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AN EMPIRICAL INVESTIGATION OF  
WIRTSCHAFTSPRÜFER INDEPENDENCE

By

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## ABSTRACT

### AN EMPIRICAL INVESTIGATION OF WIRTSCHAFTSPRÜFER INDEPENDENCE

By

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German auditors (Wirtschaftsprüfer) have been severely criticized in the financial press and the German accounting literature. Wirtschaftsprüfer (WPs) have been accused of lacking independence on a number of occasions. This study investigates empirically the perceptions of WPs independence by German auditors and by users of financial statements audited by WPs. The controversy surrounding the independence status of the German accounting profession suggests that there may be a considerable lack of consensus among and between WPs and users of audited financial statements concerning the circumstances which would render the auditors not independent in appearance from their audit clients.

In conducting the study, a random sample of WPs was selected to represent the German accounting profession. Two distinct financial statement user groups representing the investors' and creditors' point of view were identified as bank directors of investment departments (LWPs) and bank directors of loan departments

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(LKRs). A non-random sample of the larger banking institutions located in the 12 largest cities in Germany was selected and questionnaires (written in German) were mailed to each of the banks, one questionnaire to the director of the investment department and one to the director of the loan department of the selected banks, as well as to the random sample of Wirtschaftsprüfer. Branch banks were included for a few of the very large banks only.

The questionnaire contained a number of separate auditor-client relationships for which the sample subjects were asked whether they considered the auditors involved to be independent or not independent from their audit client. The types of auditor-client relationships investigated included the following categories:

- (a) Financial interest (direct and indirect)
- (b) Bookkeeping and EDP services
- (c) Family relationships
- (d) Occupations with conflicting interest
- (e) Business and other similar relationships

LWPs and LKRs were also asked to indicate on a five-point Likert-type scale the extent to which each of the situations would affect their financial decisions, a "1" representing a strongly negative influence and a "5" representing a strongly positive effect on their financial decisions.

The results of this study indicate that for most of the auditor-client relationships investigated there were no differences in the majority responses between the three experimental groups. In only 3 out of a total of 27 auditor-client relationships



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did the majority response of WPs differ from the majority response of both financial statement user groups. LWPs and LKRs were of divided opinion on 4 auditor-client relationships which implies that WPs agreed with one user group but not with the other.

The hypothesis tests of whether there is a consensus within each of the three experimental groups indicated that for a significant number of situations the null hypothesis of no consensus could not be rejected at a confidence level of 95 percent. Consensus was defined as a statistically significant majority of opinion using the Binomial Test. The WP responses showed no consensus in 9 out of 27 situations. The number of auditor-client relationships on which LWPs and LKRs could not reach a consensus were 11 and 7, respectively. Of the 9 situations on which WPs could not reach a consensus concerning the auditors independence status none are specifically disallowed by currently effective regulations covering the ethical conduct of Wirtschaftsprüfer.

The results of testing the effect of financial statement users' perceptions of auditors' independence on their financial decisions revealed that for most of the auditor-client relationships investigated there was a statistically significant effect at a confidence level of 95 percent. For those few situations in which no effect was determined, the results could have been due entirely to chance since multiple t-Tests were employed.

Based on this study's findings the following conclusions can be made:

(a) perceptions of independence by third parties appear

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to be a factor in the decision model of audited financial statement users for financial decisions, and

- (b) more specific guidelines are needed for WPs to better ensure their independence. Guidelines seem to be especially needed for those types of situations in which no consensus was reached within any of the three experimental groups and those situations in which WPs disagreed with one or both of the financial statement user groups.

ZU MEINEN ELTERN

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## CHAPTER ONE

### INTRODUCTION

This study investigates empirically the perceptions of German auditors' (Wirtschaftsprüfer) independence by German auditors and by users of financial statements that are audited by German auditors.

One of the major issues facing the German accounting profession is the independence of auditors from their clients. German accountants have been the target of some severe criticism in the financial press and in the accounting literature.<sup>1</sup> Some of this criticism is similar to the criticism expressed in the United States, questioning the auditors' ability to remain independent from those who pay their audit fees.<sup>2</sup> Even though the independence of Wirtschaftsprüfer (WPs) has been questioned for a long time, the call for better conventions and regulations has become more accentuated in recent years.<sup>3</sup>

Various cases of corporate bankruptcy occurring shortly after an unqualified opinion had been issued have raised some doubts about the value of the WPs' work and their ability to arrive at objective and unbiased decisions.<sup>4</sup> Suggestions have been made to strengthen the WPs' independence status by having more specific rules guiding the auditors' conduct, changing the liability laws to allow a third party to sue for damages for less than

only gross negligence by the auditor, establishing an SEC type government agency, etc. These suggestions are discussed in more detail in Chapter Three.

The reason auditors' independence has been an issue for so long, in Germany as well as in the United States, is inherent in the unique role of the auditor in the business society and the intrinsically difficult problem of applying the concept of independence to the real world. The auditor is engaged and paid by his client (the auditee) to express an opinion on the auditee's financial statements. These financial statements are then used by third parties (users of financial statements) as one source of information on which to base economic decisions. Thus, the auditor's primary responsibility is to the users of financial statements, and the main purpose of the audit function is to lend credibility to the financial statements to help protect lenders and investors and to provide for a more efficient flow of capital.

In order to fulfill the function assigned to him by society, the auditor must be independent from his client, i.e., he must be able to form his opinions and audit judgments objectively and derive these in an unbiased fashion.

Thus, the auditor's independence is one of the most, if not the most, important auditing standards. The Chairman of the Securities and Exchange Commission (SEC), H. M. Williams shares the view of many when he says that "independence is the auditor's single most valuable attribute".<sup>5</sup> However, the concept of independence has come to mean not only the ability of the auditor

to make objective and unbiased decisions while performing the audit, but also that others believe that he is able to do so. The former is usually referred to in the U.S. accounting literature as independence in fact and the latter as independence in appearance. For an auditor to fulfill his role as an unbiased judge of financial statements, he must be both.

Even though these two types of independence are implicit in the audit function, they are explicitly demanded from the German auditor by law and regulations<sup>6</sup> as they are required for U.S. auditors by their Code of Ethics and SEC rulings.<sup>7</sup>

Independence in fact is an individual auditor's perception concept and may differ between auditors. Consequently, in a situation where one auditor will decline an audit engagement because he feels that he is not able to make independent audit decisions, another auditor may honestly believe that he can make independent decisions. As discussed in Chapter Three, this type of independence is not objectively measurable and it is not practical to devise any specific rules dealing with independence in fact.

This study deals with independence in appearance as perceived by WPs and by German bank directors of loan departments (LKR) and investment departments (LWP). As is explained more fully in Chapter Three, specific rules are appropriate to deal with independence in appearance. It is felt that this study will provide empirical evidence of how WPs and two important financial statement user groups perceive the appearance of auditors' independence in order to determine the extent to which specific rules on independence in appearance are needed. Due to the types of

auditor-client relationships investigated, this research may also be helpful in providing U.S. rule making bodies and U.S. practitioners with some insight as to how auditors in another country view some of the independence issues.

### Research Objective

The controversy surrounding the independence status of the German accounting profession, as expressed in the German financial press and accounting literature, suggests that there is a considerable lack of consensus concerning the circumstances which would render the auditor not independent from his audit client. Such lack of agreement may imply that:

- (i) perceptions of what constitutes an independent (or not independent) auditor-client relationship differ between auditors themselves and/or between auditors and users of financial statements; or
- (ii) current independence rules and regulations are perceived to be insufficient (or even improper) by users of financial statements and perhaps by WPs, as some criticism by accounting practitioners seems to indicate;<sup>8</sup> or
- (iii) it is a combination of the first two factors.

This investigation attempts to clarify the "state of being" of these perceptions and their meanings. To broaden the scope of this study, the situations investigated include a number of auditor-client relationships for which the American Institute of Certified Public Accountants' (AICPA) and the SEC's position concerning auditors' independence is known.

The objective of this research is four-fold: first, to investigate the German accounting profession as to its regulations,



laws, guidelines and literature that relate to this study of WPs' independence; second, to provide empirical evidence concerning the perceptions of auditors' independence in appearance within the German auditing profession, and between WPs and users of financial statements audited by German auditors; third, to determine whether the financial decisions by users of financial statements are affected by their perceptions of the independence status of the auditor; and fourth, to compare how German auditors' perceptions of independence differ from the positions taken by the AICPA and the SEC as to the relationships between auditor and auditee that render the auditor independent or not independent.

### Research Hypotheses

The various hypotheses to be tested are stated in their null form below. The research hypotheses and their statistical forms are presented in Chapter Four. There are a total of nine different hypotheses:

- I.  $H_0$ : There is no consensus among Wirtschaftsprüfer (WPs) regarding their perceptions of the concept of auditors' independence.
- II.  $H_0$ : There is no consensus among Leiter der Kreditabteilung (LKRs) of banks located in Germany regarding their perceptions of the concept of auditors' independence.
- III.  $H_0$ : There is no consensus among Leiter der Wertpapierabteilung (LWPs) of banks located in Germany regarding their perceptions of the concept of auditors' independence.
- IV.  $H_0$ : There is consensus among Wirtschaftsprüfer (WPs) regarding their perceptions of the concept of auditors' independence that coincides with AICPA rulings on independence.

- V.  $H_0$ : There is consensus among Wirtschaftsprüfer (WPs) regarding their perceptions of the concept of auditors' independence that coincides with SEC rulings on independence.
- VI.  $H_0$ : There are no differences regarding the perception of the concept of auditors' independence between Wirtschaftsprüfer (WPs), Leiter der Kreditabteilung (LKR) and Leiter der Wertpapierabteilung (LWP) of banks located in Germany.
- VII.  $H_0$ : There are no differences regarding the perception of the concept of auditors' independence between Wirtschaftsprüfer (WPs) and Certified Public Accountants (CPAs).
- VIII.  $H_0$ : Leiter's der Kreditabteilung (LKR) perceptions regarding the concept of auditors' independence have no effect on their lending decisions.
- IX.  $H_0$ : Leiter's der Wertpapierabteilung (LWP) perceptions regarding the concept of auditors' independence have no effect on their investment decisions.

### Importance of the Study

The importance of this research lies not only in its contribution to German accounting practice but also to accounting practice in the United States and international practice of professional accounting. Each category is discussed separately.

### Contribution to German Accounting Practice

The German auditor's conduct is guided mainly by general rules, regulations and conventions. There are only a few types of auditor-client relationships which are specifically prohibited due to lack of auditors' independence in appearance. The German auditor does not have the advantage of his U.S. counterpart, especially those CPAs with SEC clients, who can consult a lengthy

casuistry such as Accounting Series Releases (ASRs) 126 and 234 which enumerates circumstances that will impair independence. Empirical evidence indicating how German auditors perceive the concept of independence would provide some insight concerning how practitioners have been interpreting those general rules of conduct and whether the practitioners are in agreement with some of the specific rules in existence for German auditors. Any lack of consensus among WPs' perceptions of independence would suggest a need for more specific guidelines.

By investigating the perceptions of German financial statement users concerning auditors' independence, a better understanding of how these users' perceptions of independence differ from those expressed by WPs can be gained to determine potentially sensitive auditor-client relationships. Since the two financial statement user groups were asked to indicate how their independence perceptions would affect their financial decisions, the results of this study will provide some evidence as to whether WPs' independence is as important an issue as is claimed in the literature.

#### Contribution to U.S. Accounting Practice

This study investigates areas of conflict regarding the concept of independence for the German auditing profession. However, since the purpose of auditing is, or should be, similar for all countries as long as the economic systems are similar, the areas of conflict chosen are, with few exceptions, also areas of conflict in the United States.

Even though the auditor-client relationships investigated

are limited due to the nature of the research tools employed, an effort was made to include situations between auditors and their clients which are of particular interest to the U.S. accounting profession due to differences in independence rules promulgated by the AICPA and the SEC. Thus, this study may provide empirical support for either the AICPA or SEC position regarding auditors' independence. In a sense it may also serve partly as a follow-up study of prior research done in 1973 by Lavin concerning the independence status of U.S. auditors.<sup>9</sup> Lavin's research included a mail survey questioning CPAs and two different financial statement user groups as to their perceptions of auditors' independence for a variety of different auditor-client relationships. He found that the respondents to his survey did not as a whole agree with either the positions taken by the AICPA or the SEC on auditors' independence.

Furthermore, this study will give limited insight to U.S. auditors who must rely on the work of German auditors that is incorporated in the U.S. parent company's consolidated financial statements, as to the degree to which their German counterparts agree with U.S. rules on independence. Even though perceptions on independence may not be substituted for actual behavior, questions could be raised if the results show that German auditors tend to disagree with most U.S. independence rules. For example, the SEC, via ASR 112, requires foreign auditors of a U.S. subsidiary, with minor exceptions, to conform to the SEC standards of independence in an audit of the consolidated financial statements of a U.S. corporation.

Considering the size of U.S. direct investment which at the end of 1977 had a book value of \$10.4 billion, and the fact that Germany has the most highly industrialized economy in Europe,<sup>10</sup> would suggest that an investigation into the independence of their auditors may be of benefit to a rising number of non-German investors of German corporations. It has been suggested that there is not a very high correlation among the movements of world stock markets which implies that the risk of a given stock portfolio could be reduced by diversifying abroad. For example, Morgan Guarantee Trust Co. aims to have approximately five percent of the \$10.2 billion employee benefit fund equities it manages invested in foreign stocks.<sup>11</sup> It is predicted that this trend of U.S. financial institutions investing in foreign stocks will increase in the future.<sup>12</sup>

It seems that three factors: the soundness of the German economy, the relative stability of its currency supported by the second largest exporting industry in the world, and an inflation rate consistently among the lowest of all Western countries, make stocks of German corporations a prime target for U.S. and other non-German investors.

#### Contribution to International Accounting Practice

At the 11th International Accountants Congress, hosted by the German accounting profession in Munich in October of 1977, the International Federation of Accountants (IFAC) was founded. The IFAC is comprised of 63 organizations representing 600,000 accountants in 49 countries and replaces the 11-nation International

Coordinating Committee for the Accounting Profession (ICCAP).

The purpose of the IFAC is to develop compatible guidelines in technical, ethical and educational areas for the international accountancy profession.<sup>13</sup> Its first president is Dr. Goerdeler, a past president of the German Institute of Certified Public Accountants (Institut der Wirtschaftsprüfer).

International accounting standards are issued by the International Accounting Standards Committee (IASC) which thus far has issued ten International Accounting Standards. Even though the IASC has not yet dealt with the standard of independence, it is just a matter of time until it will have to confront this issue. Any empirical evidence, even if it is, in a strict sense, limited to the accounting profession of one country, may prove helpful for the decision making process of this international accounting body.

The German accounting profession appears to be of special interest since it is one of the best developed professional accounting bodies in Western Europe.<sup>14</sup>

Consequently, investigating how German auditors perceive auditors' independence should play a role in the formulation of any international accounting or auditing standards.

#### Summary and Outline of Research

This study attempts to provide some empirical evidence concerning the perceptions of auditors' independence as perceived by German auditors and two user groups of financial statements. The concept of independence is made up of two parts -- independence in fact

and in appearance. Independence in appearance is a collective perception concept that rests on an empirical foundation. It is this part of auditors' independence which is investigated in this research effort.

However, this investigation is constrained by the limited number of auditor-client relationships, and any conclusions reached must of necessity be confined to those situations investigated.

This research is presented in six chapters. In Chapter Two the German accounting profession is discussed, including the professional duties of WPs and their organizational structure. The German accounting literature is reviewed in Chapter Three. In the same chapter a framework is developed to resolve the independence problem, given certain assumptions. Chapters Four and Five deal with the research design employed and the results of the survey, respectively. A summary, conclusions and suggestions for future research are presented in Chapter Six.

## CHAPTER ONE -- FOOTNOTES

1. See Chapter Three for a discussion of some of the criticism.
2. For the most recent criticism on the U.S. accounting profession, see The Accounting Establishment: A Staff Study, by Lee Metcalf, Chairman (Washington, D.C., U.S. Government Printing Office, 1977).
3. Two of the more vocal critics are: Kicherer, H-P., "Zur Unabhängigkeit des Abschlussprüfers," Die Aktiengesellschaft (February 1972) pp. 37-40; Richter, M., "Die Stellung des Abschlussprüfers im Entscheidungs - und Kontrollprozess der Aktiengesellschaft," Diskussionsbeiträge - Fachbereich Wirtschaftswissenschaft, Universität des Saarlandes (September 1977).
4. The Herrstatt Bank bankruptcy in 1974 is one of the better known cases which was also covered in the U.S. financial press. See, Kruk, M., Wirtschaftsprüfer als Aufsichtsräte? Gefahren für den Ruf des Berufsstandes, Frankfurter Allgemeine Zeitung (April 9, 1975) p. 13.
5. The CPA letter (January 23, 1978) p. 1.
6. Gesetz über eine Berufsordnung der Wirtschaftsprüfer (Wirtschaftsprüferordnung) i.d.F. der Bekanntmachung der Neufassung v. November 5, 1975 (Düsseldorf, IdW-Verlag GmbH, 1976) pars. 43 and 49.
7. For AICPA rulings see: Code of Professional Ethics, American Institute of Certified Public Accountants (March 1975 ed.); for SEC rulings see: Rule 2-01 of Regulation S-X as discussed in: Accounting Series Release No. 126 (July 5, 1972).
8. See Huppertz, W., "Die widersprüchliche Lage des Wirtschaftsprüfers bei der Abschlussprüfung," Blick durch die Welt--Handelsblatt (November 4, 1976) pp. 4-5.
9. Lavin, D., "Perceptions of the Independence of the Auditor," The Accounting Review (January 1976) pp. 41-50.
10. Overseas Business Reports, U.S. Department of Commerce (December 1977) p. 11.
11. Has Morgan Started Something?, Forbes (April 3, 1978) pp. 114.
12. Ibid.



13. The CPA letter (October 24, 1977) p. 3.
14. See Lafferty, M. J., "Dominant in Europe," The Accountant (November 14, 1974) pp. 640-644.

## CHAPTER TWO

### THE GERMAN ACCOUNTING PROFESSION

In this chapter the German accounting profession is discussed by focusing on the following main areas:

1. Organization and structure of the German accounting profession
2. Professional qualifications
3. Purpose of the German auditor's Opinion (Bestätigungsvermerk)
4. Development and sources of accounting and auditing principles and standards
5. Professional duties and responsibilities of Wirtschaftsprüfer.

The purpose of this discussion is to present a cursory overview of the German accounting profession and to provide the necessary background to interpret the research findings as to its applicability to U.S. and international accounting practice.

#### Organization and Structure of the German Accounting Profession

Mandatory audits of corporations are performed in Germany by Wirtschaftsprüfer (WP), roughly the equivalent of the Certified Public Accountant (CPA) in the United States. Even though the auditing function dates back to at least the Nineteenth Century, it was not until 1931 that the profession of WP came into existence by government action.<sup>1</sup> At this time, the Institut der Wirtschaftsprüfer (IdW) was founded with the purpose of developing accounting

and auditing principles and standards by advising the Legislature on accounting and auditing matters and by issuing various Opinions (Fachgutachten) and Statements (Stellungsnahmen). The IdW, as Abel points out, "is a professional association in many ways similar to the American Institute of Certified Public Accountants."<sup>2</sup>

Membership in the IdW is voluntary, although approximately 87 percent of all WPs are members.<sup>3</sup> Currently, there are about 3,500 WPs and with a few exceptions, all are practicing accountants.

The profession is formally organized into the WP Chamber (Wirtschaftsprüferkammer), a public sector organization which is loosely supervised by the Federal Ministry of Economic Affairs (Bundeswirtschaftsministerium). All WPs must be members of the Wirtschaftsprüferkammer (WPK). The dues collected from each WP make the WPK a financially self-supporting organization, financially independent from the government. In essence, the WPK is run by the profession itself, which was the intention of the government when establishing the WPK.

#### Relationship between the Wirtschaftsprüferkammer and the Institut der Wirtschaftsprüfer

Even though the WPK and the IdW are two separate organizations, the former being an organization of the public sector (Körperschaft des öffentlichen Rechts) and the latter a private sector organization (Verein), the relationship between the two is one of close co-operation. They are both located in the same building, the Wirtschaftsprüferhaus in Düsseldorf, can be reached under the same telephone number, and often use the same stationery with both names in the letterhead.

Since a number of WPs serve on committees of either body, the fact that these are indeed two separate entities becomes somewhat blurred. Nonetheless, the functions of the WPK are primarily to oversee the profession's ethical practices, advise WPs on various matters involving conduct and ethical considerations, initiate disciplinary action when deemed necessary, maintain the professional roster (Berufsregister), and issue and update periodically the Directives (Richtlinien für die Berufsausübung der Wirtschaftsprüfer).<sup>4</sup>

The IdW's function deals mainly with the interpretive technical aspects of the profession. A large number of committees work on various accounting and auditing problems and their findings and recommendations are published by the IdW as Statements (Stellungsnahmen) and Opinions (Fachgutachten).<sup>5</sup> These pronouncements are usually heeded by the profession. Even though they do not have the force of law, a WP must justify departure from any of the IdW's pronouncements. In case of a legal dispute, noncompliance would certainly be considered a negative factor in any court proceedings.<sup>6</sup>

The IdW also has its own publishing house (Verlag) and publishes many books that are of interest to the profession, including all of its in-house work; e.g., The WP-Handbook (WP-Handbuch) and the bi-weekly Die Wirtschaftsprüfung, the IdW's accounting journal.

The WPK keeps its members up-to-date mainly with its publication of the Fachnachrichten and the Mitteilungsblatt der Wirtschaftsprüferkammer, which to some extent duplicate information that is already included in the IdW's accounting journal and/or vice versa.

### Size of the WP Profession

As noted earlier, there are about 3,500 Wirtschaftsprüfer registered in Germany.<sup>7</sup> For a country of over 62 million inhabitants, with per capita income comparable to that of the United States, this is a surprisingly small number. In contrast, the U.S. has in excess of 160,000 CPAs. The question that arises is how such a small body of professional accountants can meet the accounting needs of such a large and highly industrialized country as Germany. Apparently the work is done and, according to officials of the WPK and the IdW, there is no shortage of WPs and there are no plans to increase significantly the size of the profession.<sup>8</sup>

Some of the reasons that may explain the relatively small size of the German accounting profession are:

- (i) A five year work experience requirement must be met before sitting for the WP-exam. (Until recently it was six years). For persons without a Diplom,<sup>9</sup> the experience requirement is ten years.
- (ii) The WPK's Directives allow a one to five ratio of WPs to assistants. Therefore the audit personnel could actually be 21,000 persons and probably is.
- (iii) The Professional Law (Wirtschaftsprüferordnung) prohibits WPs from engaging in incompatible occupations, e.g., employment as an internal auditor for a corporation would result in loss of his WP certificate. Such a person would no longer be counted as a WP, contrary to U.S. practices, where a large number of CPAs are not involved in public accounting but are employed by corporations as controllers, financial officers, etc. Therefore, the number of registered WPs is very close to the number practicing.
- (iv) There are relatively few entities that must undergo a mandatory annual audit.<sup>10</sup>

- (v) There are approximately 15,000 Certified Tax Consultants (Steuerberater) that do most of the tax work and also set up financial statements, similar to unaudited financial statements in the U.S.<sup>11</sup>

Thus given these considerations, it is conceivable that there are indeed sufficient WPs to do the required accounting work.<sup>12</sup>

#### Characteristics of the Profession

The WP profession is predominantly male. Less than two percent of the WPs are female.<sup>13</sup> A large number of WPs (sixty-six percent) are also qualified as Steuerberater, and approximately five percent have a law degree. About thirty percent hold a doctoral degree and a few even hold the title of professor.<sup>14</sup>

The profession is about equally divided into those WPs who are single practitioners and those who practice with an auditing association<sup>15</sup> (Wirtschaftsprüfungsgesellschaft). Most of the Wirtschaftsprüfungsgesellschaften (WPGs) employ less than five WPs. There is, however, some concentration. The ten largest WPGs employ approximately twenty percent of all WPs.<sup>16</sup>

Most of the WPGs are organized as corporations, the majority being limited liability companies (Gesellschaften mit beschränkter Haftung) although a small number are organized as public corporations (Aktiengesellschaften). Both organizational structures permit outside shareholders, even though an Aktiengesellschaft (AG), being a public corporation, is required to publish audited financial statements.<sup>17</sup> Ownership of WPGs by non-WPs is allowed under the law and, to some degree, still exists. The largest shareholder of the biggest WPG, Treuarbeit AG, is the Federal

government of Germany.

A study by Schruoff, published in 1973, disclosed the relationship of shareholders of certain WPGs and shareholders of audit clients and points out the possible illegality of some of these relationships, as well as the shadow it casts on the independence of those WPGs.<sup>18</sup> As a result of this study, some stockholders divested themselves of a portion of their financial interest in WPGs.<sup>19</sup>

#### "Big Eight" International Accounting Firms

All of the "Big Eight" accounting firms are represented in Germany. Five are affiliated with German WPGs, and three are not.<sup>20</sup> Approximately five percent of all WPs are associated with or employed by "Big Eight" accounting firms.<sup>21</sup> Since a large number of these WPs are also associated with at least one German WPG, it is difficult to make any inferences about the market share these "Big Eight" accounting firms have in Germany based on the number of WPs employed. It is not uncommon for a WP to belong to more than one WPG.<sup>22</sup>

It may be of interest to note that most of the "Big Eight" accounting firms are organized as Gesellschaften mit beschränkter Haftung (GmbHs), as are most of the German WPGs.

Even though a GmbH is only liable up to its paid-in capital, a WPG is exempted from this type of limited liability. Regardless of the structure of the organization in which a WP practices, his maximum liability is 500,000 Deutsche Mark per audit. The law mandates that each WP must have sufficient liability insurance. Any agreement that fixes liability below 500,000 Deutsche Mark per audit is void.

### Professional Qualifications

To gain entry to the German public accounting profession, an applicant must meet the requirements delineated in the Wirtschaftsprüferordnung (WPO). The general requirements are:

1. A Diplom from a university in one of the following areas: economics, business, law, agriculture, or engineering.
2. Five years of practical experience, four years of which should consist of relevant auditing experience.
3. Successful completion of a written examination, consisting of questions dealing with auditing, economics, business-economics (Betriebswirtschaft), business law, and tax law. There are seven separate parts taken on seven different days, each lasting between four to six hours.<sup>23</sup>
4. Successful completion of an oral examination before a board of examiners.

To take the examinations, the applicant must have satisfied the five year work experience requirement.<sup>24</sup> The examinations can only be repeated twice and must be passed in their entirety at one time.<sup>25</sup>

It is generally agreed that the examinations are quite difficult



to pass and that people who do not plan to stay in public accounting usually do not take them.<sup>26</sup>

#### Purpose of the German Auditor's

##### Opinion (Bestätigungsvermerk)

An unqualified standard auditor's opinion reads as follows:

"The accounting, the annual financial statement and the management report which I (we) have examined with due care, comply with law and company's statutes."<sup>27</sup>

The audit objective of the German auditor emphasizes compliance with accounting standards as anchored in laws; but, as the codified auditing standards point out, the audit purpose is also that within the framework of compliance with the law the financial statements should "permit as accurate a view as possible of the financial position and results of operation."<sup>28</sup> The WP is not "responsible for the failure to discover defalcations and similar crimes unless he should have discovered them by applying generally accepted auditing standards and techniques."<sup>29</sup>

For comparison purposes, the objective of U.S. audits is stated below: "The objective of the ordinary examination of financial statements by the independent auditor is the expression of an opinion on the fairness with which they represent financial position...in conformity with generally accepted accounting principles."<sup>30</sup>

Since relevant laws are to the German auditor accounting principles which by definition are generally accepted due to the force of law, the audit objective of the WP and of the CPA

are basically the same.<sup>31</sup> Both are interested in a fair view (or as accurate a view as possible) of the financial position of the audited entity within the framework of generally accepted accounting and auditing principles.<sup>32</sup> Consequently, research into German auditors' independence may also be of benefit to the U.S. accounting profession since the audit purposes of the profession in the two countries are compatible.

#### Development and Sources of Accounting and Auditing Principles and Standards

Accounting and auditing principles and standards that must be observed by force of law are determined in general by Federal Company Laws. That accounting principles and standards are based in law is also reflected by the fact that the WP in his audit report does not give his opinion as to the fairness of the financial statements as does the U.S. auditor, but merely attests that the audited financial statements comply with the law.

German Company Law has been a federal matter since 1870.<sup>33</sup> Consequently, "the necessity to treat the issuance of securities as a separate matter of national concern against the backdrop of divergent state law did not arise. The absence of charter-mongering practices may be the reason that Germany has no regulatory enactments comparable to our (U.S.) federal securities laws."<sup>34</sup>

The most recently enacted Company Laws are the Stockcorporation Law of 1965 (Aktiengesetz 1965) and the Disclosure Law

of 1969 (Publizitätsgesetz).<sup>35</sup> Considering that the Stockcorporation Law of 1965 is a revision and update of the Stockcorporation Law of 1937, would suggest that new company laws are very slow in the making.<sup>36</sup> Since law making is essentially a political process, the resulting legislation is often not all-inclusive and requires authoritative interpretation. Commentaries (Kommentare) interpreting and explaining the law are published and revised periodically. There are a number of Commentaries available. Some of the revisions of these Commentaries reflect court interpretations of the law; however, many interpretations are made by the authors of these Commentaries.<sup>37</sup> A number of the authors or co-authors of these Commentaries are WPs, some of whom hold very important positions in the WPK and/or the IdW. The Commentaries are an important authoritative source for the practicing auditor and to some extent help form accounting and auditing standards.

The WP-Handbuch, published by the IdW also provides authoritative guidance to the members of the German accounting profession. It presents interpretations of the laws, directives, rules and regulations, and discusses auditing techniques. The WP-Handbuch is revised every four or five years, (the latest revision was completed in 1977) and could be considered a factor in formulating and applying accounting standards.

Another source of guidance for the WP are the numerous Opinions and Statements by the various committees of the IdW which are generally observed by the profession since, as mentioned earlier, noncompliance may have adverse consequences to the WP in a legal dispute. The IdW's Opinions and Statements serve the same purpose

as AICPA pronouncements concerning auditing and accounting matters and statements issued by the Financial Accounting Standards Board (FASB) in the United States. The Opinions and Statements give technical guidance to the profession as to what are generally accepted accounting and auditing standards. Thus, the German codified auditing standards (revised in 1977) are entirely the product of committees of the IdW.<sup>38</sup>

The pronouncements by the WPK also shape accounting and auditing standards, especially the Directives and the advice given to the WP profession by the WPK.

Even though a direct comparison of the development of German and U.S. accounting and auditing standards and principles is rather difficult, it seems that the WP profession has as much influence in determining these standards and principles in Germany as does the U.S. accounting profession in the United States. Any differences in the generating process are more in form than in substance, including the formulating of the Stockcorporation Laws on which the WP profession has exerted a strong influence.

#### Professional Duties and Responsibilities of Wirtschaftsprüfer

The conduct of a Wirtschaftsprüfer is guided mainly by the Wirtschaftsprüferordnung, the Directives of the WPK, and the Stockcorporation Law. These three sources of authoritative guidance will be discussed separately.

### The Wirtschaftsprüferordnung (WPO)

The WPO is the Professional Law (Berufsordnung) of the WP. It has been in existence since 1961 and is revised from time to time. The latest revision was completed at the end of 1975.

The WPO regulates the professional conduct of the accounting profession. Paragraph 43 requires the WP to exercise his profession independently, conscientiously, discreetly, (verschwiegen) and responsibly. It also states that he must not engage in activities which are incompatible with his profession or the reputation of the WP profession. Activities that are compatible with the profession of Wirtschaftsprüfer include all consulting and trustee activities, any other professional activity in the areas of engineering and law, employment at a research institute, or college teaching. A WP is also permitted to engage in any kind of writing or any other artistic activity.<sup>39</sup>

Paragraph 49 of the WPO mandates that a WP must decline an engagement if there is reason to believe that the circumstances may cause his independence to be questioned (Besorgnis der Befangenheit).<sup>40</sup> The WPO is silent as to what circumstances would impair independence.

### The Directives (Richtlinien) of the Wirtschaftsprüferkammer (WPK)

The WPK derives its legal authority to issue the Directives to the WP profession from the WPO. These Directives are revised periodically. The latest revised version was mailed to all WPs in December 1977.<sup>41</sup>

The Directives elaborate on paragraphs 43 and 49 of the

WPO and discuss the important characteristics of the WP profession in more detail. The WPK considers the following attributes to be all-important:

1. Due care (Gewissenhaftigkeit)
2. Individual responsibility (Eigenverantwortlichkeit)
3. Secrecy (Verschwiegenheit)
4. Impartiality (Unparteilichkeit)
5. Independence and unbiasedness (Unabhängigkeit and Unbefangenheit)

Each characteristic will be discussed briefly.

The requirement of exercising due care is similar to the U.S. auditing standard of due care and thus needs no further elaboration here.

Individual responsibility stresses that the individual WP is responsible for his decisions and cannot shirk this responsibility. Thus, the audit report is always signed by the WP in charge of the audit. For larger audit clients, two individual signatories may sign the audit report. The purpose of this requirement is to underline that auditing is a Profession (freier Beruf), in contrast to an employee-employer relationship. WPs employed by WPGs are indeed employees, but since by law a WP in a WPG must have procuration (prokura), this is considered sufficient for a WP in such a position to be responsible for his decisions.

The requirement for secrecy mandates that a WP or any of his assistants must not divulge confidential or inside information nor use it for personal gain. The profession considers secrecy

so important that WPs must have their assistants and/or employees sign a written statement swearing themselves to secrecy.

Impartiality refers mainly to WPs who are called to testify as expert witnesses. It applies to auditing as well but it seems that this would be covered by the mandate for independence and unbiasedness which appear to be stricter requirements than impartiality.

The independence and unbiasedness standards state that a WP must be free from influences, connections and considerations which could impair his independence and unbiasedness. Furthermore, it compels a WP to decline an audit engagement when his independence is impaired or if he feels himself to be biased even in cases where the applicable law concerning the selection of an auditor would not prohibit such an engagement.

In the WPK's latest revision of the Directives, the WPK has finally taken a stand concerning direct financial interest of a WP in his client firm. Effective January 1979, a WP who owns any shares of a client firm will not be considered independent if auditing this client's records. The Directives also prohibit a WP from auditing a client when he has basically prepared the financial statements of the client. The Directives are less specific for other auditor-client relationships.

### The Stockcorporation Law

The Stockcorporation Law of 1965 specifies how financial statements of a corporation (usually an AG) must be prepared and mandates that they be audited by WPs. This law deals with the

problem of ensuring auditor and/or WPG independence by listing a limited number of cases in which auditors are not considered to be independent. Any audited financial statements would be null and void (nichtig) in these cases.

The Stockcorporation Law of 1965 specifies that only WPs and WPGs may act as auditors for mandatory audits. The auditor-client relationships which are covered by this law prohibit a WP from performing an audit if he:

- 1a) is or was within the last three years prior to his appointment a member of the board of management or of the supervisory board or an employee of the company to be audited;
- 2a) is a legal representative or member of the supervisory board of a legal entity; member of a partnership or owner of a sole proprietorship, if such legal entity, partnership, or sole proprietorship is related to the company to be audited;
- 3a) is an employee of an enterprise related to the company to be audited.

An auditing firm (WPG) may not act as auditors

- 1b) if it or any enterprise related to it is related to the company to be audited;
- 2b) if a legal representative of an auditing firm which is a legal entity, or a partner of an audit firm, could not act as auditor pursuant to 1a, 2a, and 3a above;
- 3b) if a member of the supervisory board of an auditing firm could not act as auditor pursuant to 1a above.<sup>42</sup>

This casuistry was limited to these basic situations intentionally. As early as 1959 the Government Draft (Referentenentwurf) of the Stockcorporation Law of 1965 was discussed by the IdW. The IdW concluded that the circumstances which would render the audited financial statements null and void should be limited



to very basic situations that would be readily apparent to all. They thus welcomed the very limited casuistry delineated in the final law.

