the literature states. For this reason room for interviewees to give their own insights on the presented subjects was given. This allowed for a broader view on audit quality than what could be found in the literature, and led to additional factors of influence on quality to be found. In addition to this, the respondents were asked about existing theory, and what their opinions on it are, which was done to see how the factors found in existing literature relate to practice.

Furthermore, the definition of audit quality by DeAngelo (1981), which is often used in the literature, seems to be mainly aimed at quantitative research. Therefore, the interviews also included questions on how auditors would define audit quality themselves. This allowed for a more fitting description of what audit quality entails. As a logical follow up to this description, and as an addition to this, there was subsequently asked where the problems are in realising quality according to that definition.

Findings of the interviews and observations were compared to internal e-mails about audit quality, which were sent to all offices of the firm. These e-mails were sent as a part of the program to improve audit quality, and consist of information on the program, consequently this includes factors that are of importance for maintaining audit quality. Analysis of these e-mails allowed for a comparison of communication from the top of the firm to what the view is in practice. It was made possible to access these e-mails due to the role as intern I had in the firm.

Finally, findings in the thesis are reviewed by an auditor employed by the firm. The auditor reviewing was assigned as a mentor for me, due to my role as intern. This review provided feedback on factual correctness of the made analysis, and is subsequently processed in the final version of the thesis.

At the moment of this study the Dutch audit market is characterized by a shortage in accountants, which leads to time constraints, and limitations for audit firms. This might be of influence for the perception that auditors have of audit quality, and might have its effect on audit quality itself. In the interviews the effects of this situation were also discussed to gain some insights into the effects that this has.

Existing research often sees auditing companies as a whole. However, it might be more insightful for research to shift this perspective to a single office. This is because an individual audit engagement is typically conducted by a single audit office (Francis, 2004). A Big 4 office firm is not that big anymore when shifting to the office level of analysis (DeAngelo, 1981). For example, Enron only represented 2% of Arthur Anderson’s revenue, but it represented more than 35% of the revenue for the Houston office, which was auditing Enron (Francis, 2004). This thesis is in line with this statement, since the case is at an office level. This allows to put the relation more into perspective, as well as to provide a more in-depth analysis of the single office.

4. Empirical Analysis

This chapter discusses empirical findings of the research. First, in section 4.1, the audit process is discussed. This is done to provide insight into the audit profession and give context on the findings that follow. The description explains the multiple processes that are part of an audit. After that, section 4.2 provides an overview of how auditors define audit quality themselves. The view resulting from this is subsequently compared to the view existing in the literature. In essence, this part revolves around the first sub-question: "*What is audit quality?*". Determining what is seen as audit quality in practice allows for further analysis on what factors may influence quality. This analysis is done in section 4.3. In this section, first the indicators that were found in the literature study are compared to audit quality in practice. For extra clarity, this is done in the same order as was done in the literature review. This part is mainly involved with the second sub-question: "*How do the factors in the literature relate to audit quality in practice?*". After that, additional factors that decide audit quality, that remained undiscussed in the literature, are reviewed. Those factors are divided into two different categories, client characteristics and working systematically and structured. This part answers the third sub-question: *"By what other factors can audit quality be influenced?"*.

4.1. The audit process

The typical audit process starts with the client- and engagement- acceptance. At this phase an assessment is made whether the client actually can become a client and if they, for example, are not on any blacklist somewhere in the world. After that an engagement letter is sent to the client. When the engagement letter is signed by client, the 'Scope & Strategy' phase starts. This phase involves setting up the files, identifying accounts, processes and risks, making a risk estimation, and, based on that, deciding the approach of the audit. Often the goal is to have completed this phase around August or September.

After that, the interim starts. In this phase the goal is to get a good view of the client, to identify the processes and the controls at the client. Some things that may be brought to attention here is what the client does, what has changed since the last audit, what their control environment is, how their control environment may have changed, or what the tendencies at the client are, for example which accounts the client may prioritize. At this stage walk-through tests are done, and interviews are held to gather information on the client.

During the interim, auditors determine for which processes they can rely on a controls strategy. If the processes can be relied on, this means that less substantive activities have to be performed in the check of the financial statements. So, more steps have to be performed for accounts in which internal processes cannot be used. The check of the financial statements is usually performed in springtime. At this check on the financial statements the accounts on the balance sheet and the accounts in the profit and loss statement will be audited.

Thereafter is the conclusion phase. During this phase it is looked at which misstatements are found, what the cause of these misstatements is, if they have to be extrapolated, and if larger samples have to be taken. Finally, an auditor's report will be made, which gives either an unmodified opinion, qualified opinion or an adverse opinion.

This is the way the process is recorded in theory. However, in practice there are often differences from this approach, and certain activities can cost more time than was originally planned. Results of this can mainly be seen in springtime, when closing the books. This may lead to an audit process being completed later. During the audit, the possibility for unexpected events will always exist. These events are what may result in differences in the execution of the made plan of approach. There can be things that are better than expected, or worse than where expected. The auditor continually has to respond to these unexpected events, which of course explains why there often will be differences between the plan of approach and the execution. This entire process will not be the same for every client. Different clients will require different approaches:

"It is of course different per client. I think that, around seventy percent is the same, and there is thirty percent that is specific for a client." (Interview 2, staff)

In essence, the main line of work will stay the same, but it will be specified to the characteristics of the client. Different clients may require a different approach:

"Conceptually, your work is always the same. In concept you always compare the statements of a client to a standard. The thing that is accounted, is simply the annual report, and you can compare that to the standard, title 9 BW2 or IFRS. In that sense your work is always the same. However, different types of companies require a wide range of different norms. (…) It is really important to know your client well, and to base your risk assessment on that, and eventually make your activities specific for that client, which is in a certain industry. I audit a car dealer,

those have completely different risks than a building company. (...) that also means your audit work is very different, it can vary enormously." (Interview 4, senior staff)

The approach may also be adjusted for specific client risks. Different clients will have different incentives to alter their financial reports. Different financial situations generate different incentives, which might be in opposing directions. The activities performed have to be adjusted to that:

"If you have clients that, for example, are in trade, they want to generate a lot of revenue and profit. In that case you specifically adjust your activities to look if they don't pull their revenue forward, or if they delay their costs to the next year, which makes them not counting that this year. But you do, for example, have clients that don't have that risk, who, for example, are subsidized. If they get too much turnover, they won't receive subsidy anymore, so they want to delay turnover to next year, and pull costs, which are related to next year, forward to this year. So it differs per client, but you will always have your standard activities." (Interview 5, staff)

Different types of companies will have different aspects in their annual reports that can ask for a different approach. Companies in different sectors may even have different regulations, which also demands the approach to be adjusted to that. This means that the audit process can differ per client, and will vary because of different client characteristics. However, the general line of work is something that does not vary widely per client.

4.2. Defining audit quality

In general the respondents seemed to see an audit as good quality, if the auditor thoroughly understands what is happening at the client. In other words, an auditor does need to understand what processes are present at a client to perform an audit of good quality.

"An audit is of good quality at the moment that you covered all risks that are present within your activities, so if you have mitigated all risks. (…) You have to touch on the essence of a company, of an organisation. If you audit a health care institution, you have to touch upon the essence of that health care institution. If you audit a trading company, you have to touch the essence of that company, and you have to know what it does. (…) You have been at [transport

company], they do logistics services, so you have to get the essence of logistics service, you have to touch those, and then you get the whole company, that's what it is about. (…) Subsequently you can make the process a lot harder, because it's not that they just transport pineapple juice from point A to point B, but they also blend the pineapple juice, put the pineapple juice into packaging, they store it, whatever they do with it. And after that they clean the things where they store it in. All those kind of things are added to it, it all starts at the essence of the company, with what it once started. That's very important, that you have that, that you touch that. That you tackle the risks in that, but also that you grab the risks that are present in other areas at such an organisation." (Interview 3, senior)

The idea that you have to understand the company and that you need to get a grip of what the client does to be able to perform a good audit is something that multiple respondents did acknowledge. If an auditor understands the client completely, they can have much more certainty in their judgment of the client. This allows for more trust in their own judgment for an auditor, and more certainty in the formed conclusions:

"For me quality is the moment that you feel like you really understand everything at the client, and that you can say with great certainty: 'there are no misstatements in this'." (Interview 2, staff)

A further indicator of audit quality is that the financial statements need to be compliance with law, regulations and audit standards:

"*We have the ISAs, the International Standards of Auditing, translated from English to the COS, 'Controle en Overige Standaarden' [Audit and Other Standards], we have to follow those as accountant. Certain things are further worked out in our own [audit firm] control measure (…), that is our handbook with all quality demands. If we carry those out, we have performed an audit of good quality." (Interview 6, senior manager)*

Both these views can be combined in the view that an audit is of good quality, if you can give enough certainty to the conclusions that you draw. Getting a grip of the company helps in this, because it helps in providing certainty about your conclusions. Following regulations contributes to this by providing a guideline that helps in what evidence is needed to draw a conclusion that gives enough certainty:

"What I think myself is that you can sign off, so provide the audit report, if you have completed enough procedures to substantiate your conclusion. That means that you need to have enough evidence in your engagement. And that you can't have outstandings or whatever. If you have that, all accounts have enough substantiation, then you have adequate audit quality I think." (Interview 7, senior staff)

An extra element that can be added to this is the role of efficiency. A client, and accordingly the users of financial statements, do want to have an audit report on time:

"At the moment you audit a listed company, they want to be able to report their figures at the end of February, and that will require an auditor's opinion. So you need to design an audit in the way that it is efficient I think" (Interview 4, senior staff)

What however should be noted is that the definition of audit quality is a matter of perspective. The viewpoints on audit quality can be dependent on the person that defines it. A client will have a different opinion on audit quality than an auditor has:

"Your client can think something is quality if you reach the deadline, if you help the client, think along how certain things have to be booked. A client can see that as an audit of good quality. But the supervisor, AFM, doesn't have to do anything with that. Reaching deadlines and thinking along with the client, the AFM doesn't care about that. They say something is quality if you followed all ISAs and all COS." (Interview 6, senior manager)

The definition of DeAngelo (1981) that was introduced in the first chapter is something that respondents did only seem to agree to partly. In favour of the definition, it was often stated that if an audit is of good quality, all material misstatements will have been found and reported. Some criticism on this definition was that it was too focused on finding problems, that it does not revolve around the base of an auditors work, that efficiency and materiality are also important aspects of quality, that it does not include the compliance to audit standards, and that it does not contain all factors that might play a role, since audit quality is a very broad concept. The general idea here seems to be that the definition does cover an important aspect of audit quality, but that it does not cover every aspect of it, and that it is not easy to cover every aspect in a single definition.

4.3. Factors influencing audit quality

In this section factors influencing audit quality as found in practice are discussed. This is done in the same order as is done in the literature review. Starting with the knowledge of a client, and following up with auditor independence, auditor capabilities and time constraints. These factors are supplemented by factors that were found in practice, but not in the literature. Factors not found in the literature are divided into client characteristics and working systematically and structured.

4.3.1. Knowledge of a client

Knowledge of a client is something that increases over time. Enough knowledge of a client gives the auditor an idea of the basic workings of this client. Understanding the basic workings allows for more focus on specific details. This means that this focus on details is stronger in later years of an audit. Whereas in the first year of an audit, the focus will be more on the basic principles of the client:

"If you are for the first time at a client, we have to initiate everything. The problem with that is, you don't know the client. So you have to… You will always not see things. Just because you don't know. You don't have experience with the client yet, you do have experience in the sector, you have a certain background, so you now certain things, but you can't always see everything. I think the longer you are at a company, the deeper you can delve into it, the better you know the client, the better you understand the client, and the easier it is to look at exceptions, instead of what the general line is of what is happening over there. (…) Every year you develop yourself tremendously, and every year you improve your files. Every year it becomes better, and it becomes easier, which means that you can deliver a higher quality." (Interview 1, staff)

The main cause for not being able to collect all necessary information from the client is a lack of knowledge of the internal workings of a client. The restrictions that an auditor faces in the initial years of an audit play an important role in this. These restrictions may result from both the side of the auditor and the side of the client. Both the auditor and the client may become tired of the whole process, which results in a lower audit quality:

"For example, I have some clients for the first year. Because you have to see so much, and learn so much... at a certain moment you are full [with information] or there is no time left anymore. At a certain moment it has been enough, at that moment the clients are also done with it. It becomes too much to process at once." (Interview 2, staff)

An auditor's knowledge of a client may increase over time. The ability to delve deeper into the controls and the system at the client improves after extended tenure at the same client. After a certain period however, it is imaginable that most processes at the client are known to the auditor, and learning process comes to a halt:

"It [knowledge about a client] can grow every year, but it is sort of a decreasing curve. At the start you learn about the client very fast, but at a certain moment, that decreases. At that moment you know the client. So I think that at a given moment there is sort of a maximum to it, or an optimum, after a few years you know the client reasonably well." (Interview 6, senior manager)

A basic understanding of a client might also be obtained by getting some industry knowledge. Clients in the same industry will, to a certain extent, have some similarities to each other. These similarities indicate an overlap of usable knowledge. Knowledge obtained at one client can be brought over to use at a similar client:

"I have audited municipalities, those have very specific legislations and regulations. If you are there just one time, then you don't really… You do your thing, and hear from people what the legislation and regulations are. But after you have done that three times, you will know it yourself. And also with the construction company, I audit one construction company, and only

at the end of the audit I feel like I really understand the work in progress position. Then I know how it works, and I could apply it to another client if needed. But if you do not have such a client, you won't do that for another year. And next year you think: 'How did it work again?'. If you work more in a single sector, I am certain quality goes up." (Interview 2, staff)

Besides the knowledge a single auditor obtains, the firm also obtains knowledge as a whole. Files from previous years can always be reviewed, and consulted to deliver a better audit in the current year. For example the question "*How did we solve this last year?*" could be overheard multiple times at client locations. Of course there lurks a danger in this. The possibility that an auditor will just repeat the steps he went through last year, without critically assessing the approach, does exist:

"We always have our file, and in our file you can always look at what is done last year, and you should actually always use last year's file, as some sort of cheat sheet. Have things happened, or have we seen things, that were strange… well, you take extra notice of those things this year. (…) You should always deviate from what happened the year before. My opinion is that you can always perform better. If you don't improve yourself, you won't improve your file." (Interview 1, staff)

Furthermore, the obtained knowledge of a client allows to focus on particularities. If the general line of work at the client is known, it allows to focus on particularities:

"If [audit firm] has already been there [at the client], there are memo's that show how we, as [audit firm], want to have it when we perform the audit. We can use that as a basis, it saves a lot of time, which allows to zoom in on particularities. If you have to invent the wheel again yourself, you lose a lot of time, time you could have used to dive into irregularities." (Interview 2, staff)

However, the benefits that come from using previous documents in activities are weakened down by changing the audit team. The documents of previous years can still be consulted, but the general knowledge of the client, and with that the ability to focus on details, are less present in a new team:

"I think that if there are just new people in the team, they will all have to gain an understanding of the client. So they will have it more difficult to delve deep into the client. I think that if you have a team that has been going to a client for a year long, they can exactly see how processes are designed at the client, which makes it easier to ask deeper questions." (Interview 6, senior manager)

Something that might affect the advantage of using documentation from previous audits is that things may change within a certain firm. This might make it required to perform an audit with another approach:

"They [client firms] can for example switch to a new automation system, which gives different procedures. It is possible that there is a new controller over there that looks at things in a different manner, who may have less affinity with delivering an annual report. It is possible that there is a CFO that does not do a quality test on things that are delivered. That is mainly involved with all kinds of takeovers, and other stuff. That can have some influence on the entire process. Saying it are different nuances is possibly expressed too weakly… We do notice there are differences in that." (Interview 3, senior)

The possibility for changes at a client firm indicates that relying too much on the files from previous years may result in a lower quality. These files will not be specified on the differences that have occurred within the client, but will be aimed at the previous situation at the client. So, if an auditor places too much trust in firm knowledge from previous audits, this may be problematic.

In sum, having the same client for multiple years results in obtaining knowledge of that client, which can be used to perform an audit that has a higher quality. In the first year this knowledge cannot be used, so this will result in a lower quality audit. Not all knowledge can be obtained in the first year due to limitations in the client and in the auditor, which results in lower audit quality in the first year of an audit. Having knowledge of the industry the client operates in, negates this effect somewhat, and helps in performing a better initial audit. Firm knowledge is something that also helps in improving audit quality, since this knowledge can be transferred through documents, and consulted in an audit.

4.3.2. Auditor Independence

Just as in the literature study, auditor independence is divided here into familiarity to a client, the size of the client as related to the audit firm, the financial condition of the client and quasi rents. This is done because the literature study stated that all these factors could possibly influence audit quality. For a more clear comparison to the literature, the same order is used here.

4.3.2.1. Familiarity to a client

Becoming (too) familiar with a client may result in more knowledge, but it does also have its drawbacks. For instance an auditor may become too easy-going. This might result in looking at the wrong things, and not being critical enough, which might lower audit quality. After repeating the process for several years in a row, the auditor may begin repeating tasks from the previous years on auto-pilot. This means that information will be less critically assessed, which in turn indicates a lower audit quality:

"I do notice that things are being rolled through more quickly [after an extended tenure] (…) Although there will always be thought put into it, there will never be rolled through something blindly, but I do notice that, at an initial audit, the first time you dive really deep into the processes to think about all risks, that in the second year you are tempted to repeat what you have said last year. On the one side this brings a lot of efficiency, on the other side you have to beware of not losing your critical angle, and just repeating what you have done last year." (Interview 4, senior staff)

This simply rolling through last year's documents might lead to overlooking relevant information. A team might become less critical over time, whereas a new team would be more critical towards the client:

"I think that if you have been too long at such a client, it can have a negative impact on quality, because you don't see certain things anymore. So you need new people, who look at it with a fresh and critical view, that ask detailed questions because they don't know the client that well, you can obtain a lot from that." (Interview 7, senior staff)

Consequently, one might think that changing up the audit team might lead to a more critical look at the audit work performed in the previous year. As Carey & Simnett (2006) note, audit partner rotation may reduce the familiarity threat. In other words, the auditor will be more independent in the initial years of the audit, and thus have a more critical approach towards the client:

"I think that if the whole team stays the same, then the tendency to literally roll through is large, at which there will always be room for improvement, but the tendency is large. But at the moment that a new team performs the audit, and it is still [audit firm], but a new team, it will still be rolled through, but there will be looked more critically at the whole approach towards the audit. At the moment we do have a new team, but it is also a new client for [audit firm], then there will be the most critical approach I think. Those gradations do exist." (Interview 4, senior staff)

What however should be noted here, is that in the last case (having both a new team and a new firm), knowledge of the client will be less, as is indicated in section 4.3.1. This indicates that, when forming a team for a client an audit firm has to make consideration between the knowledge of a client that the team has, and the critical angle that is brought:

"Of course you have the documentation of last year as a base, but if someone else comes to the client, that person will definitely ask good questions. That person will not just roll through documentation of last year, but will ask critical questions. Did you think of this? Why aren't these documents in the file from last year? Why didn't we identify these risks last year? That does have impact on your quality." (Interview 7, senior staff)

Next to a less critical approach after extended tenure, and thus not noticing irregularities, too much familiarity may also lead to an auditor being less inclined to report if they did find an irregularity. A new auditor would more easily do something with an irregularity found after an extended tenure. If the auditor does report something after auditing at the client for several years in a row, they basically admit that they have not noticed that irregularity in previous audits at the client. One can imagine that delivering that message does come with some feelings of awkwardness. That might be a reason for an auditor to be reluctant to notify the client of a problem that has slipped through in previous audits:

"For example you can be at a client for twenty years in a row, and then you suddenly notice a provision, of which you think… You have let that go through every year, and then, after ten years, to suddenly say: 'No, this is not good', that is something that feels like… You are supposed to do it, but then you should also have done it the year before, or the year before that. That is something that increases the threshold. Suppose a new accountant would come, he can simply say: 'We do something about that provision immediately, it is wrong'. But if you have been there for ten years, and you build a relationship for ten years, and you didn't notice it yourself last year, then it keeps becoming consistently harder to notify the client." (Interview 2, staff)

This is also in line with previously mentioned statements, that a new audit team might bring a more critical angle with it. This critical angle can in this situation also lead to being more inclined to report irregularities.

When being aware that their work is going to be reviewed by another auditor in the next year, auditors may be more inclined to report found irregularities. For instance, using the example used in the last quote, if the auditor knows that their work will be done by another auditor next year, they might more easily address the client on the irregularity that is found. They want to leave a good record for the next accountant that takes over the client:

"I think it lowers the threshold to clean it up after all. Also because you know that other accountants will do something about the situation. Of course, you do want to leave a good file for the other accountant, and you don't want them to suddenly find ten mistakes of yours. (…) If you would arrive at a new client, you would immediately say 'put it away, away with it'. If you have been there for a longer time, you would let it stay more simply, because, for example… you become more easy-going." (Interview 2, staff)

Being more inclined to do something about found misstatements is one thing. The knowledge that a new audit team will take over might also give a motivation to perform an audit with as much quality as possible:

“[When performing a last year audit] often they [auditors] will say: ‘We want to leave our mark here, we still want to show how good we can perform. So I would say, that in the last year they want to show ‘look, this is what we can do for you’’ (…) So, in fact, just to show that they can do it.” (Interview 5, staff)

Remarkably enough, the relation between client familiarity and audit quality is something that might work in opposing ways for different clients:

“If you have been at a client for a long time, you get bias, you get prepossession. You become less critical towards certain clients. There are also clients, I could imagine, if people work there that you don’t like that much, that you become more critical.” (Interview 3, senior)

In which direction, and how strong, this relation works out, might be something that is dependent on the personality of an auditor. As Windsor & Warming-Rasmussen (2009) already noted, an auditor’s personality traits leads to auditors having various ethical predispositions in response to conflict. Intuitively, one might say that this results in auditors reacting differently on different personality traits in clients.

Becoming too familiar with a client may lead to reduced auditor independence. Too much familiarity may lead to a less critical attitude. Resulting in being less likely to find misstatements, and being less likely to report found misstatements. Changing up the audit team is something that might improve the critical attitude. This works in two ways. Firstly, the new audit team will be more critical. Secondly, this makes an auditor more inclined to deliver good quality for the next team that is going to take over the engagement.

4.3.2.2. Audit firm size relative to client size

As mentioned before, the current Dutch market is characterized by a shortage in accountants. During observations it became clear that the Big 4 offices try to battle this shortage by reducing the amount of held clients. Mainly the smaller clients, which struggle with delivering the quality the audit firm demands of them, will be cut out of the client portfolio. This is something that might of course influence the relation between the auditor and the client:

"They try to say goodbye to the smaller client. At the moment that a client is not willing to pay for the audit quality we deliver, then we will be more inclined to take distance from that client. So the tendency to cater to them will be less. (…) I think that at bigger clients the tendency to maintain them is higher, but the possibilities in that are very limited. It's not that we can condone control differences to please them, so we still have them as clients in the next year. That is of course not how it works. I don't think that that plays a large role." (Interview 4, senior staff)

What should however be noted, is that it is not just size that influences the choice whether to keep auditing a client. The quality of the internal controls at a client plays an important role:

"Whether it is a big or small company… I do not think that really matters. I think it's more a matter of the quality of the client itself. How they have arranged it [their controls], and what their fee is, than whether it is big or small." (Interview 1, staff)

Additionally, the importance of maintaining a client might be something that mainly partners of the audit firm get involved in. It is not something that staff members need to worry about. This indicates that the pressure to maintain clients will barely influence the job a staff member performs:

"I'd rather lose a difficult client than maintain it, because for me, I'm at the client, I have to work there, I see the financial plan. I don't know how much [audit firm] earns on a client, I don't really care about that either. For me it's about if I can perform my job well at a client and if I feel nice over there." (Interview 2, staff)

The general line of speech here seems to be that the independence of staff members will not be influenced to a large extent, but that partner's independence might be influenced by client size. However, possibilities to cater to a client's needs will be limited, due to controls that are set up to prevent too much compliance.

4.3.2.3. Financial condition of the client

The financial condition at a client is another factor that might influence the audit process. If the client has financial problems, this might result in the auditor becoming stricter. An auditor will perform a stricter audit if a client is having financial struggles, or if it performs well year after year. The financial condition of a client is something that is taken into consideration in the risk assessment. Extra attention will be paid to areas where a chance for fraud exists:

"At the moment a company does not perform well financially, it will be more likely to have going concern issues. (…) That is a risk, and that also gives risk in the annual report. At the moment that the company performs badly, they will be more inclined to embellish. They will be more inclined to not include a provision, although it is mandatory. (…) This can also happen in the other direction. For example at the moment that a company performs well year after year, they might be inclined to increase costs, with the goal to pay less corporate taxes. For example by having a provision that is not supposed to exist. So, the financial situation of a client does certainly have influence on your approach, your risk assessment, at everything you do." (Interview 4, senior staff)

In contrast to this, the effect of a client in financial struggles can work in two directions. On the one hand, as described before, an auditor might become stricter. On the other hand, the auditor may become more lenient, as a form of sympathy. Which of the directions is chosen seems like something that depends on multiple factors, like the auditor's personality traits and their relation to the client. Of course, in this situation lenience will also be restricted by controls and regulations. But the relation to the client might cause some lenience from the auditor:

"If you know, for example, that someone will be punished, you might be less tempted to do a proposition for something, if you know he will suffer for it. Suppose, that they don't deliver the right documents for the audit, then you can invoice more work. If you did not have to invoice more work in the last five years, because the controller does his work well, and suddenly he does not perform well. For example if he is sick, or his wife is sick, you will be less strict towards that man. Because you know him, and you know his situation. If you come at the company for the first year, you'll be more inclined to say: 'Fine, but this is a company, [supposed to be]

professional, just deliver those pieces, otherwise you'll receive an invoice'. I think you'll become more lenient after time." (Interview 2, staff)

The above evidences that how an auditor reacts on a poor financial condition at a client also corresponds with the relation an auditor has with the client. How, and to what extent, an auditor is influenced might be depending on their character. Some auditors might be more easily convinced to help the client out than others.

In conclusion, an auditor will be stricter if the financial situation of a client gives reason for the client to alter financial results. This can be both in times where the client struggles with its financial condition and at times where the client performs well year after year. This finding is in contrast with Knapp (1985) and Windsor & Warming-Rasmussen (2009), who state that an auditor will be more critical at a client with a bad financial condition, and less critical at a client with a good financial condition. Furthermore, the relation an auditor has with the client might influence this effect.

4.3.2.4. Quasi rents

Quasi rents in theory should give the incentive to auditors to hold on to a big client. This should be the case, because initial high first year costs can be earned back. In the case study however, this did not become apparent.