For circumstances not specifically covered by the Stock-corporation Law of 1965, the auditor, as the IdW points out, should be guided by the principles of the profession (Berufsgrundsätze des Berufsstandes) which mandate that a WP must decline an (audit) engagement if he is not free from influences, connections and considerations when making decisions and judgments.<sup>43</sup>

Besides the limited casuistry, the Stockcorporation Law of 1965 has a second provision to ensure a suitable auditor. Paragraph 163 states that the auditor's engagement may be terminated and "the court shall appoint another auditor...if this appears to be mandatory for a personal reason of the elected auditor; especially if partiality (Besorgnis der Befangenheit) must be presumed. The motion [of dismissal]...can only be made by a person who has objected to the selection of the auditors in records of the [shareholders'] meeting."<sup>44</sup>

Adler/Düring/Schmaltz, in their interpretations of this paragraph, comment that for an auditor not to be independent in appearance (Besorgnis der Befangenheit) there must be circumstances which provide for self-interest in the results of the audit by the auditor. They cited as one example a situation where an auditor owned a significant number of stocks of the auditee, and as another example the situation where an auditor may have to consider the interests or wishes of third parties (such as relatives).<sup>45</sup>

This opportunity to object to the proposed auditor or WPG at the annual stockholders' meeting would appear to be a good vehicle to help ensure selection of a suitable auditor. However, it has very seldom been employed, if ever.<sup>46</sup> The WP or WPG proposed by management to do the audit is usually elected by the stockholders at the annual stockholders' meeting without objection.

#### Summary Remarks

The preceding discussion seems to indicate that the German accounting profession is well organized and that competency levels of WPs are at least equivalent to U.S. CPAs based on educational backgrounds, work experience and examination requirements.

The general rules and regulations regarding the requirement for auditors' independence are similar to those governing U.S. auditors. However, specific guidelines to determine what constitutes an independent (or not independent) auditor-client relationship are few in number.

The German accounting profession recognizes that for an auditor to be truly independent he must be independent in fact as well as independent in appearance. This is the same concept of independence accepted by the U.S. accounting profession.<sup>47</sup> The identical concepts of independence and the fact that the purpose of the German auditors' work is basically the same as that of his U.S. counterpart, make findings of empirical research on the concept of independence of German auditors possibly useful

to the accounting profession in the United States as well.

In the following chapter the concept of independence will be examined and the relevant German literature will be reviewed to provide a conceptual framework for this empirical study.

## CHAPTER TWO--FOOTNOTES

1. Koch, W., Der Beruf des Wirtschaftsprüfers (Berlin: Duncker & Humblot, 1957), p. 55.
2. Abel, R., The German Experience with Uniform Accounting and its Relevance to the U.S. Controversies on Uniformity (Unpublished Ph.D. dissertation, Columbia University, 1967), p. 78.
3. Wirtschaftsprüferkammer, WP-Verzeichnis 1976/77 (Düsseldorf: IdW-Verlag GmbH, 1977), p. LIII and p. X. As of December 1976, there were 3,339 Wirtschaftsprüfer of which 2,913 were members of the IdW.
4. For a complete list of the duties and responsibilities of the WPK see, Gesetz über eine Berufsordnung der Wirtschaftsprüfer (Wirtschaftsprüferordnung) Stand: November 5, 1975 (Düsseldorf: IdW-Verlag GmbH, 1976), pp. 37-44.
5. For a list of committees see, WP-Handbuch 1973 (Düsseldorf: IdW-Verlag GmbH, 1973), pp. 88-89.
6. Ibid., p. 53.
7. As of December 1976, there were 3,339 WPs registered with the Wirtschaftsprüferkammer, according to the WP-Verzeichnis 1976/77.
8. Per conversation of this researcher with Mr. Pfefferer of the WPK and with Mr. Kaminski of the IdW on December 12, 1977.
9. A Diplom is approximately equivalent to a Master's degree in the United States.
10. Per Budde, 2,218 mandatory audits were performed by WPs in 1975; see Budde, H., "Stellungnahme re: 'Die Kontrolle der Kontrolleure', V. Emmerich, in Busse von Colbe, W., and Lutter, M., (eds): Wirtschaftsprüfung Heute: Entwicklung oder Reform? Ein Bochumer Symposium (Wiesbaden: Verlag Dr. Th. Gabler, 1977), p. 234.
11. Many bank loan officers are making loan decisions based on financial statements prepared by Steuerberater and in many cases do not insist on financial statements audited by WPs.

12. As of January 1978 there was still a controversy between representatives of the Wirtschaftsprüfer profession and the Steuerberater profession about who shall audit GmbHs if audits of this type of business organization become mandatory. See Forster, K.-H., "Institut der Wirtschaftsprüfer für einheitlichen Prüferberuf!" Die Wirtschaftsprüfung (Heft 4, 1978), pp. 100-103.
13. If we consider WPs to be equivalent to partners and managers in U.S. accounting firms, it seems that this breakdown of male and female auditors is similar to present U.S. conditions. See The Accounting Establishment: A Staff Study, by Lee Metcalf, Chairman (Washington, D.C. U.S. Government Printing Office, 1977), Appendix D.
14. In Germany, academic degrees become part of a person's name. Thus, all titles and degrees are listed in the WP-Verzeichnis 1976/77 from which this information was extracted.
15. For an exact breakdown see WP-Verzeichnis 1976/77, p. XI.
16. Per WP-Verzeichnis 1976/77, there were 601 WPs out of a total of 3,339 WPs that were affiliated or employed with the 10 largest WPGs. For a surrogate of size the numbers of WPs affiliated or employed were used.
17. The GmbH is a statutory closed corporation, shares of which are not freely negotiable. An overwhelming majority of businesses in Germany are organized as GmbHs. The reason for the popularity of this corporate form, according to Juenger and Schmidt, lies in the "great latitude in shaping its constitution to accomodate management and quotaholders by appropriate charter provisions." (page 3). In addition, as Juenger and Schmidt (page 3) point out, "quotaholders can, by entering into an appropriately drafted limited partnership arrangement with their company, avoid a double tax burden and enjoy the advantages of partnership taxation without losing the benefits of perpetuity and limited liability." Currently, only the larger GmbHs' financial statements must be audited by WPs; however, the Legislature is also considering mandatory audits for GmbHs of smaller size.

The AG, on the other hand, is a public corporation. Its shares are freely negotiable and, unless the articles of incorporation provide for registered shares, are issued in bearer form. Rules for incorporation of an AG, as Juenger and Schmidt (page 5) point out, "is conceived as an important transaction hedged with substantial safeguards. The articles of incorporation are an integral part of the organizational process which is designed to impart information and to assure adequate capitalization." The financial statements of an AG must be audited by WPs.

Even though a vast majority of German businesses are organized as GmbHs, the lack of free negotiability of its shares makes organization as an AG mandatory for those businesses intending to sell shares to the public. Consequently, AGs, although fewer in number, "represent by far the greater concentration of economic power" (Juenger and Schmidt, page 4).

For a more detailed account, see Juenger, F. K. and Schmidt, L. (translators), German Stock Corporation Act (Köln, Chicago: Verlag Dr. Otto Schmidt KG - Commerce Clearing House, Inc., 1967), pp. 1-21.

18. See Schruff, L., Der Wirtschaftsprüfer und seine Pflichtmandate (Düsseldorf: IdW-Verlag, GmbH, 1973).
19. For example, the Treuarbeit AG's majority shareholder, the Federal Government of Germany, reduced its share-holdings from 69.2 percent to 50 percent. See Commerzbank, (ed.), Wer Gehört zu wem - A guide to capital links in West German companies (1977), p. 768.
20. This is based on information included in the WP-Verzeichnis 1976/77 which shows various members of the Board of Management (Vorstand) of a German WPG also as belonging to one of the "Big Eight" accounting firms. The "Big Eight" accounting firms that were thus affiliated with German WPGs are: Arthur Young & Company is affiliated with Intrarevisio Beratungs-und Treuhand GmbH WPG; Coopers & Lybrand with Treuhand-Vereinigung AG WPG; Deloitte, Haskins & Sells with Dr. Wollert - Dr. Elmendorf KG WPG; Touche Ross & Co. with Treuverkehr AG WPG; Peat, Marwick, Mitchell & Co. with ATB Allgemeine Treuhand und Beratungsgesellschaft WPG. Not affiliated with any German WPG are the following "Big Eight" accounting firms: Arthur Andersen & Co.; Whinney, Murray, Ernst & Ernst; Price Waterhouse & Co. Treuarbeit AG WPG, the largest German WPG, has a special agreement of cooperation with Peat, Marwick, Mitchell & Co. concerning the audits of German subsidiaries firms located in the United States and Canada, according to the 1976 Annual Report of the Treuarbeit AG WPG.
21. Per information extracted from WP-Verzeichnis 1976/77.
22. See WP-Verzeichnis 1976/77.
23. For more details, see Wolff, J., "Die Änderung der Prüfungsordnung für Wirtschaftsprüfer," Die Wirtschaftsprüfung (Heft 1/2, 1976), pp. 1-4.
24. For additional qualifications, see WP-Handbuch 1977 (Düsseldorf, IdW-Verlag GmbH, 1977), pp. 9-15.

25. For exceptions to this rule, see Prüfungsordnung für Wirtschaftsprüfer, Stand December 5, 1976 (Düsseldorf: IdW-Verlag GmbH, 1976), par. 18.
26. Niehus, R. J., "The Public Accounting Profession in Germany," The Accountant (January 4th, 1973), p. 13.
27. Institut der Wirtschaftsprüfer, Fachgutachten 1/1977-Generally accepted standards for the audit of financial statements, Sonderdruck aus der Zeitschrift Die Wirtschaftsprüfung (1977), p. E27.
28. Ibid., p. E3.
29. Ibid., pp. E4-E5. Prior to Statement on Auditing Standards No. 16, issued in January 1977 by the Auditing Standards Executive Committee of the AICPA, the German position on the detection of defalcations and errors was almost identical to the position taken by the AICPA. See Statement on Auditing Standards No. 7, (November 1972) section 110.05. However, SAS No. 16 seems to attribute somewhat more importance to the detection of fraud in the audit function than is apparent in the German position on this subject.
30. American Institute of Certified Public Accountants, Statement on Auditing Standards No. 2 (New York: AICPA, 1973), p. 2.
31. See, for example, Goerdeler, R., "A True and Fair View - or Compliance with the Law and the Company Statutes," Die Wirtschaftsprüfung (Heft 19, 1973), pp. 517-525.
32. See Parczyk, W., "Die amerikanischen Grundsätze ordnungsmässiger Abschlussprüfung im Vergleich zu deutschen Prüfungsmaximen," Der Betrieb (Nr. 30, 1970), pp. 73-76.
33. Mining companies are exempted. They are covered under state (Länder) legislation. See Juenger, F. K., and Schmidt, L., German Stock Corporation Act, pp. 4-5.
34. Ibid., p. 4.
35. The Disclosure Law merely extends applicability of the Stockcorporation Law of 1965 to certain larger business entities not organized as an AG. For more information, see Mueller, R., and Galbraith, E. G. (eds. and translators). The German Stock Corporation Law, the German Law on the Accounting by major Enterprises other than Stockcorporations - Bilingual Edition (Frankfurt: Fritz Knapp Verlag, 1976), pp. 494-500.

36. There is the so-called Little Reform Bill which became law in 1960. This bill's major feature is the requirement that the income statement must be prepared in conformance with a model income statement incorporated in the bill. See Raetsch, H., "Financial Statements under the New Stock Corporation Law of the Federal Republic of Germany," Arthur Young Journal (April 1960), pp. 1-11.
37. The most widely used Commentary, often referred to as the "Bible" of the WP, is Adler/Düring/Schmalz, Rechnungslegung und Prüfung der Aktiengesellschaft - Fourth Edition, bearbeitet von: Schmaltz, K.; Forster, K.-H.; Goerdeler, R.; Havermann, H. (Stuttgart: C. E. Poeschel Verlag, 1971).
38. Institut der Wirtschaftsprüfer, Fachgutachten 1/1977, 2/1977, 3/1977, Sonderdruck aus der Zeitschrift Die Wirtschaftsprüfung (German-English).
39. Wirtschaftsprüferordnung, par. 43.
40. Paragraph 49 of the WPO reads as follows: "Der Wirtschaftsprüfer hat seine Tätigkeit zu versagen, wenn...die Besorgnis der Befangenheit bei der Durchführung eines Auftrages besteht."
41. Wirtschaftsprüferkammer, Richtlinien für die Berufsausübung der Wirtschaftsprüfer und vereidigten Buchprüfer (December 1, 1977).
42. Aktiengesetz 1965, paragraph 164 (own translation). This translation draws heavily from the translation by Juenger, F. K., and Schmidt, L., German Stock Corporation Act.
43. WP-Handbuch 1977, p. 50.
44. Mueller, R., Galbraith, E. G., p. 211. According to Richter (page 6) this provision does not necessarily represent any protection. Richter claims that no incident is known where the auditors were dismissed under the provision of paragraph 163 of the Stockcorporation Law of 1965. See Richter, M., "Die Stellung des Abschlussprüfers im Entscheidungs- und Kontrollprozess der Aktiengesellschaft," Diskussionsbeiträge-Fachbereich Wirtschaftswissenschaft, Universität des Saarlandes (September 1977).
45. Adler/Düring/Schmalz, Band II, pp. 198-203. It should be noted that this was written prior to the December 1977 revision of the WPK's Directives. Prior to this revision, the WPK did not specifically prohibit WPs from owning shares in their audit client firms.
46. See Footnote 44.
47. In Chapter Three the translation conventions used will be discussed in more detail.



## CHAPTER THREE

### THE INDEPENDENCE ISSUE IN GERMANY AND THE CONCEPT OF AUDITORS' INDEPENDENCE

In this chapter the German accounting literature, its views of the WP independence issue and the solutions that have been suggested will be examined. A framework to resolve the independence problem will be developed, given certain assumptions.

#### Introduction

There is general agreement among auditors and users of audited financial statements that independence of the external auditor is important. Many consider it the most important attribute of the auditor and the auditing profession.<sup>1</sup> As Wilcox comments, "independence is an essential auditing standard because the opinion of the independent accountant is furnished for the purpose of adding justified credibility to financial statements which are primarily the representations of management. If the accountant were not independent of the management of his client, his opinion would add nothing."<sup>2</sup>

The AICPA has defined independence as the "ability to act with integrity and objectivity."<sup>3</sup> Even though the "qualities of integrity and objectivity are not precisely measurable, the profession nevertheless constantly holds them up to members

as an imperative."<sup>4</sup>

However, this type of independence, also referred to in the U.S. accounting literature as independence in fact, is only one of two components of what will be called "Total Independence". The other component is known in the U.S. literature as independence in appearance. Whereas independence in fact deals with the auditor's state of mind or attitude toward the audit object, independence in appearance, as Arens & Loebbecke point out, "is dependent on others' interpretation of this independence [in fact]".<sup>5</sup> Thus, for an auditor to lack independence in appearance it is not necessary for him to be not independent in fact, just having his independence questioned by a legitimate third party is sufficient to render him consequently not (totally) independent. It seems that the requirement for independence in appearance may be the stricter of the two requirements.

As noted in the preceding chapter, the German auditor must be independent in fact as well as not lacking independence in appearance, as mandated by paragraphs 43 and 49 of the Wirtschaftsprüferordnung.<sup>6</sup> Richter considers both requirements to be of equal importance.<sup>7</sup> Both are necessary for German auditors to be independent. The WP-Handbuch points out that it is the professional duty of a WP to consider if his independence in appearance could be questioned for a logical and sound reason (sachlich vernünftiger Grund) by a third party in which case he must decline his (audit) services. Such a charge cannot be repudiated if the WP himself feels he does not lack an unbiased attitude toward the audit object. The overriding factor is whether a third party, by

considering all facts and circumstances, could question the independence and objectivity of the auditor.<sup>8</sup>

#### Discussion of the Issues Raised and Solutions

##### Suggested in the German Accounting

##### Literature Concerning WP Independence

The German accounting literature has dealt extensively with the problem of WP independence. An entire issue of the Betriebswirtschaftliche Forschung und Praxis published in 1976 was devoted to this subject and the recent Bochumer Symposium dealt with the auditor independence issue in great detail.<sup>9</sup> Many suggestions have been made of how to better ensure auditors' independence.

Some authors advocate strengthening the independence status by using the existing institutions and legal conventions while others have called for drastic changes such as proposing the governmentalization of the audit function.

Thus far the U.S. terminology of independence has been used when translating German auditing requirements and research from the German literature, since it more or less seems to convey the best interpretation of the German terms. However, it may be helpful to discuss the German concept of independence in some more detail to provide a better basis for the reader's understanding.

The German independence issue is sometimes discussed as consisting of three, not two, components as listed below, followed by their English translation:

##### 1. Unabhängigkeit

## 2. Unbefangenheit

## 3. Besorgnis der Befangenheit

Cassel's German and English Dictionary translates Unabhängigkeit as: independence; autonomy; Unbefangenheit means: impartiality, freedom from bias; Besorgnis der Befangenheit literally translates as: fear or apprehension of partiality.<sup>10</sup>

There is no doubt that Unabhängigkeit and Unbefangenheit are very closely related and usually are used together, sometimes interchangeably, when referring to the auditor's ability to act with objectivity and integrity during an audit. The Wirtschaftsprüferkammer in its Directives uses the two terms together when it mandates that a WP must be "free from influences...that might impair his Unabhängigkeit and Unbefangenheit when performing his [audit] duties".<sup>11</sup> Some authors, however, perceive significant differences between the two terms. Jäckel contends that Unabhängigkeit refers to the legal and economic freedom (Bindungslosigkeit) of the auditor from his audit client.<sup>12</sup> Unabhängigkeit to him always represents an "äusseres Verhältnis", a relationship readily discernable by an outside observer. Jäckel believes Unbefangenheit refers to the auditor's inner unbiased attitude (innere Einstellung) to the audit and his audit client. Both concepts are in close relationship to one other, with Unbefangenheit, according to Jäckel, being the more encompassing requirement.

This definition of Unbefangenheit corresponds closely with the U.S. term of independence in fact. Richter refers to Unbefangenheit as faktische Unabhängigkeit, which is the literal translation of independence in fact.<sup>13</sup>

Unabhängigkeit, on the other hand, seems to correspond more closely to the U.S. term of independence in appearance, if Jäckel's definition is followed. To pursue Jäckel's reasoning, Besorgnis der Befangenheit also represents the concept of independence in appearance (actually, the appearance of dependence) since, for Besorgnis der Befangenheit to exist, it is not necessary to prove that the auditor is not independent in fact (unbefangen). It suffices if a third party may legitimately question the auditor's independence status.

To summarize, Jäckel's interpretation of the terms Unabhängigkeit and Besorgnis der Befangenheit both correspond closely to the U.S. concept of independence in appearance. However, Jäckel categorizes independence in appearance as Unabhängigkeit if it refers to an auditor-client relationship prohibited by the casuistry of paragraph 164 of the Stockcorporation Law of 1965, and independence in appearance is referred to as Besorgnis der Befangenheit if it is not--thus representing a general catch-all clause which complements the specific casuistry.<sup>14</sup>

It seems that this distinction is somewhat academic. Others consider Unabhängigkeit and Unbefangenheit to be practically synonyms; both corresponding closely to the U.S. concept of independence in fact, i.e., referring to the auditor's perception of his ability to make objective audit decisions. Independence in appearance is usually meant by the concept of Besorgnis der Befangenheit, referring to the perception of a legitimate third party as to the auditor's independence status.<sup>15</sup> Consequently, the casuistry of paragraph 164 of the Stockcorporation Law of

1965 is considered by these authors a description of auditor-client relationships dealing with Besorgnis der Befangenheit (independence in appearance) only.

In this study, Besorgnis der Befangenheit is interpreted as coinciding with the U.S. concept of independence in appearance (or lack of it). Unbefangenheit is usually translated as independence in fact. Unabhängigkeit is translated as independence (or independence in fact if the author used it interchangeably with Unbefangenheit), unless it is apparent that the author uses Unabhängigkeit according to Jäckel's definition, in which case it will be translated as independence in appearance.

#### Auditor-Client Relationships that May Impair

##### Auditors' Independence in Appearance

Independence in fact, as noted above, is concerned with the auditor's mental attitude toward the audit object. Wysocki concludes correctly that such an independence concept cannot be codified into specific professional guidelines.<sup>16</sup> Realizing this, rule makers in Germany, as well as in the United States, try to attack the independence problem by utilizing the second component comprising the Total Independence concept--independence in appearance. They specify a number of auditor-client relationships in which lack of auditors' independence is suspect, i.e., the auditor is not considered independent in appearance. Wysocki agrees that it is of no concern in these cases whether the auditor is indeed not independent in fact.

Auditor-client relationships that may impair independence

in appearance have been categorized in a number of different groups and sub-groups. Wysocki's grouping of causes that may infringe upon auditors' independence in appearance involves only two types of auditor-client relationships which seem to cover every situation. They are relationships in which the auditor:

1. has a self-interest (including economic or other personal interest) in the audit results, and those
2. in which the auditor has to take into consideration someone else's interest (economic or personal) in the audit results.

Personal self-interest is considered to be present in situations where the auditor has a financial interest in the audit, either as a stockholder or creditor. Economic self-interest is defined by Wysocki as the auditor's dependency on the audit fees from a particular client, i.e., the economic necessity for the auditor to retain the client for future engagements (Kundenabhängigkeit). Other personal self-interest includes any auditor's relationship to the audit object, e.g., a situation where an auditor must pass judgment on audit evidence which he helped create.

Most discussions concerning the independence concept however, deal with the relationships of the auditor to a third party which could affect his objectivity toward the audit work. Wysocki cites the Directives of the WPK which caution that independence in appearance may not be present for relationships between the auditor and someone affected by the audit results that are of a personal, family, or business nature.

Wysocki realizes that the limited specific guidelines available to the WP to determine what relationship will impair his

independence in appearance are not complete by any standard. As an example of the type of auditor-client relationship not covered by any specific rules, he considers a situation where a close relationship exists between an auditor and a high-level executive of an audit client, which, to Wysocki, may impair the auditor's independence in appearance.<sup>17</sup>

#### Criticism of the WP Profession Independence Status Raised in the German Accounting Literature

The auditor independence issue has come into focus during recent years because of a number of widely publicized bankruptcies of corporations whose financial statements had been audited by WPs, and usually had received an unqualified auditor's opinion.<sup>18</sup> The popular press may have been unfair in some cases by generalizing from some unfortunate incidents to the entire profession. The possibility, as Knief aptly notes, that the public may misunderstand what the auditor's opinion entails, might explain most of the criticism raised in the press.<sup>19</sup> It does not, however explain away some of the criticism raised by members of academe and from members of the WP profession itself.<sup>20</sup>

The independence problem originates first, in the inherent difficulties in applying the concept of independence to the real world and second, in the lack of more specific guidelines covering independence in appearance.

The criticism revolves mainly around the laws and regulations covering auditors' conduct, specifically the Stockcorporation



Law of 1965 and the Wirtschaftsprüferordnung, as well as around the role of the WPK in issuing guidelines and regulating the profession.

The Stockcorporation Law of 1965 with its limited casuistry of paragraph 164 is severely criticized by Westrick. He points out that this law does not deal with the following issues:<sup>21</sup>

1. An auditing firm could be auditing a corporation even if a member of a supervisory board of the auditing firm is at the same time also a member of the managing board of a corporation that has a significant influence on a corporation to be audited.
2. A Wirtschaftsprüfer who is a majority or sole stockholder of a corporation could perform the audit of this corporation providing that the Wirtschaftsprüfer is not considered an enterprise (Unternehmen).<sup>22</sup>
3. The casuistry of paragraph 164 leaves open the question of whether an auditing firm may audit a corporation if both have the same majority stockholder.<sup>23</sup>
4. The casuistry does not deal with the problem of economic client dependency (Kundenabhängigkeit).<sup>24</sup>

Westrick admits that even if these loopholes were closed, there would still be many questions left unanswered. He feels that a catch-all clause (Generalklausel) ought to be added to the casuistry.

It should be noted that Westrick made these statements in response to the Government Draft (Referentenentwurf) of the 1965 Stockcorporation Law, a long time before final enactment of the law. However, his objections were not heeded since essentially no changes were made pertaining to this issue in the final form of the law.

Supporters of the current paragraph 164, which include the IdW, felt that due to the severe consequences of violation of

paragraph 164 (the audited financial statements would be declared void in such a case), the casuistry should not be extended since the WP is also bound by the professional law which requires the auditor to be independent.<sup>25</sup>

In contrast, the Stockcorporation Law of 1937 did have something resembling a general clause concerning auditors' independence in paragraph 137 which excluded the following from performing an audit:

- a) any member of the board of directors and any employees of the corporation to be audited,
- b) any member of the board of directors and any employees of a corporation that is dependent on or is dominated by the corporation to be audited,
- c) any person whose business management (Geschäftsführung) is significantly influenced by any of the individuals mentioned in (a) or (b).<sup>26</sup>

Comparing these requirements, especially (b) and (c) with the casuistry of the Stockcorporation Law of 1965, it is obvious that the new law cannot be considered to have strengthened the independence requirements, but for the sake of clarity, it eliminated some of the ambiguity of (b) and eliminated the requirement under (c) entirely.<sup>27</sup>

The justification for these changes, endorsed by the professional organizations of the Wirtschaftsprüfer, was that the severe consequence of nullification of the financial statements was too strong a measure to be based on anything less than clear-cut guidelines. Furthermore, proponents of the limited casuistry of paragraph 164 argued that the professional law (WPO, paragraph 43 and especially paragraph 49) already includes a general clause

to cover other auditor-client relationships. Violation of the professional law, in contrast to the corporation law, will not result in nullification of the audited financial statement and thus does not expose a WP to liability claims from the audited corporation for invalid financial statements, but may result in a professional-court proceeding.<sup>28</sup> Apparently, this is considered a less severe consequence by the profession's institutions. Considering that the punishment may be more than mere censure--in its most severest form, expulsion from the WP profession--it seems that the consequences for disregarding the tenets of the WPO would still be quite sufficient to act as an effective deterrent.

Karehnke feels that paragraph 164 of the Stockcorporation Law of 1965 in conjunction with paragraph 49 of the WPO provides the WP with sufficient guidance.<sup>29</sup> Others have serious doubts about the proper interpretation of either regulation.<sup>30</sup>

Some have argued that paragraph 164 of the Stockcorporation Law of 1965 covers the "more serious" cases where independence in appearance is not given, whereas paragraph 49 of the WPO deals with the "lighter" cases. However, Adler/Düring/Schmaltz point out that this is not a correct interpretation of the law. Other auditor-client relationships, such as close family ties between an auditor and his client may impair independence in appearance, but are more difficult for a third party to recognize. Their threat to independence can only be determined, they assert, by considering the special circumstances surrounding each case.<sup>31</sup>

Adler/Düring/Schmaltz consider the casuistry of paragraph 164 of the Stockcorporation Law of 1965 to be special cases of

independence in appearance violations and thus falls simultaneously under paragraph 49 of the WPO. However, they claim that it does not follow that other cases of corporate law (gesellschaftsrechtlicher Art) can be construed by paragraph 49 of the WPO. They believe that paragraph 164 of the Stockcorporation Law of 1965 exhausts this type of auditor-client relationships.<sup>32</sup>

This somewhat surprising conclusion can only be understood if it is intended to refer to the fact, using Wüstemann's thoughts on the matter, that there are no other auditor-client relationships that lead to nullification of the audited financial statements, even if lack of independence can be proven.<sup>33</sup>

The WPK voiced its position when discussing Schruff's study which dealt to a significant degree with ownership identities of Wirtschaftsprüfungsgesellschaften and their clients. In his study, Schruff disclosed a number of actual cases in which auditing firms (mostly those organized as an Aktiengesellschaft) and their clients were owned to various degrees by the same entity.

It seems logical to question such relationships, unthinkable to any U.S. auditor, as to a possible impairment of independence in appearance. However, the WPK concluded that the relationships disclosed by Schruff do not exceed the limits of the casuistry in paragraph 164 of the Stockcorporation Law of 1965. With this interpretation, the WPK agreed with Adler/Düring/Schmaltz that paragraph 164 is a lex specialis, thus prohibiting simultaneous application of paragraph 49 of the WPO, which is considered a lex generalis, by implication.<sup>34</sup>

Realizing that a legal definition of the relationship between

paragraph 49 of the WPO, a professional law, and paragraph 164 of the Stockcorporation Law of 1965 has not been established, the WPK indicated that it will follow closely any developments in court cases and in Commentaries of professional and corporate law rulings which concern the auditor and his selection process.<sup>35</sup>

The Wirtschaftsprüferordnung is also criticized for being less effective than is sometimes claimed by various proponents of the status quo, since this professional law, especially paragraphs 43 and 49, is left to the interpretation of each WP and/or auditing firm. Kicherer complains that there is no competent and neutral authority which could decide in a particular case when an auditor should not be considered independent. He believes that the regular courts are neutral but lack competency, whereas the Institut der Wirtschaftsprüfer and the Wirtschaftsprüferkammer are competent but cannot be considered neutral since they are dominated by the WPs themselves.<sup>36</sup> Thus, the problem, as Kicherer sees it, lies exactly in the unsatisfactory interpretation of paragraph 49 of the WPO.<sup>37</sup>

It could be concluded that at the heart of the independence problem is the fact that the individual WPs or auditing firms are left to their own interpretation of what constitutes a relationship in which the auditor is considered to be independent in appearance and what relationship is prohibited.

However, it could be argued that the WPK's Directives represent guidelines to help the auditor in this dilemma. Wüstemann comments, though, that the WPK goes from the premise that the auditor is able to recognize when his independence in appearance is impaired.

This is reflected in the way the Directives are worded. They do not contain any mandatory edicts (Musserwartungen), and could be deviated from, thus making a successful professional court proceeding rather uncertain.<sup>38</sup>

#### Solutions Suggested in the German Accounting Literature

The German accounting literature is rife with suggestions for strengthening the independence of Wirtschaftsprüfer. As discussed above, many have criticized the present conditions; however, most critics not only criticize but also make suggestions of how to improve the situation. Even though it is apparent to most of these critics that achievement of perfection concerning auditors' independence is practically impossible, it is felt that certain changes would result in greater credibility of the auditor's work and of the WP profession as a whole.

The major suggestions will be discussed by dichotomizing them into proposals involving structural changes of the WP profession and those that could be implemented within the current structure. This dichotomy is only employed to facilitate the discussion. It is not intended for any other purpose.

#### Proposals Involving Structural Changes of the WP Profession

Time and again, the suggestion is made for the establishment of an SEC type federal government agency (Aktienamt).<sup>39</sup> It is argued that an Aktienamt in charge of ensuring auditors' independence is the best way to deal with the independence problem.<sup>40</sup>

However, views differ as to the degree of responsibility and power the proposed government agency should be granted.

At one end of the spectrum, the moderate view would like to see the Aktienamt function along lines similar to that of the Securities and Exchange Commission in the United States. At the other end of the spectrum, the extreme position calls for a government agency to take over the audit function entirely, having government employees perform all mandatory audits. In the middle of the spectrum are those proponents of an SEC type government agency having the additional responsibility of assigning auditors to audits and/or even paying the audit fees directly to each auditor.

Opponents to the idea of government intervention, no matter how little, do not believe that this would solve all the independence problems, nor do they believe that such a drastic step is warranted. Schulze-Osterloh is convinced that an Aktienamt (along SEC lines) would significantly change the structure of the accounting profession.<sup>41</sup> Leffson, usually quite critical of the present status of the WP profession, also thinks that, for the time being, an Aktienamt is not called for. He states that the WPO has given the profession the right and the privilege to govern and control itself. As long as the profession carries out these duties conscientiously, there is no need to have an Aktienamt as an additional governmental watch-dog. However, if the profession does not do so, Leffson warns, the creation of such a government agency will become unavoidable. It is up to the WP profession, he asserts, to counteract the widespread suspicion that the

profession's self-regulating effort has not been vigorous enough.<sup>42</sup>

Westrick also thinks that such a drastic measure is unwarranted, especially since the reasons for the current credibility gap by the public have their roots in the Stockcorporation Law itself, since it has no provisions to secure auditors' independence in many situations. He asserts that having the Federal Government take over the audit function is a harsh verdict of distrust against the WP profession and could not possibly be pronounced any stronger.<sup>43</sup>

Another proposal to strengthen the credibility of the auditing profession is discontinuing the practice of having non-WPs hold a financial interest in auditing firms, as well as disallowing ownership of one auditing firm by another auditing firm.<sup>44</sup> Germany seems to be unique among the Common Market countries in allowing persons or entities outside of the accounting profession to hold an ownership interest in auditing firms. That this practice casts a shadow on the entire profession's integrity and independence cannot seriously be refuted. In light of Schruoff's research which discloses the relationships between stockholders of Wirtschaftsprüfungsgesellschaften (WPGs) and stockholders of their clients, it seems difficult to understand that such situations still exist.<sup>45</sup> The defense that these relationships are not considered improper, according to the Stockcorporation Law of 1965, and thus don't impair independence in appearance, is unconvincing.

Most of the larger WPGs that have outside stockholders are partially or fully owned by commercial banks and/or the government. It is true that the auditing function was first performed by banks



who founded the first auditing firms to assure themselves of the financial position of certain business entities, but the argument and justification, that the practice has a historical basis is too simplistic.<sup>46</sup>

Wüstemann questions the motives of any outside entity that invests in a WPG. It could be for valid investment reasons. However, it should be noted that the profit motive is not permitted to be a primary goal of a WPG. Is it, Wüstemann argues, that these investors want to assure themselves that the WPG stays independent and impartial, implying that this cannot be achieved with ownership by others? Turning this argument around, their ownership similarly would instill doubts by others regarding their auditors' independence. A third reason for ownership in a WPG, Wüstemann speculates, may be to control the WPG, an effort that de lege lata is prohibited.<sup>47</sup>

#### Proposals Not Involving Structural Changes of the WP Profession

The practice of the auditee essentially electing the auditor has long been regarded as an anomaly. Schmalenbach, in 1949, wrote that having a corporation elect its own auditors is an absurdity, since it is not common practice in life to leave the selection of the examiner to the person that needs to be judged independently.<sup>48</sup>

Those who do not advocate a government agency selecting the auditor, propose, as an alternative, to increase the period of auditor election to more than one year. Some consider election for three to six years to give management less power over the auditor.<sup>49</sup> Even though German corporations (Aktiengesellschaften)

rarely change their auditors, it is felt that election for several years at a time is still desirable. Richter believes that knowledge of this practice of infrequent auditors' changeover is not as effective in giving encouragement to the auditor for a clear presentation of his audit findings as auditors' election for a multi-year period.<sup>50</sup>

It should be recalled that for mandatory audits the auditor is elected by the stockholders at the annual stockholders' meeting. However, this election process, as Richter notes, is considered a preprogrammed formal ritual. There are no known cases in which stockholders rejected the proposed auditors (not counting those cases where there was an interim change in the majority stockholder identity).<sup>51</sup>

#### Broadening Auditors' Liability

Under present German law a WP is generally only liable to a third party if this third party, for instance a stockholder, relied on incorrect financial statements and suffered a financial loss from any decision made, and if the auditor has performed his duties in such a way as to purposely misrepresent given facts.<sup>52</sup> Various authors have suggested broadening the liability of auditors to third parties to allow a third party liability which makes an auditor vulnerable to litigation if he was negligent (fahrlässig) in performing his duties.<sup>53</sup> Others want to increase the present limited liability of DM 500,000 per case to, perhaps, unlimited liability.<sup>54</sup>

Westrick considers a broadened third party liability a powerful

tool to ensure independence.<sup>55</sup> However, others question the effectiveness of such a change in liability. Schulze-Osterloh believes that facilitating third party suits by making an auditor liable for negligence will have little effect since the third party must know the details and circumstances, at least in approximate terms, which led to the supposedly incorrect audit decision. Without this knowledge the plaintiff cannot make any pertinent accusations.<sup>56</sup> He also points out that a proper judicial judgment can only be arrived at if the WP is not bound by the standard of secrecy. Schulze-Osterloh feels it is doubtful that the WP is allowed to speak freely under present regulations even if it is to defend himself.<sup>57</sup>

Others are opposed to extending third party liability because it may invite all kinds of unjustified law suits which would tie up the profession's resources. They point to the increase in liability suits in the U.S., claiming that it did not solve the U.S. profession's problems.<sup>58</sup> However, Richter quotes a study by Bedingfield which determined that as a result of the increased law suits involving auditors, certain changes have been made by U.S. accounting firms, especially: better supervision and training of audit personnel, an increase in the audit intensity, and more selectiveness when deciding whether to accept an audit engagement.<sup>59</sup>

#### Incompatible Activities

It has been estimated that approximately 30 percent of the WP profession's revenue comes from management consulting.<sup>60</sup> Even though the WPO explicitly lists consulting (Beratung) as an

activity compatible with the profession, the widespread practice has come under criticism as being a detriment to the profession's credibility.

Some consider practically all consulting to be incompatible with the auditor's functions, while others are more concerned with the consulting work for clients that are at the same time also audit clients.