A possible explanation might be that the pressure to keep clients is less in the current audit market, as a result of the shortage in auditors. Where audit firms are actually actively involved in reducing the amount of clients:

"Every year we make the consideration [which clients to keep], that's what you see now with the audit quality that has to go up. We have to think whether we can still deliver the quality that is expected from us. That keeps getting more important. Of course, it's always a matter of costs and benefits. Do we earn on it? Are we able to plan it in a good way? That's often something, does it fit in our planning process? And does the partner have enough space in his portfolio? In general, at least how we have them now, we do take a critical look, which client can we go on with, to which client do we say goodbye?" (Interview 5, staff)

An important factor in deciding whether a client will be maintained is efficiency. It becomes a matter of the audit fee versus the required work. If the delivery of required documents and information is subpar, the audit will be deemed to be less efficient, and relations with the client will be less likely to be continued:

"I am less involved in that process myself, but from [audit firm] we look at what a good client is, in terms of efficiency. It doesn't really matter if it is a big or a small firm, we look at efficiency. We look at how the audit is going. Is it efficient, do they deliver information on time, and are we helped if we work there? Those factors play a role I, think." (Interview 7, senior staff)

However, this is only part of an explanation. The audit firm will still want to hold on to certain clients, while rather getting rid of others. This choice mainly depends on the quality of insight and documents the client is able to deliver, and the amount of work required at the client versus the audit fee.

Another factor that may contribute to quasi rents not really being recognized in the interviews is that it is a task of the partners to maintain clients. On the one hand, this tells that this effect might be represented more at higher levels in the organization. On the other hand, this makes clear that the effects of quasi rents are not really brought over to the audit staff.

What however is still something to take into consideration is that the possibilities in this are limited, and that an auditor cannot do everything to please a client due to regulations. What further became evident is that obtaining high audit quality, under pressure of the AFM, was seen as more important than maintaining client fees. So, quasi rents are something that, at the moment of research, are not emphasized by the firm.

4.3.3. Auditor capabilities

Auditor capabilities can be split into personal capabilities and team capabilities. Personal capabilities of an auditor are, of course, important for the entire audit process, but respondents often seemed to note that the composition of an audit team is also something that is important. The team needs to have a connection with each other.

4.3.3.1. Personal capabilities

By far, the personal capability that respondents emphasized the most was auditor experience. Experience brings effectivity and efficiency with it, which makes it more likely that an audit is of high quality:

"I think the most important [factor], for quality, is simply experience. If you have people that understand it, that can direct people, who also can explain to a customer what we want, I think that gives a lot of efficiency, and a lot of effectivity in an audit. If you can guarantee upfront that you have that, in the planning phase (…), then you can really deliver quality." (Interview 5, staff)

Experience is also something that allows you to think more critically and more analytically, and to understand what work you are doing. It helps increasing knowledge over time:

"In the beginning you know one account of the annual report, or two accounts. You see it once, somebody explains it, and you understand it a bit, but you don't fully understand it. (…) If you look at it the following year, you think, 'I should have had more focus there', 'I should have been more precise there'. Then you can connect different accounts to each other, because you get more experience. Also in general, because you know you don't have to learn as much anymore. You're at a certain level of knowledge at the client." (Interview 2, staff)

More experience can also help in your relation with the client. It can help in knowing how to act at a client, and how to be more critical towards that client. Experience might provide more knowledge on how to best deal with the client:

"If you have new clients, it may be good to immediately set boundaries, to immediately show who you are, what you do, and what you can do. You should not start with less, you should always start with more, and be stricter. In that case you can always go back. If you begin weak, you can't become tough later. In my experience, you immediately have to start tough [at a client]. (…) When I started in accountancy in '92 I wasn't that way either, it is something you learn over time. Seniority really helps. It's not fun to grow old, but seniority does help." (Interview 3, senior)

Experience is something that can help in showing more attitude towards a client. Over time an auditor will gain more expertise, and this expertise may help in acting more critical, and being less accommodating towards the client:

"The first two years you think 'The controller is probably right and I'm probably wrong, because I don't really understand it'. After the second or third year, you start to think 'Those controllers actually aren't that smart, I am right.' At that moment you can resist [the controller], and say 'You are simply wrong'." (Interview 2, staff)

Specific experience, for instance experience in a certain industry, is also a factor that may increase audit quality. Since audits in similar industries show similarities (this is further explored in section 4.3.3.), industry expertise is a factor that can help in developing a grip of a client, and performing a first year audit much more efficiently. Having previously worked in a certain industry may for example help in this:

"That's also something that has to do with experience and seniority. I currently help with auditing [transport company], because I have been a controller for two years at a transport company. So I know what happens over there. So I don't need a lot of time to get to know the company, and to see what it is about. So, what is important when performing a first year audit somewhere, is that you have someone in your team that has, preferably, a lot of experience with that kind of company. That is what it is about. So I think branch specialization is an important aspect in auditing." (Interview 3, senior)

In addition to working experience in a certain sector being helpful in the audit process, it might also be helpful to have audit experience in a certain sector. By having this audit experience, a lot of specific expertise can be gained from a sector. This is especially the case if that sector consists of irregular regulations, because in that instance more specific knowledge is needed:

"You can also see at [audit firm] that people are specialized within sectors. The different sectors, like I said, are public, municipalities or semi-government, that kind of entities.

Healthcare is a distinct sector. You often see that people that audit building companies also audit multiple building companies, because those are somewhat specific. Financial services is entirely a different branch inside [audit firm], (…), profit is somewhat pooled together, at which you still see specialties. (…) I think the most important is that you specialize per sector if it has distinct legislation and regulation. I think that gives the most efficiency per specialization, and also a better quality." (Interview 4, senior staff)

In sum, experience is an important characteristic that can help in performing an audit of high quality. Both the knowledge and the attitude that come with experience might help in producing an audit of high quality. In addition to this, certain specialized experience, like experience in a specific industry, might also help in delivering a high quality audit.

4.3.3.2. Team capabilities

For the quality of an audit, the quality of the entire team is important. Firstly, a team obviously needs to consist of enough individual talent and expertise. Without that, it becomes a lot harder to perform an audit of high quality. Secondly, it is important that an audit team fits together well, that the team members have a connection with each other.

The first part, having an audit team that consists of enough knowledge, is something that is essential for audit quality:

"If you don't have a good team, then you can do your best, you can work fifty hours a week, sixty hours, or work seventy hours in a week, but it will be difficult to deliver good quality. If you, for example, don't have a manager or a senior, it becomes tough, because you just need certain facets in a good team. You need people that have a certain knowledge about the client, or that have knowledge in general. Who can direct, yes, that's what you need. If you don't have that, it becomes difficult. I don't say it is impossible, but it becomes challenging." (Interview 1, staff)

That this is something that can affect the quality as a result of a better understanding seems obvious. In addition to this however, experience is also something that can help in client relations:

“If you are there yourself for the first year, then you don’t have experience yourself. In that case the client can do what they want with you. They can easily fool you. If you are there with an experienced team, with a senior or a manager that is present a lot, you notice that the client will notice ‘I can’t fool him, they know how things are done. If I don’t perform well, they come by, and I get scolded’. As a team, you notice that if you are with more people, and have more experience, also at the client, you notice that it becomes easier. Because, if you have an experienced team, but no experienced team at the client, where everyone is new [at the client]. Then it remains harder than if one person has been there for five years.” (Interview 2, staff)

Experience with a specific client is also important to have in a team that has to perform an audit. An auditor in the team with experience at the client can point the rest of the team in the right direction, explain the controls at the client, and can tell them which person at the client they can best consult with. Having a good mix of experience may help with this:

“You need to have mix, a good pyramid as we call it, not just starters. It’s fine to have a starter on your team, but you do have to make sure you have people with two years of working experience, three years of working experience, five years of working experience, seven years of working experience, so a good mix of your team.” (Interview 6, senior manager)

The second part, that it is important that an audit team fits together well, can be important in having a team that can perform on multiple areas:

“Team composition is of course difficult, because you need critical people in a team, but you also need people that get along with the client, because, how do you bring the message? That you have to deliver an unpleasant message that is evident, that you have to do that. It’s about, how do you bring it? At one client you can be ice cold, at another client you have to nuance it more.” (Interview 3, senior)

This quote indicates that there has to be a match between the clients and the audit teams personalities. This is important, because this makes interaction easier. Additionally, this may interact with industry specialization. Client personality is something that can be connected to industry. For example, an audit at the health care sector generally needs a more soft and understanding approach towards the client. While in an audit at the building sector, an auditor generally needs to be direct towards the client, and be able to stand up for themselves.

Consequently, it may be beneficial for an auditor to specialize themselves in a sector that suits their character best. This means that the auditor will both have a character with which collaborating with a client is better, and have the specialized knowledge to perform a qualitative audit.