A recent empirical study by Richter revealed that more than 70 percent of business journalists surveyed considered management consulting by WPs for their audit clients to impair the auditor's independence because:<sup>61</sup>

1. WPs audit their own decisions and recommendations,
2. WPs are personally interested in the audit results, especially if their consulting was deficient,
3. WPs can't guard impartially the interests of financial statement users and their own clients at the same time,
4. during the consulting work, close relationships between management and auditors develop, and
5. economic dependency of the auditor is strengthened due to increased revenues from a given client.

However, approximately 65 percent of the WPs questioned did not consider management consulting to infringe upon their independence status since,

1. their professional code requires them to decline engagements which impair their independence,
2. out of self interest, they refuse certain engagements, and
3. the information gained from consulting more than offsets any possible impairment of independence.

It should be noted, that this study was criticized by the WPK,

among other things, on the grounds that business journalists are not a good surrogate for users of audited financial statements.<sup>62</sup>

#### Extension of the Casuistry and Related Suggestions

As noted earlier, the individual WP (and WPG) has relatively few specific and detailed guidelines which help in deciding what constitutes an auditor-client relationship that infringes on auditors' independence in appearance. Wüstemann seems to put the independence problem in proper perspective when he notes that the auditing function is performed by different individuals who must comply to the same measurements and requirements. Therefore, it would be in the spirit of the mandate for auditors' independence, to establish a list of auditor-client relationships which in essence impair the auditor's independence in appearance. He concedes that such a list could subjectively be considered by the parties involved as unjust, nonetheless it would facilitate the independence problem, contribute to uniform handling, and provide legal certainty.

Wüstemann points out that for reasons of practicability it is impossible to accomodate each and every concerned party. Nonetheless, he feels that the profession should consider any auditor-client relationship in which the auditing profession itself suspects impairment of independence (Befangenheit) or where lack of independence in appearance is shown. Wüstemann states that to construct such a list, high standards must be used to ensure the auditor's impartiality and credibility.<sup>63</sup>

Schruff is working along similar lines for a better way to

strengthen auditors' independence. Whether independence in appearance is impaired in a certain auditor-client relationship depends upon the subjective evaluation of the relationship by the financial statement users (Adressaten). Therefore, he reasons, the refutation of this charge can only be based on conventions which have established what situations represent a lack of independence in appearance. Such conventions have not been constructed. They must be achieved and arrived at in the accounting literature and need the consensus of all persons concerned.

What must be done, urges Schruff, is to establish minimum and maximum limits. The minimum limits should be determined with the help of the materiality principle which is applicable to any type of information dissemination. Any auditor-client relationship that falls under this minimum limit is considered immaterial and consequently, would not affect auditors' independence. The maximum limit that needs to be established would determine that any auditor-client relationship above this limit is, a priori, considered to impair auditors' independence.<sup>64</sup>

Under Schruff's proposal, an auditor would be guided by definite and specific rules. If he encounters a situation that falls above the maximum limit, he must decline the audit engagement. However, if the relationship lies below the minimum limit, the auditor is considered independent and can accept the engagement, ceteris paribus. If he finds himself in a situation that falls between the two limits he will be allowed to accept the audit engagement, but, as Schruff qualifies, he must disclose the relationship so that each individual user of the resulting audited

financial statements can form his own opinion of the auditor's independence.<sup>65</sup>

Schruff feels that these conventions should be established by court rulings.<sup>66</sup> It seems that determining the minimum and maximum limits is in essence an empirical question, since it deals solely with the concept of independence in appearance.

The premise of Schruff's suggestion is his belief that without the above discussed minimum and maximum limits, it would be necessary to disclose a large variety of auditor-client relationships that may impair independence in appearance. The limits thus are used to classify sensitive auditor-client relationships into those that do not impair auditors' independence and those that do. There is a wide band of situations between the two extremes where the judgment is still out or where opinions are divided.

#### Implications

Even though the preceding discussion of the German accounting literature concerning the auditor's independence status was limited to a few main points mentioned in the literature, it nonetheless provides a summary view sufficient to allow the reader to familiarize himself with the challenge facing the WP profession.

The WPK more often than not has found itself in a position of defending the status quo, claiming that present rules and regulations are sufficient, implying that any of the changes suggested are uncalled for. However, repeated criticism in the literature and the financial press of the status quo, as well as the desire to conform to a higher degree with other countries'

independence standards, especially U.S. standards, seem to have weakened the WPK's resistance for change.

The latest WPK Directives, issued in December 1977, is the WPK's first step in taking a firm approach by specifically prohibiting certain auditor-client relationships. For example, auditors will not be considered independent in a situation in which they own any shares, no matter how few, of their audit clients. This is a significant departure from the WPK Directives of July 1974, in which it was suggested that independence in appearance may be impaired when an auditor has a financial interest in his client.<sup>67</sup> This change in wording is a significant departure from the WPK's apparent premise that WPs are able to determine for themselves when their independence in appearance is impaired.

There is little doubt that there is a need for more specific guidelines covering independence in appearance. To discourage improprieties by broadening auditors' liability, considered a deterrent, is bound to force some auditors to reconsider their auditor-client relationships more carefully and may possibly result in more resignations from questionable audit engagements. However, in ensuring independence in appearance it is a rather blunt tool, less effective and efficient than other available tools.

Independence in appearance is a concept concerned with the collective perceptions of users of financial statements. It is, as Richter notes, an empirical concept (Tatbestand).<sup>68</sup> To leave the auditor without comprehensive specific guidelines as to what those perceptions of financial statement users are, is inefficient and unfair to the WP profession. As will be argued in the next



section, even under ideal conditions, it is, in general, impossible for all members of the auditing profession to be independent in appearance in every case without specific guidelines.

#### Conceptual Foundation of the Concept of Total Independence

As noted in the preceding section, for a WP to be independent he must be independent in fact and in appearance. These two components make up the "Total Independence" concept. Both requirements are mandated by the WP's professional law (WPO).

To achieve this independence, the German auditor is guided by a general rule, paragraph 43 of the WPO which requires each WP to be independent in fact when performing an audit. To help the WP decide whether a certain auditor-client relationship impairs his independence in appearance, there is a general rule, paragraph 49 of the WPO, which mandates that he must be independent in appearance. In addition to paragraph 49 of the WPO there is also the limited casuistry of paragraph 164 of the Stockcorporation Law of 1965 which gives specific guidelines for a selected number of situations, and the Directives of the WPK which point out certain types of relationships that may impair independence in appearance but basically leave it to the WP as to how to interpret and apply them to real situations.<sup>69</sup>

Below it will be argued that a general rule is sufficient to ensure independence in fact, given certain assumptions. However, to assure independence in appearance, a general rule will not be sufficient for all cases, even under the most ideal conditions.

Each component that makes up the concept of Total Independence is discussed separately below.

#### Independence in Fact

Independence in fact is a concept of an individual auditor's perception. It is generally agreed that there cannot be any objectively measurable guidelines that are also operational. It is this component of the Total Independence concept to which the AICPA refers to in the Statement of Auditing Standards which states that "the possession of intrinsic independence is a matter of personal quality rather than of rules that formulate certain objective tests."<sup>70</sup>

To ensure independence in fact in all cases, all that is necessary is a general rule such as paragraph 43 of the WPO, mandating auditors' independence in fact, assuming that all auditors are ethical, i.e., no auditor will accept an audit engagement if he believes he cannot perform his duties objectively and unbiasedly during the audit.

Whether this assumption holds is an empirical question that is beyond the scope of this study. However, there is no reason to doubt that the German accounting profession in general consists of highly ethical and professional people. Intentional unethical conduct seems to be the rare exception that occurs in any professional group.

To have specific rules detailing every possible auditor-client relationship is an inappropriate tool to ensure auditors' independence in fact. It is inappropriate because it unduly

restricts acceptance of audit engagements in those cases where the individual auditor honestly believes that he can be independent in fact while the specific rules may, a priori, disallow such an auditor-client relationship.

Even with a long casuistry and given the above inefficiencies that it will cause, in order to ensure auditors' independence in fact, it is probably impossible to cover all situations. Thus, a general rule would still be required in addition to the casuistry. As noted above, a general rule alone would be sufficient and is most appropriate.

However, a general rule is subject to individual interpretation. Since perceptions of a general rule are bound to differ for some persons, different auditors will arrive at different decisions concerning acceptance or rejection of an audit engagement based on the criterion of independence in fact. Thus, the general rule will result in divergent interpretations in many cases. Nonetheless, we will have achieved independence in fact for all auditors, given the original assumption of ethical behavior.

### Independence in Appearance

In contrast to independence in fact, independence in appearance is a concept of the collective perceptions of users of financial statements. Under this criterion an auditor must appear to be independent to a third party. Whether the auditor is independent in fact is of no concern under this criterion.

Below, independence in appearance will be discussed under two different rules to guide the auditor. First, a general rule

will be employed requiring an auditor to be independent in appearance, such as paragraph 49 of the WPO, then specific rules will be applied covering each conceivable auditor-client relationship.

#### Scenario A

The following assumptions are used:

1. all auditors are guided only by a general rule requiring them to decline any audit engagement which would impair their independence in appearance;
2. a third party representing all users of financial statements is able to make a decision whether, as to all possible auditor-client relationships, they do impair independence in appearance or not;
3. all auditors will decline an audit engagement if their interpretation of the general rule indicates that they are not independent in appearance.

Since the auditors do not know any of the specific rules of the third party, they will have to judge individually each situation when confronted with it. Each auditor must decide for himself how he perceives the third-party-rule for the situation at hand. Since each decision is of a dichotomous type, accept or reject the audit engagement, auditors can be categorized into two groups: those that perceive the rules of the third party correctly, Group I, and those that perceive them incorrectly, Group II, (assuming that the situations dealt with were only those where the third party has ruled that the auditor would not be independent in appearance). Group II thus will be violating the independence in appearance requirement, even though ethical behavior of all auditors was assumed.

However, Group II, in general, will not know that they violated

their code concerning independence in appearance. In a similar future situation they are likely to arrive at the same decision again. Only when the auditor-client relationships are exposed to the public, for example, through bankruptcies of their audit clients, will these relationships be evaluated. The auditor may be surprised to learn that he violated his professional code of ethics concerning the requirement of independence in appearance.

Even though an individual auditor's perception of independence in appearance may agree with the third party rules in many instances, common sense would suggest that sooner or later he will violate the rules unknown to him, unless, of course, the third party rules are always less stringent than the individual auditor's perceptions of the third party rules. In such a case the auditor, assuming he is also independent in fact, may decline an audit engagement even though he is not required to.

In sum, a general rule will not ensure independence in appearance for all situations. It is a sufficient rule only in the extreme (and trivial) case where all auditor-client relationships are considered independent in appearance by the third party. However, in this unlikely case, no rules are needed, general or otherwise. A general rule is inefficient since it may result not only in WPs accepting audit engagements that should not be accepted, but also in rejecting audits that could have been performed.

## Scenario B

Assumption 1 from Scenario A will be changed from a general rule to specific rules that have been determined by the third party. In this case each auditor knows the independence in appearance rules established by the third party for all possible auditor-client relationships. Since ethical behavior of all auditors is assumed, independence in appearance is assured for all audit engagements.

In theory at least, the following sufficient conditions are needed to ensure Total Independence, i.e., independence in fact and in appearance:

1. a general rule mandating independence in fact;
2. specific rules covering all auditor-client relationships where independence in appearance is not given;
3. ethical auditor behavior, i.e., auditors will decline any audit engagement which either impairs their independence in fact or independence in appearance, or both, as determined under (1) and (2).

These conditions will guarantee Total Independence for the auditing profession. However, to apply this concept in practice may be somewhat difficult. Some of the difficulties will be explored below.

### Relationship Between Independence in Fact and Independence in Appearance

As noted earlier, Total Independence is made up of independence in fact, which is an individual (perception) concept, and independence in appearance, which is a collective (perception) concept.

TABLE 1  
Type of Auditor-Client Relationships

Auditor-Client Relationship	Total Independence	
	Independent in fact	Independent in appearance
Type A	Yes	Yes
Type B	Yes	No
Type C	No	No
Type D	No	Yes

For an auditor to be independent as required, he must be both.<sup>71</sup>

Consider Table 1, depicting the four different types of auditor-client relationships that may occur. This table will be referred to frequently in the following discussion.

If all auditor-client relationships were of Type A or Type C, there would be no need for specific rules covering independence in appearance. In either type of auditor-client relationship, the auditors' perceptions regarding his independence in fact coincide with the perception of users of financial statements regarding independence in appearance. Having auditors rely on complete specific rules covering independence in appearance would also ensure independence in fact since they both coincide. Either way, if all possible auditor-client relationships were of Type A and Type C, there could not be any problem with the auditor's independence status assuming ethical behavior. Any

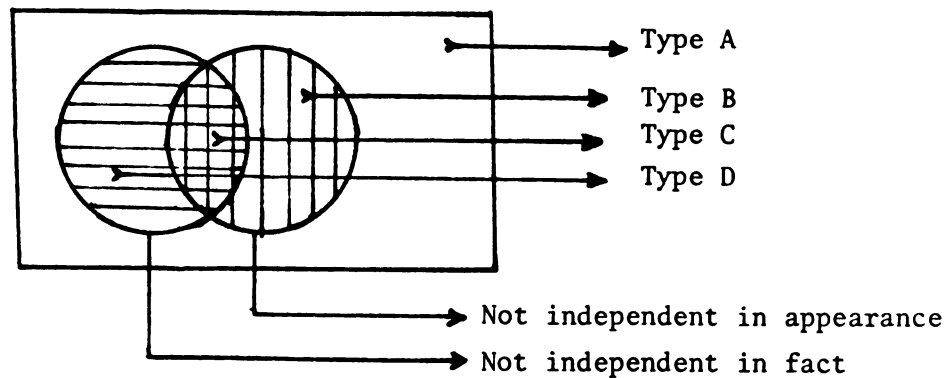
issue stemming from these types of relationships (actually only Type C) can only be caused by unethical behavior as defined earlier.

If all possible relationships were of Type B and Type D, there would be a potential problem by relying on only one component of the Total Independence concept. In a Type D situation, relying solely on independence in appearance rules will not ensure Total Independence. In this situation, reliance must be placed on the auditor's ethical standards to reject the engagement since he is not independent in fact. However, since he appears independent to users of financial statements, they will not know about his status, since independence in fact is an individual auditor perception concept. He could only be judged after the fact, i.e., if it becomes known that he did not make independent or unbiased audit decisions.

For a Type B relationship, total independence can be ensured by relying on independence in appearance rules. Without specific independence in appearance rules there is a chance that the individual auditor will misjudge his independence in appearance status since he feels he is independent in fact. It seems that this type of auditor-client relationship would be of greatest concern to the auditing profession. Consequently, to have specific rules to guide each member of the accounting profession with his independence in appearance status seems to be important. Even if ethical behavior by all members of the auditing profession is assumed, without specific independence in appearance rules, there is the potential of noncompliance with the requirement of Total Independence.



FIGURE 1



The four possible auditor-client relationships can also be shown graphically with the help of a Venn diagram as depicted in Figure 1.

In sum, in a Type A or C relationship, the auditors' perceptions of independence in fact and the perception of independence in appearance by financial statement users are identical. Type B represents a relationship in which users of financial statements have a perception of independence that is stricter than the auditors' perceptions of their own independence. In a Type D relationship the opposite is true. Using the Venn diagram, only the area outside both circles represents auditor-client relationships in which the auditor is truly independent.

#### Implications and Summary Remarks

In the preceding discussion it was concluded that without specific rules guiding the auditor as to what auditor-client relationships impair independence in appearance, auditors'

independence cannot be assured in all cases, even using the most ideal assumptions.

Although it seems unlikely that complete rules of independence in appearance covering every possible auditor-client relationship could be devised, a first step toward this goal is to determine empirically how perceptions of independence in appearance differ between auditors and users of audited financial statements. Using the terminology of Table 1, it seems that specific guidelines are especially needed for Type B relationships. Without specific guidelines covering independence in appearance, the auditor may not reach the proper accept/reject decision concerning a given audit engagement, since he considers himself independent in fact in a Type B relationship.

Another conclusion from the discussion is the underlying implication that for Type A and Type C relationships, reliance on only one component of the Total Independence concept would result in Total Independence. However, as long as the auditor knows that he must be both independent in fact and in appearance, he may unnecessarily reject an audit engagement of Type A in the absence of specific independence in appearance rules. It seems that the only auditor-client relationships which are in less need of specific independence in appearance rules are Type C and Type D. Since the auditor considers himself to be not independent in fact he will reject the audit engagement without concern for any independence in appearance rules. As noted in the discussion of the German accounting literature, several authors have suggested attacking the independence problem by extending specific guidelines

concerning independence in appearance. Wüstemann and Schruoff both suggested this alternative in general terms. Others used a more piecemeal approach, calling for discontinuance of certain auditor-client relationships currently in existence in Germany.<sup>72</sup>

By dichotomizing the Total Independence concept into independence in fact and independence in appearance, it was possible to reason that to assure independence in fact, a general rule is most efficient, assuming ethical auditors' behavior. Of course, if ethical behavior cannot be assumed the concept is of no value. Without ethical behavior, the very existence of the entire accounting profession is of no value, once the public becomes aware of this. The very foundation of the auditing profession rests on public trust.

It was shown in Chapter Two, and again in Chapter Three, that the German auditing profession lacks extensive specific independence in appearance rules. It is the contention of this study that most of the current criticism stems from the lack of such specific rules. If this criticism is to subside, an extension of the present limited casuistry seems worthwhile so that the credibility of the WP profession can reach the level of public trust it needs to fulfill its function in today's complex society.

This research empirically investigates the perception of certain groups of users of financial statements and the perception of WPs as to the auditors' appearance of independence in a variety of different auditor-client relationships to ascertain the degree to which auditors and users of financial statements agree or disagree in these situations.

In the following chapter, selected auditor-client relationships, the research design and methodology are discussed.

## CHAPTER THREE-FOOTNOTES

1. For example, quoting the International Study Group (paragraph 2) "Independence has long been one of the most important attributes of the public accounting profession. It is the fundamental philosophical foundation that makes it possible for persons with diverse interests in the financial statements of a company, such as stockholders, potential stockholders, creditors, governmental agencies, and others, to rely on the opinion of the auditor. Independence has been expected by users of financial statements to the point where auditors recognize it as a primary attribute to be maintained under all circumstances." See Accountants International Study Group, Independence of Auditors (October 1976).
2. Kane, R. L. (ed.), CPA Handbook (New York: The AIA, 1952), Chapter 13, p. 8.
3. American Institute of Certified Public Accountants, Code of Professional Ethics - March 1975 Edition (New York: AICPA, 1975), p. 6.
4. Ibid.
5. Arens, A. A., and Loebbecke, J. K., Auditing: An Integrated Approach (New Jersey: Prentice Hall, Inc., 1976), p. 34.
6. Gesetz über eine Berufsordnung der Wirtschaftsprüfer (Wirtschaftsprüferordnung) i.d.F. der Bekanntmachung der Neufassung v. November 5, 1975 (Düsseldorf, IdW-Verlag GmbH, 1976), pp. 32-37.
7. Richter, M., "Die Unabhängigkeit des Wirtschaftsprüfers," Universität des Saarlandes (July 1976), p. 51.
8. Institut der Wirtschaftsprüfer, WP-Handbuch 1977 (Düsseldorf: IdW-Verlag GmbH, 1977), p. 51.
9. Papers presented with subsequent panel discussions are compiled in Busse von Colbe, W., and Lutter, M. (eds.): Wirtschaftsprüfung Heute: Entwicklung oder Reform? Ein Bochumer Symposium (Wiesbaden: Verlag Dr. Th. Gabler, 1977).
10. Betteridge, H. T. (ed.): Cassell's German & English Dictionary (London: Cassel & Company Ltd, 1962).
11. Wirtschaftsprüferkammer, Richtlinien für die Berufsausübung der Wirtschaftsprüfer und vereidigten Buchprüfer (December 1, 1977), p. 7.

12. Jäckel, G., Die Unabhängigkeit der Abschlussprüfer bei der Pflichtprüfung von Aktiengesellschaften der Öffentlichen Hand (Hamburg: R. V. Decker Verlag, G. Schenk GmbH, 1960), p. 38.
13. Richter, M., p. 1.
14. Jäckel, G., p. 38.
15. Richter, M., pp. 1-3.
16. Wysocki, K. V., Betriebswirtschaftliches Prüfungswesen, Prüfungsordnungen und Prüfungsorgane (München: Verlag Franz Vahlen, 1972), p. 131.
17. Ibid., pp. 131-133.
18. Some of the more recent bankruptcies are: Herrstatt Bank, SB-Mehrwert, and Stumm; see Wintermann, J., "Renaissance des Testats," Börsen Zeitung (April 4, 1977), p. 1 ff.
19. Knief, P., "Der Wirtschaftsprüfer im Spannungsfeld zwischen gesetzlichem Auftrag und öffentlicher Erwartung," Betriebswirtschaftliche Forschung und Praxis (Heft 2, 1976), pp. 114-119. See also pp. 121-122 for a summary of headlines concerning criticism of the WP profession that were published in newspapers and periodicals in the last few years.
20. For example, the criticism and questions raised by Schruoff, L., "Zur Objektivierung des Unabhängigkeitspostulats bei Jahresabschlussprüfungen," Betriebswirtschaftliche Forschung und Praxis (Heft 2, 1976), pp. 140-150; Kicherer, H.-P., "Kummer mit der Unabhängigkeit," Der Volkswirt (Nr. 16, April 18, 1969), pp. 38 ff.; Leffson, U., "Erkenntniswert des Jahresabschlusses und Aussagewert des Bestätigungsvermerks," Die Wirtschaftsprüfung (Heft 1/2, 1976), pp. 4-9.; Huppertz, W., "Die widersprüchliche Lage des Wirtschaftsprüfers bei der Abschlussprüfung," Blick durch die Wirtschaft - Das Handelsblatt (November 4, 1976), pp. 4-5.
21. Westrick, P. Abschlussprüfung und Abschlussprüfer nach geltendem und zukünftigem Recht (Heidelberg: Verlagsgesellschaft "Recht und Wissenschaft" MBH, 1963), pp. 86-87.
22. This situation is prohibited by the 1977 revision of the WPK's "Richtlinien...", to be effective January 1, 1979.

23. Westrick must be referring to those situations where the Federal government has been a majority stockholder of both the WPG and the auditee. Recent court rulings by the German High Court (Bundesgerichtshof) have established that the Federal government under certain circumstances is considered an enterprise (Unternehmen). In such a case, the casuistry of the Stockcorporation Law of 1965 applies, which implies that this criticism may no longer be valid. However, court rulings have gone beyond the casuistry. The High Court also determined that less than a 50 percent ownership of one entity by another entity could be considered as "affiliated" enterprises (verbundene Unternehmen) if special circumstances suggest a dominating influence of one by the other. See, "Aus der Rechtsprechung," Die Wirtschaftsprüfung (Heft 3, 1978), pp. 80-84.; and Müller, H. P., "Anmerkungen zum Urteil des BGH vom 13. Oktober 1977 über die aktienrechtliche Unternehmenseigenschaft von Gebietskörperschaften," Die Wirtschaftsprüfung (Heft 3, 1978), pp. 61-67.; also, "Lufthansa Urteil," Die Aktiengesellschaft (Nr. 12, 1975), pp. 330-333.
24. This may also be a problem in the United States that has not been resolved. However, the SEC approved certain rules in June 1978 which will require companies to disclose (1) the percentage of total non-audit service fees to the total annual audit fee, (2) individual non-audit services which have fees greater than three percent of the annual audit fee, (3) all non-audit services provided by the independent auditor. See The CPA Letter (Nr. 13. July 1978), p. 1.
25. See WP-Handbuch 1977, p. 50.
26. This researcher's translation of paragraph 137 of the Stockcorporation Law of 1937 as quoted in; Karehnke, H., "Zur Unabhängigkeit des Abschlussprüfers," Die Aktiengesellschaft (June 1971), p. 179.
27. The Stockcorporation Law of 1965 eliminated some of the ambiguity of the Stockcorporation Law of 1937 by defining "affiliated enterprises" (verbundene Unternehmen) and uses this term in the casuistry of paragraph 164 of the 1965 law.
28. Kicherer, H.-P., Grundsätze ordnungsmässiger Abschlussprüfung (Berlin: Duncker-Humblot, 1970), p. 106.
29. Karehnke, H., p. 179.
30. Kicherer, H.-P., "Zur Unabhängigkeit des Abschlussprüfers", Die Aktiengesellschaft (February 1972), pp. 37-40.

31. Adler/Düring/Schmaltz, Rechnungslegung und Prüfung der Aktiengesellschaft - Fourth Edition - Band 2, bearbeitet von: Schmaltz, K.; Forster, K.-H.; Goerdeler, R.; Havermann, H. (Stuttgart: C. E. Poeschel Verlag, 1971), p. 224.
32. Ibid.
33. Wüstemann, G., Probleme der Glaubwürdigkeit von Abschlussprüfern: Wirtschaftsprüfer und Certified Public Accountant (Frankfurt: Verlag Harri Deutsch, 1975), p. 59.
34. If both, lex specialis and lex generalis cover the same situation, lex specialis takes precedence over any lex generalis. See Leffson, U., "Erkenntniswert des Jahresabschlusses...", pp. 7-8.
35. Mitteilungsblatt der Wirtschaftsprüferkammer Nr. 67 (April 2, 1976), p. 9.
36. Kicherer, H.-P., "Kummer mit der Unabhängigkeit," pp. 38-39.
37. Kicherer, H.-P., "Zur Unabhängigkeit des Abschlussprüfers," p. 38.
38. Wüstemann, G., p. 62. This criticism is somewhat lessened by the WPK's Directives issued in December 1977. In this revision, the WPK does use mandatory edicts regarding two types of auditor-client relationships, namely, direct stock-ownership by a WP in his audit client and maintaining the audit clients books and records.
39. An Aktienamt is a federal government agency whose responsibility would include the supervision and control of activities relating to stock corporations, similar to the function of the SEC in the United States.
40. See Richter, M., Die Sicherung der aktienrechtlichen Publizität durch ein Aktienamt (Köln: Carl Heymanns Verlag KG, 1975).
41. Schulze-Osterloh, J., "Referat: Stellung und Unabhängigkeit des Wirtschaftsprüfers," in: Busse von Colbe, W., and Lutter, M. (eds.), p. 112.
42. Leffson, U. in: "Meinungsspiegel," Betriebswirtschaftliche Forschung und Praxis (Heft 2, 1976), p. 219.
43. Westrick, P., p. 83.
44. See Leffson, U., "Erkenntniswert des Jahresabschlusses...", pp. 4-9.



45. Schruff, L., Der Wirtschaftsprüfer und seine Pflichtprüfungsmandate (Düsseldorf: IdW Verlag GmbH, 1973).
46. Wüstemann, G., pp. 109-110.
47. Ibid.
48. See Dürhammer, W. W., Unabhängigkeit des Abschlussprüfers im Aktiengesetz und in der Praxis (Düsseldorf: Handelsblatt GmbH, 1971), p. 38.
49. Richter, M., "Die Stellung des Abschlussprüfers im Entscheidungs- und Kontrollprozess der Aktiengesellschaft," Diskussionsbeiträge - Fachbereich Wirtschaftswissenschaft, Universität des Saarlandes (September 1977); also, the proposed 5th Directive of the EEC recommends that the auditor be elected for at least three years but not more than six years at a time. See Kaminski, H., "Überblick über die im Jahre 1972 von den Gremien der Europäischen Gemeinschaften veröffentlichten Richtlinien und Stellungnahmen," Journal UEC (April 1973), pp. 82-88.
50. Richter, M., "Die Stellung des Abschlussprüfers...", p. 25.
51. Ibid., p. 6.
52. See Westrick, P., pp. 89-90., and Czech, H. W., "Die Haftung des Wirtschaftsprüfers gegenüber Dritten," Betriebs-Berater (June 10, 1975), pp. 723-726.
53. For example, Westrick, P., p. 106., and Kicherer, H.-P., "Kummer mit der Unabhängigkeit," p. 42., and Richter, M., Die Sicherung der aktienrechtlichen Publizität..., pp. 186-188, seem to favor a broadened liability to third parties.
54. For example, Emmerich, V., "Die Kontrolle der Kontrolleure," in Busse von Colbe and Lutter, M., p. 226, believes that the present liability could be significantly increased, even though not unlimited, to make it still insurable.
55. Westrick, P., pp. 103-104.
56. Schulze-Osterloh, J., pp. 109-110.
57. Ibid., p. 109.
58. Havermann, H., "Meinungsspiegel," Betriebswirtschaftliche Forschung und Praxis (Heft 2, 1976), pp. 213-216.
59. Bedingfield, J., "Effect on recent litigation on Audit Practice," Journal of Accountancy (May 1974), pp. 55-62.

60. Per conversation of this researcher with Mr. Kaminski, Secretary (Geschäftsführer) of the IdW, on December 12, 1977.
61. See, "Reaktion mit Emotion," Wirtschaftswoche (Nr. 29, 1976), pp. 42-43.
62. See Thümmel, M., "Dr. Richters Fragebogen," Leserbriefe, Handelsblatt (June 26, 1976), p. 9., and Richter, M. "Ergebnisbericht über die schriftliche Befragung zur Unabhängigkeit des Wirtschaftsprüfers," Unpublished Summary (June 16, 1976), pp. 3-5.
63. Wüstemann, G., pp. 62-63.
64. Schruff, L., "Zur Objektivierung des Unabhängigkeitspostulats...", pp. 145-150.
65. Ibid., p. 150. An example of such a situation is the recently enacted disclosure requirement by the SEC as described in Footnote 24.
66. Schruff, L., "Zur Objektivierung des Unabhängigkeitspostulats...", p. 149.
67. Wirtschaftsprüferkammer, Richtlinien für die Berufsausübung der Wirtschaftsprüfer und vereidigten Buchprüfer (July 1974).
68. Richter, M., "Diskussionsbeitrag zum Referat: Stellung und Unabhängigkeit des Wirtschaftsprüfers," von J. Schulze-Osterloh, in: Busse von Colbe, W. and Lutter, M. (eds.), p. 129.
69. See Wirtschaftsprüferordnung, pars. 43 and 49.; Juenger, F. K. and Schmidt, L. (translators), German Stock Corporation Act (Köln, Chicago: Verlag Otto Schmidt KG - Commerce Clearing House, Inc., 1967), par. 164.; Wirtschaftsprüferkammer, Richtlinien... (1977), pp. 7-9.
70. American Institute of Certified Public Accountants, Statements of Auditing Standards No. 1 (New York: AICPA, 1972), paragraph 220.03.
71. This requirement exists for WPs and CPAs alike.
72. See Leffson, U., "Erkenntniswert des Jahresabschlusses...", pp. 4-9.

## CHAPTER FOUR

### RESEARCH DESIGN AND METHODOLOGY

The objective of this study is to investigate the perceptions of Wirtschaftsprüfer and two groups of financial statement users concerning the appearance of independence of German auditors for selected auditor-client relationships.<sup>1</sup> In this chapter the research design and methodology that is used to examine empirically the appearance of WPs' independence are discussed. The discussion is divided into five sections:

1. Types of auditor-client relationships investigated
2. Research medium employed
3. Target groups selected
4. Participation of target groups
5. Hypotheses and statistical tests

#### Types of Auditor-Client Relationships Investigated

There is, no doubt, a very large number of potential or actual auditor-client relationships in which the auditors' appearance of independence could be questioned. Any investigation in this area must of necessity be limited either to a representative sample of these questionable auditor-client relationships and/or to a nucleus of the more pressing problem-relationships facing

the auditing profession today. A convenient tool to discuss questionable (or potentially questionable) auditor-client relationships is to categorize them into a manageable number of groups. As mentioned in the preceding chapter, Wysocki was able to condense all types of auditor-client relationships into only two main groups. However, for this discussion, the following categorization is employed which is used in the U.S. literature and, to some degree, also in the German accounting literature:<sup>2</sup>

1. Financial interest (direct and indirect)
2. Bookkeeping and electronic data processing (EDP) services
3. Family relationships
4. Occupations with conflicting interest
5. Business and other similar relationships

The significance of each category is discussed briefly below, and where appropriate, a comparison between U.S. and German accounting practice is made.

#### Financial Interest (direct and indirect)

The U.S. auditor is provided with very definite guidelines as to what relationships would render him not independent in appearance concerning financial interest in an audit client. Both the SEC and the AICPA prohibit an auditor to have any direct financial interest and any material indirect financial interest in audit clients.<sup>3</sup> The debate as to what constitutes a material indirect financial interest is still ongoing in the United States, mainly because the concept of materiality has not been sufficiently researched to develop definite guidelines.<sup>4</sup> However, there is

little doubt that current AICPA and SEC rules greatly assist the auditor in deciding whether to accept or reject an audit engagement for this type of auditor-client relationship.

The German auditor has less guidance in this matter. No specific rules are currently effective concerning this type of situation. The Stockcorporation Law of 1965 avoids this issue completely and the Wirtschaftsprüferordnung does not directly deal with it.

The Directives of the Wirtschaftsprüferkammer (WPK), however, do contain an admonition that this type of situation may possibly impair independence in appearance.<sup>5</sup> This, of course, is not a definite prohibition. A case in point is Niehus' thought on this matter when he notes that "...conspicuously absent from the code [WPO] is the express rule that the Wirtschaftsprüfer may not own any shares in his client company. This in no way means that he may be a shareholder or in any other way related to his client company. This follows from the overriding rule of independence, which in its final analysis is a state of mind."<sup>6</sup>

Nonetheless, the WPK in the December 1977 revision of its Directives took the view that any direct ownership of client shares by WPs will be considered to impair independence in appearance and thus will be expressly forbidden, effective January 1, 1979.<sup>7</sup> Even though the Directives are usually effective when published, the WPK felt it necessary to give those who owned client stocks sufficient time to dispose of them. Apparently, they assumed that a number of WPs do indeed own shares of their audit clients. As an aside, it may be of interest to point out

that concealment of stock ownership is relatively simple since the practice of issuing bearer shares is quite common in Germany.<sup>8</sup>

It should also be noted that the new rule regarding stock ownership of client shares covers only those clients that are audited by the WP (or the auditing firm or auditing group with which he is associated). The rule does not apply to ownership of companies not audited by the WP even though their parent or a subsidiary may be audited by him.<sup>9</sup> Thus it applies only to a direct financial interest with direct being defined in the most limited possible sense.<sup>10</sup>

Another issue concerning financial interest that has been in the limelight in recent years is the ownership of auditing firms and some of their client firms by the same stockholders. The government, at the Federal as well as at the regional level, and some of the larger banks have been the worst offenders of this practice.<sup>11</sup> So far, the WPK has taken the position that under current law and regulations simultaneous ownership of WPGs and their audit clients is allowed as long as it does not exceed 50 percent of shares outstanding.<sup>12</sup> However, this interpretation has been challenged by various authors as well as by recent court decisions.<sup>13</sup>

#### Bookkeeping and EDP Services

To provide bookkeeping or accounting assistance to audit clients has been a time honored practice for auditors in Germany as well as in the United States. The AICPA recognizes this and thus far has not considered this practice, even if extensive,

to impair the auditors' independence in appearance.<sup>14</sup> The SEC, on the other hand, considers the appearance of the auditors' independence to be impaired in such a case.<sup>15</sup>

The WPK's Directives are the only authoritative source for the German auditor that deals with this type of auditor-client relationship. Until the December 1977 revision, the Directives expressly permitted an auditor to assist in the preparation of the financial statements. This activity per se was not considered to impair the auditor's independence in appearance. However, the WPK added the caveat that independence in appearance may be impaired if the auditor has to pass judgment on audit evidence that has been substantially created by the auditor himself.<sup>16</sup> This has been interpreted by some to mean that doing in effect the entire bookkeeping for a client does impair the auditor's independence in appearance.<sup>17</sup>

The latest revision of the Directives, however, is more specific. It explicitly prohibits a WP from performing the audit if he has prepared (or substantially prepared) the financial statements of his audit client.<sup>18</sup> This represents a major change in the WPK's philosophy toward taking a clear stand on certain independence issues, as it did on direct financial interest. It is a departure from past Directives which merely pointed out sensitive situations which may or could impair auditors' independence but left the auditor with no firm guidance. Even with these more explicit guidelines, it is of interest to determine how this issue is viewed by WPs and users of financial statements; whether these groups are in general agreement with the rule as well as what their





perceptions are of this type of situation for selected auditor-client relationships.