Pulling this off, and having everyone in the setting that suits them best, might however be a tough thing to do. This has to do with the shortage in auditors at the job market. Because of this, audit firms can struggle with the right team composition. It can be hard to keep enough experience inside the firm:

"Something that you can see at this moment, that makes it hard to deliver good audit quality, is that you have a very limited team. As well in size, the amount of people, as in experience. (…) There is a lot of outflow in the entire accountancy. The people that stay are divided over multiple clients, they have less time, and in that way it becomes a vicious circle. The people that remain keep getting busier, because the regulations keep demanding more from them, while there are constantly less people available. So pressure becomes higher, and that's a reason for people to leave the profession." (Interview 4, senior staff)

In conclusion, two main things have to be taken into consideration when forming a team. Firstly, the team needs enough individual expertise. This is essential to perform a high quality audit. Secondly, an audit team needs the right mix of people. For instance, a team needs critical people, as well as people that are proficient in communicating with the client. Furthermore, a team needs to have the right mix of experience. Current constraints in the job market for auditors, might hinder an organization in this. Nevertheless, these two things are important in forming a team that can perform a high-quality audit.

4.3.4. Time constraints

Time constraints may also have their effects on audit quality. The shortage of accountants limits the available hours an audit firm has. This can result in struggles to meet deadlines, overtime and having problems getting the right team on the right client. All of which may result in a lower quality. A reason for time constraints might be unforeseen events that occur:

"Suppose that upfront you think you need 800 hours to do the audit, but eventually it is much more complex than expected, or things don't work out in your favour, or the client did a takeover that, for example, still has to be audited. In that case, you find out during the trajectory that you might need a thousand hours, and you don't have that amount of people, then people have to work in the evening to complete the audit. That could be a threat to your quality. If you have to do it in the evening, people are less sharp." (Interview 6, senior manager)

The struggle to meet deadlines may also lead to people rushing their work in order to finish it in time, which in turn might lower audit quality:

"If you are really busy, people may be tempted to rush work, or to set priorities, and that can make the quality of certain files become lower. That's a danger you always have to keep in mind." (Interview 1, staff)

Next to rushing work, overtime may have other drawbacks. Auditors are human, and will also have their limits to which extent they can work:

"It can become an ethical choice. You want to serve the client well, but on the other side, you also want to have a life. You can keep running for fifty or sixty hours, but at a certain moment it's been enough." (Interview 2, staff)

Time constraints may also have their effects on team composition. Because of limited auditors available, it may lead to less experienced auditors on an audit team that would ideally be the case:

"It's really important that there are enough senior team members, and that they are involved enough. Also the involvement of the partner and the manager is important. They are also really busy, which makes their involvement lower. While it is proven that that increases audit quality. (...) Senior team members are always more busy than first- and second years assistants, which

makes involvement of these layers lower than is desirable. And that that is essential for quality, I'm sure of that." (Interview 4, senior staff)

Subsequently, the lack of experience in audits may have a stronger effect for small clients than for large client. Experienced auditors will be busier than non-experienced auditors. This results in experienced auditors having to make choices between clients. They have to divide their attention over multiple clients, which may result in them prioritizing more important clients, and paying less attention to small clients. Having to switch between clients might make it harder to concentrate on a single client:

"Especially in the busy season you have multiple clients at a time, which sometimes makes you unable to focus on one client, and I think myself, that if you can't focus your quality lowers. That's how I look at it. Suppose you have two weeks to do a single client, then you should really just do that client, and not switch continuously. Because in that case, you are unable to focus. (…) For example, you are busy at a single client for half a day, and in the afternoon you are busy with another client. Then you just start getting into it, and then you have to do something else again. You have to shift continuously, and that does impact your quality I think, and it is also not efficient." (Interview 7, senior staff)

Furthermore, the workload may result in tiredness, which might make people sloppy, and take the quality of an audit down with it:

"People are tired, which makes them make mistakes more quickly. They have to push themselves, which does have consequences. Sometimes you can work until eleven o'clock in the evening, then you aren't sharp the next day. You have to take that into consideration." (Interview 1, staff)

In sum, time constraints may make auditors rush their work, become sloppier and force them to set priorities. It may also have its influence on team composition, as it will be harder to compose a team that has everything a client needs, when all auditors are busy at other clients.

Time constraints will make audit quality go down. This means that in certain periods, like the so called busy season, audit quality might become lower.

4.3.3. Client characteristics

Client characteristics are also a thing that influence audit quality. The influence of multiple client characteristics on quality is something that was heavily emphasized as a factor of influence on quality in the interviews, whereas the observations seemed to support this. However, the effect of client characteristics is something that is pushed to the background in existing literature. This might possibly be due to the positivistic nature of research on the subject. The positivistic nature of this research makes it required to be able to generalize findings. Transforming clients into homogeneous entities allows for this generalization, but may also have caused this aspect largely being ignored. Since industry market shares are not divided equally between audit firms (Francis, 2004), this might be a factor that influenced the results.

In multiple interviews the typology of a client was seen as something that influences the audit process. Two of these specifically named the typologies from Starreveld. An overview of these typologies, is presented below. The overview is an adaptation from Starreveld et al. (1998) as presented in Vaassen et al. (2009).

Figure 2: Typology of organizations as used by Vaassen et al. (2009), adapted from Starreveld et al. (1998)

Classification			**Examples**
Organizations with a dominant flow of goods	Trade organizations	Cash sales	Supermarkets, department stores, petrol stations
		Credit sales	Mail order companies, wholesalers
	Production organizations	Production to stock	Brickyards, beer breweries, paper mills
		Mass customization	Computer assembly companies, car assembly companies, single cut clothing manufacturing
		Agrarian and extractive organizations	Dairy farms, mines, oil companies
		Production to order	Shipyards, aircraft factories, contractors, film companies
Organizations without a dominant flow of goods	Service organizations with a limited flow of goods	Limited flow of own goods	Restaurants, newspaper publishers
		Limited flow of goods owned by third parties	Auctioneers, dry cleaners, bicycle repair stores, garages
	Service organizations that put space and electronic capacity at their customers' disposal	Disposition of specific space	Hotels, hospitals, oil pipeline companies, airlines, water companies, gas companies, transportation companies
		Disposition of specific electronic capacity	Internet providers, telecom providers, electricity companies
		Disposition of nonspecific space	Swimming pools, cinemas, concert halls, railway companies
	Service organizations that put knowledge and skills at their customers' disposal	Selling man hours	Public accounting firms, law firms, cleaning service companies
		deployment of intellectual property	Software producers, car navigation companies, information brokers, traders of bitable goods
		Sale of financial products	Banks, insurance companies, investment companies, pension funds
	Governmental and other not-for-profit organizations		Ministries, government agencies, police organizations, prisons, universities, municipalities, foundations, associations and nongovernmental organizations (NGOs)

An example of how companies with the same typologies are similar in the activities that have to be performed, and how experience might help in getting to understand a typology is named in the next quote. The examples named are a factory that produces machines and a factory that produces tank trailers, which are both '*production to order*'. These two examples are compared to mass production, or '*production to stock*' in the overview of Starreveld above:

"In the autumn, I have audited a company that made degradable packaging (…) process wise, that's mass production. (…). If you name machine technology, you need less machines to reach the same turnover. So you are more involved in production per piece, so that gives differences. But, in the end, if you take a machine factory and you take a factory that produces tank trailers, those are comparable. You go there as accountant, and if you say that you have to go to a machine factory that makes machines to order for certain companies, then you know that it all starts with quotation trajectories. So you know that there have to be pre-calculations somewhere. You know there may be intermediate settlements. From your knowledge and experience in an organization, you know what to expect." (Interview 3, senior)

So, knowledge of a certain typology can help in auditing other firms with the same typology. This helps the auditor know what sort of processes can be expected. When going down in the overview presented in figure 2, auditing may become more straightforward:

"You have the typologies of Starreveld (…) If you look at that, you can see that if you go further down, so the further you go into the service industry, the harder it is to perform the standard duties" (Interview 1, staff)

This is in line with the description used by Vaassen (2009), who notes that from an internal control perspective a flow of goods can be helpful, because it allows for a number of strong and straightforward internal controls. An example of this is that at a company with a dominant flow of goods, stock can be counted. If a flow of goods becomes less distinctive, so it goes further down the presented schedule, measurement points will also be less visible. What should however be kept in mind considering these typologies is that no company will exactly fit within a theoretic model, but that a theoretic model can offer a guideline for what to take into consideration.