#### Family Relationships

In general, the U.S. auditor is not considered to be independent if a close family member serves in an executive position in a client firm and is involved in financial decision making. The positions of the AICPA and the SEC agree in general terms. Several specific rulings exist to guide the U.S. auditor in deciding whether to accept an audit engagement or not.<sup>19</sup>

The German auditor, though, has no specific rules covering situations where a close relative of an auditor is a leading employee of an audit client. The Directives of the WPK do mention, however, that a close family relationship between an auditor and an executive of an audit client company may impair independence in appearance.<sup>20</sup> Whether it does or not is left to the individual WP or WPG to decide.

This study's purpose is also to provide empirical evidence concerning the degree to which certain family relationships are perceived to impair independence in appearance by WPs and important financial statement user groups.

#### Occupations with Conflicting Interest

It seems that all occupations that do not have as their objective the element of impartial judgment are, a priori, incompatible with the audit function. The U.S. auditor is restrained from performing certain services for an audit client. For example,

the SEC has concluded that a CPA will not be independent in appearance if he acts as counsel, broker-dealer, or actively engages in direct competition in a commercial enterprise with an audit client.<sup>21</sup> The AICPA has a similar view on this issue. However, any CPA can engage in any kind of legal activity or profession without losing his CPA certificate as long as he does not engage in audit work that may be conflicting with his non-auditing activities.

In Germany, any activity that is not considered compatible with the status of the WP profession is prohibited, no matter how it relates to any audit engagements, if at all.<sup>22</sup> Violation of this rule may result in the loss of the WP title. The major purpose of this rule is not necessarily to strengthen the auditors' independence status per se, but to enhance and maintain the reputation of the auditing establishment as a profession (freier Beruf) and the reputation of WPs as professionals. Thus management consulting and legal counseling (especially if the WP also has a law degree) are explicitly considered compatible occupations and are officially sanctioned. There is some question, however, as to the kind of activity that falls under management consulting (Unternehmensberatung).<sup>23</sup> Similarly, it could be questioned whether the function of general counsel performed by the auditor still is compatible if performed for an audit client.

#### Business and Other Similar Relationships

The U.S. auditor in general is prohibited from maintaining any kind of close business relationship with his audit clients.

Both the AICPA and the SEC agree that this would impair the auditor's independence status.<sup>24</sup>

The WPK in its Directives also warns that a close business relationship with a leading client employee may impair the auditor's appearance of independence.<sup>25</sup> Certain other auditor-client relationships have also come under closer scrutiny in the German accounting literature and the financial press. Two of special note are economic client dependency (Kundenabhängigkeit) and membership on Supervisory Boards of corporations related in some way to an audit client corporation. Whereas the former type of relationship has also been discussed extensively in the U.S. accounting literature, the latter type does not per se apply to the U.S. business environment.<sup>26</sup> Each type is discussed separately below.

#### Economic Client Dependency

The reason that the SEC has not made a specific ruling on this issue may be partially explained by the fact that usually only large accounting firms have SEC clients and thus fall under SEC jurisdiction. There is very little chance that any one of the audit fees and/or consulting fees received from one client account for more than a small part of total revenue of any given accounting firm.<sup>27</sup>

Some authors in the German accounting literature have called for definite percentage rules, since it is felt that the appearance of an auditor's independence is impaired if an auditing firm derives a major portion of its total revenue from one audit client.<sup>28</sup>

British auditors, for example, are advised by the Joint Committee of the Institutes of Chartered Accountants in England, Wales, Scotland and Ireland that any member of their institute "should make sure that the fees received from any one client or group of associated clients do not exceed 15 percent of his total fee income."<sup>29</sup>

The WPK in the 1977 revision of its Directives acknowledges that a WP who receives a significant portion of his total income from one audit client may impair his independence. However, the WPK falls short of setting specific limits, implying that each situation must be considered on its own merits.

#### Wirtschaftsprüfer on Supervisory Boards

Prior to the issuance of the December 1977 revision of the WPK's Directives, the only authoritative source dealing with the propriety of WPs sitting on Supervisory Boards of corporations was the limited casuistry of paragraph 164 of the Stockcorporation Law of 1965.<sup>30</sup>

In one of the most publicized recent bankruptcies of a German enterprise, the Herrstatt Bank, it was disclosed that the leading member of the accounting firm that audited Herrstatt Bank was also a member of the Supervisory Board of the Gerling Global Bank, an affiliate of Herrstatt Bank.<sup>31</sup> However, a judicial/professional investigation requested by the auditor himself resulted in dismissal of any charges because it was ruled that the circumstances did not violate paragraph 164 of the Stockcorporation Law of 1965 and that the auditor had not violated (intentionally

or by neglect) paragraph 49 of the WPO.<sup>32</sup>

Nonetheless, the Herrstatt Bank bankruptcy did strike a chord with the WPK since, in the same issue of the Mitteilungsblatt der Wirtschaftsprüferkammer that publicized the acquittal of all charges against the auditor of Herrstatt Bank, the WP profession was advised to exercise due judgment when considering a position on a Supervisory Board even if the position would not per se violate Stockcorporation Law.<sup>33</sup>

The WPK also discusses this issue in its December 1977 Directives. For the first time, the Directives forbid WPs from holding memberships on Supervisory Boards already prohibited by the Stockcorporation Law of 1965. However, the Directives go beyond the casuistry of paragraph 164 of the Stockcorporation Law of 1965 when voicing reservations concerning the situation where an auditor is a member of the Supervisory Board of a company which, though not a related enterprise as defined by corporate law,<sup>34</sup> is connected to the audit client company on a financial or other basis.<sup>35</sup>

What these financial or other connections are is left to the interpretation of the individual WP or WPG. It should be noted that this new rule does not become effective until January 1, 1979 to allow affected WPs to resign either their Supervisory Board posts or certain audit engagements.

## Criteria for the Selection Process of Chosen Auditor-Client Relationships

This study investigates selected auditor-client relationships covering the five types of situations discussed above. To maximize the potential benefit of this research, situations were selected that are of interest not only to the German WP profession but to the U.S. accounting profession as well. Auditor-client relationships that were not of importance to the U.S. profession were included in the study only if they were of major importance to the German WP profession. Seventeen different situations were selected using this criterion. Since a number of situations consisted of several separate auditor-client relationships, the total number of situations investigated were twenty-seven. Ten of the situations selected were taken from Lavin's questionnaire.<sup>36</sup>

Lavin conducted an empirical study in 1973 concerning U.S. CPAs and U.S. users of financial statements about their perceptions of auditors' independence. Twelve separate auditor-client relationships from Accounting Series Release (ASR) 126 were selected by Lavin on which both the AICPA and the SEC have taken a position concerning their interpretation of the described auditors' independence status. Since the SEC and the AICPA do differ on some of the independence issues, even though both supposedly base their rulings on third party perceptions of independence in appearance, Lavin wanted to gather empirical support for either one (or none) of the positions.

Questions two and twelve of Lavin's questionnaire were deleted from this study since they were considered nonapplicable

to the German environment. The remaining ten situations chosen from Lavin's study are of importance to the German WP profession. To replace them with ten different situations would not have improved the relevance of this study. Including these ten situations in the present study allows a comparison of the results with Lavin's results, including some interesting findings that may support either the AICPA or SEC position on certain issues.

Of course, perceptions may change over time, and the time lag between Lavin's research and this study may confound the comparison between CPAs' perceptions on independence and those obtained from WPs. However, the SEC issued ASR 234 in December 1977, to update prior rules on auditors' independence, particularly ASR 126, issued in 1972. It seems that the SEC's view of what constitutes an independent auditor-client relationship has not changed significantly between 1972 and 1977.

#### Research Medium Employed

There are basically two methods of data collection available for survey research. They are, (a) personal interview and (b) mail questionnaire. Each method has some advantages over the other.

The major advantage of a personal interview is that the researcher can be assured that the subject selected in the sample is indeed answering the questions. The interviewer can also call in advance to arrange the interview at a convenient time for the respondent so that nonresponses can be minimized. In addition, the researcher can be assured that all questions will be answered.<sup>37</sup>

The major advantage of a mail questionnaire is that a large number of people can be reached at a reasonable cost, allowing for a relatively large sample size. In addition, since each subject in the sample receives exactly the same information, the responses are not confounded by possible interviewer's bias.

A mail questionnaire was employed for this study because the questions presented are concise and relatively easy to comprehend. There was also no reason to believe, a priori, that persons other than those approached would respond to the questionnaire, since the type of questions asked and the subject under study are of importance to the persons in the sample.

#### The Questionnaire

The questionnaire included a set of instructions explaining the questionnaire and gave a definition of auditors' independence pointing out that an auditor must not only be able to make objective and unbiased audit decisions but must also appear to be independent. (See Appendix A, B, and C for sample questionnaires.)

The main body consisted of 27 separate situations of auditor-client relationships that were to be answered with a "Yes"/"No" response, i.e., "Independent"/"Not Independent". For questionnaires sent to users of financial statements, each respondent was also asked to indicate how each situation presented would affect his financial decision, using a five-point Likert-type scale response. A very limited section was devoted to some background information on the respondent and space for additional comments.

Each questionnaire was accompanied by a cover letter signed



by the Chairman of the Department of Accounting and Financial Administration at Michigan State University. The cover letter and the questionnaire were in German. (See Appendix A, B, and C for sample of cover letters.) It was felt that an English language questionnaire might cause some people to think that the situations described were not applicable to Germany. The possibility that a number of sample subjects might not have responded or might have responded improperly because they were not sufficiently fluent in English was also considered a factor.

The situations selected from Lavin's questionnaire were translated into German and certain words and expressions were translated to convey the spirit rather than the word.<sup>38</sup> Minor changes were made in the German translation.<sup>39</sup>

#### Verification of the Questionnaire Design

The form of the questionnaire closely followed the design of Lavin's questionnaire. Lavin pretested his questionnaire extensively which resulted in some revisions to the final questionnaire. Written permission was obtained from Dr. Lavin to use his results in this study. Dr. Lavin did not indicate any problem with his questionnaire design.

Even though this questionnaire addressed an audience similar to Lavin's, extra care was taken in the translation. The validity of the translation as well as appropriate usage of German terms was verified as follows: the initial German version of the questionnaire was reviewed by a member of the Department of German and Russian at Michigan State University and necessary modifications

were made. The questionnaire was then reviewed by a prominent German Wirtschaftsprüfer who is also affiliated with one of the "Big Eight" accounting firms. In addition, two more German accounting professionals also reviewed the questionnaire in detail. Suggestions made were incorporated and resulted in certain changes in wording and terms as well as the addition of three more questions to the preliminary questionnaire.

It was felt that this procedure provided reasonable assurance that the design of the questionnaire and the questions asked were appropriate. Even though extensive field testing on a larger sample of German respondents is theoretically a preferred practice, this was not done in order to minimize biased responses. Since the WP profession is a relatively small group, mailing a pilot questionnaire to a larger sample of WPs far in advance of the mailing of the final questionnaire may have resulted in either:

- a) group responses rather than responses of individual perceptions, or
- b) no responses due to a possible negative influence by the professional organizations.

Although either consequence could also have occurred without the mailing of a pilot questionnaire, it was felt that having no preliminary mailing would result in an acceptable response rate before any interference by the professional organizations could take effect.

A case in point is Richter's research in 1975, which consisted of a mail survey concerning certain groups' perceptions of WPs performing management consulting services for their audit clients.<sup>40</sup> The professional organizations, apparently fearing negative

repercussions to the WP profession, interfered with his research by mailing two separate letters to all WPs noting that they had serious reservations about Richter's research and thus did not endorse it.<sup>41</sup> According to Richter, no more questionnaires from WPs were returned to him after this. However, he had already received a somewhat satisfactory response rate before these letters were received by WPs. Whether Richter would have received many more responses without this interference by the WPK and IdW is debatable.

For the same reason, this researcher did not schedule an interview with representatives from the IdW and the WPK until the first mailing of the questionnaire was sent out. However, during the December 12, 1977 meeting with Mr. Kaminski from the IdW and Mr. Pfefferer from the WPK, the questionnaire was discussed in detail and no objections were raised as to the propriety of the research subject and methodology.<sup>42</sup> Any inquiries to the IdW and/or WPK by sample subjects concerning this research were responded to neutrally by these professional organizations.<sup>43</sup>

However, a number of WPs apparently did request an interpretation from the WPK of how current regulations could be interpreted in answering the questionnaire.<sup>44</sup> Two questionnaires were received that were not individually answered but had the WPK's interpretation attached as a substitute for their responses. Since the objective of this study is to ascertain individual perceptions of auditors' appearance of independence, these questionnaires were not included in the tabulation of the results.

### Target Groups Selected

As noted earlier, the study focuses on auditors' independence in appearance as perceived by WPs and users of financial statements audited by WPs.

#### Wirtschaftsprüfer Sample

To obtain a representative sample of WPs, 380 WPs were randomly selected from the most current WP-directory (1976/77 WP-Verzeichnis), which lists all WPs licensed to practice as of December 1, 1976. An additional 40 WPs were randomly selected from those WPs that were listed as belonging to one of the "Big Eight" international accounting firms, to provide additional responses from this group for use in various comparisons.

#### Users of Financial Statements

In the German accounting literature users of financial statements are sometimes identified as investors, creditors, and employees of the audited firm as well as the public in general.<sup>45</sup> In U.S. accounting research, financial analysts and bank loan officers are frequently used to represent investors' and creditors' groups. Actual stockholders are used less frequently to represent the investor group apparently because of the difficulty in obtaining a sample and the possibility of a very low response rate.<sup>46</sup>

Richter used journalists of the German financial press as a user group of financial statements.<sup>47</sup> He considered them to be an important user group since they are also opinion leaders (Meinungsmultiplikatoren). However, the WPK criticized this selection as being slanted in representing all users of financial statements.<sup>48</sup>

In this study leading bank officers of the larger banking institutions in Germany were used to represent financial statement users. Directors of investment departments (Leiter der Wertpapierabteilung - LWP) and directors of loan departments (Leiter der Kreditabteilung - LKR), were chosen to represent the investors' and creditors' point of view. Financial analysts in brokerage firms such as exist in the United States are not common in Germany. A German resident contemplating to purchase stocks of German corporations would call his banker, just as his U.S. counterpart would call his stockbroker. Leading bank officers of the larger banks were considered, a priori, to represent a well-informed and important user group of audited financial statements.

Even though there are over 6,000 banks located in Germany with over 37,000 branches,<sup>49</sup> it was felt that a random selection would be inappropriate because it would include too many smaller banks which not only are less likely to use audited financial statements to any great extent to make loan decisions, but also are less likely to deal with common stock securities.

Thus a nonrandom selection was performed as follows: using the Rand McNally International Bankers Directory, Final 1976 Edition, all banks in the 12 largest cities in Germany having over 500 million Deutsche Mark in assets were selected. Since there are a few very large banks that have branches many times the size of small and medium banks, the branches of four of those "mammoth" banks (Grossbanken) in each of the selected cities were included in the sample as well. Also included in the sample were 12 subsidiaries of foreign banks located in Germany (8 U.S.

banks, and one bank each from the Netherlands, France, England, and Japan). A total of 110 different banks (including the foreign banks) and 44 branches were selected.<sup>50</sup>

One questionnaire was sent to the director of the investment department (LWP) and one questionnaire was sent to the director of the loan department (LKR) of each of the banks and branch banks selected. Since the names of the sample subjects were not readily available, the questionnaires were mailed to the Leiter der Wertpapierabteilung and to the Leiter der Kreditabteilung of each bank in the sample.

#### Participation of Target Groups

The questionnaires were mailed to the sample subjects from Germany on November 25, 1977. A stamped, self-addressed return envelope to this researcher's temporary German address were included. The return envelopes were numbered for identification purposes. A follow-up mailing which included a second request to reply, another copy of the questionnaire and another self-addressed return envelope was sent on December 16, 1977 to those that had not responded as of that date.

Responses received as of March 15, 1978, are included in the study. Most responses were received prior to January 1, 1978. Eighty-six percent of the responses from LWPs, 93 percent from LKRs and 87 percent of the responses from WPs were received prior to January 1, 1978.

As Tables 2, 3, and 4 indicate, the rate of responses were as follows: WPs, for the general sample, 35 percent; for LKRs

63.6 percent for main offices, and 22.7 percent for branch banks; for LWPs 40 percent for main offices, and a zero response rate for branch banks. However, due to nonusable responses, the responses that could be used in the final tabulations were 28.4 percent for WPs, 44.5 percent for LKRs in main offices, and 28.2 percent for LWPs in main offices. Bank branch offices had a rate of usable responses for LKRs of 13.6 percent and a zero response rate for LWPs. The sub-sample for "Big Eight" WPs had a 25 percent response rate with a usable response rate of 20 percent.

The lower response rate of usable responses for LKRs from branch banks as compared to LKRs from main offices was 13.6 percent and 44.5 percent, respectively. This may be explained partially by the fact that the LKRs of branch offices might have thought that the questionnaire did not apply to them since they belonged to a branch bank. The possibility cannot be ruled out that interest in this research is of lesser interest to branch LKRs than to LKRs in main offices due possibly to the different types of loans granted which require less involvement with audited financial statements.

The zero response of LWPs of branch offices may be explained as follows:

- a) Investment decisions are more centralized and may not be made at the branch level at all.
- b) One of the main offices of the four "mammoth" banks declined to participate and may have informed the branches.
- c) Another of these four banks completed the questionnaire at the main office but indicated that they did not appreciate that "leading men in various branches of their bank had also received questionnaires." Apparently they thought that one questionnaire per bank was sufficient.

TABLE 2

## Participation by Wirtschaftsprüfer (WPs)

	General Sample		Additional "Big Eight" WPs	
	#	%	#	%
Sample subjects	380	100.0	40	100.0
Responses received	133	35.0	10	25.0
Nonusable responses	25	6.6	2	5.0
Usable responses	108	28.4	8	20.0

TABLE 3

## Participation by Directors of Loan Departments (LKR's)

	Main Office		Branch Office	
	#	%	#	%
Sample subjects	110	100.0	44	100.0
Responses Received	70	63.6	10	22.7
Nonusable responses	21	19.1	4	9.1
Usable responses	49	44.5	6	13.6

TABLE 4

## Participation by Directors of Investment Departments (LWPs)

	Main Office		Branch Office	
	#	%	#	%
Sample subjects	110	110.00	44	100.0
Responses received	44	40.0	0	0.0
Nonusable responses	13	11.8	0	0.0
Usable responses	31	28.2	0	0.0



- d) It is possible that because so few, if any, investment decisions are made at the branch level, the auditors' independence may simply be taken as given. This attitude was even stated in some of the nonusable responses of bank officers of non-branch banks.

### Nonusable Responses

Since there is a relatively large proportion of nonusable responses among all three sample groups, it is appropriate to analyze these. Tables 5, 6, and 7 summarize the reasons stated by the sample subjects for not completing the questionnaire as requested. As these tables show, the reasons for not completing the questionnaire vary. Of the WPs that returned the questionnaire incomplete, 40.7 percent indicated that they were either retired (18.5 percent), had no time to spare (11.1 percent) or could not answer the questions with a simple yes or no (11.1 percent).

For LKRs, 68 percent of those that returned the questionnaire unanswered indicated that they did so for "fundamental reasons" (28 percent), believed that the auditor-client relationships described did not exist in Germany (24 percent), or considered the research to be of no relevance to them (16 percent).

The LWPs who explained their noncompliance with the research request indicated that their banks had no stock dealings and thus disqualified themselves from answering the questionnaire (30.8 percent). Other reasons varied from their banks not being "true" banks, to being a subsidiary of another bank, and to having the bank's accounting personnel complete the questionnaire.

TABLE 5  
Analysis of Nonusable Responses - WPs

	#	%
Subject had retired	5	18.5
No time to fill out the questionnaire	3	11.1
Could not answer with a simple yes or no	3	11.1
No reasons given	2	7.4
Subject had passed away	2	7.4
Mailed WPK's interpretation only	2	7.4
Were waiting for results of this researcher's meeting with officials of the WPK and IdW	2	7.4
Didn't know if IdW had approved research	1	3.7
Questionnaire was passed on to higher-ups	1	3.7
Subject belonged to an audit association for co-ops*	1	3.7
Subject was out of the country	1	3.7
Subject did not perform any audits	1	3.7
Subject needed more time	1	3.7
Not answered for "fundamental reasons"***	1	3.7
Only asked for summary of research results***	1	3.7
	Rounding	0.1
	Total	<u>27</u>
		<u>100.0</u>

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\*Prüfungsverband

\*\*Grundsätzliche Erwägungen

\*\*\*He may have filled out the questionnaire since two questionnaires were received in neutral envelopes that were postmarked from the same city

TABLE 6

## Analysis of Nonusable Responses - LKRs

	#	%
Not answered for "fundamental reasons"	7	28.0
Believed situations did not exist in Germany	6	24.0
Research not relevant to them	4	16.0
No time to fill out questionnaire	2	8.0
Claimed to have mailed questionnaire*	2	8.0
Independence more complex than questionnaire indicates	1	4.0
Questionnaire was passed on to higher-ups	1	4.0
No reasons given	1	4.0
Not involved in extending credit to business	1	4.0
	<u>25</u>	<u>100.0</u>

\*Two questionnaires were returned with no identification number. One of these was postmarked from the same city as one of the two nonrespondents. The other questionnaire was returned from a city 200 miles away from the location of the other nonrespondent.

TABLE 7

## Analysis of Nonusable Responses - LWPs

	#	%
Bank not involved with stock dealings	4	30.8
Subject's bank not a "true" bank	1	7.7
Belonged to a subsidiary where no investment decisions were made	1	7.7
Believed situations did not exist in Germany	1	7.7
Believed there was no independence problem	1	7.7
Research not relevant to them	1	7.7
No reasons given	1	7.7
No time to fill out questionnaire	1	7.7
Not answered for "fundamental reasons"	1	7.7
Accounting department filled out questionnaire	1	7.7
	<u>13</u>	<u>100.0</u>
Rounding		(0.1)
Total	<u>13</u>	<u>100.0</u>

### Analysis of Usable Responses from Bank Officers

Table 8 gives a breakdown of banks selected from the 12 largest German cities, by city. Branches are not included in this table.

From this table it can be seen that for LKRs the rate fluctuates between cities from 28.6 percent to 100.0 percent. However, this may partly be due to chance because of the small number of banks selected in some cities.

For LWPs the response rate for cities that responded was approximately at the overall average and above. However, for banks located in four cities, the response rate was zero. It could be speculated that banks located in these four cities either have few or no stock dealings or LWPs are not concerned about auditors' independence. It should be noted that the response rate for LWPs is consistently below those of LKRs, except for Frankfurt where the response rates of both LWPs and LKRs were the same. Perhaps auditors' independence may be of greater concern to the lending decision than to the investment decision.

### Comments on Nonresponse Bias

With any research involving mailed questionnaires, there is the possibility that there are significant differences between those sample subjects that responded to the questionnaire and those that did not. This is a problem that exists if there is a significant proportion of nonrespondents. Thus, the responses received may not be representative of the population from which the original sample was selected. In this study the nonresponse rate for WPs was 66 percent. For LKRs and LWPs the nonresponse

TABLE 8

Breakdown of Banks Selected by City (not including branches)

City	Total banks selected		Usable Responses LKRs		Usable Responses LWPs	
	#	%	#	%	#	%
Berlin	7	6.4	3	42.9	2	28.6
Bremen	7	6.4	4	57.1	0	0.0
Dortmund	2	1.8	1	50.0	0	0.0
Düsseldorf	9	8.2	4	44.4	2	22.2
Essen	3	2.7	3	100.0	1	33.3
Frankfurt	38	34.5	13	34.2	13	34.2
Hamburg	15	13.6	5	33.3	4	26.7
Hannover	6	5.5	4	66.7	2	33.3
Köln	8	7.2	5	62.5	4	50.0
München	6	5.5	4	66.7	3	50.0
Nürnberg	2	1.8	1	50.0	0	0.0
Stuttgart	7	6.4	2	28.6	0	0.0
Total	<u>110</u>	<u>100.0</u>	<u>49</u>	<u>44.5</u>	<u>31</u>	<u>28.2</u>

rates were 48.1 percent and 71.4 percent, respectively.

Even though it is difficult to determine to what extent nonresponse bias exists, if at all, since by definition a non-respondent does not respond, a test used by Buzby<sup>51</sup> which may determine the possible presence of a significant nonresponse bias was applied. This test, suggested by Oppenheim, goes from the premise that "respondents who send in their questionnaires very late are roughly similar to nonrespondents."<sup>52</sup>

To perform this test for the randomly selected WP sample, the mean responses were computed for each of the 27 auditor-client relationships investigated by setting an "Independent" response equal to one and a "Not independent" response equal to zero. These mean responses were computed for the last 14 returned questionnaires and for the first 14 questionnaires received. (These were the total usable questionnaires received during the first two days.) A t-Test was performed to test for significant differences between the means of the early and late respondents.<sup>53</sup>

The test results failed to show any significant differences of the mean responses at an alpha level of 0.05 for 26 out of 27 situations. Most alpha levels exceeded 0.35. Examining the value of the t-statistics did not reveal a subtle bias either. Thirteen of the signs were negative, 11 were positive and in 3 cases the t-statistic was zero. As Buzby notes, "a few of the more significant t's could still be the result of chance because of the large number of tests conducted."<sup>54</sup> Thus, it may be concluded that the above test results tend to indicate a lack of a material nonresponse bias in the WP sample.

A similar test for nonresponse bias was not performed for LKRs and LWPs since the number of responses were too small to obtain a sufficient sample of late respondents to make this test meaningful. However, there is no reason to believe that LKRs and LWPs would have a nonresponse bias different from WPs.

### Hypotheses and Statistical Tests

There are a total of nine hypotheses to be tested in this study. To facilitate the discussion, these hypotheses are grouped by the statistical procedures employed to test the null hypotheses in each of the categories. Each hypothesis is stated in both the null and alternative form. The expected results and the statistical tools to test each null hypothesis will be discussed.

#### Hypotheses I through V

- I.      $H_0$ : There is no consensus among Wirtschaftsprüfer (WPs) regarding their perceptions of the concept of auditors' independence.  
         $H_1$ : There is consensus among Wirtschaftsprüfer (WPs) regarding their perceptions of the concept of auditors' independence.
- II.     $H_0$ : There is no consensus among Leiter der Kreditabteilung (LKRs) of banks located in Germany regarding their perceptions of the concept of auditors' independence.  
         $H_1$ : There is consensus among Leiter der Kreditabteilung (LKRs) of banks located in Germany regarding their perceptions of the concept of auditors' independence.
- III.    $H_0$ : There is no consensus among Leiter der Wertpapierabteilung (LWPs) of banks located in Germany regarding their perceptions of the concept of auditors' independence.  
         $H_1$ : There is consensus among Leiter der Wertpapierabteilung (LWPs) of banks located in Germany regarding their perceptions of the concept of auditors' independence.

Hypotheses I through V cont.

- IV.  $H_0$ : There is consensus among Wirtschaftsprüfer (WPs) regarding their perceptions of the concept of auditors' independence that coincides with AICPA rulings on independence.
- $H_1$ : There is no consensus among Wirtschaftsprüfer (WPs) regarding their perceptions of the concept of auditors' independence that coincides with AICPA rulings on independence.
- V.  $H_0$ : There is consensus among Wirtschaftsprüfer (WPs) regarding their perceptions of the concept of auditors' independence that coincides with SEC rulings on independence.
- $H_1$ : There is no consensus among Wirtschaftsprüfer (WPs) regarding their perceptions of the concept of auditors' independence that coincides with SEC rulings on independence.

For the purpose of testing various hypotheses, consensus is defined operationally as a statistically significant majority of opinion. Webster's New Collegiate Dictionary defines consensus as (1) group solidarity in sentiment and belief; (2) general agreement; and (3) the judgment arrived at by most of those concerned. It appears that any aggregate opinions within a given group that range between a simple majority of opinion to unanimity represents a consensus. A simple majority of opinion is the minimum requirement for a consensus to exist. In a democratic society such as the United States or Germany, for many decisions of national importance, for example political elections or passage of most laws, a simple majority of votes is sufficient.

Even though in this study consensus is defined as a statistically significant majority of opinion, the degree of consensus is presented as proportions of responses as well as in the form of frequencies. As Lavin notes, this "allows the reader to evaluate



the degree of consensus from his or her own perspective."<sup>55</sup>

#### Expected Results and Statistical Tests

Since WPs, LKRs, and LWPs each represent a distinct group of professionals, one would expect, a priori, that a high degree of consensus exists on any matter of importance within each group. However, recent controversy surrounding the WP profession's independence status suggests some disagreement concerning a number of issues. It is expected that, despite the controversy, there are still enough members in each group with the same view to result in a consensus within each of the three groups. (Consensus is defined as a statistically significant majority at a significance level of alpha less or equal to 0.05.)

In regard to hypotheses IV and V, there is general agreement among internationally active accountants and accounting scholars that the U.S. has stricter and more explicit rules regarding auditors' independence than many other countries, including Germany. Even though rules and regulations do not necessarily reflect the perceptions of individuals, it is believed that WPs' perceptions will not agree with most SEC and AICPA rules. For situations in which the AICPA has taken a different (softer) stance than the SEC, the WPs' perceptions of independence are expected to coincide with those of the AICPA.<sup>56</sup>

#### Statistical Tests Employed

To test hypotheses I, II, and III, the Binomial Test was used since the study is a one-sample design and the data were in

two discrete categories (independent versus not independent).

The following statistical hypothesis was used to test these three hypotheses:

$$H_0: P = Q = 0.5$$

$$H_1: P \neq Q$$

where  $P$  = proportion of responses expected in the "Independent" category, and

$Q$  = proportion of responses expected in the "Not independent" category.

Since consensus was defined as a statistically significant majority of responses in one of the two categories, no consensus thus represents the situation where responses are equally divided into the two categories, i.e.,  $P$  is equal to  $Q$ . To find any statistically significant difference of perception within the three sample groups, the Binomial Test was used since the data are binomially distributed.<sup>57</sup> The binomial distribution is the sample distribution of the proportion we might observe in random samples drawn from a two-class population. The Binomial Test indicates whether it is reasonable to believe that the proportions observed in the sample were drawn from a population having a specified value of  $P$ .

Although the value of  $P$  may vary between populations, it is fixed for any one population. However, even if the value of  $P$  is known for a given population, a random sample of observations from that population is not expected to contain exactly  $P$  proportions in one category and  $Q$  proportions of cases in the other category due to random effects.

As Siegel notes, the binomial distribution tends toward the normal distribution as the sample size (n) increases. The normal distribution is a good approximation when P is close to 0.5 and the sample size exceeds 25, which is the case for all three sample distributions under study. In this case, the sample distribution of the observed frequency (x) is approximately normal with a mean equal to nP and a standard deviation equal to nPQ.

The Null hypothesis is tested as follows:

$$z = \frac{x - \mu_x}{\sigma_x} = \frac{x - nP}{\sqrt{nPQ}}$$

where z is normally distributed with a mean equal to zero and unit variance.

Whether an obtained z is significant, in which case the null hypothesis must be rejected, can be determined by referring to a normal distribution table. With an alpha level equal to 0.05, a probability value greater than 0.05 would indicate that the null hypothesis cannot be rejected. A probability value from the normal distribution table equal to or less than 0.05 would indicate that the null hypothesis is not probable and should be rejected.

For hypotheses IV and V, the statistical hypothesis was defined as:

$$H_0: R = K$$

$$H_1: R \neq K$$

where R = represents the consensus response of WPs and

K = represents AICPA (SEC) rulings concerning auditors' independence.

For example, for hypothesis IV, the Binomial Test as described

above is applied to determine if there is a statistically significant majority opinion of WPs concerning a given auditor-client relationship tested. If the Binomial Test does not reveal a statistically significant majority of responses that are in agreement with the AICPA position concerning auditors' independence for this particular situation, the null hypothesis must be rejected and we could conclude that for the situation tested there is no consensus of WPs who agree with the independence rulings of the AICPA. This test is applied separately for each of the situations where the AICPA position is known. For hypothesis V the same procedures are employed using SEC rulings.

#### Hypotheses VI and VII

- VI.  $H_0$ : There are no differences regarding the perception of the concept of auditors' independence between Wirtschaftsprüfer (WPs), Leiter der Kreditabteilung (LKR) and Leiter der Wertpapierabteilung (LWP) of banks located in Germany.
- $H_1$ : There are differences regarding the perception of the concept of auditors' independence between Wirtschaftsprüfer (WPs), Leiter der Kreditabteilung (LKR) and Leiter der Wertpapierabteilung (LWP) of banks located in Germany.
- VII.  $H_0$ : There are no differences regarding the perception of the concept of auditors' independence between Wirtschaftsprüfer (WPs) and Certified Public Accountants (CPAs).
- $H_1$ :: There are differences regarding the perception of the concept of auditors' independence between Wirtschaftsprüfer (WPs) and Certified Public Accountants (CPAs).

#### Expected Results and Statistical Tests

Referring to hypothesis VI, it seems that there should be differences of perception among the three populations tested.



Each group has some characteristics which differ from the other groups. However, they also share certain characteristics such as a thorough knowledge of financial statement analysis. Concerning hypothesis VII, it appears that there should be few differences between German and U.S. auditors' perceptions of independence since both perform similar functions. However, rules and regulations differ significantly for a number of auditor-client relationships and may have had an influence on the perception of the individual auditors. It is felt that this influence as well as other factors that do differ as described in Chapter Two and Chapter Three, would lead to the conclusion that there are significant differences between the two groups.

#### Statistical Tests Employed

The Chi Square Test of Homogeneity was used to determine whether significant differences between groups existed; three groups for hypothesis VI, and two groups for hypothesis VII. The following statistical hypothesis is used to test hypothesis VI:

$$H_0: P_1 = P_2 = P_3$$

$$H_1: P_1 \neq P_2 \neq P_3$$

where  $P_1$  = proportion of "Independent" responses from WPs

$P_2$  = proportion of "Independent" responses from LKRs

$P_3$  = proportion of "Independent" responses from LWPs.

For hypothesis VII the statistical form is:

$$H_0: P_1 = P_4$$

$$H_1: P_1 \neq P_4$$

where  $P_1$  = proportion of "Independent" responses from WPs

$P_4$  = proportion of "Independent" responses from CPAs as obtained from Lavin's research findings.

If there are no differences in perceptions of auditors' independence between the groups tested, then the proportions of "Independent" responses (or "Not independent" responses) will be the same for each population under study. On the other hand, if the Chi Square Test finds significant differences between the experimental groups, the null hypotheses of no differences must be rejected. In essence, this test determines whether the three samples for hypothesis VI (and the two samples for hypothesis VII) may be regarded as being drawn from the same population.

The Chi Square Test may be used to determine the significance of differences between two or more independent groups when the data consists of frequencies in discrete categories.<sup>58</sup> To test the null hypothesis, the following formula can be used:

$$\chi^2 = \sum_{i=1}^r \sum_{j=1}^k \frac{(O_{ij} - E_{ij})^2}{E_{ij}}$$

where  $O_{ij}$  = observed number of cases categorized in the  $i$ th row of the  $j$ th column

$E_{ij}$  = number of cases expected under the null hypothesis to be categorized in the  $i$ th row of the  $j$ th column.

$r$  = number of rows

$k$  = number of columns.

The values of  $\chi^2$  yielded by this formula are distributed approximately as chi square with  $(r - 1)(k - 1)$  degrees of freedom.

Whether the computed test statistic ( $\chi^2$ ) is significant, i.e., the null hypothesis must be rejected, can be determined

by reference to a table of critical values of  $\chi^2$ s. A value of  $\chi^2$  which is equal to or greater than the value given for a significance level of  $\alpha = 0.05$ , indicates that the null hypothesis is false and should be rejected. In probability terms, if the probability associated with the computed value of  $\chi^2$  is equal or less to 0.05, the null hypothesis is not probable and consequently should be rejected. Of course, if the probability associated with the computed value of  $\chi^2$  is greater than  $\alpha = 0.05$ , the null hypothesis should not be rejected.

#### Hypotheses VIII and IX

VIII.  $H_0$ : Leiter's der Kreditabteilung (LKR's) perceptions regarding the concept of auditors' independence have no effect on their lending decisions.

$H_1$ : Leiter's der Kreditabteilung (LKR's) perceptions regarding the concept of auditors' independence have an effect on their lending decisions.

IX.  $H_0$ : Leiter's der Wertpapierabteilung (LWP's) perceptions regarding the concept of auditors' independence have no effect on their investment decisions.

$H_1$ : Leiter's der Wertpapierabteilung (LWP's) perceptions regarding the concept of auditors' independence have an effect on their investment decisions.

For both, investment and lending decisions, many factors enter into the decision making process. The decision maker's perception of the independence of the auditor of a firm's financial statements is only one of these factors. Nonetheless, it is expected that the perception of auditors' independence has an observable effect on the financial decisions by users of audited financial statements.