Another characteristic of a client that can be important for the outcome of the audit process are the internal controls of the client. If the client has good internal controls, the auditor can trust on this, and has to perform more activities. In this situation it can be harder to guarantee that no material misstatements present:

"If you can rely on the systems, it will become easier for yourself. But the conditions to be able to rely on such a system are very strict. If you can't rely on it, you have to do extra work activities, so the risk that you make a mistake also increases. If you have a really well-arranged company, then the audit becomes easier than at a company where it is chaos, where no one knows who does what. That makes it more difficult. In that case guaranteeing quality may be problematic." (Interview 1 staff)

It is of course not just that being able to rely on a client's internal controls is easier, it also brings extra security and certainty. If the internal controls of a client are reliable, then you can trust in the correctness of the underlying reporting figures. This means that if the controls work perfectly, you have certainty that the reporting figures are correct. In contrast to this, if you take a sample, even if everything in the sample is correct, a chance that there are some misstatements outside of the sample will always exist. Good internal controls can give more certainty to the auditor about their audit quality:

"Preferably, you want to be able to rely on what the client does, that gives the most certainty. You can take a sample of a hundred things, but if you can conclude twenty-five times that the process at the client, so how they have internally arranged it, works fine, in that case it produces a lot more value than your sample of one hundred." (Interview 2, staff)

The size of a client is something that is related to the quality of internal controls. In general, a larger company will have better internal controls. This will also have its workings on the design of the audit process:

"I think the biggest difference is in the size of the client. At really large clients we start sooner with the scope and strategy. We also place some more emphasis on the interim, because you

can rely on the processes there, because large companies have their internal processes arranged better than small companies. So, at large clients you see that scope and strategy happens on time, and that the interim is done in autumn. At smaller clients you see that scope and strategy and the interim often is limited in hours, and the focus is entirely on the end of the year, because everything over there is substantive testing." (Interview 4, senior staff)

However, internal controls do not necessarily have to be better for bigger clients. A small clients might as well have good internal controls or a big client might neglect their controls:

"It is not definitely the case that a big client is qualitatively better, and a small client qualitatively worse. A small client can deliver everything with quality, and have very good procedures. A big client can have very good procedures on paper, but not follow up on it. Look for example at [client firm], that's a large client at us, I think it's a large client, with a turnover above hundred million, and all procedures there could all be a bit better." (Interview 3, senior)

The difference between a small and a big company seems to mainly be the possibility to set up good procedures. A big firm has more possibilities to set up good controls, and have better arranged internal processes than a small company, but this is not necessarily the case. Small companies might however have less opportunity to set up good internal controls, because of their limited size:

"In general the bigger clients will have their internal control better arranged, in comparison to small clients. For example, segregation of duties. If you audit a small client, and the whole financial department consists of two, three people, then it is of course difficult to have adequate segregation of duties within a process. At bigger clients that's a lot easier. But at big clients we also see that internal controls aren't on point." (Interview 7, senior staff)

In the case a large company does not have reliable internal controls, auditing a small client might even be easier, and thus give more quality, than at a large client:

“The only difference [between a small and a large client], you have a lot more influence [from outside at a large firm]. For example, I have a client, [company name], that is very large, that has to do with other countries. In that case there are a lot of influences on the process. If you have a standard small client, five people work there, Piet checks and Henk makes the invoice, let me say it like that. In that case it all is a bit easier.” (Interview 1, staff)

Client size has further influence on the complexity of an audit, and as one might think, an audit that is complex needs more expertise and time to come to good audit quality:

“Look, if you have a small trading company right around the corner, so to say, or you have a bakery around the corner, then it is easier to organise, and you probably have only one person to contact. You probably have one person who does the administration, so you have short lines. No politics so to say, all very simple. If you audit a company like [large client firm], then you have an international audit, where you have to direct all [audit firm] accountants around the world. Where you have to know what happens around the world. Where you have to think really far ahead. Organising such an audit costs a lot of time. So the difference in client size affects organization [of an audit] a lot.” (Interview 6, senior manager)

The way that these complexities and extra requirements are dealt with is by sending people with specific knowledge and expertise to these large clients. So, people that are able to deal with the complexities that arise at those clients:

“Because if you have a few colleagues that are very specifically very good in something, then you won’t send them to the bakery around the corner, because that is easier to audit. You put them on the team of [large client firm], because over there the specific, specialised knowledge is needed to deliver good audit quality. (…) If you have the larger clients, you’ll need the most people, but also the people with the most knowledge. Because it is complex over there.” (Interview 6, senior manager)

Client attitude may also be a factor that influences the quality of an audit. The company culture is something that can decide how a client deals with their internal controls, and how important these internal controls are generally considered to be:

"And some clients, yeah, they just don't care. They think of the total picture, the number below the line. They put everything on one ledger, on one account. Absolutely not insightful. For us, in the audit, also not simple. Some clients don't care, and some clients are just structured, 'that account comes over there, and that one over there'. That differs a lot per client." (Interview 2, staff)

The attitude of a client might also influence the quality of the audit in another way. If a client is willing to cooperate and deliver the right pieces of information, an audit may become substantially easier to perform, which gives a higher audit quality:

"Does it feel obligatory for the client or are they actually happy to see you? [If clients are happy to see you] their attitude is like 'show us, is it right what we do? Are there certain risks?'. Some other clients see it as obligatory, they have to do it, but they'd rather not." (Interview 2, staff)

This attitude of a client can have an influence on communication with the auditor. This can in turn influence the audit quality:

"Yes, if you for example face time constraints, or find something in the end of the audit. At a client where you could easily communicate, or where you had enough time planned, then reporting a mistake is less of an issue, than at a client that will argue with you about it." (Interview 2, staff)

The relationship with the client, might however improve over time. A client that does not want to cooperate and deliver the right information initially, might be willing to do so after extended time, when the client gets a better understanding of the job of the auditors:

“To a certain extent, you raise the client. At a certain time, it can be a bit of a bully, and after some time, he might get the idea why you are there, and what you do. And if you sometimes help a client out, with some sort of advice, or certain insight, then you can win the client over. In that case they are more willing to work in your favour. And at a certain moment, if they are willing to work in your favour, they are more open towards you. At that moment you get to know more from them, and it becomes easier for you. In that case it is easier to come over and to start conversations. At the moment a client does not want to work with you, you will notice that. You can feel a blockade to go to the client. It’s a bit of interaction.” (Interview 2, staff)

Both the internal controls of a client and the client attitude are factors that influence how the delivery of documents and information from the client will be. If the delivery of this is good, the auditor will be able to deliver more quality:

“The delivery of a client surely has strong influence on audit quality. If the client has an administration that’s a mess, you will see it back in de quality of the audit. (…) If it is a huge mess at the client’s administration, we often say ‘shit in, shit out’. If the client really doesn’t perform, that will translate often to a bad audit quality. Because in that case you have loose ends everywhere, questions that are unanswered, all information you get from the client is often initially inadequate, so you have to get back to them. That makes it very hard to perform a qualitatively good audit.” (Interview 6, senior manager)

In conclusion, client characteristics may influence the work an auditor performs greatly. The typology model of Starreveld is something that is recognized in practice by auditors, and can alter activities that have to be performed. And different audit activities per client, do of course indicate that quality might also differ. Knowledge and experience within a typology might help in increasing audit quality. Next to this, the quality of the internal controls of a client are a determinant for audit quality. If the auditor is able to rely on the internal controls of a client, audit quality will be higher. Another client characteristic that might influence audit quality is the attitude at a client. A client that is more willing to cooperate leads to a higher audit quality. The attitude of a client is however something that may change over time, as the relation with the auditor changes. Both the quality of internal controls and the attitude of the clients will influence the quality of the information and documents the client delivers. And as is clearly illustrated in the last quote, by '*shit in, shit out'*, if the input (the deliverance from the client) is of bad quality, the output (the audit) will be of bad quality.

4.3.5. Working systematically and structured

Working structured, and documenting everything well is something that might also improve audit quality. An example of this is already mentioned before, where was noted that often memo's with information of last year's audit are used. This is something that can only be done if everything is documented clearly. This means that the more standardized and uniform information is documented, the easier it will be to get used to the way of documenting of someone else:

"What you see with us, everyone has a different manner of documenting, and what I notice is that you always have to get used to the way of documenting of someone else." (Interview 1, staff)

Furthermore, working well structured might lead to tasks being completed more consistently, without missed step:

"What I think is important is that you always check if you did do everything. We have certain working steps, those include a description of tasks, those are often fairly standard working steps. Everyone does take a look at them, but they do not really look at it. Sometimes you see that we miss things or that things that we have seen aren't documented. And what you can see, slowly but surely we get more forms for those standard things. (…) We have IPE, which is Information Produced by the Entity. So, if you have received a document of the client, how did you decide whether that document was reliable? (…) We have a mandatory template for that, which you always have to fill in. If you did not do that, you have a problem so to say. That kind of thing makes the quality of your file go up slowly but surely. Of course it can always improve, but I think we are making progression." (Interview 1, staff)

However, this standardization may also have its adverse effects. It might lead to people being less critical towards the work they perform, and just performing on some sort of auto-pilot:

"Well, the goal is more consistency in a file, and also in the different documents. I think myself, so to say, I see the big danger that you stop thinking because of that. Because if you are checking a certain account, and if you have those standard templates, then you'll just finish off those standard templates. That makes you think less, and just do what that says. But suppose you can prepare it all yourself, a working paper, that triggers you to really think about it. What is the goal? Which activities do I have to perform to achieve that goal? So I think that standardisation has a negative impact on your audit quality." (Interview 7, senior staff)

In line with the role of standard procedures, audit quality also has to do with management at the start of the audit, and making a good engagement plan. Having a clear plan of what to do may improve audit quality:

"It [audit quality] does not just have to do with the client, but also clearly with management at the start of the engagement, making choices at the beginning of the engagement, How are we going to audit it? You need to think well about the tools you use, and how you use those tools, and if it is possible to even use those tool (...). It is also about management of people or team composition. And if you know, I'm sorry to say so, but that you get a lot of interns, then you have to provide enough guidance for them. (…) guidance needs to be good, you can't leave people to their fate." (Interview 3, senior)

Good planning also plays a role in the ability to work systematically and structured. During the busy season, a good plan of approach can help in working more efficiently:

"Factually, the busy season is just all companies having an annual report which has to be audited. That's where you return to the phase of planning, if you have performed that well, then you know what is going on, and what can be going on. That's also where experience comes around the corner. How did that play out in the last couple of years? What did take a long time? What did cost less time? Those are things that you can consult in the making of the next plan of approach. That's the way you can set up a very efficient audit with which you can finish within the agreed upon timespan. Busy season will still be busy, but if you do that, it becomes easier." (Interview 5, staff)

In contrast to this, the risk analysis is something that may happen throughout the entire audit period. This is because, during the audit unexpected events may occur. Things may disappoint or be better than expected. This means that during the entire audit process it is needed to react on new matters. So, if this is the case, following an exact plan of approach may become nearly impossible.