### Statistical Tests Employed

Hypotheses VIII and IX are tested using the following statistical hypothesis:

$$H_0: \mu_1 = \mu_2$$

$$H_1: \mu_1 \neq \mu_2$$

where:  $\mu_1$  = mean of the financial decision of those who perceive the auditor to be "independent"

$\mu_2$  = mean of the financial decision of those who perceive the auditor to be "not independent".

The mean response was computed for the 5-point decision scale of those respondents who perceived the auditor to be independent ( $\mu_1$ ) and of those respondents who perceived the auditor to be not independent ( $\mu_2$ ).

The t-Test was used to test whether there was a statistically significant difference between the two means in order to make inferences concerning the differences between the population means of the two groups.<sup>59</sup> If it is found that the sample means are significantly different, the null hypothesis should be rejected. However, if no statistically significant differences are found, the conclusion could be reached that the perception of independence has no effect on the respondents' financial decisions.

The t-statistic can be computed using the following formula:

$$t = \frac{\bar{x}_1 - \bar{x}_2 (\mu_1 - \mu_2)}{Sp^2 \left( \frac{1}{n_1} + \frac{1}{n_2} \right)}$$

where  $\bar{x}_1, (\bar{x}_2)$  = mean of the financial decision of those respondents who perceive the auditor to be "independent" ("not independent")

$\mu_1, (\mu_2)$  = population mean of the financial decision of those who

perceive the auditor to be "independent" ("not independent")

$S_p^2$  = the pooled variance of the sample distribution of the two types of respondents which is computed as follows:

$$S_p^2 = \frac{(n_1 - 1) S_1^2 + (n_2 - 1) S_2^2}{n_1 + n_2 - 2}$$

where  $S_1^2$  ( $S_2^2$ ) is the variance of the sample distribution of those respondents who perceive the auditor to be "independent" ("not independent").

$n_1$  ( $n_2$ ) = sample size of those respondents that perceived the auditor to be "independent" ("not independent").

Referring to a table of critical values for  $t$ , it can be determined whether the computed  $t$ -statistic is statistically significant or not. A probability associated with the computed  $t$ -value which is equal to or less than  $\alpha = 0.05$  indicates that the null hypothesis is not probable and thus should be rejected. On the other hand, if the probability associated with the computed  $t$ -value is greater than 0.05, the null hypothesis should not be rejected.

#### Additional Comments

To perform the various statistical tests and procedures, use was made of the Statistical Package for the Social Sciences (SPSS) made available on the Computer System at Michigan State University.<sup>60</sup> Some computations were performed manually.

In the following chapter the results of the hypothesis tests are discussed. Since each auditor-client relationship described in the questionnaire is a separate issue, each is considered a separate variable and is analyzed and tested individually.

## CHAPTER FOUR--FOOTNOTES

1. The term auditor is used in this chapter to refer not only to a single auditing practitioner but also to refer to an auditing firm.
2. See Accounting Series Release No. 126 (1972); also Rappaport, L. H., SEC Accounting Practice and Procedure - Third Edition (New York: The Ronald Press Company, 1972), Chapter 26.
3. See Security and Exchange Commission, Regulation S-X - Rule 2-01 (1972); and American Institute of Certified Public Accountants, Code of Professional Ethics (New York: AICPA, 1975), Rule 101.
4. See, FASB Discussion Memorandum: An Analysis of Issues related to Criteria for Determining Materiality, Financial Accounting Standards Board (March 21, 1975).
5. Wirtschaftsprüferkammer, Richtlinien für die Berufsausübung der Wirtschaftsprüfer und vereidigten Buchprüfer (July 1974), p. 7.
6. Niehus, R. J., "The Public Accounting Profession in Germany," The Accountant (January 4, 1973), p. 14.
7. Wirtschaftsprüferkammer, Richtlinien für die Berufsausübung der Wirtschaftsprüfer und vereidigten Buchprüfer (December 1, 1977), pp. 7-8.
8. This practice also has other ramifications. To quote Juenger and Schmidt: "The possibility of loss inherent in the ready negotiability of such an instrument [bearer shares], and the impossibility for the stock corporation to communicate directly with its anonymous owners, make it advisable to deposit the certificate with banks for safe keeping and the collection of dividends. The banks...soon obtained blanket authorization for the exercise of voting rights from their depositors... The bankers' vote, combined with their own large holdings and those controlled by them through investment funds, is a major factor in the dominant role played by German financial institutions. See, Juenger, F. K. and Schmidt, L., German Stock Corporation Act (Köln, Chicago: Verlag Dr. Otto Schmidt KG - Commerce Clearing House, Inc. 1967), pp. 9-10.
9. This view was also expressed by the WPK. See Appendix D, Fragen 11 und 12.

10. The new Directives of the WPK do not prohibit ownership of audit client shares by the spouse of the auditor. This type of relationship is expressly prohibited for U.S. auditors since this is considered to be a situation involving a direct financial interest.
11. See Schruff, L., Der Wirtschaftsprüfer und seine Pflichtprüfungsmandate (Düsseldorf: IdW-Verlag GmbH, 1973).
12. Mitteilungsblatt der Wirtschaftsprüferkammer Nr. 67 (April 2, 1976), p. 9.
13. See, "Aus der Rechtsprechung," Die Wirtschaftsprüfung (Heft 3, 1978), pp. 80-84.; and Müller, H. P., "Anmerkungen zum Urteil des BGH vom 13. Oktober 1977 über die aktienrechtliche Unternehmenseigenschaft von Gebietskörperschaften," Die Wirtschaftsprüfung (Heft 3, 1978), pp. 61-67; also, "Lufthansa Urteil," Die Aktiengesellschaft (Nr. 12, 1975), pp. 330-333.
14. AICPA, Code of Professional Ethics; Concepts of Professional Ethics - Rules of Conduct - Interpretation of Rules of Conduct (March 1975 Edition) American Institute of Certified Public Accountants (1975), pp. 29-30.
15. See Rappaport, L. H., Chapter 26, pp. 40-44.
16. WPK, Richtlinien... (1974), p. 8.
17. See Budde, W., in: Busse von Colbe, W., and Lutter, M. (eds.): Wirtschaftsprüfung Heute: Entwicklung oder Reform? Ein Bochumer Symposium (Wiesbaden: Verlag Dr. Th. Gabler, 1977), p. 137.
18. WPK, Richtlinien... (1977), p. 8.
19. See, for example, AICPA, Code of Professional Ethics (1975), pp. 30-32; also, see Rappaport, L. H., Chapter 26, pp. 48-51; and Accounting Series Release No. 126 (1972).
20. WPK, Richtlinien... (1977), p. 7.
21. Accounting Series Release No. 126 (1972).
22. See Gesetz über eine Berufsordnung der Wirtschaftsprüfer (Wirtschaftsprüferordnung) i.d.F. der Bekanntmachung der Neufassung v. November 5, 1975 (Düsseldorf, IdW-Verlag GmbH, 1976), pp. 33-34.

23. For example, is managing an office building considered management consulting and thus a compatible activity or is it considered a business activity and thus is not permitted? The WPK in its response to this research considered it a compatible activity, whereas a prominent German WP reached the opposite conclusion. See Appendix B, Frage 4.
24. See Accounting Series Release No. 126 (1972) and, AICPA, Code of Professional Ethics (1975), pp. 30-32.
25. WPK, Richtlinien... (1977), p. 7.
26. German corporations have two boards of directors, namely the supervisory board (Aufsichtsrat) and the board of management (Vorstand). The supervisory board's function is to oversee management, including the board of management. In the U.S. the functions of both types of directors are combined into one board of directors. If we translate Aufsichtsrat as "board of directors", then this type of auditor-client relationship also applies to the United States. However, a U.S. auditor is prohibited from serving on the board of directors of an audit client.
27. Havermann claims that the SEC limits any accounting firm from deriving more than 5 percent of its total revenue from any one audit client. See, "Meinungsspiegel," Betriebswirtschaftliche Forschung und Praxis (Heft 2, 1976), p. 217. However, there is no such rule currently in effect or being contemplated, according to a member of the SEC staff. (Per telephone conversation by this researcher with a member of the SEC staff on May 31, 1978).
28. Knief, P., "Der Wirtschaftsprüfer im Spannungsfeld zwischen gesetzlichem Auftrag und öffentlicher Erwartung," Betriebswirtschaftliche Forschung und Praxis (Heft 2, 1976), p. 138.
29. Accountants International Study Group, Independence of Auditors (October, 1976), par. 30.
30. However, the WPK urged its members in 1975 (Mitteilungsblatt Nr. 64, p. 4) to seek their advice when considering acceptance of a supervisory board position which may compromise the profession. See, WP-Handbuch 1977 (Düsseldorf: IdW-Verlag, 1977), p. 51-52.
31. See Kruk, M., "Wirtschaftsprüfer als Aufsichtsräte? Gefahren für den Ruf des Berufsstandes," Frankfurter Allgemeine Zeitung (April 9, 1975), p. 13.
32. See, Mitteilungsblatt der Wirtschaftsprüferkammer Nr. 67 (April 2, 1976), p. 10.

33. Ibid. (Anlage), pp. 1-2.
34. "Related enterprise" is defined in paragraph 15 of the Stockcorporation Law of 1965 as follows: "Related enterprises are legally independent enterprises which, in relation to each other are majority-owned and majority-owning enterprises (§ 16), controlled and controlling enterprises (§ 17), members of an affiliated group of companies (§ 18), interlocking enterprises (§ 19), or parties to an enterprise agreement (§ 291, 292)." See Juenger, F. K., and Schmidt, L. (translators) German Stock Corporation Act (Köln, Chicago: Verlag Dr. Otto Schmidt KG - Commerce Clearing House, Inc. 1967), pars. 15-19, 291-292.
35. WPK, Richtlinien... (1977), p. 8.
36. Lavin's selection criteria included that the situations should be "representative examples of cases in which an auditor might appear to be lacking in independence with respect to an audit client." See Lavin, D., "Financial Statement Users' and Accountants' Perceptions of the Independence of the Auditor in Selected Client-Auditor Relationships" (Unpublished Dissertation, University of Illinois, 1974), pp. 85-86.
37. For a more detailed account, see Leabo, D. A., Basic Statistics - Fifth Edition (Homewood: Richard D. Irwin, Inc., 1976), pp. 46-48.
38. Since the organizational form of partnership is not common in Germany, partner is translated as Wirtschaftsprüfer. It was felt that this translation was the most appropriate for the German accounting environment. A Wirtschaftsprüfer's position in an accounting firm is similar to a U.S. partner's position. He has procuration (Prokura), and usually shares in the profits of the firm.
39. In question 4 of the questionnaire, partner was translated as a "staff member of the accounting firm with 5 years auditing experience." This was done to minimize nonresponses to this question since the professional law (WPO) seems to indicate that managing a building is incompatible with the reputation of the WP profession.
40. Richter, M., "Die Unabhängigkeit des Wirtschaftsprüfers", Universität des Saarlandes (July 1976).
41. See Thümmel, M., "Dr. Richter's Fragebogen," Leserbriefe - Das Handelsblatt (June 26, 1976), p. 9.
42. This researcher was informed by representatives of both institutions that they have adopted a policy of non-interference in any ongoing research projects involving the WP profession.

43. Dr. Brönner, President of the regional office of the Institut der Wirtschaftsprüfer in Berlin, notified by WPs in Berlin who had received a questionnaire, discussed the research questionnaire in a special subcommittee meeting. Since this subcommittee could not reach unanimous independence decisions on most of the auditor-client relationships investigated, this researcher was informed by Dr. Brönner that any research findings from this study must be interpreted cautiously. The response rate from WPs living in Berlin seems not to have been negatively affected, however, since it was above the average response rate for WPs in general.
44. A copy of the WPK's interpretation of current auditor independence rules and regulations pertaining to the specific auditor-client relationships described in the questionnaire can be found in Appendix D. These are in essence the same responses given by Mr. Pfefferer of the WPK during the December 12, 1978 meeting of this researcher with Mr. Pfefferer of the WPK and Mr. Kaminski of the IdW.
45. See Richter, M., Die Sicherung der aktienrechtlichen Publizität durch ein Aktienamt (Köln: Carl Heymanns Verlag KG, 1975), p. 100.
46. For example, Ziegler, in 1976, mailed a questionnaire to bankers, financial analysts and individual stockholders, which dealt with the attitude of these three groups toward the auditor's standard report. The response rate of individual stockholders was only 10 percent, compared to 54 and 40 percent for bankers and financial analysts, respectively. See, The Commission on Auditors' Responsibilities. M. Cohen, Chairman (1978), p. 183-184.
47. Richter, M., "Die Unabhängigkeit des Wirtschaftsprüfers,".
48. Richter does not claim that this group is representative of all financial statement users. He speculated, however, that public opinion about the Wirtschaftsprüfer is heavily influenced by the (subjective) opinions of this group. He quotes some evidence which suggests that financial journalists usually are more critical than other groups. See Richter, M., "Die Unabhängigkeit des Wirtschaftsprüfers," p. 22.
49. "Die grössten Banken in Deutschland: 50 Riesen," Capital (November 1977), p. 144.
50. Some of these mammoth banks have more than one main office; however, in this study only one of the main offices was treated as a "main office" bank. The other main offices were treated as "branch offices".

51. Buzby, S. L., "Selected Items of Information and Their Disclosure in Annual Reports," The Accounting Review (July 1974), pp. 423-435.
52. Oppenheim, H. N., Questionnaire Design and Attitude Measurement (New York: Basic Books, 1966), p. 34.
53. The t-Test is discussed on pages 115-116 in this chapter.
54. Buzby conducted 38 different t-Tests of which 36 failed to achieve an alpha level of 0.15 or less. See Buzby, S. L., p. 427.
55. Lavin, D., "Perceptions of the Independence of the Auditor," The Accounting Review (January, 1976), p. 43.
56. The areas in which the AICPA and the SEC have taken different positions involve mainly EDP and bookkeeping services. For a detailed account of differences between the AICPA and SEC concerning auditors' independence, see Lavin, D., "Financial Statement Users' and Accountants' Perceptions...", pp. 73-77.
57. This discussion is mainly based on Siegel, S., Nonparametric Statistic for the Behavioral Sciences (New York: McGraw-Hill Company, Inc., 1956), pp. 36-42.
58. For a more detailed discussion, see Siegel, S., pp. 104-11.
59. For a discussion of the t-Test, see Smith, L. H., and Williams, D. R., Statistical Analysis for Business: A Conceptual Approach (Belmont: Wadsworth Publishing Company, Inc., 1971), pp. 393-429.
60. See Nie, N. H., Bent, D. H., and Hull, C. H., Statistical Package for the Social Science - Second Edition (New York: McGraw-Hill Book Company, 1976).



## CHAPTER FIVE

### RESULTS OF THE SURVEY

In this chapter the responses from the mail survey are discussed and analyzed. There are a total of 17 questions describing a variety of auditor-client relationships. However, since a number of questions involve multiple separate situations, a total of 27 auditor-client relationships were investigated. Since each of these 27 auditor-client relationships essentially is a separate issue and thus represents a separate variable, each is discussed and analyzed individually.

The following discussion deals with two major issues:

(a) the perceptions of auditors' independence by the three experimental groups under study, namely WPs, LKRs, and LWPs, and (b) the financial decisions of LKRs and LWPs.

The first part of the discussion involves the analysis of the responses of the three groups under study concerning their perceptions of auditors' independence and the testing of null hypotheses I through VII. Various background variables are analyzed to determine their influence on the responses of the sample subjects.

In the second part, the responses of LKRs and LWPs concerning the effect of their perceptions of auditors' independence on their financial decisions are analyzed. This includes the testing of

null hypotheses VIII and IX.

### Perceptions of Auditors' Independence

The situations investigated in this study are analyzed and discussed by the categories of auditor-client relationships presented in Chapter Four. The individual situations are not discussed in the same order as they are presented in the questionnaire. Table 9 lists all auditor-client relationships investigated and is included for easy reference. The results of testing hypotheses I through VII at a significant level of  $\alpha \leq 0.05$  are also summarized in this section in Tables 28 and 31.

It should be noted that some situations were not used to test certain null hypotheses. As mentioned in Chapter Four, hypothesis VII, involving a comparison of WPs' and CPAs' perceptions concerning auditors' independence in appearance, was only tested on 10 of the 27 situations investigated. The remaining 17 situations were not used to test null hypothesis VII since CPAs' perceptions for those 17 situations have not been empirically investigated.<sup>1</sup>

Hypothesis IV and V also were not tested on certain auditor-client relationships that were investigated in this study. These hypotheses deal with a comparison of consensus responses of WPs with relevant AICPA rulings (hypothesis IV) and appropriate SEC rulings (hypothesis V). Situation 6A through 6E, Situations 17A through 17E, and Situation 16 were not used to test null hypotheses IV and V, because Situations 6A through 6E and Situation 16 apply only to the German accounting environment. Situation 17A through

TABLE 9

Auditor-Client Relationships Investigated<sup>2</sup>

- 
1. Pursuant to a plan of recapitalization, the existing debt of the company was exchanged for five-year promissory notes. The accounting firm received the same kind of promissory notes in payment of its audit fee.
  2. A partner in an accounting firm whose proposed Client A was a wholly owned subsidiary of Corporation B, owned one percent of the stock of Corporation B. The partner who owns these stocks would not in any way be involved with the year-end audit.
  3. A partner in an accounting firm whose proposed Client A was a wholly owned subsidiary of Corporation B, owned one percent of the stock of Corporation B. The partner who owns these stocks would be in charge of the year-end audit.
  4. A client of an accounting firm was engaged in the business of selling franchises. Two partners of this accounting firm invested approximately five percent of their personal fortunes to buy one half of the stock of a corporation which held a franchise granted by this client. Except for the payment of a percentage of sales to the franchisor client, the franchise operated independently.
  5. A partner in an accounting firm owned stocks of a proposed client for which he was engaged to do the year-end audit. Consider each of the following situations separately.
    - Situation A. The partner owned a very small number of shares of the client amounting to less than one percent of his net worth.
    - Situation B. The partner owned 3 percent of the client's stock amounting to 10 percent of his net worth.
    - Situation C. The partner owned 10 percent of the client's stock amounting to 10 percent of his net worth.
  6. A bank acquired a large number of shares of Company S. In addition, the same bank also owned shares of the auditing firm that was engaged to perform the year-end audit of Company S. Consider each of the following situations separately.
    - Situation A. The bank owned approximately 10 percent of the outstanding stock of the auditing firm.
    - Situation B. The bank owned between 11 and 24 percent of the outstanding stock of the auditing firm.

TABLE 9  
(continued)

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- Situation C. The bank owned between 25 and 49 percent of the outstanding stock of the auditing firm.
- Situation D. The bank owned exactly 50 percent of the outstanding stock of the auditing firm.
- Situation E. The bank owned more than 50 percent of the outstanding stock of the auditing firm.
7. In addition to the audit, an accounting firm provided services for the client which included maintaining the journals and ledgers, making adjusting entries and preparing financial statements.
  8. In order to keep certain information confidential, the client had the accounting firm perform the following services in addition to the audit:
    - (a) prepare the executive payroll
    - (b) maintain selected general ledger accounts in a private ledger.
  9. From the books of original entry, client personnel prepared printed tapes that could be read on an optical scanner and sent the tapes to the accountants' office. The accountants forwarded the tapes to a service bureau. The accountants received the print-outs of the financial statements and general ledgers and sent them to the client. The accountants did not edit the input data prior to transmission to the service bureau. The accountants provided this service in addition to the audit.
  10. A was the controller of Company Z. He was not an elected officer nor did he have any stock holdings in Company Z. A's brother, B, was a partner in the public accounting firm that audits Company Z's books. However, B was not the partner in charge of the audit.
  11. A partner in a public accounting firm had a brother-in-law who was sales vice president for a recently acquired client. The brother-in-law was not directly involved in the financial affairs of the company and the partner was not connected with the audit in any way.
  12. A partner in an accounting firm managed a building owned by an audit client.

TABLE 9  
(continued)

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13. A partner in an accounting firm (qualified as a lawyer) also acted as the general counsel for an audit client. He received fees for such legal services and, through the accounting partnership, for accounting services rendered concurrently.
  14. An accounting firm had its office in a building which was owned by a client. The accounting firm occupied approximately 25 percent of the available office space in the building, and the client occupied the remainder.
  15. An accounting firm rented block time on its computer to a client when the client's computer became overburdened.
  16. A partner of an accounting firm was also a member of the Supervisory Board of Corporation *L*. Corporation *L* was one of the largest suppliers of Corporation *M*. The accounting firm was engaged to perform the year-end audit of Corporation *M*.
  17. A certain portion of an accounting firm's revenue consisted of audit fees from one particular client. Consider each of the following situations separately. The fees from this particular client represented approximately:
    - Situation A: 5 percent of total revenue
    - Situation B: 10 percent of total revenue
    - Situation C: 25 percent of total revenue
    - Situation D: 50 percent of total revenue
    - Situation E: 75 percent of total revenue
-

17E were not used for these hypothesis tests because neither the AICPA nor the SEC have stated their position on these auditor-client relationships.

To facilitate the following discussion, the results of testing hypotheses I, II, III, and VI are included in the discussion of each of the situations investigated. Although the reader can determine the results for hypotheses IV, V, and VII from this discussion, the results of these hypothesis tests are also discussed in a separate section and are summarized in Table 28 to eliminate repetition in the discussion that follows.

#### Financial Interest (direct and indirect)

Six different auditor-client relationships are investigated in this category. Since the situations are discussed in a different order than they were presented in the questionnaire that was mailed to the sample subjects, the question number used in the questionnaire for each situation is given in brackets for cross-reference.<sup>3</sup>

Situation 1 - Pursuant to a plan of recapitalization,  
(Question 6) the existing debt of the company was  
exchanged for five-year promissory  
notes. The accounting firm received  
the same kind of promissory notes in  
payment of its audit fee.

There is no specific rule that forbids a WP from undertaking an audit under these circumstances. Even the WPK's interpretation of this situation notes that the means by which the auditor is paid plays no role in the judgment of an auditor's independence.

As a *non sequitur* they point out that providing credit to an audit client via postponement of payment of fees is sometimes questionable.<sup>4</sup>

Both the AICPA and the SEC have ruled that the auditor is not considered to be independent in this situation.<sup>5</sup>

Lavin's research found that loan officers and financial analysts both considered the auditors<sup>6</sup> to be not independent (63 percent and 75 percent, respectively) whereas members of the AICPA were evenly divided, indicating no consensus among this group.<sup>7</sup>

Table 10 shows that 54.2 percent of the WPs considered the auditors to be independent, as did 54.8 percent of LWPs that responded. However, only 38.2 percent of LKRs considered the auditors to be independent.

TABLE 10

## Analysis of Responses to Situation 1

	WPs		LKRs		LWPs	
	#	%	#	%	#	%
Independent	58	54.2	21	38.2	17	54.8
Not independent	49	48.8	34	61.8	14	45.2
Total	<u>107</u>	<u>100.0</u>	<u>55</u>	<u>100.0</u>	<u>31</u>	<u>100.0</u>
Mean <sup>8</sup>	0.542		0.382		0.548	

Binomial Test:

Probability of no consensus (p): 0.7113                      0.1048                      0.7201

Chi Square Test:  $\chi^2 = 4.1150$

Significance level = 0.1278

Degrees of Freedom = 2

### Conclusions from Statistical Tests

As noted in Chapter Four, the Binomial Test was used to test null hypotheses I, II, and III. The p-values of the Binomial Test for all three groups were in excess of the significance level of  $\alpha = 0.05$ .<sup>9</sup> Therefore, null hypotheses I, II, and III which state that there is no consensus within each experimental group could not be rejected since no statistically significant majority of opinion was indicated.

The results of the Chi Square Test of Homogeneity, which was employed to test whether the three experimental groups could be regarded as being drawn from the same population (null Hypothesis VI), proved not to be statistically significant. The obtained  $\chi^2$ -value of 4.1150 was statistically significant at  $\alpha = 0.1278$ . Since this exceeds the specified alpha level of 0.05, null hypothesis VI, which states that there are no differences between the three experimental groups, cannot be rejected.

The results of the Chi Square Test are consistent with the result of the Binomial Test. However, the fact remains that LKRs did take the opposite position of both the WPs and the LWPs. Nonetheless, the differences were not statistically significant.

Situation 2 - A partner in an accounting firm whose  
(Question 11) proposed Client A was a wholly owned  
subsidiary of Corporation B, owned one  
percent of the stock of Corporation B.  
The partner who owns these stocks  
would not in any way be involved  
with the year-end audit.



Since this situation represents an auditor with a direct financial interest, both the SEC and the AICPA consider the auditing firm not to be independent. For the German auditor there are no rules forbidding this type of relationship. Even the December 1977 revision of the WPK's Directives does not prohibit this type of situation. According to the WPK's interpretation of the applicable rules, this situation is not prohibited.<sup>10</sup>

As can be seen from Table 11, a large majority of each of the three groups considers the auditing firm to be independent in this case. The fact that the partner in question is not involved in the audit may have made a great difference in the perceptions of the auditors' appearance of independence. Of the WPs responding, 87 percent considered the auditors to be independent in this case, as

TABLE 11

## Analysis of Responses to Situation 2

	WPs		LKR's		LWPs	
	#	%	#	%	#	%
Independent	94	87.0	53	98.1	26	86.7
Not independent	14	13.0	1	1.9	4	13.3
Total	<u>108</u>	<u>100.0</u>	<u>54</u>	<u>100.0</u>	<u>30</u>	<u>100.0</u>
Mean	0.870		0.981		0.867	

Binomial Test:

Probability of no consensus (p): <0.0001      <0.0001      <0.0001

Chi Square Test:  $\chi^2 = 5.4557$

Significance level = 0.0654

Degrees of Freedom = 2

did 98.1 percent of the LKRs, and 86.7 percent of the LWPs.

#### Conclusions from Statistical Tests

The p-values obtained by applying the Binomial Test for all three groups were far below the significance level of  $\alpha = 0.05$ . Therefore, null hypotheses I, II, and III which state that there is no consensus within a group must be rejected since a statistically significant consensus was indicated for all three experimental groups.

The results of the Chi Square Test were consistent with the results of the Binomial Test by proving not to be statistically significant. The obtained  $\chi^2$ -value of 5.4557 was significant at  $\alpha = 0.0654$ . Since this exceeds the specified alpha level of 0.05, null hypothesis VI which states that there are no differences of perception of auditors' independence between the three experimental groups cannot be rejected.

Situation 3 - A partner in an accounting firm whose (Question 12) proposed client was a wholly owned subsidiary of Corporation B, owned one percent of the stock of Corporation B. The partner who owns these stocks would be in charge of the year-end audit.

This situation is exactly the same as the previous one except that in this case the partner in question will be in charge of the audit. As noted above, the AICPA and the SEC do not differentiate between the two situations; thus, in this case the auditing firm involved is also considered not to be independent.

The WPK also does not differentiate between this case and the previous case as expressed in their interpretation of existing rules.<sup>11</sup> The WPK considers the auditing firm to be independent which is contrary to the AICPA and SEC position.

However, the three groups tested disagreed with the view of the WPK. Only 45.4 percent of all WPs responding, 49.1 percent of LKRs, and 41.4 percent of all LWPs who responded considered the auditing firm still to be independent. Apparently, the fact that the partner in question will be in charge of the audit affected their perception of the auditors' independence in appearance.

TABLE 12

## Analysis of Responses to Situation 3

	WPs		LKRs		LWPs	
	#	%	#	%	#	%
Independent	49	45.4	27	49.1	12	41.4
Not independent	<u>59</u>	<u>54.6</u>	<u>28</u>	<u>50.9</u>	<u>17</u>	<u>58.6</u>
Total	<u>108</u>	<u>100.0</u>	<u>55</u>	<u>100.0</u>	<u>29</u>	<u>100.0</u>
Mean	0.454		0.491		0.414	

Binomial Test:

Probability of no consensus (p): 0.6439                      0.9999                      0.4583

Chi Square Test:  $\chi^2 = 0.47621$

Significance level = 0.7881

Degrees of Freedom = 2

### Conclusions from Statistical Tests

The Binomial Test showed that null hypotheses I, II, and III which state that there is no consensus within each experimental group could not be rejected. The computed p-values were all in excess of  $\alpha = 0.05$ . Thus it can be concluded that no statistically significant consensus was present in each group.

The Chi Square Test showed that there were no significant differences between the three groups and thus null hypothesis VI, which states that there are no differences of perceptions concerning auditors' independence between the three experimental groups, cannot be rejected. The computed  $\chi^2$ -value of 0.4762 corresponds to an alpha of 0.7881 which is far in excess of the set  $\alpha = 0.05$ .

Situation 4 - A client of an accounting firm was engaged in the business of selling franchises. Two partners of this accounting firm invested approximately five percent of their personal fortunes to buy one half of the stock of a corporation which held a franchise granted by this client. Except for the payment of a percentage of sales to the franchisor client, the franchise operated independently.

The AICPA and the SEC both agree that under these circumstances the accounting firm's independence is impaired.

The results of Lavin's research show that among the CPAs responding to his survey, only 25 percent considered the accounting firm still to be independent, as did 32 percent of the loan officers and 20 percent of the financial analysts.

The WPK in its response to this situation indicated that the

TABLE 13

## Analysis of Responses to Situation 4

	WPs		LKR		LWPs	
	#	%	#	%	#	%
Independent	58	54.7	33	60.0	19	65.5
Not independent	<u>48</u>	<u>45.3</u>	<u>22</u>	<u>40.0</u>	<u>10</u>	<u>34.5</u>
Total	<u>106</u>	<u>100.0</u>	<u>55</u>	<u>100.0</u>	<u>29</u>	<u>100.0</u>
Mean	0.547		0.600		0.655	
<u>Binomial Test:</u>						
Probability of no consensus (p): 0.6374			0.1770		0.1360	
<u>Chi Square Test:</u> $\chi^2 = 1.2303$						
Significance level = 0.5406						
Degrees of Freedom = 2						

circumstances are hardly applicable to the German business environment since franchising is an American invention which so far has found little application in Germany.<sup>12</sup> However, an article by Wrabetz in 1974 suggests that franchising has become a more common practice in recent years and thus, theoretically, it does apply.<sup>13</sup>

As Table 13 indicates, 54.7 percent of the WPs responding considered independence not to be impaired. A similar view was expressed by 60 percent of the LKR responding and 65.5 percent of the responding LWP.

### Conclusions from Statistical Tests

Even though the majority of respondents in each group considered the auditors independent, the null hypotheses of no consensus within each group could not be rejected. As can be seen from Table 13, the Binomial Test resulted in p-values which exceeded  $\alpha = 0.05$  for all three groups. Thus, null hypotheses I, II, and III cannot be rejected.

The results obtained from the Chi Square Test indicate that null hypothesis VI cannot be rejected. The computed  $\chi^2$ -value of 1.2303 corresponds to an alpha level of 0.5406. Thus, it can be concluded that there are no differences between the three groups concerning their perceptions of the concept of auditors' independence.

Situation 5 - A partner in an accounting firm owned  
(Question 14) stocks of a proposed client for which the accounting firm was engaged to do the year-end audit. Consider each of the following situations separately.

- A. The partner owned a very small number of shares of the client amounting to less than one percent of his net worth.
- B. The partner owned 3 percent of the client's stock amounting to 10 percent of his net worth.
- C. The partner owned 10 percent of the client's stock amounting to 10 percent of his net worth.

All three situations are clearly prohibited by the AICPA and the SEC since they represent a direct financial interest of

an auditor in a client firm.

The latest revision of the WPK's Directives also prohibits any direct financial interest of an auditor in an audit client. Therefore, in all three situations, an auditing firm would be lacking the appearance of independence beginning January 1, 1979.<sup>14</sup>

The results of this survey differ from these official guidelines. As Table 14 shows, for Situation 5A, 75.5 percent of all WPs responding, 89.1 percent of all LKRs, and 90.0 percent of all LWPs responding to the questionnaire considered the auditors to be independent.

For Situation 5C, the results are almost reversed. Here, 20.6 percent of the WPs, 27.3 percent of the LKRs, and 16.7 percent of the LWPs responding considered the auditors to be independent.

Results for Situation 5B are mixed. Whereas a majority of LKRs (56.4 percent) still considered the auditors to be independent under the described circumstances, only 31.1 percent of the WPs, and 46.7 percent of the LWPs considered the auditors to be independent.

The perceptions of each group are consistent in that the larger the amount of client-owned stocks, the fewer the responses in the "Independent" category.

#### Conclusions from Statistical Tests

For Situation 5A and Situation 5C, the p-values obtained from the Binomial Test proved to be below  $\alpha = 0.05$  for all three groups indicating that the null hypotheses of no consensus must be rejected. Thus, for Situation 5A there was a statistically

TABLE 14

## Analysis of Responses to Situation 5

	WPs		LKR		LWP	
	#	%	#	%	#	%
<u>Situation 5A</u>						
Independent	80	75.5	49	89.1	27	90.0
Not independent	<u>26</u>	<u>24.5</u>	<u>6</u>	<u>10.9</u>	<u>3</u>	<u>10.0</u>
Total	106	100.0	55	100.0	30	100.0
<u>Situation 5B</u>						
Independent	33	31.1	31	56.4	14	46.7
Not independent	<u>73</u>	<u>68.9</u>	<u>24</u>	<u>43.6</u>	<u>16</u>	<u>53.3</u>
Total	106	100.0	55	100.0	30	100.0
<u>Situation 5C</u>						
Independent	22	20.6	15	27.3	5	16.7
Not independent	<u>85</u>	<u>79.4</u>	<u>40</u>	<u>72.7</u>	<u>25</u>	<u>83.3</u>
Total	107	100.0	55	100.0	30	100.0
Situation 5A - Mean	0.755		0.891		0.900	
Situation 5B - Mean	0.311		0.564		0.467	
Situation 5C - Mean	0.206		0.273		0.167	
<u>Binomial Test:</u>						
Probability of no consensus (p):						
Situation 5A	<0.0001		<0.0001		<0.0001	
Situation 5B	0.0007		0.4188		0.8555	
Situation 5C	<0.0001		0.0010		0.0003	
<u>Chi Square Test</u>	<u><math>\chi^2</math></u>		<u>Significance level</u>			
Situation 5A	6.1356		0.0465			
Situation 5B	10.0422		0.0066			
Situation 5C	1.5220		0.4672			



significant consensus within each of the three groups that the auditors were perceived to be independent. Similarly, for Situation 5C, there was a statistically significant consensus within each experimental group that the auditors were perceived not to be independent under the circumstances described. Consequently, hypotheses I, II, and III must be rejected for these two auditor-client relationships.

For Situation 5B, the results of the Binomial Test were mixed. Even though among WPs, the p-value obtained was below the  $\alpha = 0.05$  indicating consensus within this group, for LKRs and LWPs the p-values obtained proved to be greater than  $\alpha = 0.05$ . Thus, for LKRs and LWPs the null hypothesis of no consensus could not be rejected. Therefore, null hypothesis I cannot be rejected, whereas hypothesis II and III must be rejected since the computed p-values exceeded the predetermined  $\alpha$  level of 0.05 by a wide margin.

The results obtained from the Chi Square Test indicated that for Situation 5A and Situation 5B, hypothesis VI of no differences of perceptions concerning auditors' independence between the three groups must be rejected. Whereas these results are consistent with those obtained from the Binomial Test for Situation 5B, they are not consistent with those obtained from Situation 5A. This can be explained by the definition of consensus in this study. For Situation 5A, even though the majority responses were significant for all three groups, the degree of consensus differed between 75.5 percent for WPs to 90.0 percent for LWPs, causing the  $\chi^2$ -statistic to be significant at an  $\alpha$  level of 0.05.

For Situation 5C, the  $\chi^2$ -value obtained corresponds to a

probability level of 0.4672 which is greater than  $\alpha = 0.05$ , indicating that null hypothesis VI of no differences between the three groups cannot be rejected.

Situation 6 - A bank acquired a large number of shares of Company *S*, large enough to enable the bank to significantly influence the management of Company *S*. In addition, the same bank also owned shares of the auditing firm that was engaged to perform the year-end audit of Company *S*. Consider each of the following situations separately.

(Question 15)

- A. The bank owned approximately 10 percent of the outstanding stock of the auditing firm.
- B. The bank owned between 11 and 24 percent of the outstanding stock of the auditing firm.
- C. The bank owned between 25 and 49 percent of the outstanding stock of the auditing firm.
- D. The bank owned exactly 50 percent of the outstanding stock of the auditing firm.
- E. The bank owned more than 50 percent of the outstanding stock of the auditing firm.

Since non-CPAs are not permitted to have a financial interest in an auditing firm in the United States, the above described auditor-client relationships are, for the U.S., of a hypothetical nature only. For Germany, these situations are of interest because ownership by non-WPs is allowed and occurs in practice.

The WPK's interpretation of current regulations concerning these situations is that Situations 6A through 6D are allowed

under professional law, implying that the auditing firm is considered to be independent in appearance.<sup>15</sup>

Situation 6E is prohibited by paragraph 164 of the Stock-corporation Law of 1965. However, as the WPK in its response to this question noted, independence may be impaired even if ownership is less than 50 percent if there are special circumstances which would make it appear that the bank has a dominant influence (herrschenden Einfluss) on management.<sup>16</sup>

As Table 15 indicates, all three experimental groups' perceptions are stricter than current law.

For Situation 6A, a majority in each group considered the auditing firm to be independent under these circumstances, namely 57 percent of all WPs responding, 79.2 percent of all LKRs, and 65.5 percent of all LWPs responding.

For Situation 6B, the WPs are almost evenly divided in the "Independent" and "Not independent" category (49.5 percent versus 50.5 percent). Among LKRs, 66 percent considered the auditing firm to be independent, as did a small majority, 51.7 percent, of all LWPs that responded to the questionnaire.

However, for Situation 6C, 6D, and 6E, less than 50 percent of all respondents in each group considered the auditing firm to be independent. The percentage of responses in the "Independent" category declined in each category as the stock ownership of the bank increased. The percentages of responses in the "Independent" category for Situation 6C were as follows: WPs, 22.4 percent; LKRs, 43.4 percent; and LWPs, 24.1 percent. The response rates for Situation 6D were: WPs, 15.9 percent; LKRs, 32.1 percent;

TABLE 15

## Analysis of Responses to Situation 6

		WPs		LKR's		LWPs	
		#	%	#	%	#	%
<u>Situation 6A</u>							
Independent		61	57.0	42	79.2	19	65.5
Not independent		46	43.0	11	20.8	10	34.5
Total		<u>107</u>	<u>100.0</u>	<u>53</u>	<u>100.0</u>	<u>29</u>	<u>100.0</u>
<u>Situation 6B</u>							
Independent		53	49.5	35	66.0	15	51.7
Not independent		54	50.5	18	34.0	14	48.3
Total		<u>107</u>	<u>100.0</u>	<u>53</u>	<u>100.0</u>	<u>29</u>	<u>100.0</u>
<u>Situation 6C</u>							
Independent		24	22.4	23	43.4	7	24.1
Not independent		83	77.6	30	56.6	22	75.9
Total		<u>107</u>	<u>100.0</u>	<u>53</u>	<u>100.0</u>	<u>29</u>	<u>100.0</u>
<u>Situation 6D</u>							
Independent		17	15.9	17	32.1	5	17.2
Not independent		90	84.1	36	67.9	24	82.8
Total		<u>107</u>	<u>100.0</u>	<u>53</u>	<u>100.0</u>	<u>29</u>	<u>100.0</u>
<u>Situation 6E</u>							
Independent		12	11.2	14	26.4	4	13.8
Not independent		95	88.8	39	73.6	25	86.2
Total		<u>107</u>	<u>100.0</u>	<u>53</u>	<u>100.0</u>	<u>29</u>	<u>100.0</u>
Situation 6A - Mean		0.570		0.792		0.655	
Situation 6B - Mean		0.495		0.660		0.517	
Situation 6C - Mean		0.224		0.434		0.241	
Situation 6D - Mean		0.159		0.321		0.172	
Situation 6E - Mean		0.112		0.264		0.138	
Probability of no consensus (p):							
Situation 6A		0.3421		<0.0001		0.1360	
Situation 6B		0.6867		0.0270		0.9999	
Situation 6C		<0.0001		0.4101		0.0081	
Situation 6D		<0.0001		0.0127		0.0005	
Situation 6E		<0.0001		0.0008		0.0001	
<u>Chi Square Test:</u>		<u><math>\chi^2</math></u>	<u>Significance Level</u>				
Situation 6A		7.6724	0.0216				
Situation 6B		3.9999	0.1353				
Situation 6C		7.9644	0.0186				
Situation 6D		5.9121	0.0520				
Situation 6E		6.2435	0.0441				

and LWPs, 17.2 percent.

For Situation 6E, only 11.2 percent of WPs considered the auditing firm to be independent, as did 26.4 percent of LKRs, and 13.8 percent of LWPs. As can be seen from these figures, the percentage of "Independent" responses are consistently the lowest for WPs, whereas the LKRs had the highest rate of "Independent" responses for all of these five auditor-client relationships.

#### Conclusions from Statistical Tests

The p-values obtained from applying the Binomial Test indicate that for Situations 6A and 6B, null hypotheses I and III, which state that there is no consensus among WPs and LWPs, respectively, concerning their perception of the concept of auditors' independence cannot be rejected. For LKRs, null hypothesis (II) of no consensus must be rejected for Situations 6A and 6B since the computed p-value obtained from the Binomial Test was less than  $\alpha = 0.05$ .

For Situation 6C the results of the Binomial Test are exactly reversed. Thus, for this auditor-client relationship null hypotheses I and III must be rejected, whereas null hypothesis II, concerning LKRs perceptions of auditors' independence cannot be rejected.

In applying the Binomial Test for the responses to Situation 6D and 6E, p-values were obtained that were all below the critical alpha level of 0.05. Thus, for these two auditor-client relationships null hypotheses I, II, and III which state that there is no consensus regarding the perceptions of auditors' independence within the groups of WPs, LKRs, and LWPs, respectively, must be rejected.

The Chi Square Test of Homogeneity was applied to test

null hypothesis VI which states that there are no differences regarding the perceptions of auditors' independence between WPs, LKRs, and LWPs. The results of the Chi Square Test, as can be seen from Table 15, indicate that null hypothesis VI may be rejected for Situations 6A, 6C, and 6E since the computed  $\chi^2$ -statistics correspond to a significance level which is less than the set alpha of 0.05. For Situations 6B and 6D the opposite conclusions are reached. Here the  $\chi^2$ -statistics correspond to a significance level greater than alpha = 0.05, indicating that null hypothesis VI may not be rejected for these two situations. It should be noted that for Situations 6D and 6E the significance values are very close to 0.05, indicating that null hypothesis VI was barely rejected for Situation 6E and not rejected for Situation 6D.

#### Bookkeeping and EDP Services

Under this category, three situations were investigated, corresponding to questions 2, 3, and 5 of the questionnaire.

Situation 7 - In addition to the audit, an accounting firm (Question 2) provided services for the client which included maintaining the journals and ledgers, making adjusting entries and preparing financial statements.

The AICPA does not consider the auditors to be lacking independence if they prepare the financial statements and make bookkeeping and adjusting entries to the client's books. The SEC has ruled in the above case that the auditing firm will not be considered independent under these circumstances.

The 1977 revision of the WPK Directives prohibits an auditor from performing these services for an audit client. The WPK in response to this question interpreted their rule accordingly.<sup>17</sup> Prior to the 1977 revision, the Directives did not explicitly prohibit preparation of an audit client's financial statements.

Lavin's research findings indicate that for the AICPA members in his sample, only 36 percent of those that responded considered the auditing firm to be independent under these circumstances, whereas 55 percent of the loan officers and 53 percent of financial analysts sampled fell into the "Independent" category.

As can be seen from Table 16, only 41.7 percent of the WPs responding considered the auditing firm to appear to be independent, as did 45.2 percent of all LWPs. However, among LKRs, 70.4 percent considered the auditing firm to be independent, which is a decisive majority.

#### Conclusions from Statistical Tests

The p-values obtained from applying the Binomial Test for WPs and LWPs exceed  $\alpha = 0.05$ , indicating that the null hypotheses of no consensus within these two groups cannot be rejected. For LKRs, however, the computed p-value of 0.0038 is far below  $\alpha = 0.05$ , which suggests that the null hypothesis of no consensus should be rejected. This implies that there is a statistically significant majority within this experimental group, which, as defined earlier, represents a consensus.

As Table 16 indicates, the computed  $\chi^2$ -statistic of 12.2484 is significant at  $\alpha = 0.0022$ . Since this significance level

TABLE 16

## Analysis of Responses to Situation 7

	WPs		LKR's		LWPs	
	#	%	#	%	#	%
Independent	45	41.7	38	70.4	14	45.2
Not independent	<u>63</u>	<u>58.3</u>	<u>16</u>	<u>29.6</u>	<u>17</u>	<u>54.8</u>
Total	<u>108</u>	<u>100.0</u>	<u>54</u>	<u>100.0</u>	<u>31</u>	<u>100.0</u>
Mean	0.417		0.704		0.452	
<u>Binomial Test:</u>						
Probability of no consensus (p): 0.2179			0.0038		0.7201	
Chi Square Test: $\chi^2 = 12.2482$						
Significance level = 0.0022						
Degrees of Freedom = 2						

is less than  $\alpha = 0.05$ , hypothesis VI, which states that there are no differences of perceptions between the three groups must be rejected. Thus the results of the Chi Square Test are consistent with those obtained from the Binomial Test.

Situation 8 - In order to keep certain information confidential, the client had the accounting firm perform the following services in addition to the audit:

- (a) prepare the executive payroll
- (b) maintain selected general ledger accounts in a private ledger.

The AICPA and SEC disagree about this situation since it involves bookkeeping services. The SEC considers the auditing firm to lack independence in appearance whereas the AICPA considers



the auditing firm to be independent.

It is not clear whether the 1977 revision of the WPK's Directives could be definitely interpreted as disallowing the above described auditor-client relationship. The bookkeeping services provided in this case are somewhat limited in scope and thus, the Directives could possibly be interpreted as allowing such a relationship. Under the Directives in effect prior to December 1977, this situation seems to be clearly permissible. However, the WPK's interpretation of their own Directives consider the above situation to represent a relationship that is prohibited by the 1977 revision of the Directives.<sup>18</sup>

Lavin found that 59 percent of the CPAs that responded to his questionnaire considered the auditing firm to be independent, as did 67 percent of the loan officers and 57 percent of the financial analysts in his sample.

As is shown in Table 17, 77.8 percent of the WPs responding, as well as 81.8 percent of LKRs and 64.5 percent of LWPs who responded considered the auditing firm to be independent under these circumstances. Thus individual WPs, LKRs, and LWPs perceive this relationship differently than the Wirtschaftsprüferkammer.

#### Conclusions from Statistical Tests

The p-values computed by applying the Binomial Test reveal that for WPs and LKRs the null hypotheses (null hypotheses I and II) must be rejected since the p-values for these two groups are far less than  $\alpha = 0.05$ . Consequently, it can be concluded that there is a consensus within each of these two groups concerning

TABLE 17

## Analysis of Responses to Situation 8

	WPs		LKR		LWP	
	#	%	#	%	#	%
Independent	84	77.8	45	81.8	20	64.5
Not independent	<u>24</u>	<u>22.2</u>	<u>10</u>	<u>18.2</u>	<u>11</u>	<u>35.5</u>
Total	<u>108</u>	<u>100.0</u>	<u>55</u>	<u>100.0</u>	<u>31</u>	<u>100.0</u>
Mean	0.778		0.818		0.645	

Binomial Test:

Probability of no consensus (p): <0.0001      <0.0001      0.1496

Chi Square Test:  $\chi^2 = 3.4610$

Significance level = 0.1772

Degrees of Freedom = 2

the perceptions of auditors' independence with regard to this particular issue. The Binomial Test for LWPs indicated no consensus within this group. Since the Binomial Test considers sample size, the smaller the sample the larger the proportion must be in order to reject the null hypothesis. Even though 64.5 percent in this case agreed that the auditing firm was considered to be independent, null hypothesis III could not be rejected for an alpha = 0.05.

The computed  $\chi^2$ -statistic of 3.461 is significant at alpha = 0.1772 which exceeds 0.05. This indicates that the null hypothesis VI of no differences regarding the perception of auditors' independence between the three experimental groups cannot be rejected.

Situation 9 - From the books of original entry, client (Question 5) personnel prepared printed tapes that could be read on an optical scanner and sent the tapes to the accountants' office. The accountants forwarded the tapes to a service bureau. The accountants received the print-outs of the financial statements and general ledgers and sent them to the client. The accountants did not edit the input data prior to transmission to the service bureau. The accountants provided this service in addition to the audit.

In this particular situation, the SEC has ruled that the auditors' independence would be adversely affected. The AICPA, however, considers the described service a purely mechanical function which in itself would not impair the auditors' independence.

TABLE 18

Analysis of Responses to Situation 9

	WPs		LKR		LWP	
	#	%	#	%	#	%
Independent	101	94.4	49	92.5	28	90.3
Not independent	<u>6</u>	<u>5.6</u>	<u>4</u>	<u>7.5</u>	<u>3</u>	<u>9.7</u>
Total	<u>107</u>	<u>100.0</u>	<u>53</u>	<u>100.0</u>	<u>31</u>	<u>100.0</u>
Mean	0.944		0.925		0.903	

Binomial Test:

Probability of no consensus (p): <0.0001      <0.0001      <0.0001

Chi Square Test:  $\chi^2 = 0.6712$

Significance level = 0.7078

Degrees of Freedom = 2

The German auditor who looks for specific guidance as to how the Directives of the WPK or other regulations apply for this auditor-client relationship would find little help. Even the spirit of the Directives seems to provide little guidance. Thus the auditor would have to ask himself if the described situation would be acceptable with regard to his independence status if he were confronted with it.

The WPK in response to this question indicated that this situation would impair independence in appearance and consequently, is not permissible.<sup>19</sup>

Lavin's survey indicated that 86 percent of the CPAs responding to Situation 9 considered the auditors to be independent under those circumstances, as did 70 percent of the loan officers, and 63 percent of the financial analysts sampled.

As Table 18 shows, an overwhelming majority within each of the three groups sampled considered the independence of the auditors to be unaffected by the circumstances described. Of the WPs who responded, 94.4 percent considered the auditors to be independent. Of the LKRs and LWPs responding, 92.5 percent and 90.3 percent, respectively, indicated the same perceptions. These findings are surprising only in light of the WPK's conclusion concerning this question. The results are consistent with those obtained by Lavin.

#### Conclusions from Statistical Tests

Since such an overwhelming majority considered the auditors to be independent in this case, it is not surprising that the

p-values obtained from the Binomial Test are close to zero, indicating that null hypotheses I, II, and III must be rejected, and the alternative hypotheses, which state that there is a consensus among WPs, LKRs, and LWPs, respectively, may be accepted.

The  $\chi^2$ -value of 0.6912 corresponds to an alpha value of 0.7078 which exceeds  $\alpha = 0.05$ . Thus, null hypothesis VI cannot be rejected, implying that there are no differences of perceptions regarding auditors' independence for the circumstances described. These findings are consistent with those obtained from the Binomial Test.

#### Family Relationships

In this category two auditor-client relationships were investigated, corresponding to questions 7 and 8 of the questionnaire.

Situation 10 - A was the controller of Company Z. He was  
(Question 7) not an elected officer nor did he have any  
holdings in Company Z. A's brother, B,  
was a partner in the public accounting  
firm that audits Company Z's books.  
However, B was not the partner in charge  
of the audit.

The AICPA considers the accounting firm to be not independent if the audit is performed by members from the same office in which B works. If the audit is performed by auditors that belong to an office other than the one in which B works, the accounting firm's independence is not considered to be impaired. The SEC has ruled that under the circumstances described in Situation 10, an accounting firm cannot be considered to be independent.

Lavin's results show that a statistically significant majority of the experimental groups sampled considered the accounting firm to be independent under these circumstances, 58 percent of the CPAs responding, 78 percent of the loan officers and 69 percent of the financial analysts who responded to his survey.

The WPK's Directives, as noted in the preceding chapter, do contain a warning that a close relationship between a leading employee of an audit client, which could be that of a close relative, may cause an auditor's appearance of independence to be impaired.<sup>20</sup> The WPK's response to this question was that the situation described is not prohibited under paragraph 164 of the Stockcorporation Law of 1965 and of paragraph 49 of the WPO, implying that the auditors are considered to be independent in appearance under these circumstances.<sup>21</sup>

The results of this survey, as summarized in Table 19, indicate general agreement with the WPK's interpretation of pertinent regulations. Eighty-five percent of the WPs responding, 90.9 percent of the LKRs responding, and 83.9 percent of the LWPs who responded considered the auditing firm to be independent for this particular auditor-client relationship.

#### Conclusions from Statistical Tests

As summarized in Table 19, the p-values computed by applying the Binomial Test are all close to zero, indicating that the null hypotheses of no consensus within each group must be rejected. Consequently, the alternative hypotheses I, II, and III which state that there is consensus concerning the perception of

TABLE 19

## Analysis of Responses to Situation 10

	WRs		LKRrs		LWPs	
	#	%	#	%	#	%
Independent	91	85.0	50	90.9	26	83.9
Not independent	<u>16</u>	<u>15.0</u>	<u>5</u>	<u>9.1</u>	<u>5</u>	<u>16.1</u>
Total	<u>107</u>	<u>100.0</u>	<u>55</u>	<u>100.0</u>	<u>31</u>	<u>100.0</u>
Mean	0.850		0.909		0.839	
<u>Binomial Test:</u>						
Probability of no consensus (p): <0.0001			<0.0001		0.0002	
<u>Chi Square Test:</u> $\chi^2 = 1.2948$						
Significance level = 0.5234						
Degrees of Freedom = 2						

auditors' independence within each of the three experimental groups may be accepted.

The Chi Square Test revealed that the obtained  $\chi^2$ -value of 1.2948 is significant at alpha = 0.5234. This implies that null hypothesis VI, which states that there are no differences of perceptions regarding the concept of auditors' independence between the three groups, cannot be rejected. Consequently, it cannot be refuted that the responses received from all three groups could all have come from one homogeneous population.

Situation 11 - A partner in a public accounting firm had  
(Question 8) a brother-in-law who was sales vice president for a recently acquired client. The brother-in-law was not directly involved in the financial affairs of the company

and the partner was not connected with the audit in any way.

The SEC and the AICPA both consider independence not to be impaired under these circumstances, mainly because a sales vice president is not directly involved with the financial affairs of the company.

Lavin's research indicates that most of the respondents to this survey agreed with this position. Eighty-eight percent of the CPAs responding, 93 percent of the loan officers, and 96 percent of the financial analysts who responded to this question considered there to be no impairment of auditors' independence under those circumstances.

The WPK in response to this question also believed that the auditors' independence would not be impaired in this situation.<sup>22</sup> The majority of the three experimental groups sampled agreed with the WPK's view. As Table 20 indicates, 96.3 percent of WPs, 96.4 percent of the LKRs, and 90.3 percent of the LWPs considered the auditors to be independent in this particular case.

#### Conclusions from Statistical Tests

Since the percentage of respondents in the "Independent" category for each experimental group was very similar, the statistical tests applied did not yield any unexpected results.

The Binomial Test revealed p-values of nearly zero, indicating that the null hypotheses of no consensus within each group (null hypotheses I, II, and III) must be rejected.



TABLE 20

## Analysis of Responses to Situation 11

	WPs		LKR's		LWP's	
	#	%	#	%	#	%
Independent	104	96.3	53	96.4	28	90.3
Not independent	<u>4</u>	<u>3.7</u>	<u>2</u>	<u>3.6</u>	<u>3</u>	<u>9.7</u>
Total	<u>108</u>	<u>100.0</u>	<u>55</u>	<u>100.0</u>	<u>31</u>	<u>100.0</u>
Mean	0.963		0.964		0.903	

Binomial Test:

Probability of no consensus (p): <0.0001      <0.0001      <0.0001

Chi Square Test:     $\chi^2 = 2.1174$

Significance level = 0.3469

Degrees of Freedom = 2

The  $\chi^2$ -statistic of 2.1174, as indicated in Table 20, proved significant at alpha = 0.3469. This suggests that hypothesis VI (no differences of perception between the three groups) cannot be rejected, since the significance level exceeds 0.05.

## Occupations With Conflicting Interest

Two situations were investigated in this category corresponding to questions 4 and 14 of the questionnaire.

Situation 12 - A partner in an accounting firm managed  
(Question 4) a building owned by an audit client.

Both the SEC and the AICPA agree that this situation will render the accounting firm not independent. The majority of

respondents to Lavin's survey also considered independence to be impaired. Only 12 percent of the CPAs, 42 percent of the loan officers, and 30 percent of the financial analysts considered the accounting firm still to be independent.

Since it was felt that this activity was, a priori, prohibited from being performed by a Wirtschaftsprüfer, the wording of the German questionnaire was changed. Instead of "partner", the German version uses "a member of the auditing staff with five years audit experience" to prevent a high nonresponse rate to this question. However, the professional organization (Wirtschaftsprüferkammer) interpreted "the management of a building" as management consulting work (Beratungstätigkeit) which is permitted for WPs and consequently considered independence not to be impaired.<sup>23</sup>

Table 21 summarizes the responses to Situation 12. As indicated, 77.8 percent of WPs, 70.9 percent of LKRs, and 80.0 percent of the LWPs responding also considered the auditors to be independent. Thus, the AICPA, SEC, and U.S. groups surveyed had one view of this auditor-client relationship whereas the German WPK and the German groups surveyed espoused the opposite view. Whether the change in the German translation had a significant impact on the three German experimental groups' responses cannot be determined.

#### Conclusions from Statistical Tests

The p-values obtained from applying the Binomial Test were all less than 0.05. Consequently, the null hypotheses of no consensus within each of the three groups must be rejected and

TABLE 21

## Analysis of Responses to Situation 12

	WPs		LKR's		LWPs	
	#	%	#	%	#	%
Independent	84	77.8	39	70.9	24	80.0
Not independent	<u>24</u>	<u>22.8</u>	<u>16</u>	<u>29.1</u>	<u>6</u>	<u>20.0</u>
Total	<u>108</u>	<u>100.0</u>	<u>55</u>	<u>100.0</u>	<u>30</u>	<u>100.0</u>
Mean	0.778		0.709		0.800	
<u>Binomial Test:</u>						
Probability of no consensus (p):			<0.0001	0.0027	0.0014	
<u>Chi Square Test:</u> $\chi^2 = 1.2347$						
Significance level = 0.5394						
Degrees of Freedom = 2						

the alternative hypotheses I, II, and III which state that there is consensus within each group can be accepted.

Null hypothesis VI, which states that there are no differences in perception between the experimental groups could not be rejected since the  $\chi^2$ -value obtained corresponds to a significance level of 0.5394 which exceeds the set  $\alpha = 0.05$  by a considerable margin. Thus it may be concluded that there are no differences of perceptions regarding auditors' independence between WPs, LKR's, and LWPs for this auditor-client relationship.

Situation 13 - A partner in an accounting firm qualified as a lawyer) also acted as the general counsel for an audit client. He received fees for such legal services and, through the accounting

partnership, for accounting services rendered concurrently.

The AICPA has ruled that independence would be impaired under these circumstances.<sup>24</sup> The SEC's position is similar since it has ruled that an auditor cannot act as legal counsel to an audit client.

The Wirtschaftsprüferordnung considers the activity of providing legal advice compatible with the WP profession. The WPK's response to this question also reiterates this fact and concludes that auditors' independence is unaffected under the circumstances described for this auditor-client relationship.<sup>25</sup>

As Table 22 shows, 61.2 percent of WPs who responded to this situation also considered the auditors to be independent. However, only 44.4 percent of LKRs, and even fewer (36.7 percent) of the LWPs who responded shared this view. Apparently, users of financial statements take a stance in this situation that is opposite to that of individual WPs and the Wirtschaftsprüferkammer.

Thus, the German WPs and the WPK both seem to disagree with the position taken by the AICPA and the SEC. However, LKRs and LWPs tend to agree with the AICPA's and SEC's viewpoint.

#### Conclusions from Statistical Tests

As can be seen from Table 22, the p-values obtained by applying the Binomial Test all exceeded  $\alpha = 0.05$ , indicating that the null hypotheses (I, II, and III) of no consensus within each group cannot be rejected. For WPs, the achieved significance level of 0.0774 exceeds the set  $\alpha$  of 0.05 by a small margin.

TABLE 22

## Analysis of Responses to Situation 13

	WPs		LKR's		LWPs	
	#	%	#	%	#	%
Independent	63	61.2	24	44.4	11	36.7
Not independent	<u>40</u>	<u>38.8</u>	<u>30</u>	<u>55.6</u>	<u>19</u>	<u>63.3</u>
Total	<u>103</u>	<u>100.0</u>	<u>54</u>	<u>100.0</u>	<u>30</u>	<u>100.0</u>
Mean	0.612		0.444		0.2005	
<u>Binomial Test:</u>						
Probability of no consensus (p): 0.0774			0.4966		0.2005	
<u>Chi Square Test:</u> $\chi^2 = 7.5202$						
Significance level = 0.0233						
Degrees of Freedom = 2						

However, since the Binomial Test takes into account sample size, a smaller sample necessitates a larger majority in the "Independent" or "Not independent" category to prove statistically significant. Thus, even though the percentage in the "Not independent" category is 63.3 percent for the LWPs as compared to the WPs "Independent" category of 61.2 percent, the p-value was 0.2005 for the LWPs as compared to 0.0774 for WPs. However, since both values exceeded alpha = 0.05, the conclusions reached are the same.

The Chi Square Test showed results contrary to those obtained from the Binomial Test. Whereas the Binomial Test indicated no consensus for each of the three groups, the computed  $\chi^2$ -value of 7.5202 corresponds to a probability level of 0.0223. Since this is less than alpha = 0.05, hypothesis VI must be rejected and

it may be concluded that there are differences between WPs, LKRs, and LWPs concerning their perceptions of auditors' independence for the circumstances described in Situation 13.

#### Business and Other Similar Relationships

Four situations were investigated in this category corresponding to questions 1, 9, 16 and 17 of the questionnaire.

Situation 14 - An accounting firm had its office in a building which was owned by a client. (Question 1) The accounting firm occupied approximately 25 percent of the available office space in the building, and the client occupied the remainder.

Both the SEC and the AICPA agree that an accounting firm cannot be considered independent under those circumstances. Lavin's research indicates, however, that a majority in each of the three groups that responded to this question perceived auditors' independence not to be impaired. Among the CPAs questioned, 68 percent thought independence was unimpaired as did 61 percent of the loan officers and 60 percent of the financial analysts who responded.

German regulations do not specifically mention this type of relationship. The WPK in its response to this question considered the circumstances alone not significant enough to impair independence in appearance.<sup>26</sup>

Table 23 summarizes the responses received. Of the WP-respondents, 75.9 percent considered the auditing firm to be independent. A similar proportion of LKRs and LWPs also considered

TABLE 23

Analysis of Responses to Situation 14

	WPs		LKR		LWP	
	#	%	#	%	#	%
Independent	82	75.9	39	70.9	23	74.2
Not independent	<u>26</u>	<u>24.1</u>	<u>16</u>	<u>29.1</u>	<u>8</u>	<u>25.8</u>
Total	<u>108</u>	<u>100.0</u>	<u>55</u>	<u>100.0</u>	<u>31</u>	<u>100.0</u>
Mean	0.759		0.709		0.742	
<u>Binomial Test:</u>						
Probability of no consensus (p):			<0.0001	0.0027	0.0107	
<u>Chi Square Test:</u> $\chi^2 = 0.4795$						
Significance level = 0.7868						
Degrees of Freedom = 2						

the appearance of independence not to be impaired, 70.9 percent and 74.2 percent, respectively.

#### Conclusions from Statistical Tests

The Binomial Test revealed that the majority in each group who considered the auditing firm to be independent was statistically significant for the set  $\alpha = 0.05$ . As Table 23 indicates, the p-values obtained were all below the 0.05 level. Thus, null hypotheses I, II, and III, which state that there is no consensus within each of the three experimental groups, must be rejected.

The Chi Square Test supported the findings of the Binomial Test since the computed  $\chi^2$ -value of 0.4795 corresponds to a significance level of 0.7868 which exceeds  $\alpha = 0.05$  by a wide

margin. Thus, null hypothesis VI (no differences of perceptions of auditors' independence between the three groups) cannot be rejected. As a matter of fact there is better than a 78 out of a 100 chance that null hypothesis VI is true.

Situation 15 - An accounting firm rented block time  
(Question 9) on its computer to a client when the  
client's computer became overburdened.

This is a situation in which the AICPA and the SEC have taken different positions. The AICPA considers these circumstances by themselves not to be sufficient to impair auditors' independence. The SEC believes that auditors' independence in appearance is impaired and thus ruled accordingly by prohibiting this auditor-client relationship.

Lavin found that most respondents in his sample considered the accounting firm to be independent. Eighty-eight percent of the CPAs, 85 percent of the loan officers, and 87 percent of the financial analysts who responded to Lavin's survey agreed with the position taken by the AICPA.

This type of situation is not specifically covered by any laws or regulations governing the conduct of WPs. In its response to this particular question, the WPK noted that the described circumstances by themselves are not sufficient to impair the auditors' independence status. They also noted that renting computer time to an audit client generally is no reason to prohibit the auditor from performing the audit.<sup>27</sup>

The results of the responses to this situation are summarized



TABLE 24

## Analysis of Responses to Situation 15

	WPs		LKR		LWP	
	#	%	#	%	#	%
Independent	97	89.8	52	94.5	29	93.5
Not independent	<u>11</u>	<u>10.2</u>	<u>3</u>	<u>5.5</u>	<u>2</u>	<u>6.5</u>
Total	<u>108</u>	<u>100.0</u>	<u>55</u>	<u>100.0</u>	<u>31</u>	<u>100.0</u>
Mean	0.898		0.945		0.935	

Binomial Test:

Probability of no consensus (p): <0.0001      <0.0001      <0.0001

Chi Square Test:  $\chi^2 = 1.2350$

Significance level = 0.5393

Degrees of Freedom = 2

in Table 24. Apparently, the majority of the three groups sampled also perceived the circumstances as not to impair the auditors' appearance of independence. Eighty-nine and eight-tenths percent of the WPs, 94.5 percent of the LKR, and 93.5 percent of the LWP responding to this situation were in the "Independent" category. These results seem to support the position taken by the WPK concerning this auditor-client relationship.

## Conclusions from Statistical Tests

The p-values computed by applying the Binomial Test all were close to zero, indicating that the null hypotheses which state that there is no consensus within each of the three groups must be rejected. Thus we can conclude that there is a statistically

significant majority within WPs, LKRs, and LWP's concerning the perception of auditors' independence.

The results of the Chi Square Test indicated that null hypothesis VI, which states that there are no differences of perception between the three groups sampled, cannot be rejected. As Table 24 shows, the computed  $\chi^2$ -value of 1.2350 corresponded to a significance level of 0.5393, which is far in excess of the set  $\alpha = 0.05$ .

Situation 16 - A partner of an accounting firm was  
(Question 16) also a member of the Supervisory Board  
of Corporation *L*. Corporation *L* was  
one of the largest suppliers of Corporation *M*. The accounting firm was  
engaged to perform the year-end audit  
of Corporation *M*.

This situation is unique to the German business environment due to the different corporate structure of German business entities.<sup>28</sup> This particular auditor-client relationship is not covered and thus, not prohibited, by paragraph 164 of the Stock-corporation Law of 1965. The 1977 revision of the WPK's Directives also does not specifically deal with this situation even though it does caution the Wirtschaftsprüfer that it is questionable to accept a Supervisory Board position in a corporation which has financial or other interrelationships with an audit client.<sup>29</sup> The WPK, in response to this question, considered the above relationship to be one that does not adversely affect independence in appearance.<sup>30</sup>

As Table 25 shows, 61.7 percent of the WPs who responded to the questionnaire considered the accounting firm to be independent,

TABLE 25

Analysis of Responses to Situation 16

	WPs		LKR		LWP	
	#	%	#	%	#	%
Independent	66	61.7	35	63.6	14	48.3
Not independent	<u>41</u>	<u>38.3</u>	<u>20</u>	<u>36.4</u>	<u>15</u>	<u>51.7</u>
Total	<u>107</u>	<u>100.0</u>	<u>55</u>	<u>100.0</u>	<u>29</u>	<u>100.0</u>
Mean	0.617		0.636		0.483	

Binomial Test:

Probability of no consensus (p): 0.0553                      0.0581                      0.9999

Chi Square Test:  $\chi^2 = 2.0903$

Significance level = 0.3516

Degrees of Freedom = 2

as did 63.6 percent of the responding LKR. However, only 48.3 percent of the LWP considered the accounting firm to be independent under the circumstances described in Situation 16.

## Conclusions from Statistical Tests

The Binomial Test resulted in p-values that all exceeded alpha = 0.05, indicating that there was no consensus within each of the three experimental groups and thus, null hypothesis I, II, and III cannot be rejected. It should be noted, as can be seen from Table 25, that for WPs and LKR, the computed p-values are just barely larger than 0.05. However, for LWP, the p-value is approximately one, indicating a near certainty that there is no consensus within the LWP group regarding the auditors' independence

for this auditor-client relationship.

The Chi Square Test results indicated a  $\chi^2$ -value of 2.0903 with a corresponding significance level of 0.3516, exceeding the set alpha of 0.05. Consequently, null hypothesis VI cannot be rejected. Thus, it can be concluded that there are no differences of perception regarding the concept of auditors' independence between WPs, LKRs, and LWPs.

Situation 17 - A certain portion of an accounting firm's  
(Question 17) revenue consisted of audit fees from one particular client. Consider each of the following situations separately. The fees from this particular client represented approximately:

- A. 5 percent of total revenue
- B. 10 percent of total revenue
- C. 25 percent of total revenue
- D. 50 percent of total revenue
- E. 75 percent of total revenue

The AICPA and the SEC so far have declined to take a definite stand on the issue of economic client-dependency. Both leave it to the individual auditor (or individual accounting firm) to decide what percentage of total revenue would impair his(its) independence status. As mentioned in Chapter Four, the British accounting institutions recommend 15 percent as a cut-off to their auditors.

The WPK in its Directives touches on this subject but falls short of making specific recommendations. The Directives do warn, however, that in cases where the audit fees obtained from a client

consistently represent a significant part of the auditor's total revenue, the auditor might not be considered to be independent.<sup>31</sup>

In response to Situation 17A through 17E, the WPK explains that other circumstances must also be considered in making a judgment on the auditors' appearance of independence. Therefore, the guidelines were intentionally left vague to allow for other circumstances such as if the auditor just started his own business or if he performed his profession as a hobby without much consideration about the fees.<sup>32</sup>

Table 26 summarizes the responses to these particular auditor-client relationships including the relevant statistics. For Situation 17A and 17B there is a large majority within each of the three groups that considered independence not to be impaired under these circumstances. For Situation 17A, 96.3 percent of the WPs, 94.5 percent of the LKRs and 100.0 percent of the LWPs fell into the "Independent" category. For Situation 17B, the "Independent" responses were 91.5 percent for the WPs, 85.5 percent for the LKRs, and 83.3 percent for the LWPs responding to this situation.

For Situation 17C the results are less unified. Whereas 52.4 percent of the WPs considered the accounting firm still to be independent, only 30.9 percent of the LKRs, and 40.0 percent of the LWPs thought so.

For Situation 17D and 17E the results are virtually the opposite of those obtained for Situation 17A and 17B. For Situation 17D, only 17.1 percent of the WPs, 7.3 percent of the LKRs, and 20.0 percent of the LWPs considered the accounting firm to be

TABLE 26

## Analysis of Responses to Situation 17

		WPs		LKR's		LWPs	
		#	%	#	%	#	%
<u>Situation 17A</u>							
Independent		103	96.3	52	94.5	30	100.0
Not independent		4	3.7	3	5.5	0	0.0
Total		<u>107</u>	<u>100.0</u>	<u>55</u>	<u>100.0</u>	<u>30</u>	<u>100.0</u>
<u>Situation 17B</u>							
Independent		97	91.5	47	85.5	25	83.3
Not independent		9	8.5	8	14.5	5	16.7
Total		<u>106</u>	<u>100.0</u>	<u>55</u>	<u>100.0</u>	<u>30</u>	<u>100.0</u>
<u>Situation 17C</u>							
Independent		55	52.4	17	30.9	12	40.0
Not independent		50	47.6	38	69.1	18	60.0
Total		<u>105</u>	<u>100.0</u>	<u>55</u>	<u>100.0</u>	<u>30</u>	<u>100.0</u>
<u>Situation 17D</u>							
Independent		18	17.1	4	7.3	6	20.0
Not independent		87	82.9	51	92.7	24	80.0
Total		<u>105</u>	<u>100.0</u>	<u>55</u>	<u>100.0</u>	<u>30</u>	<u>100.0</u>
<u>Situation 17E</u>							
Independent		12	11.2	4	7.3	5	16.7
Not independent		95	88.8	51	92.7	25	83.3
Total		<u>107</u>	<u>100.0</u>	<u>55</u>	<u>100.0</u>	<u>30</u>	<u>100.0</u>
Situation 17A - Mean		0.963		0.945		1.000	
Situation 17B - Mean		0.915		0.855		0.833	
Situation 17C - Mean		0.524		0.309		0.400	
Situation 17D - Mean		0.171		0.073		0.200	
Situation 17E - Mean		0.112		0.073		0.167	
<u>Binomial Test:</u>							
Probability of no consensus (p):							
Situation 17A		<0.0001		<0.0001		<0.0001	
Situation 17B		<0.0001		<0.0001		0.0003	
Situation 17C		0.9904		0.0065		0.3616	
Situation 17D		<0.0001		<0.0001		0.0014	
Situation 17E		<0.0001		<0.0001		0.0003	
<u>Chi Square Test:</u>		<u><math>\chi^2</math></u>		<u>Significance level</u>			
Situation 17A		1.6500		0.4382			
Situation 17B		2.2282		0.3282			
Situation 17C		7.0028		0.0302			
Situation 17D		3.5838		0.1666			
Situation 17E		1.7776		0.4111			

independent. In Situation 17E, 11.2 percent of the WPs, 7.3 percent of the LKRs, and 16.7 percent of the LWPs believed the firm was still independent. Thus it seems that there is little doubt among WPs and users of financial statements alike about auditor's independence in appearance if the audit fees from one client represents 10 percent or less, or 50 percent or more of total revenue.