Something that may however help in avoiding these unexpected events is data-analysis and process mining:

"We have internal professional meetings, which are directed into the usage of data-analysis and process mining. There are some partners that have seen the advantage of this, because it can map processes that they hadn't seen before. And if, in the early phase of the audit, so in the planning phase, you acknowledge that, then you can take it with you in the audit. At that moment you know, that everything that you could know, and everything that you could have done, that that is implemented [into the audit]" (Interview 5, staff)

Data-analysis can help in obtaining insight into a company more quickly. This acquired insight can help in forming a plan of approach that is clearly adjusted to the characteristics of the client firm:

"With data-analysis you can for example print a map of a ledger. With that you can see which bookings are made during the year in the ledger, who did it, when it happened. (…) For example with turnover, if you have a trading company that sells a lot of seasonal stuff, you would expect a peak in the vacation period or in December during the holidays. If you don't see that, and you see with the help of data-analysis that that doesn't happen, then you can asked aimed questions to people. To management or other people that are involved in the process. (...) I think the main advantage of data-analysis is that you can easily and quickly obtain insight in processes. Process mining is actually the same, but at the process level. So, which processes are the base of, for example, generating income. And if you start the process-mining, and subsequently see, this process is responsible for this turnover, this process is responsible for that turnover. Eventually you get a list, this is the turnover, and these are the underlying processes. Then you can simply ask yourself whether you have included all of them in the interim." (Interview 5, staff)

Of course, it is important to note here that data-analysis and process mining are quite new concepts. So, they will not be fully developed. This means that they probably cannot guarantee that no unexpected events occur. However, it can reduce the likelihood of that happening.

Despite the benefits of data-analysis and process mining, there are still things that can be different than what was planned, which cannot be predicted by these methods:

"Before you start you can make a very good planning, so you can make a good estimation of how much hours you need, from which level, and how many years of experience. But it can always happen that a colleague becomes sick, that a colleague quits, or that the client made a mess of it himself. You can't estimate those things upfront, but you do encounter that during the year." (Interview 6, senior manager)

In sum, working structured and systematically might help in improving audit quality. The more standardized documents become, the more clear they will be for interpretation of others, and the more help they might be in the next audit. Furthermore, working more structured might help in avoiding missed steps. However, it may also have the disadvantage of reducing critical thinking. A good plan of approach is something that can improve audit quality. To improve the quality of the planning phase, data-analysis and process mining can help in getting a scope of the client firm. This helps avoiding unexpected events. However, not all events can be avoided.

4.4. Audit quality described by accountants compared to the tone at the top

While conducting the interviews, the case office had a program in which audit quality was heavily emphasized. This allows to compare the answers of the respondents with the vast amount of e-mails that was sent in order to communicate the factors of the program. So, the tone at the top can be compared with what the respondents acknowledged in practice.

These e-mails where mainly aimed at achieving a high score in audit quality reviews (AQR). These AQR's are an internal program, to check audit quality, and to maintain audit quality as something that is kept in the spotlight. Key considerations in this program include:

1. Focus on the application of professional scepticism – "*This is defined as having an attitude that includes a questioning mind, being alert to conditions which may include possible misstatement due to fraud or error and a critical assessment of audit evidence.*

Our audit methodology requires the application of due professional scepticism throughout the audit, especially in relation to evaluation of the risk of fraud or other areas of significant risk." *(Internal e-mail correspondence, 23-5-2018).* Previous AQR's showed that this may especially be problematic in areas involving the audit of fair values, asset impairments, going-concern or other accounts that involve that involve significant client estimates or judgment.

2. Focus on the involvement of the EQR (Engagement Quality Review) and effectiveness of the EQR process – The EQR process is a process where an engagement is reviewed by an audit partner, other than the one that performed the audit itself, to check the quality. *"For any significant AQR findings an assessment will be made on whether they should have been identified also as part of the EQR process. It is also important to identify good practices in the execution of the EQR process and communicate these to the office." (Internal e-mail correspondence, 23-5-2018).*
3. Evaluation of audit documentation – *"In addition to planning and performing audit procedures in accordance with professional standards and firm guidance, the execution of a high quality audit includes appropriately and contemporaneously documenting – in the audit work papers – the audit plans and approach and the audit evidence gathered and evaluated during the audit, including disconfirming evidence and the related conclusions." (Internal e-mail correspondence, 23-5-2018).*

The first point is something that does not completely seem to match with the definition of audit quality that was found in the interviews. Having a grasp of the company, and being able to explain everything that occurs at that company is one thing. Having a critical outlook towards these internal processes is another. Respondents did of course acknowledge the importance of being critical when asked, but it was not something that immediately came to mind when discussing what the most important aspects of audit quality are. The aspect of critical thinking seems to be much more present in the organizational view of quality, the tone at the top, than the view that is used in practice. This may however also have to do with that respondents did think of critical thinking as something that is so self-evident, it was not named in the interviews.

The second point can be found back in the answers by respondents, albeit indirectly. Multiple respondents noted that lately more emphasis was being put on audit quality, and that quality was tested more often. Including more factors that involve quality into the EQR is in line with this statement.

The third point was something that auditors named as a factor that could influence audit quality. Good documentation may help in performing a better audit next year, since this allows to consult with documents of previous years. This statement was laid out in section 4.3.5. What the internal correspondence did however not take into consideration are the adverse effects this might have, that more extensive documentation might lead to less critical thinking. This view is directly opposed to what internal correspondence stated.

Further internal e-mails sent to the whole company state five points that should be considered to aim the company culture more towards audit quality:

"You will undoubtedly already be aware of the must-haves for a quality-oriented culture. We have defined five: work and document in accordance with the [audit firm name] method, manage your projects properly, ensure effective team meetings, use data analytics, and ensure effective coaching and reviews." (Internal e-mail correspondence, 15-5-2018)

All of these five points passed by in the interviews to a certain extent. This means that the points that are stated here are acknowledged in practice.

In sum, the view of audit quality is generally in line with the tone at the top. There are however some aspects in which they differ from each other. This indicates that the way a person looks at what is audit quality is, might be affected by context. A uniform definition might be impossible to give. What however seemed to be much emphasized by the people that have to deliver quality is that it is important to fully understand a client firm, and get insight in their processes.

5. Discussion & Conclusion

5.1. Conclusion

The thesis forms two main conclusions: (1) What the meaning of audit quality is in practice and (2) what important determinants of audit quality are. Both the meaning of audit quality and the determinants of audit quality show some similarities and some differences to existing theory.

5.1.1. The meaning of audit quality

Audit quality is a concept that can be hard to define. This has to do with the multiple viewpoints on the matter, and the multiple factors that come into play. From an accounting perspective, an important aspect of audit quality is that conclusions can be drawn with enough certainty. Getting a good understanding of the client firm and following audit standards are an important part of this.

This is not entirely in line with the definition handled by DeAngelo (1981), which states the following:

"The quality of audit services is defined to be the market-assessed joint probability that a given auditor will both (a) discover a breach in the client's accounting system, and (b) report the breach. The probability that a given auditor will discover a breach depends on the auditor's technological capabilities, the audit procedures employed on a given audit, the extent of sampling, etc. The conditional probability of reporting a discovered breach is a measure of an auditor's independence from a given client."

Respondents seemed to note that a good audit will include discovering breaches in the clients accounting system and reporting these discoveries. However, the definition was seen as incomplete, and missing relevant aspects. It does for example not include the extent to which an auditor understands the client, the aspect of efficiency and timeliness, and the compliance with auditing standards. From an auditor's perspective, all of these notions are of importance.

5.1.2. Determinants of audit quality

The factors that influence audit quality according to the literature are often also acknowledged by respondents to occur in practice. Out of the named factors, only quasi rents and client size seemed to be something that was not recognized. This may however have to do with the situation on the job market for auditors in the Netherlands, which reduces the pressure for audit firms of having to maintain clients.

Multiple determinants of audit quality where found in the case study. Some are in line with existing theory, and some differ from existing theory.