#### Conclusions from Statistical Tests

Table 26 summarizes the relevant statistics. The p-values obtained from the Binomial Test were all less than  $\alpha = 0.05$  for Situations 17A, 17B, 17D, and 17E. Thus, for these four separate situations, null hypotheses I, II, and III must be rejected and the alternative hypotheses, which state that there is a consensus within each group concerning their perception of auditors' independence, may be accepted.

The p-values computed for Situation 17C were greater than 0.05 for WPs and LWPs indicating no consensus within each of these two experimental groups. Thus, null hypotheses I and III cannot be rejected. For LKRs, the obtained p-value was less than  $\alpha = 0.05$ , indicating that for this group the null hypothesis (II) of no consensus must be rejected.

The results obtained from applying the Chi Square Test are consistent with those obtained from the Binomial Test. For Situation 17A, 17B, 17D, and 17E, null hypothesis VI, which states that there are no differences of perception concerning the auditors' independence between the three experimental groups, cannot be

rejected. The  $\chi^2$ -values obtained all correspond to significance levels exceeding  $\alpha = 0.05$ .

For Situation 17C, the computed  $\chi^2$ -value corresponds to a significance level which is less than  $\alpha = 0.05$ . Consequently, for this situation the null hypothesis of no differences between the three groups must be rejected.

#### Hypotheses IV, V, and VII

These three hypotheses deal with a comparison of WP majority responses and the positions expressed by the AICPA (null hypothesis IV) and the SEC (null hypothesis V). Null hypothesis VII states that there are no differences between the perceptions of WPs and CPAs concerning the concept of auditors' independence for a number of selected auditor-client relationships.

#### Hypotheses IV and V

Table 27 presents a comparison of the WP consensus responses with relevant AICPA and SEC rulings. As can be seen from Table 27, WPs disagreed on a significant number of auditor-client relationships with either the AICPA or the SEC or both. Table 28 lists the null hypothesis test results for  $\alpha \leq 0.05$ . Inspection of Table 28 reveals that null hypothesis IV which states that there is a consensus among WPs' perceptions concerning auditors' independence that coincides with the position taken by the AICPA is rejected for 9 situations and not rejected for 6 situations. Situation 10 describes an auditor-client relationship where a partner of the accounting firm had a brother who was the controller of the



TABLE 27  
Comparison of Consensus Responses of WPs and Rulings of  
the AICPA and the SEC

Relationship	Consensus response		
	WPs	AICPA	SEC
1	Independent*	Not independent	Not independent
2	Independent	Not independent	Not independent
3	Not independent*	Not independent	Not independent
4	Independent*	Not independent	Not independent
5A	Independent	Not independent	Not independent
5B	Not independent	Not independent	Not independent
5C	Not independent	Not independent	Not independent
7	Not independent*	Independent	Not independent
8	Independent	Independent	Not independent
9	Independent	Independent	Not independent
10	Independent	**	Not independent
11	Independent	Independent	Independent
12	Independent	Not independent	Not independent
13	Independent*	Not independent	Not independent
14	Independent	Not independent	Not independent
15	Independent	Independent	Not independent

\* Not a statistically significant consensus

\*\* If the auditors are from a different office--Independent  
If the auditors are from the same office--Not independent

TABLE 28  
 Summary of Testing Hypotheses IV, V, and VII  
 for the Situations Investigated  
 (Null Hypotheses Rejected at  $\alpha \leq 0.05$ )

Type of Auditor- Client Relationship	Situation	H <sub>0</sub> : IV (AICPA)	H <sub>0</sub> : V (SEC)	H <sub>0</sub> : VIII WPs vs. CPAs
Financial Interest	1	rejected	rejected	not rejected
	2	rejected	rejected	**
	3	rejected	rejected	**
	4	rejected	rejected	rejected
	5A	rejected	rejected	**
	5B	not rejected	not rejected	**
	5C	not rejected	not rejected	**
Bookkeeping and EDP	7	rejected	rejected	not rejected
	8	not rejected	rejected	rejected
	9	not rejected	rejected	not rejected
Family Relationships	10	*	rejected	rejected
	11	not rejected	not rejected	rejected
Conflicting Occupations	12	rejected	rejected	rejected
	13	rejected	rejected	**
Business Relationships	14	rejected	rejected	not rejected
	15	not rejected	rejected	not rejected

\* If auditors are from a different office - don't reject H<sub>0</sub>.  
 If auditors are from the same office - reject H<sub>0</sub>.

\*\* No data available for CPAs.

company to be audited. The partner in question was not in charge of the audit. The AICPA's position is that the accounting firm is considered to be independent only if the partner belongs to a different office not involved with the audit. Under these circumstances, null hypothesis IV cannot be rejected. However, the accounting firm is not considered to be independent by the AICPA if the partner belongs to the same office that performs the audit. Under those conditions the null hypothesis must be rejected.

Similar results were obtained for null hypothesis V. This null hypothesis, which states that there is a consensus among WPs whose perceptions regarding auditors' independence coincide with the position taken by the SEC, was rejected for 13 of the 16 applicable auditor-client relationships tested. The null hypothesis could not be rejected for 3 situations at a significance level of 0.05. It should be noted that for three of the situations investigated where the AICPA had ruled the auditors to be independent whereas the SEC had ruled the opposite, a consensus of WPs agreed with the AICPA position.

#### Hypothesis VII

Null hypothesis VII states that there are no differences of perceptions between WPs and CPAs regarding the concept of auditors' independence. As noted earlier, the results obtained from Lavin's 1973 survey were used to test this hypothesis. Thus the null hypothesis could only be tested for those situations that were also investigated by Lavin. It should be noted that Lavin received 202 usable responses from CPAs representing a response

TABLE 29

## Comparison of Majority Responses of WPs and CPAs

Relationship	Response	WPs	CPAs
1	Independent	54.2%	50.2%
4	Independent Not independent	54.7%	74.6%
7	Not independent	58.3%	64.4%
8	Independent	77.8%	58.7%
9	Independent	94.4%	85.9%
10	Independent	85.0%	57.7%
11	Independent	96.3%	87.6%
12	Independent Not independent	77.8%	88.1%
14	Independent	75.9%	68.2%
15	Independent	89.8%	88.0%

rate of 58 percent.

Table 29 presents a comparison of majority responses of WPs and CPAs. Inspection of Table 29 reveals that the same majority responses were obtained by both groups for 8 out of 10 situations. WPs arrived at a majority opinion that was opposite the majority opinion reached by CPAs in only 2 situations (Situation 4 and 12). Situation 4 deals with auditors who invested in a corporation which held a franchise granted by an audit client. A majority of WPs, 54.7 percent (even though not a statistically significant majority) considered the accounting firm to be independent, whereas 74.6 percent of the CPAs responding to Lavin's survey considered the accounting firm's independence to be impaired. Situation 12 deals with a partner of an accounting firm who managed a building for an audit client. For this situation 77.8 percent of WPs fell in the "Independent" category, whereas an even higher proportion of CPAs, 88.1 percent fell into the "Not independent" category. These strongly opposing views may be partially explained, as was noted earlier, by the wording in the German translation which, to prevent a possibly high nonresponse rate to this question, changed "partner" to "a member of the audit staff with five years audit experience". However, it seems unlikely that this translation convention was solely responsible for causing such a difference in perceptions between WPs and CPAs. It appears that there would be differences in perceptions between WPs and CPAs for this situation even if the change in the translation had not been made.

Although WPs' majority responses coincided with the majority responses obtained from CPAs in 8 out of 10 auditor-client relationships,

the degree of those majority responses between WPs and CPAs differed sufficiently to cause the Chi Square Test to show significant results for a number of situations. This indicates that there are statistically significant differences in perception of auditors' independent between WPs and CPAs. Besides the two situations where opposite majority opinions were obtained, the Chi Square Test also detected differences in the responses of WPs and CPAs for an additional 3 situations. Table 28 gives the results of the test of null hypothesis VII by applying the Chi Square Test of Homogeneity. In all three of these situations, the degree of consensus was consistently higher for WPs than for CPAs. Closer examination of Table 29 reveals that for all of the 8 situations where both WPs' and CPAs' majority responses fell into the "Independent" category, the degree of consensus is consistently higher for WPs than for CPAs, even though there was statistical significance for 3 situations only. Apparently, WPs take a "softer" stance than CPAs in all the situations investigated for which CPAs' responses were available.

#### Summary of Independence Decisions

The survey results and analysis revealed that for most of the auditor-client relationships investigated WPs agreed with users of financial statements. Only for Situations 6B, 13, 17C did WPs disagree with both LKRs and LWPs. In Situation 6B, which involved simultaneous ownership by a bank of the auditing firm and its audit client, a slight majority of WPs considered the auditing firm to be not independent, whereas a majority of LKRs

and LWPs thought otherwise. However, only for LKRs was the majority statistically significant, indicating consensus. Similarly, in Situation 13, involving legal counseling by an auditor, a majority of WPs considered the accounting firm still to be independent, whereas a majority of LKRs and LWPs did not.

For Situation 17C, which deals with an auditor-client relationship where the accounting firm derived 25 percent of its total revenue from audit fees from one client, WPs considered independence not to be impaired whereas a majority of LKRs and LWPs were of the opposite opinion. There were also a number of situations where LKRs and LWPs were of divided opinion and thus WPs agreed with only one of the two user groups. In only one situation (Situation 16) did WPs agree with LKRs but not with LWPs, whereas in three situations (1, 5B, and 7) the majority of WPs agreed with the majority of LWPs but not with the majority of LKRs.

Table 30 provides a summary of the results of the survey. As can be seen from Table 30, in most of the situations investigated the three experimental groups each voiced the same majority opinion.

As was seen earlier from Table 28, which summarizes the results of the auditor-client relationships also investigated by Lavin in 1973, WPs agreed with CPAs' perceptions in 8 out of 10 situations. Only in two situations did the WPs responses differ from those obtained from CPAs by Lavin, namely Situation 4 and Situation 12. It was noted that for all 8 situations where both WPs' and CPAs' majority opinions were in the "Independent" category the degree of consensus was consistently higher for WPs than for CPAs. The

TABLE 30

## Summary of Consensus for 27 Auditor-Client Relationships

Relationship	Consensus Response	WPs	LKRs	LWPs
1	Independent	54.2%		54.8%
	Not independent		61.8%	
2	Independent	87.0%	98.1%	86.7%
3	Not independent	54.6%	50.9%	58.6%
4	Independent	54.7%	60.0%	65.5%
5A	Independent	75.5%	89.1%	90.0%
5B	Independent		56.4%	
	Not independent	68.9%		53.3%
5C	Not independent	79.4%	72.7%	83.3%
6A	Independent	57.0%	79.2%	65.5%
6B	Independent		66.0%	51.7%
	Not independent	50.5%		
6C	Not independent	77.6%	56.6%	75.9%
6D	Not independent	84.1%	67.9%	82.8%
6E	Not independent	88.8%	73.6%	86.2%
7	Independent		70.4%	
	Not independent	58.3%		54.8%
8	Independent	77.8%	81.8%	64.5%
9	Independent	94.4%	92.5%	90.3%
10	Independent	85.0%	90.9%	83.9%
11	Independent	96.3%	96.4%	90.3%
12	Independent	77.8%	70.9%	80.0%
13	Independent	61.2%		
	Not independent		55.6%	63.3%
14	Independent	75.9%	74.2%	70.9%
15	Independent	89.8%	94.5%	93.5%
16	Independent	61.7%	63.6%	
	Not independent			51.7%
17A	Independent	96.3%	94.5%	100.0%
17B	Independent	91.5%	85.5%	83.3%
17C	Independent	52.4%		
	Not independent		69.1%	60.0%
17D	Not independent	82.9%	92.7%	80.0%
17E	Not independent	88.8%	92.7%	83.3%



difference proved significant for 3 out of those 8 situations at an alpha level of 0.05.

The comparison of majority responses by WPs with AICPA and SEC rulings revealed that WPs tended to disagree with these rules for a significant number of situations. Out of a total of 11 separate situations for auditor-client relationships where both the SEC and AICPA are of the same opinion, WPs disagreed in 7 and agreed in 4 situations. In situations where the AICPA and SEC are of divided opinion, WPs agreed with the position of the AICPA on four occasions and with the SEC position on one occasion. For Situation 10, WPs disagreed with the SEC position and disagreed with the AICPA "home office" rule. In this particular case, the WPs agreed with the AICPA's "other office" rule.

As was described in the analysis, not all of the majority opinions were statistically significant. Tables 28 and 31 provide a summary of the results obtained from the hypothesis tests. This summary gives a concise view of the statistical test results of the null hypotheses tested at an alpha level of  $\leq 0.05$ .

### Background Variables

The impact of various background variables were investigated by performing a variety of statistical tests. The Chi Square Test of Homogeneity was employed to test whether there were significant differences in the responses received from WPs affiliated with the international "Big Eight" accounting firms and those WPs that were not affiliated with such firms. However, applying this test to each of the situations investigated showed no statistically

TABLE 31  
Summary of Testing Hypotheses I, II, III, and VI for the  
Situations Investigated

(Null Hypotheses Rejected at  $\alpha \leq 0.05$ )

Type of Auditor-Client Relationship	Situation	H <sub>0</sub> : I (WPs)	H <sub>0</sub> : II (LKR's)	H <sub>0</sub> : III (LWPs)	H <sub>0</sub> : VI (No differences)
<b>Financial Interest</b>					
	1	not rejected	not rejected	not rejected	not rejected
	2	rejected	rejected	rejected	not rejected
	3	not rejected	not rejected	not rejected	not rejected
	4	not rejected	not rejected	not rejected	not rejected
	5A	rejected	rejected	rejected	rejected
	5B	rejected	not rejected	not rejected	rejected
	5C	rejected	rejected	rejected	not rejected
	6A	not rejected	rejected	not rejected	rejected
	6B	not rejected	rejected	not rejected	not rejected
	6C	rejected	not rejected	rejected	rejected
	6D	rejected	rejected	rejected	not rejected
	6E	rejected	rejected	rejected	rejected
<b>Bookkeeping and EDP</b>					
	7	not rejected	rejected	not rejected	rejected
	8	rejected	rejected	not rejected	not rejected
	9	rejected	rejected	rejected	not rejected
<b>Family Relationships</b>					
	10	rejected	rejected	rejected	not rejected
	11	rejected	rejected	rejected	not rejected
<b>Conflicting Occupations</b>					
	12	rejected	rejected	rejected	not rejected
	13	not rejected	not rejected	not rejected	rejected
<b>Business Relationships</b>					
	14	rejected	rejected	rejected	not rejected
	15	rejected	rejected	rejected	not rejected
	16	not rejected	not rejected	not rejected	not rejected
	17A	rejected	rejected	rejected	not rejected
	17B	rejected	rejected	rejected	not rejected
	17C	not rejected	rejected	not rejected	rejected
	17D	rejected	rejected	rejected	not rejected
	17E	rejected	rejected	rejected	not rejected

significant differences between the two groups. Since there were only eleven WPs among the respondents who belonged to "Big Eight" accounting firms, the results of the Chi Square Test should be interpreted cautiously since the sample may not have been large enough to identify significant differences between the two groups, if there were any differences. However, the Chi Square Test of Homogeneity was also employed to test for significant differences between WPs belonging to auditing firms that were also involved with the audit of subsidiaries of U.S. companies, and WPs who belonged to auditing firms not involved with this type of audit. Table 32 indicates the responses to each situation presented to these two groups. There were 28 WPs affiliated with auditing firms that performed audits of U.S. subsidiary companies and 79 WPs belonging to auditing firms that were not involved with audits of U.S. subsidiary companies. The results of the Chi Square Test showed that the responses did not differ significantly between the two groups for most auditor-client relationships investigated.

Only for Situation 5B did the computed  $\chi^2$ -value prove to be significant for a set alpha of 0.05. Even though a majority of both groups considered the auditors involved not to be independent, the percentages differed significantly, 89.3 percent for WPs affiliated with auditing firms involved with audits of U.S. subsidiaries and 61 percent for WPs affiliated with auditing firms that were not involved with audits of U.S. subsidiaries.

It could be concluded that, except for Situation 5B, the perceptions of auditors' independence by WPs are not affected

TABLE 32

Comparison of Responses From WPs Associated with WPGs Involved  
in Auditing U.S. Subsidiary Firms ( $WP_{us}$ ) with  
WPs Not Associated with Such WPGs ( $WP_{na}$ ).

Situation		$WP_{us}$		$WP_{na}$		$\chi^2$	$\alpha$ -level
		#	%	#	%		
1	Independent	12	42.9	45	57.7	1.276	0.259
	Not independent	16	57.1	33	42.3		
		28	100.0	78	100.0		
2	Independent	24	85.7	69	87.3	0.011	0.915
	Not independent	4	14.3	10	12.7		
		28	100.0	79	100.0		
3	Independent	9	32.1	40	50.6	2.151	0.143
	Not independent	19	67.9	39	49.4		
		28	100.0	79	100.0		
4	Independent	19	73.1	39	49.4	3.540	0.060
	Not independent	7	26.9	40	50.6		
		26	100.0	79	100.0		
5A	Independent	18	66.7	61	78.2	0.881	0.348
	Not independent	9	33.3	17	21.8		
		27	100.0	78	100.0		
5B	Independent	3	10.7	30	39.0	6.348	0.012
	Not independent	25	89.3	47	61.0		
		28	100.0	77	100.0		
5C	Independent	2	7.1	20	25.6	3.236	0.072
	Not independent	26	92.9	58	74.4		
		28	100.0	78	100.0		
6A	Independent	13	48.1	47	59.5	0.643	0.423
	Not independent	14	51.9	32	40.5		
		27	100.0	79	100.0		
6B	Independent	11	40.7	41	51.9	0.606	0.436
	Not independent	16	59.3	38	48.1		
		27	100.0	79	100.0		

TABLE 32  
(continued)

Situation		WP <sub>us</sub> # %		WP <sub>na</sub> # %		$\chi^2$	$\alpha$ -level
6C	Independent	6	22.2	18	22.8	0.0425	0.837
	Not independent	21	77.8	61	77.2		
		27	100.0	79	100.0		
6D	Independent	4	14.8	13	16.5	0.0106	0.918
	Not independent	23	85.2	66	83.5		
		27	100.0	79	100.0		
6E	Independent	3	11.1	9	11.4	0.097	0.755
	Not independent	24	88.9	70	88.6		
		27	100.0	79	100.0		
7	Independent	7	25.0	38	48.1	3.629	0.057
	Not independent	21	75.0	41	51.9		
		28	100.0	79	100.0		
8	Independent	20	71.4	64	81.0	0.629	0.428
	Not independent	8	28.6	15	19.0		
		28	100.0	79	100.0		
9	Independent	27	96.4	73	93.6	0.007	0.936
	Not independent	1	3.6	5	6.4		
		28	100.0	78	100.0		
10	Independent	24	85.7	66	84.6	0.028	0.866
	Not independent	4	14.3	12	15.4		
		28	100.0	78	100.0		
11	Independent	28	100.0	75	94.9	0.402	0.526
	Not independent	0	0.0	4	5.1		
		28	100.0	79	100.0		
12	Independent	20	71.4	63	79.7	0.414	0.520
	Not independent	8	28.6	16	20.3		
		28	100.0	79	100.0		

TABLE 32

(continued)

Situation		WP <sub>us</sub> #      %		WP <sub>na</sub> #      %		$\chi^2$	$\alpha$ -level
13	Independent	12	50.0	51	65.4	1.246	0.264
	Not independent	12	50.0	27	34.6		
		<u>24</u>	<u>100.0</u>	<u>78</u>	<u>100.0</u>		
14	Independent	20	71.4	61	77.2	0.127	0.721
	Not independent	8	28.6	18	22.8		
		<u>28</u>	<u>100.0</u>	<u>79</u>	<u>100.0</u>		
15	Independent	26	92.9	70	88.6	0.076	0.784
	Not independent	2	7.1	9	11.4		
		<u>28</u>	<u>100.0</u>	<u>79</u>	<u>100.0</u>		
16	Independent	13	48.1	52	65.8	1.958	0.162
	Not independent	14	51.9	27	34.2		
		<u>27</u>	<u>100.0</u>	<u>79</u>	<u>100.0</u>		
17A	Independent	25	92.6	77	97.5	0.317	0.574
	Not independent	2	7.4	2	2.5		
		<u>27</u>	<u>100.0</u>	<u>79</u>	<u>100.0</u>		
17B	Independent	22	81.5	74	94.9	3.039	0.081
	Not independent	5	18.5	4	5.1		
		<u>27</u>	<u>100.0</u>	<u>78</u>	<u>100.0</u>		
17C	Independent	11	40.7	44	57.1	1.550	0.213
	Not independent	16	59.3	33	42.9		
		<u>27</u>	<u>100.0</u>	<u>77</u>	<u>100.0</u>		
17D	Independent	6	22.2	12	15.6	0.239	0.628
	Not independent	21	77.8	65	84.4		
		<u>27</u>	<u>100.0</u>	<u>77</u>	<u>100.0</u>		
17E	Independent	3	11.1	9	11.4	0.097	0.755
	Not independent	24	88.9	70	88.6		
		<u>27</u>	<u>100.0</u>	<u>79</u>	<u>100.0</u>		

by whether or not the auditing firm with which a WP is affiliated performs audits of U.S. subsidiaries.

The same Chi Square Test was employed to test for differences in accounting firm affiliation. Table 33 presents the four categories in which the WP responses were grouped. As can be seen from Table 33, 31.1 percent of the respondents had their own practice but were also associated with other accounting firms, and 3.9 percent belonged to an association that audits cooperatives (Prüfungsverband).<sup>33</sup> Table 33 also compares the breakdown of the sample to the breakdown of the entire WP profession.

The Chi Square Test excluded those WPs who belonged to a Prüfungsverband due to the small number in this category. The results of this test proved significant for Situation 17D only. Even though a majority of all three groups of WPs agreed that the accounting firm under the circumstances described is not considered to be independent, the response rate differed significantly. Of the WPs who are sole practitioners, 91.7 percent fell in the "Not independent" category while 87.1 percent of Group 3 and only 69 percent of Group 2 came under the "Not independent" category. Thus for Situation 17D, one could conclude that a larger proportion of WPs practicing as sole practitioners, or as sole practitioners associated with other WPGs or accounting firms, considered auditors' independence to be impaired in Situation 17D (which describes an auditor-client relationship where approximately fifty percent of an auditing firm's total revenue consisted of audit fees from one client) than did WP respondents belonging to WPGs.

At first sight, these findings appear somewhat inconsistent

TABLE 33

## Type of Accounting Firm Affiliation

## of WP Respondents

Group	Respondents		Population	
	#	%	#	%
1 Sole practitioner only	38	36.9	1,171	35.2
2 Accounting firm (WPG) only	29	28.1	1,196	36.0
3 Sole practitioner but also affiliated with WPG	32	31.1	895	26.9
4 Prüfungsverband	<u>4</u>	<u>3.9</u>	<u>62</u>	<u>1.9</u>
Total	<u>103</u>	<u>100.0</u>	<u>3,324</u>	<u>100.0</u>

TABLE 34

## Significant Differences of Responses Due

## to Accounting Firm Affiliation

Situation	Group 1		Group 2		Group 3	
	#	%	#	%	#	%
17D Independent	3	8.3	9	31.9	4	12.9
Not independent	<u>33</u>	<u>91.7</u>	<u>20</u>	<u>69.0</u>	<u>27</u>	<u>87.1</u>
	36	100.0	29	100.0	31	100.0

Chi Square Test:  $\chi^2 = 6.4265$

Significance level = 0.0402

Degrees of Freedom = 2



since sole practitioners may encounter this type of relationship more often than WPGs. However, the fact that most WPGs are auditing firms with no more than 3 or 4 WPs<sup>34</sup> may indicate that this auditor-client relationship may occur as frequently among this group, or even more frequently, since many sole practitioners derive almost all of their revenue from tax work and accounting services and not from audit work.

If one assumes that WPGs involved with audits of U.S. subsidiaries are the larger WPGs, and analysis of the respondents in this category bears this out, then most of these WPGs would very likely not have any audit fees from any one client that approaches 50 percent of their total revenue. Table 32 seems to support this reasoning. As noted above, there were no statistically significant differences between WPs belonging to WPGs involved with audits of U.S. subsidiaries and WPs belonging to WPGs that were not, for Situation 17D as well as for most other auditor-client relationships investigated. Thus it may be concluded that the type of firm affiliation has no effect on WPs' perceptions of auditors' independence for most of the situations investigated.

A Chi Square Test of Homogeneity was employed to test for significant differences between responses from WPs who performed audits and WPs who were not involved in audit work. Table 35 gives a summary of responses received from WPs to question B3.<sup>35</sup> From this table it can be seen that the largest percentage of WPs were mainly involved in both audit and tax work (42.1 percent), followed by tax work (14 percent) and audit work (13.1 percent).

To apply the Chi Square Test, these eleven groups (none

TABLE 35

Breakdown of WP Respondents by

Area(s) of Professional Emphasis

	#	%
1. Audit	14	13.1
2. Tax	15	14.0
3. Management Consulting	0	0.0
4. Other Services	3	2.8
5. Audit and Tax	45	42.1
6. Audit, Tax, and Management Consulting	12	11.2
7. Audit and Management Consulting	3	2.8
8. Audit, Tax, and Other Services	4	3.7
9. Audit and Other Services	5	4.7
10. Tax and Management Consulting	4	3.7
11. Tax and Other Services	1	0.9
12. Management Consulting and Other Services	1	0.9
Rounding	—	0.1
Total	<u>107</u>	<u>100.0</u>

of the WP responses fell into the Management Consulting only category) were collapsed into two categories, one group representing those responses from WPs indicating audit as at least one of their main areas of professional emphasis, and another group of those WPs responding who did not indicate auditing as an area of professional emphasis.

The results of the Chi Square Test did not show any statistically significant differences between the two groups at an alpha level of 0.05 for any of the situations presented. Thus one could conclude that involvement with auditing work has no effect on WPs' perceptions of auditors' independence for the situations presented.

In order to test whether the respondents' years of experience

in their current occupation affected their responses, a Pearson Correlation Test was performed for WPs, LKRs, and LWPs. To perform this test, any response in the "Independent" category was set equal to one, whereas a response in the "Not independent" category was set equal to zero. Thus, a positive correlation with years of experience for a particular situation would indicate that the more experience the respondent had the more he tended to consider the auditors to be independent in a given situation. A negative correlation would indicate the opposite.

Table 36 presents the various correlation coefficients for the three experimental groups for each of the situations investigated as well as the corresponding significance level. For the WP responses the computed correlation coefficient proved to be significant at alpha level of  $\leq 0.05$  for Situations 1, 10, and 11. Situation 1 depicts an accounting firm which received a promissory note in payment of its audit fee. Situations 10 and 11 both involve an auditor who had a close relative in a leading position at a client firm. Apparently, since the correlation was negative for Situations 10 and 11, the more experience a WP has the more he considers this situation as one that impairs auditors' independence.

For LKRs, the correlation coefficients proved significant for four situations, Situations 5B, 5C, 6D, and 6E. For all four situations, a positive correlation was found, indicating that the more experience an LKR had the more he considers the auditors to be independent in these situations. Situations 5B and 5C deal with auditors who owned shares of an audit client. Situations 6D and 6E represent a relationship in which a bank owned a significant

TABLE 36

## Pearson Correlation Coefficient for Years of Experience

Situation	WPs		LKR		LWP	
	P	$\alpha$ -level	P	$\alpha$ -level	P	$\alpha$ -level
1	0.1622	0.048*	0.0282	0.420	0.1435	0.233
2	-0.0809	0.203	-0.1793	0.099	0.0644	0.372
3	0.0580	0.276	0.1140	0.206	0.0414	0.419
4	-0.0498	0.306	0.0401	0.387	0.3377	0.042*
5A	0.0175	0.429	-0.0546	0.347	0.2388	0.111
5B	0.0209	0.416	0.2301	0.047*	0.2774	0.076
5C	-0.0740	0.225	0.3584	0.004*	0.0357	0.428
6A	-0.1223	0.105	0.0812	0.282	0.3240	0.050*
6B	-0.0239	0.403	0.0614	0.331	0.2757	0.082
6C	-0.0765	0.217	0.2174	0.059	0.2072	0.150
6D	-0.0614	0.265	0.2289	0.050*	0.4215	0.014*
6E	-0.0118	0.452	0.2497	0.036*	0.3852	0.024*
7	0.0566	0.280	0.1317	0.174	-0.1052	0.297
8	0.0466	0.316	-0.2041	0.069	0.4082	0.016*
9	0.0949	0.165	-0.1320	0.175	-0.1512	0.221
10	-0.2217	0.011*	-0.0179	0.449	-0.1356	0.246
11	-0.2372	0.007*	-0.0638	0.323	-0.0265	0.447
12	-0.1239	0.101	-0.1332	0.169	-0.2593	0.096
13	-0.0333	0.369	0.0404	0.387	0.3554	0.032*
14	-0.1096	0.129	-0.1020	0.232	0.0892	0.326
15	0.0166	0.432	-0.0426	0.380	0.1831	0.176
16	-0.0394	0.344	0.1095	0.215	0.2757	0.082
17A	-0.1083	0.133	0.0300	0.415	**	
17B	-0.1433	0.071	0.0850	0.271	-0.0312	0.437
17C	-0.0719	0.233	0.1488	0.141	0.1105	0.288
17D	-0.0991	0.157	-0.1026	0.230	0.3198	0.049*
17E	-0.1108	0.128	-0.1026	0.230	0.2730	0.080

\* Significant for  $\alpha \leq 0.05$ .

\*\* Correlation coefficient could not be computed since all responses were in one category.

portion of the stock of an audit client and at the same time partially owned the auditing firm, 50 percent in Situation 6D and over 50 percent in Situation 6E.

For LWPs, significant correlations were found in 7 out of 27 separate situations. Three of these seven correlations proved barely significant at the set alpha level of 0.05. (See Table 36). For Situations 6D and 6E, there were also positive correlations for LWPs, as well as for LKRs, as mentioned above. The remaining five situations that had statistically significant correlations dealt with bookkeeping services (Situation 8), a business relationship (Situation 4), a relationship where a member of a WPG also acted as general counsel (Situation 13), a relationship where 50 percent of a WPG's total revenue consisted of audit fees from one client (Situation 17D) and finally, a relationship similar to Situations 6D and 6E (Situation 6A) which were described when correlations of LKRs were discussed.

It should be noted that for all of these seven auditor-client relationships, the correlations were positive indicating that the more experience an LWP has the more likely he is to consider the auditors to be independent under the various circumstances described. However, the correlations were not very strong in any of the situations.

Table 37 and Table 38 give the responses to questions B2, B3, and B4 for LKRs and LWPs, respectively.<sup>36</sup> Most of the LKRs and LWPs were familiar with the audit work of WPs and considered auditors' independence to be of great importance.

For LKRs and LWPs alike, a majority used audited financial

TABLE 37

## Responses of LKRs to Questions B2, B3, and B4

B2: How familiar are you with the audit work of WPs?

	<u>Not familiar</u>			<u>Very familiar</u>		
	<u>1</u>	<u>2</u>	<u>3</u>	<u>4</u>	<u>5</u>	<u>Total</u>
Frequency	0	5	19	24	6	54
Percentage	0.0	9.3	35.2	44.4	11.1	100.0

B3: How important do you consider the independence of auditors to be?

	<u>Not important</u>			<u>Very important</u>		
	<u>1</u>	<u>2</u>	<u>3</u>	<u>4</u>	<u>5</u>	<u>Total</u>
Frequency	0	0	0	13	41	54
Percentage	0.0	0.0	0.0	24.1	75.9	100.0

B4: What percentage of your lending decisions involve the use of audited financial statements?

	<u>0%</u>	<u>1-25%</u>	<u>26-50%</u>	<u>51-75%</u>	<u>76-100%</u>	
	<u>1</u>	<u>2</u>	<u>3</u>	<u>4</u>	<u>5</u>	<u>Total</u>
Frequency	0	12	9	15	18	54
Percentage	0.0	22.2	16.7	27.8	33.3	100.0

TABLE 38

## Responses of LWPs to Questions B2, B3, and B4

B2: How familiar are you with the audit work of WPs?

	<u>Not familiar</u>			<u>Very familiar</u>		
	<u>1</u>	<u>2</u>	<u>3</u>	<u>4</u>	<u>5</u>	<u>Total</u>
Frequency	0	5	8	10	6	29
Percentage	0.0	17.2	27.6	34.5	20.7	100.0

B3: How important do you consider the independence of auditors to be?

	<u>Not important</u>			<u>Very important</u>		
	<u>1</u>	<u>2</u>	<u>3</u>	<u>4</u>	<u>5</u>	<u>Total</u>
Frequency	0	0	1	6	23	30
Percentage	0.0	0.0	3.3	20.0	76.7	100.0

B4: What percentage of your investment decisions involve the use of audited financial statements?

	<u>0%</u>	<u>1-25%</u>	<u>26-50%</u>	<u>51-75%</u>	<u>76-100%</u>	
	<u>1</u>	<u>2</u>	<u>3</u>	<u>4</u>	<u>5</u>	<u>Total</u>
Frequency	1	4	3	7	12	27
Percentage	3.7	14.8	11.1	25.9	44.5	100.0

statements as input for more than half of all their financial decisions.<sup>37</sup> Only one respondent among LKRs and LWPs did not use audited financial statements for making financial decisions. Based on these findings it cannot be denied that LKRs and LWPs present a group that does use financial statements audited by WPs in their financial decision making process.

Based on the responses to questions B2, B3, and B4, the responses of LKRs and LWPs to the various situations presented were grouped into the different categories for each of the three questions. A separate series of Chi Square Tests was applied for the responses to questions B2, B3, and B4 for both, LKRs and LWPs, to determine if there were significant differences in perception of auditors independence between the categorized groups. To allow for a more meaningful test, the categories, where necessary, were collapsed into three groups. Thus, for question B2, category 1 and 2 were collapsed into one group, and category 4 and 5 were collapsed into another group. Category 3 was left intact. The same procedures were employed for question B4. For question B3 responses fell into only three groups (two groups for LKRs) making these modifying procedures unnecessary. The results of the Chi Square Test proved statistically insignificant for most situations. Tables 39 and 40 list the responses for those situations where statistically significant differences were found between the categorized responses for LKRs and LWPs, respectively.

For LKRs question B2 categorization proved significant at  $\alpha = 0.05$  for Situation 3. Categorization of question B4 was significant for Situation 10. As is shown in Table 40, the



only significant grouping for LWP's that displayed statistically significant differences in perceptions of auditors' independence was categorization of question B3 for Situation 17E. However, the low value in some of the cells makes this result somewhat suspect.

In sum, for the overwhelming majority of situations presented, the degree to which users of financial statements were familiar with the WPs audit work (question B2), or the importance they attached to auditors' independence (question B3) or the frequency of their use of audited financial statements (question B4) had no effect on their perceptions of auditors' independence.

#### Financial Decisions

The two financial statement user groups, LKRs and LWP's, were asked not only about their perceptions of auditors' independence for the various situations presented in the questionnaire, but also how each described auditor-client relationship would affect their financial decisions. Financial decisions are defined as the lending decisions for LKRs and the investment decisions for LWP's.