In the case study, a certain learning curve could be observed. Where audit quality increases over time, as a result of more client knowledge that is obtained over the years. Auditors stated that this learning curve seemed to decrease over time. As an auditor gets to know the client better after every year, the increase of knowledge obtained per year decreases. A certain optimum, or maximum, of client knowledge that can be obtained seems to exist. The case study findings are also in line with the learning curve of Geiger & Raghunandan (2002). In addition, another finding in the case study was that client characteristics may change over time. This leads to client characteristics having to be assessed again. This makes the learning curve more dynamic. This finding can be used as an addition to Geiger & Raghunandan (2002), as they do not acknowledge that client characteristics may change over time.

In the case study, this learning curve theory seemed also to be present for specific industries. In general, this implies that due to industries having their own regulations, and having different accounts that can be of importance, an auditor can benefit from obtaining knowledge in a specific industry. This is in line with the findings of Solomon et al. (1999) who find that industry expertise leads to more knowledge of financial statements in that industry for auditors. Industry expertise can thus help in having more initial knowledge of a client in that industry. The learning curve effects seems to be applicable for industry knowledge.

Another finding in the case study was that client familiarity may lead to lower audit quality. Familiarity may lead to auditors being tempted to just repeat the steps performed in previous audits. This results in a less critical assessment of the clients financial statements. In general, this implies that too much familiarity to a client may lead to less audit quality. This finding is in line with the statements of Corbella et al. (2015), who argue that too much familiarity to a client may result in stale audits, and a decreased likelihood of the auditor taking decisions that are contrary to decisions taken in the year before. Shockley (1981) adds to this that complacency, a lack of innovation, less rigorous audit procedures, and a developed confidence in the client may occur after extended tenure. The statements of both these studies are in line with the findings of the thesis in that they both find that client familiarity leads to a less critical assessment of the client.

Auditors in the case company did not seem to be influenced by the size of the client firm, and mainly focusing on efficiency of a client. This might be in part due to the situation of the Dutch audit market, where big audit firms are reducing their amount of clients. In general, this implies that this relation might be vastly different in another audit market. The finding that audit quality is not influenced by the size of the client firm is opposed to the argumentation of Gul (1991), who argues that as a client is larger, and thus represents a larger part of income, the audit firm would be more dependent on the client.

Respondents did not seem to have their independence influenced by the financial condition of the client. Financial condition did affect auditor judgment in that the risk assessment laid out other priorities, but played no role for auditor independence. This is not in line with Knapp (1985) who argues that independence of an auditor decreases if the client is in good financial condition, because in that scenario there is not much risk for legal exposure. Legal exposure seemed not to invoke much concern. Concern was more with delivering audit quality for check-ups, which would be independent of client financial condition. This might mean that the fear of legal exposure might be smaller in practice than is thought.

Just as was the case with client size, auditors did not seem to be involved that much with audit fees, and seemed to prioritize other things. In general, this might mean that quasi rents do not play that big of a role in practice. This is not in line with DeAngelo (1981), who argues that auditor independence in initial years of an audit will be lower, because the auditors wants to earn back costs incurred in the initial year.

Auditor capabilities seem to play a role in in the case study. The most emphasized quality in the case study was experience. In contrast to this Corbella et al. (2015) argue that auditor characteristics that influence the ability to perform audits of high quality are education, training and knowledge of professional standards, independence and objectivity, their knowledge of a client's operations and industry, and an auditors working relationship with the management of the client firm. The argumentation of Corbella et al. (2015) and the findings of the case study can correspond to each other. Experience does seem to influence multiple of these factors. An auditor's knowledge of professional standards and specific industry knowledge come with experience. Furthermore, experience helps with the ability to withstand client pressure, and thus increase independence and objectivity, makes it easier to get to know a client's operations, and helps in knowing how to act towards management of the client firm. So, experience might be an important underlying factor for improving important characteristics that are named in existing literature.

Another finding in the study revolving around auditor characteristics is that the right team composition can be of importance for audit quality. With the right team composition an audit team can supplement each other, and make up for each other's shortcomings. In general, this implies that attention should be paid to having the right characteristics represented in an audit team. This finding does not seem to have much recognition in existing literature.

The case study indicated that time constraints make auditors rush work, work overtime and spread their attention over multiple clients. This leads to tiredness and less focus on clients. Unexpected events may make these factors even stronger, as there unexpectedly may be a need for more audit hours on an engagement. Time constraints may lead to a less critical attitude, as a way of completing an audit in less time. Thus, time constraints have a negative effect on audit quality. In general, this indicates that audit quality may be influenced by the effect of supply and demand in the audit market. The finding that audit quality is influenced by time constraints is in line with Deis & Giroux (1992), who argue that audit hours can be a suitable surrogate for audit quality, which implies that more time spent on an audit means better audit quality, and thus limited hours lead to less audit quality. How time constraints affect audit quality was however something that was not paid much attention to in existing literature.

In the case study, several factors influencing audit quality that were absent in the literature were found. These are divided in two categories: client characteristics and working systematically and structured. The two categories might have been overlooked for their own reasons. As a result of the quantitative nature of existing research, client characteristics might have been overlooked. The positivistic nature of this research asks for a generalization to be made of findings. Transforming clients into homogeneous entities is something that makes generalization of results easier. However, due to industry market shares not being divided equally between audit firms (Francis, 2004), this might be an important factor in determining results. Working systematically and structured might be an aspect that is overlooked in existing literature, because it revolves around the inner processes of an audit firm. The methods handled by auditors is something that does not seem to occur often in existing literature. This may be a result of existing research mainly focusing on measurable characteristics of audit firms. As a result of this, the methods handled by audit firms seem to be generalized.

In the case study client characteristics seemed to be the dominant factor deciding audit quality. A first client characteristic deemed to be of importance in the case study is the typology of a client, where different typologies require different insights. Experience in a single typology may help in the next audit for the same typology. So, in general, typology experience may help in audit quality. A second characteristic that may influence audit quality is the quality of internal controls of the client. If the auditor can trust in the processes of the client, there is less reliance on samples required. This means that conclusions can be drawn with more certainty. A big client may have more possibilities to implement good internal controls, however this is not necessarily the case. A third characteristic found in the case study is that big clients might be more complex to audit than small clients, if the internal controls are assumed to be equal. A big client has more processes going on, and more influences on the firm. This makes the audit process more complex. A fourth characteristic found in the case study is client attitude. At a client that is willing to cooperate with the auditor, the auditor is more likely to achieve high audit quality. This is because the client aiding in obtaining the right documents and required information results in an easier completion of the audit, which can consequently be done more effectively.

Another factor which is fairly overlooked by existing literature is the effect of working systematically and structured. The case study indicated that this might help in accessing previous information more clearly, and in making sure that all necessary steps are performed. However, this might also lead to the drawback of auditors not thinking critically enough, and just performing the required steps. In general, this factor seems to play a role, but it is unsure what this role is exactly. Furthermore, making a good plan of approach before the audit might improve audit quality, as it makes more clear what activities have to be performed. Data-analysis and process mining might support this process. However, not every unexpected event can be accounted for by doing this.

5.2. Discussion

Of course, not all factors are as clear cut from each other as it may seem here. Many of the factors do have a relation to each other. For example, becoming specialized in a sector might result in obtaining knowledge of a client in that sector faster. Another example is that client characteristics decide the quality of the deliverance of information, which may affect the required time, and thus time constraints. This indicates that for many of these factors considerations have to be made. For example, audit quality increases the more knowledge an auditor obtains of the client, but too much familiarity to the client leads to less audit quality. This means a balance between these two factors needs to be found, to find how long an auditor should be active at the same client.

This thesis contributes to the literature by looking at “how” audit quality is determined in practice, whereas existing literature is mainly involved with “if” audit quality relates to a certain factor. This broad outlook allowed for finding more factors than were currently present in the literature, and allowed to delve deeper into the workings of factors contributing to audit quality.

The thesis poses practical relevance in that the found determinants of audit quality can be assessed and used by audit firms to look at factors that increase quality. Taking these factors into considerations while forming policy might help in achieving a higher audit quality.

Further quantitative research might look into the effect that client characteristics have on audit quality. This could for example be done by implementing the typology model of Starreveld, looking at client firm size, or looking at client industry. These considerations for client pool might be important, since Francis (2004) noted that the client portfolios of accounting firms may be different from each other.

Another direction for future research is that a similar research could be done under different circumstances. The situation on the Dutch audit market, could have led to less problems with auditor independence, as auditors were not afraid to lose clients. This situation might be vastly different in another market.

Furthermore, it might be a possibility to look at the situation of a non-Big 4 firm as the attitude towards a client might be completely different at those firms. This might especially be an interesting research direction, since non-Big 4 firms will have clients that differ a lot from Big 4 firm’s clients.

A limitation of this thesis includes that audit quality may be a touchy subject for some respondents, as they do not want to say that they deliver bad quality. For example, one respondent noted after the interview that he had to look after his wordings with certain questions, and that that was something that should be looked through in the research.

What also should be kept in mind is that this thesis is mainly concerned with looking at what determines audit quality from an auditor’s perspective. It might be insightful for future research to also look at what forms audit quality in the eyes of client firms or of an oversight board.

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