As was explained in Chapter Four, the sample subjects were given a five-point scale ranging from 1 to 5 to answer each question. A "1" represents an auditor-relationship which has a very negative impact on financial statement users' financial decisions whereas a "5" would indicate a very positive impact on the financial decisions of these two groups of financial statement users.

There are a great many variables and factors that may influence

TABLE 39

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LKR Responses to Questions B2 and B4 to Selected Situations

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<u>Question B2</u>					
Response category		1/2	3	4/5	Total
<u>Situation</u>					
3	Independent	0	8	18	26
	Not independent	5	11	12	28
	Total	5	19	30	54

Chi Square Test:  $\chi^2 = 6.6087$

Significance level = 0.0367

Degrees of Freedom = 2

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<u>Question B4</u>					
Response category		1/2	3	4/5	Total
<u>Situation</u>					
10	Independent	10	6	33	49
	Not independent	2	3	0	5
	Total	12	9	33	54

Chi Square Test:  $\chi^2 = 10.3592$

Significance level = 0.0056

Degrees of Freedom = 2

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TABLE 40

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LWP Responses to Question B3 to Selected Situations

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Response category		3	4	5	Total
<u>Situation</u>					
17E	Independent	1	0	4	5
	Not independent	0	6	19	25
	Total	1	6	23	30

Chi Square Test:  $\chi^2 = 6.2087$

Significance level = 0.0449

Degrees of Freedom = 2

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lenders and investors in making financial decisions. Perception of auditors' independence, which is investigated in this study, is only one of the factors. If it were found that perceptions of auditors' independence have no effect on the financial decisions of users of audited financial statements, it could be argued that auditors' independence is not a factor in the financial decision making model or is a factor having insignificant weight. In this case, the importance of auditors' independence may seem somewhat overstated in both the German and United States literature.

Tables 41 and 42 present responses received from LKRs and LWPs, respectively. Table 43 presents a comparison of mean responses of LKRs and LWPs. As can be seen from Table 43, auditor-client relationships considered to be independent by LKRs and LWPs alike had a mean response ranging from 2.614 to 3.250. A response of 3.000 indicates no effect on the financial decision, either positive or negative.

The mean responses for LKRs and LWPs who considered the auditor-client relationship to impair auditors' independence ranged from 1.000 to 2.667. Even though, a priori, it could be argued that a decision maker who considers a given auditor-client relationship to impair the auditors' independence would not consider their relationship to be one that influences his financial decision positively, some respondents indicated just that. For Situations 6A through 6E, a few respondents considered the auditing firm to lack independence but stated that their financial decisions would be positively affected. These situations all involved a bank that owned stocks of both the auditing firm and its audit client.

Perhaps the fact that the bank had invested capital in the audit client firm is a signal to those few respondents that the stock of this firm is a good investment regardless of the auditors' independence status.

Table 44 summarizes the results of testing hypotheses VIII and IX. Null hypotheses VIII (IX) state that LKRs (LWPs) perceptions regarding the concept of auditors' independence have no effect on their financial decisions. To test null hypothesis VIII, mean responses of LKRs on the effect of their perceptions of auditors' independence on their financial decisions were computed for LKRs whose responses fell into the "Independent" category and for LKRs whose responses fell into the "Not independent" category for each of the situations investigated. Thus, two means were computed for each situation. The t-Test was applied to detect significant differences between the two means for each individual situation. The same procedure was employed with LWPs to test null hypothesis IX.

For LKRs the t-values obtained by applying the t-Test to the mean responses of both categories, "Independent" versus "Not independent", were mostly associated with probability values far less than  $\alpha = 0.05$ . Only for Situation 17A did the significance level exceed 0.05. Thus, for 26 of the 27 separate auditor-client relationships, the t-Test proved statistical significance, implying that null hypothesis VIII, which states that LKRs perceptions regarding the concept of auditors' independence have no effect on their lending decision, must be rejected.

For LWPs the results of the t-Tests applied to each individual

situation revealed that for seven auditor-client relationships there was no effect of LWPs' perceptions of auditors' independence on their investment decision. From Table 44 it can be seen that Situations 2, 3, 5A, 5C, 6D, 10, and 15 had t-values with corresponding probabilities exceeding the set alpha level of 0.05. For Situation 17A the t-statistic could not be computed since all LWPs considered the accounting firm to be independent in Situation 17A. For the remaining nineteen situations LWPs' investment decisions were affected significantly by their perceptions of auditors' independence.

It should be pointed out that four of the seven auditor client relationships in which LWPs perceptions of auditors' independence did not affect their investment decisions dealt with situations where auditors had a financial interest in their audit clients. Apparently, this affected their perceptions of auditors' independence to the extent that they made a judgment in this category, but the circumstances described were not such as to significantly affect their investment decisions. The other three auditor-client relationships involved the renting of computer time by auditors to their client, a situation in which a brother-in-law of one of the members of the accounting firm was the controller for the audit client and the situation where a bank owned shares of corporation as well as 50 percent of the shares of their auditors' firm. Apparently, investors did not consider these situations to be significant enough to have an effect on their investment decisions, whereas LKRs all considered them to have an effect on their lending decision.

TABLE 41

		Analysis of Lending Decision					
		<u>Impact on Lending Decision</u>					
		<u>Very Negative</u>					<u>Very Positive</u>
<u>Situation</u>		1	2	3	4	5	<u>Total*</u>
1	Frequency	15	22	14	4	0	55
	Percentage	27.3	40.0	25.5	7.3	0.0	100.0
2	Frequency	1	2	49	1	1	54
	Percentage	1.9	3.7	90.7	1.9	1.9	100.0
3	Frequency	9	24	20	1	1	55
	Percentage	16.4	43.6	36.4	1.8	1.8	100.0
4	Frequency	3	20	28	4	0	55
	Percentage	5.5	36.4	50.9	7.3	0.0	100.0
5A	Frequency	1	5	48	0	1	44
	Percentage	1.8	9.1	87.3	0.0	1.8	100.0
5B	Frequency	5	25	23	1	1	55
	Percentage	9.1	45.5	41.8	1.8	1.8	100.0
5C	Frequency	12	30	10	3	0	55
	Percentage	21.8	54.5	18.2	5.5	0.0	100.0
6A	Frequency	4	7	36	4	1	52
	Percentage	7.7	13.5	69.2	7.7	1.9	100.0
6B	Frequency	6	13	29	4	1	53
	Percentage	11.3	24.5	54.7	7.5	1.9	100.0
6C	Frequency	10	20	18	3	2	53
	Percentage	18.9	37.7	34.0	5.7	3.8	100.0
6D	Frequency	16	16	16	3	8	53
	Percentage	30.2	30.2	30.2	5.7	3.8	100.0
6E	Frequency	20	14	14	2	3	53
	Percentage	37.7	26.4	26.4	3.8	5.7	100.0
7	Frequency	4	14	18	16	3	55
	Percentage	7.3	25.5	32.7	29.1	5.5	100.0
8	Frequency	0	11	37	5	1	54
	Percentage	0.0	20.4	68.5	9.3	1.9	100.0

TABLE 41

(continued)

		Impact on Lending Decision					Total*
		Very Negative				Very Positive	
Situation		1	2	3	4	5	
9	Frequency	0	4	45	3	1	53
	Percentage	0.0	7.5	84.9	5.7	1.9	100.0
10	Frequency	0	4	49	2	0	55
	Percentage	0.0	7.3	89.1	3.6	0.0	100.0
11	Frequency	0	1	53	0	1	55
	Percentage	0.0	1.8	96.4	0.0	1.8	100.0
12	Frequency	2	17	34	1	1	55
	Percentage	3.6	30.9	61.8	1.8	1.8	100.0
13	Frequency	7	20	22	4	1	54
	Percentage	13.0	37.0	40.7	7.4	1.9	100.0
14	Frequency	0	17	35	2	1	55
	Percentage	0.0	30.9	63.6	3.6	1.8	100.0
15	Frequency	0	6	48	0	1	55
	Percentage	0.0	10.9	87.3	0.0	1.8	100.0
16	Frequency	1	14	30	8	2	55
	Percentage	1.8	25.5	54.5	14.5	3.6	100.0
17A	Frequency	0	3	48	1	1	53
	Percentage	0.0	5.7	90.6	1.9	1.9	100.0
17B	Frequency	0	12	40	1	1	54
	Percentage	0.0	22.2	74.1	1.9	1.9	100.0
17C	Frequency	6	36	12	0	1	55
	Percentage	10.9	65.5	21.8	0.0	1.8	100.0
17D	Frequency	29	21	3	1	1	55
	Percentage	52.7	38.2	5.5	1.8	1.8	100.0
17E	Frequency	38	12	3	2	0	55
	Percentage	69.1	21.8	5.5	3.6	0.0	100.0

\* Due to rounding, the total percentage may be slightly more or less than 100 percent for a number of situations.

TABLE 42

## Analysis of Investment Decision

		<u>Impact on Investment Decision</u>					
		<u>Very Negative</u>			<u>Very Positive</u>		
Situation		1	2	3	4	5	Total*
1	Frequency	8	10	11	0	0	29
	Percentage	27.6	34.5	37.9	0.0	0.0	100.0
2	Frequency	0	3	22	1	1	27
	Percentage	0.0	11.1	81.5	3.7	3.7	100.0
3	Frequency	4	8	11	5	0	29
	Percentage	14.3	28.6	39.3	17.9	0.0	100.0
4	Frequency	4	8	14	1	0	27
	Percentage	14.8	29.6	51.9	3.7	0.0	100.0
5A	Frequency	0	3	22	3	0	28
	Percentage	0.0	10.7	78.6	10.7	0.0	100.0
5B	Frequency	3	8	15	2	0	28
	Percentage	10.7	28.6	53.6	7.1	0.0	100.0
5C	Frequency	9	8	7	3	1	28
	Percentage	32.1	28.6	25.0	10.7	3.6	100.0
6A	Frequency	2	8	13	4	0	27
	Percentage	7.4	29.6	48.1	14.8	0.0	100.0
6B	Frequency	5	8	9	5	0	27
	Percentage	18.5	29.6	33.3	18.5	0.0	100.0
6C	Frequency	10	6	6	5	0	27
	Percentage	37.0	22.2	22.2	18.5	0.0	100.0
6D	Frequency	12	7	3	4	1	27
	Percentage	44.4	25.9	11.1	14.8	3.7	100.0
6E	Frequency	14	5	3	4	1	27
	Percentage	51.9	18.5	11.1	14.8	3.7	100.0
7	Frequency	6	6	11	5	1	29
	Percentage	20.7	20.7	37.9	17.2	3.4	100.0
8	Frequency	4	5	15	4	1	29
	Percentage	13.8	17.2	51.7	13.8	3.4	100.0



TABLE 42

(continued)

		Impact on Investment Decision					
		Very Negative				Very Positive	
Situation		1	2	3	4	5	Total*
9	Frequency	0	2	23	3	0	28
	Percentage	0.0	7.1	82.1	10.7	0.0	100.0
10	Frequency	0	3	24	2	0	29
	Percentage	0.0	10.3	82.8	6.9	0.0	100.0
11	Frequency	0	3	24	1	1	29
	Percentage	0.0	10.3	82.8	3.4	3.4	100.0
12	Frequency	0	5	22	1	1	29
	Percentage	0.0	17.2	75.9	3.4	3.4	100.0
13	Frequency	4	12	11	0	1	28
	Percentage	14.3	42.9	39.2	0.0	3.6	100.0
14	Frequency	2	3	22	2	0	29
	Percentage	6.9	10.3	75.9	6.9	0.0	100.0
15	Frequency	0	2	26	0	1	29
	Percentage	0.0	6.9	89.7	0.0	3.4	100.0
16	Frequency	2	7	14	3	1	27
	Percentage	7.4	25.9	51.9	11.1	3.7	100.0
17A	Frequency	0	1	24	1	1	27
	Percentage	0.0	3.7	88.9	3.7	3.7	100.0
17B	Frequency	2	4	19	2	0	27
	Percentage	7.4	14.8	70.4	7.4	0.0	100.0
17C	Frequency	4	14	8	1	0	27
	Percentage	14.8	51.9	29.6	3.7	0.0	100.0
17D	Frequency	14	8	3	2	0	27
	Percentage	51.9	29.6	11.1	7.4	0.0	100.0
17E	Frequency	18	4	3	1	1	27
	Percentage	66.7	14.8	11.1	3.7	3.7	100.0

\* Due to rounding, the total percentage may be slightly more or less than 100 percent for a number of situations.

TABLE 43

## Comparison of Means for Financial Decisions

Situation	Response	Number of LKRs' Responses	Mean of Lending Decision	Number of LWP's' Responses	Mean of Investment Decision
1	Independent	21	2.619	15	2.600
	Not independent	34	1.824	14	1.571
2	Independent	53	3.019	24	3.042
	Not independent	1	1.000	3	2.667
3	Independent	27	2.778	11	2.727
	Not independent	28	1.821	16	2.500
4	Independent	33	2.970	18	2.889
	Not independent	22	2.046	9	1.556
5A	Independent	49	3.000	26	3.000
	Not independent	6	2.166	2	3.000
5B	Independent	31	2.871	13	2.923
	Not independent	24	1.833	15	2.267
5C	Independent	15	2.733	5	2.800
	Not independent	40	1.825	23	2.130
6A	Independent	41	3.122	18	3.167
	Not independent	11	1.727	9	1.778
6B	Independent	35	3.057	14	3.214
	Not independent	18	1.833	13	1.769
6C	Independent	23	3.000	7	3.286
	Not independent	30	1.900	20	1.850
6D	Independent	17	3.059	5	3.000
	Not independent	36	1.833	22	1.864
6E	Independent	14	3.149	4	3.250
	Not independent	39	1.769	23	1.783
7	Independent	38	3.474	14	3.429
	Not independent	16	1.875	15	1.867
8	Independent	44	3.068	18	3.333
	Not independent	10	2.300	11	1.818

TABLE 43

(continued)

Situation	Response	Number of LKRs' Responses	Mean of Lending Decision	Number of LWP's' Responses	Mean of Investment Decision
9	Independent	49	3.082	27	3.074
	Not independent	4	2.250	1	2.000
10	Independent	50	3.000	25	3.000
	Not independent	5	2.600	4	2.750
11	Independent	53	3.038	26	3.077
	Not independent	2	2.500	3	2.333
12	Independent	39	2.897	23	3.044
	Not independent	16	2.125	5	2.400
13	Independent	24	3.125	10	3.000
	Not independent	30	1.967	18	2.000
14	Independent	39	3.026	21	3.048
	Not independent	16	2.125	8	2.250
15	Independent	52	2.981	27	3.037
	Not independent	3	2.000	2	2.500
16	Independent	35	3.086	14	3.286
	Not independent	20	2.650	13	2.231
17A	Independent	50	3.020	27	3.074
	Not independent	3	2.667	0	N/A
17B	Independent	46	2.957	22	3.046
	Not independent	8	2.125	5	1.600
17C	Independent	17	2.824	10	2.900
	Not independent	38	1.868	17	1.824
17D	Independent	4	3.250	5	3.000
	Not independent	51	1.490	22	1.455
17E	Independent	4	3.000	4	3.250
	Not independent	51	1.314	23	1.348

TABLE 44

Probabilities of Incorrectly Rejecting Null Hypotheses VIII and IX

Situation	Null Hypothesis VIII		Null Hypothesis IX	
	t-value	probability	t-value	probability
1	3.48	0.001	4.33	0.000
2	5.46	0.000	1.11	0.278
3	5.19	0.000	0.59	0.560
4	6.13	0.000	6.67	0.000
5A	4.72	0.000	0.00	1.000
5B	6.78	0.000	2.37	0.025
5C	4.39	0.000	1.20	0.242
6A	8.19	0.000	6.91	0.000
6B	6.67	0.000	5.27	0.000
6C	4.81	0.000	3.34	0.003
6D	4.59	0.000	1.95	0.062
6E	4.51	0.000	2.30	0.030
7	7.16	0.000	5.27	0.000
8	4.10	0.000	6.03	0.000
9	3.94	0.000	2.74	0.011
10	2.72	0.009	1.11	0.278
11	2.58	0.013	2.48	0.020
12	4.55	0.000	2.33	0.028
13	6.28	0.000	3.46	0.002
14	6.74	0.000	3.43	0.002
15	4.55	0.000	1.63	0.115
16	2.02	0.048	3.77	0.001
17A	1.54	0.131	N/A	*
17B	4.77	0.000	7.16	0.000
17C	6.19	0.000	4.97	0.000
17D	4.89	0.000	4.25	0.000
17E	5.16	0.000	4.14	0.000

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\* All responses were in one category.

TABLE 45  
Mean Responses of Financial Decisions  
by LKRs and LWP's and Significance Levels

Situation	Mean Response LWP's	Mean Response LKRs	t-value	Significance Level
1	2.103	2.123	0.12	0.906
2	3.000	2.982	0.16	0.873
3	2.607	2.291	1.56	0.123
4	2.444	2.600	0.89	0.374
5A	3.000	2.909	0.82	0.416
5B	2.571	2.418	0.86	0.395
5C	2.250	2.073	0.83	0.410
6A	2.704	2.827	0.66	0.508
6B	2.519	2.642	0.57	0.570
6C	2.222	2.377	0.63	0.532
6D	2.074	2.226	0.57	0.569
6E	2.000	2.132	0.47	0.640
7	2.621	3.000	1.55	0.124
8	2.759	2.926	0.95	0.343
9	3.036	3.019	0.16	0.873
10	2.966	2.964	0.02	0.982
11	3.000	3.018	0.20	0.843
12	2.931	2.673	1.75	0.084
13	2.357	2.482	0.61	0.546
14	2.828	2.764	0.45	0.657
15	3.000	2.927	0.72	0.471
16	2.778	2.927	0.77	0.443
17A	3.074	3.000	0.74	0.459
17B	2.778	2.833	0.39	0.694
17C	2.222	2.164	0.35	0.726
17D	1.741	1.618	0.60	0.549
17E	1.630	1.436	0.94	0.352

Lavin, when confronted with similar results, theorized that time horizons of investors and lenders differ. He argued that an investor is usually more interested in the long-run. Since the independence problem tends to disappear in the long run, it would not affect the investment decision.<sup>38</sup> Recall that Situation 17A was the only auditor-client relationship in which LKR's perceptions of auditor's independence did not affect their lending decision. However, since all LWPs believed that this situation would not impair auditors' independence, a t-value for LWPs could not be computed. Thus no comparison between LKRs and LWPs was possible for this case.

To test whether there were any differences of mean responses between LKRs and LWPs, a t-Test was employed. As can be seen from Table 45, in none of the 27 separate auditor-client relationships did the t-Test show a statistically significant difference for an alpha level of  $\leq 0.05$  between the mean responses of the two financial statement user groups.

These results are consistent with those obtained by Lavin who found a statistically significant difference for only one of 12 separate auditor-client relationships investigated. The one relationship which proved significant at an alpha level of 0.02 involved a partner in an accounting firm who was a member of a stock club which owned an immaterial interest in an audit client. This particular relationship was one of two situations from Lavin's survey that were not investigated in this study due to nonapplicability to the German environment.

The following chapter presents a summary of this research. The conclusions and limitations of this study as well as suggestions for future research are discussed.

## CHAPTER FIVE--FOOTNOTES

1. Recall that the 10 auditor-client relationships used to test differences in perceptions between Wirtschaftsprüfer and Certified Public Accountants were taken from Lavin's questionnaire. Lavin conducted his research in 1973. See, Lavin, D., "Financial Statement Users' and Accountants' Perceptions of the Independence of the Auditor in Selected Client-Auditor Relationships" (Unpublished Dissertation, University of Illinois, 1974).
2. Appendices A, B, and C contain copies of the original questionnaires in German that were mailed to the sample subjects. An English version of the questionnaires is also included in the same appendices as a reference for non-German readers.
3. See Appendices A, B, and C for a copy of the original questionnaire and the English translation of the questionnaires.
4. See Frage 6, WPK's "Interpretations", Appendix D. The Wirtschaftsprüferkammer provided this researcher with their interpretations of current regulations and laws as they apply to the auditor-client relationships investigated in this study during a meeting with Mr. Pfefferer of the WPK with this researcher on December 12, 1977. Apparently, the WPK received a number of requests from its members as to the "official" interpretation of the situations investigated, since two of the very late responding WPs included a copy of the WPK's "Interpretations" instead of answering the questionnaire individually. A copy of the WPK's "Interpretations" is included in Appendix D, and is referred to throughout this chapter.
5. Most of the AICPA and SEC rulings, or their positions concerning the auditor-client relationships investigated in this study, can be found in: Accounting Series Release No. 126 (Security and Exchange Commission, 1972); Rule 2-01-Regulation S-X, as cited in Rappaport, L. H., SEC Accounting Practice and Procedure -- Third Edition (New York: The Ronald Press Company, 1972), Chapter 26, p. 18; AICPA, Division of Professional Ethics, Summaries of Ethics Rulings, American Institute of Certified Public Accountants (1970); AICPA, Code of Professional Ethics; Concepts of Professional Ethics - Rules of Conduct - Interpretation of Rules of Conduct - (March 1975 Edition) American Institute of Certified Public Accountants (1975). Only those rulings not found in the above references will be referenced in this chapter.



6. Auditors, auditor, accounting firm, auditing firm, Wirtschaftsprüfungsgesellschaft are all interchangeably used throughout this chapter.
7. In this chapter, frequent reference is made to Lavin's research results, but will not be referenced each time with a footnote. Lavin discussed his research results in Chapter 4 of his dissertation. See Lavin, D., "Financial Statement User's and Accountants' Perceptions of the Independence of the Auditor...", (1974), pp. 102-157.
8. By setting a response in the "Independent" category equal to 1 and a response in the "Not independent" category equal to 0, the mean response is identical to the percentage of those respondents in each of the three experimental groups who responded "Independent".
9. As noted in Chapter Four, an alpha level of 0.05 is considered the cut-off between significant and not significant statistical results for this study. Thus, the various null hypotheses will not be rejected for any computed significance level which is greater than 0.05.
10. See WPK's "Interpretations", Appendix D, Fragen 11 and 12.
11. Ibid.
12. Ibid., Frage 10.
13. Wrabetz mentions some U.S. franchisers operating in Germany, for example, Coca Cola, Hertz and Avis, and also some franchises of German and/or European origin such as: Salamander Schuhshops; Rosenthal, WMF; "Wimpy Bars"; "Wienerwald" - restaurants. See Wrabetz, W., "Das Franchise System--Wesen, Inhalt und Probleme, Betriebswirtschaftliche Forschung und Praxis (Heft 3, 1974), pp. 259-264.
14. Wirtschaftsprüferkammer, Richtlinien für die Berufsausübung der Wirtschaftsprüfer und vereidigten Buchprüfer (December 1 1977), pp. 7-8.
15. See WPK's "Interpretations", Appendix D, Frage 15.
16. Ibid.
17. Ibid., Frage 2.
18. Ibid., Frage 3.
19. Ibid., Frage 5.
20. Wirtschaftsprüferkammer, Richtlinien... (1977), p. 7.

21. See WPK's "Interpretations", Appendix D, Frage 7.
22. Ibid., Frage 8.
23. Ibid., Frage 4.
24. "AICPA Ethics Division Answers Members Queries on the Ethical Code," Journal of Accountancy (July, 1974), p. 62.
25. See WPK's "Interpretations", Appendix D, Frage 13.
26. Ibid., Frage 1.
27. Ibid., Frage 9.
28. See Footnote 26, Chapter Four, concerning the make up of the corporate board of directors of German corporations (Aktiengesellschaften).
29. Wirtschaftsprüferkammer, Richtlinien... (1977), p. 8.
30. See WPK's "Interpretations", Appendix D, Frage 16.
31. Wirtschaftsprüferkammer, Richtlinien... (1977), p. 9.
32. See WPK's "Interpretations", Appendix D, Frage 17.
33. A Prüfungsverband is an organization that only audits cooperatives (Genossenschaften). For more detail, see Institut der Wirtschaftsprüfer, WP-Handbuch 1977 (Düsseldorf: IdW-Verlag, 1977), pp. 266-273.
34. See Wirtschaftsprüferkammer, WP-Verzeichnis 1976/77 (Düsseldorf: IdW-Verlag, 1977).
35. See Appendices A, B, and C for copies of the questionnaires used.
36. See Appendices B and C for copies of the original questionnaires mailed to LKRs and LWP's, respectively.
37. Some of the respondents indicated that the percentage usage of audited financial statements in their work also included those that were prepared by Certified Tax Consultants (Steuerberater).
38. Lavin, D., pp. 150-151.

## CHAPTER SIX

### SUMMARY, CONCLUSIONS, LIMITATIONS, AND SUGGESTIONS FOR FUTURE RESEARCH

The importance of the auditor's independence may only be equaled by the importance of his technical proficiency. In a highly complex and industrialized society such as Germany, the need for accurate financial information is of great importance to the society at large. The auditing profession has been recognized as playing a vital role by lending credibility to audited financial statements and thus helping to ensure a more efficient allocation of economic resources. This credibility has its foundation in the public's belief in the auditor's competence and ability to make objective and unbiased audit decisions. Thus the appearance of the auditor's independence is an all-important prerequisite to performing the audit function within a given economic environment.

This study investigated German auditors' independence for a variety of different auditor-client relationships as perceived by Wirtschaftsprüfer (WPs), and by certain groups of users of audited financial statements. In this chapter the results of this study are summarized and the conclusions reached are presented. In addition, various limitations and suggestions for future related research are discussed.

### Summary

The German accounting profession is discussed in Chapter Two by focusing on the organizational structure of the Wirtschaftsprüfer profession, as well as describing the professional duties and qualifications of WPs and the development and sources of accounting and auditing principles and standards. The German accounting profession is well organized and appears to consist of individual professionals having competency levels at least equivalent to American CPAs based on educational backgrounds, work experience and level of examination requirements.

It was also noted that the German accounting profession in comparison to many Western countries consists of a relatively small number of professionals, approximately 3500. Several reasons were presented to explain how the nation's audit needs could be satisfied with such a small group. These include the rather long work requirement before being allowed to take the WP examination, the existence of related professions performing accounting services other than mandatory audits, and the relatively small number of business entities that must by law be audited by WPs. The relevant laws and regulations covering the conduct of all members of the WP profession were discussed briefly to provide the necessary background for a better understanding of the German accounting environment and the research findings.

A review of the German accounting literature relevant to auditors' independence was presented in Chapter Three. It was noted that the German accounting profession distinguishes between independence in fact and independence in appearance on a basis

similar to that of the U.S. accounting profession. Both components of independence must be satisfied for a WP to be totally independent.

The discussion of the German accounting literature also revealed that several circumstances seem to hinder the WP profession from achieving the goal of being considered truly independent from its audit clients, in the eyes of the public. Like the U.S. profession, German auditors recently have been suffering from a credibility loss, which was partially the result of some well-publicized corporate bankruptcies that seem to suggest questionable ethical conduct and that questionable auditing procedures were used by the auditors involved in these cases. Consequently, the public has questioned the value of the WPs' audit opinion and the WPs' independence status.

The various types of auditor-client relationships that may impair auditors' independence were also discussed as they are presented in the German accounting literature. Several German authors blamed part, if not all, of the independence problem on the lack of an SEC type governmental agency (Aktienamt), on the incompleteness of the Stockcorporation Law of 1965, and/or on the purported inability or unwillingness of the Wirtschaftsprüferkammer (WPK) to provide more specific guidelines to its members. However, attention was called to the fact that parts of the revision of the WPK's Directives issued in December 1977, explicitly prohibit for the first time certain financial interests by a WP in his audit clients. The Directives also specifically note that maintaining client records and auditing them are incompatible functions.

Chapter Three develops more fully the concept of "Total

Independence" which consists of two separate components--independence in fact and independence in appearance. It was reasoned that independence in fact is a concept of individual perception of each auditor and, given certain assumptions of ethical behavior, can be assured by a general rule such as the first sentence of paragraph 43 of the WPs' professional law (WPO) for German auditors, or the first sentence of Rule 101 of the Rules of Conduct for American auditors.

Independence in appearance, however, is a collective perception concept which cannot usually be ensured by a general rule. It is argued that the most efficient way of assuring auditors' independence in appearance is the existence of a set of specific rules which prohibit those auditor-client relationships which may be considered by a legitimate third party to impair auditors' independence.

Extensive specific rules regarding auditor-client relationships that may impair the appearance of auditors' independence do not presently exist in Germany. Even though there are a few rules such as the casuistry of paragraph 164 of the Stockcorporation Law of 1965 and some new rules as proclaimed in the December 1977 revision of the WPK's Directives, the auditor is left with no specific guidance for a vast number of auditor-client relationships.

In Chapter Four, the Research design and methodology were discussed, and the results of the survey were presented and analyzed in Chapter Five. Twenty-seven separate auditor-client relationships were investigated comprising situations in the following categories:

- a) Financial interest (direct and indirect)
- b) Bookkeeping and EDP services
- c) Family relationships
- d) Occupations with conflicting interest
- e) Business and other similar relationships

Each category was discussed briefly with reference to applicable United States (both AICPA and SEC rulings) and German regulations.

Ten of the 27 situations investigated were taken from a similar survey conducted in the United States by Lavin in 1973. This allowed for some comparisons of the perceptions of auditors' independence by WPs and by CPAs.

A total of 380 WPs were randomly selected from all licensed WPs and an additional sample of 40 WPs was randomly selected from those WPs who were affiliated with a "Big Eight" accounting firm.

Bank officers who were identified as users of audited financial statements are directors of investment departments (LWPs) and directors of loan departments (LKR). Non-random samples of LKR and LWP were selected from the larger banking institutions located in the 12 largest German cities. The bank officers were employed in 114 different banks and 44 branches of four of the largest banks in Germany located in these cities. Thus the sample consisted of 158 LKR and 158 LWP.

The response rate of usable responses was: WPs, general sample -- 28.4 percent, additional "Big Eight" sample -- 20 percent; LKR, main office banks -- 44.5 percent, branch banks -- 13.6 percent; LWP, main office banks -- 28.2 percent, branch banks -- 0 percent.

The medium of a mailed questionnaire (in German) was employed to obtain the sample subjects' perceptions concerning auditors' independence in appearance for the 27 auditor-client relationships investigated. The sample subjects were asked to give a dichotomous response -- "Independent"/"Not independent" -- for each of the situations presented.

The financial statement user groups, LKRs and LWPs, were asked in addition to indicate on a five-point scale how each situation presented would affect their financial decision.

The results as analyzed in Chapter Five show that for most situations the three experimental groups arrived at the same consensus response. Consensus was defined as being a statistically significant majority of opinion. Only on three auditor-client relationships did WPs disagree with both user groups, one situation in each of the following categories: financial interest (Situation 6B), occupation with conflicting interest (Situation 13), and business and other similar relationships (Situation 17C). On four auditor-client relationships the two user groups arrived at different majority opinions, which implies that WPs agreed with one user group only. These four situations involved financial interest (Situations 1 and 5B), bookkeeping services (Situation 7), and business and other similar relationships (Situation 16). In three of these four situations the majority of WPs sided with LWPs, namely Situation 1, 5B, and 7, and only agreed with LKRs' majority responses for the remaining one situation.

The comparison with Lavin's research results and those obtained in this study showed that the WPs majority responses



tended to agree with those of CPAs. In only two out of ten situations did WPs' perceptions differ from those of CPAs. These two auditor-client relationships dealt with financial interest (Situation 4) and with a conflicting occupation (Situation 12). In these two situations, WPs considered the auditing firm to be independent whereas a majority of CPAs perceived the auditing firm to be not independent.

Another comparison of WP responses with applicable AICPA and SEC rules revealed that a majority of WPs did not agree with either institutions' rulings on a number of situations. WPs disagreed in 7 out of 11 situations where both the AICPA and the SEC rules are identical. However, for situations where the AICPA and the SEC rules are of divided opinion, WPs tended to agree more often with the AICPA rules than with those of the SEC. WPs agreed with the AICPA on 4 occasions but only for one situation did the WPs majority opinion coincide with SEC rulings.

The hypothesis tests which were used to determine whether the perception of auditors' independence have an effect on the financial decisions of users of financial statements indicated that the lending decisions of LKRs were affected in 26 out of 27 situations. The LWP's investment decisions were affected in 19 out of 27 situations by their perception of auditors' independence. Investment decisions of LWPs were unaffected by their perceptions of auditors' independence for 7 auditor-client relationships, and could not be determined for one situation where all LWPs responding considered the auditors to be independent. Four of these 7 situations dealt with relationships in which auditors had a

financial interest in their audit client, and one situation each dealt with family relationships, business relationships, and financial interests.

LWPs seem to be unaffected in their financial decisions by their perceptions of independence for more situations than LKRs. However, a test of mean responses on the effect of the financial decisions of LKRs and LWPs showed that for none of the situations tested were there statistically significant differences between the mean responses of the two groups at an alpha level of 0.05.

### Conclusions

The interpretations of the results of this study are presented in two parts: (a) those implications which pertain to the German environment only and (b) implications of interest to the U.S. and international environment.

#### Implications Pertaining to the German Environment

It was theorized in this study that the recent controversy in Germany concerning the WPs' independence status may have partially been due to a lack of specific rules concerning auditors' independence in appearance. As was reasoned in Chapter Three, specific rules dealing with auditors' independence in appearance are needed to assure "Total Independence". Without these specific rules each WP or auditing firm (WPG) must guess how a legitimate third party will view the auditors' independence status in a certain situation.

The results of the survey show that for most of the auditor-client relationships investigated, WPs tended to agree with the

two user groups sampled. However, the hypothesis tests of whether there is a consensus within the three experimental groups indicated that for a significant number of situations the null hypothesis of no consensus could not be rejected at an alpha level  $\leq 0.05$ . The WP responses showed no consensus in 9 out of 27 situations. For LWPs, there was no consensus within the group for 11 situations, 9 of which coincide with the same 9 situations where WPs could also not reach a consensus. LKRs were able to arrive at a consensus more often than either WPs or LWPs. They could not reach a consensus in only 7 situations, 5 of which were among those where both WPs and LWPs also could not reach a consensus.

The 9 situations on which WPs were unable to reach a consensus consisted of 5 auditor-client relationships involving financial interest, one situation each involving bookkeeping services, legal counseling, Supervisory Board membership and audit client fees representing 25 percent of the total of a WPG's revenue. It may be of interest to note that currently none of these 9 situations are specifically disallowed.

The Wirtschaftsprüferkammer in its interpretations of current laws and regulations pertaining to auditors' independence as they apply to the auditor-client relationships investigated in this study considered the auditors to be independent in 7 out of those 9 situations, not independent in one situation, and for one situation the WPK concluded that the situation must be judged in light of all factors and separately in each individual case.

This survey also revealed significant differences of perceptions between WPs and the WPK. On five situations where a

consensus was reached by WPs, the WPK reached the opposite judgment. Of these five situations, three auditor-client relationships involved financial interest (Situations 5A, 6C, and 6D), and two situations dealt with bookkeeping and EDP services (Situations 8 and 9). For two of those five situations, namely Situation 6C and 6D, the WPK considered the auditors to be independent whereas the consensus of WPs considered them not to be independent. For the remaining three situations the consensus response from WPs considered the auditors to be independent whereas the WPK considered the auditors to lack independence in appearance.

The fact alone that WPs were unable to reach a consensus on 9 out of 27 auditor-client relationships investigated as well as the disagreement of WP consensus responses with the interpretations by their professional organization (WPK) on an additional 5 situations seems to suggest that more specific guidelines are needed to better ensure the independence in appearance of German auditors. Guidelines appear also to be needed for those situations where no consensus was reached within any of the three experimental groups and for auditor-client relationships where WPs disagreed with one or both of the user groups. As one example, the area of legal counseling of audit clients by WPs also qualified to practice law seems to be in need of specific rules since no consensus was reached within each of the three experimental groups for this auditor-client relationship (Situation 13).

## Implications Pertaining to the U.S. and International Environment

The existence and growth of multinational corporations frequently causes auditors of the parent corporation to rely on the audit work performed by foreign auditors. Since German auditors of U.S. subsidiaries essentially must comply with relevant U.S. auditing standards, including the requirement of independence, the findings from this study allow certain interpretations and conclusions.

The comparison of WP responses to the official rulings by the AICPA and the SEC shows that for a significant number of situations WPs took a different (usually less stringent) view than did either the AICPA or the SEC. In situations where the AICPA and the SEC were of divided opinion, WPs generally sided with the position taken by the AICPA, the less stringent position.

The perceptions of WPs cannot necessarily be considered the individual WP's interpretation of current German Laws and regulations. However, for those situations not covered by specific rules these perceptions may indeed indicate the action a WP may take when confronted with actual situations similar to the ones presented in this survey.

Thus U.S. investors planning to invest in German securities should be aware that the financial statements of German corporations (many are translated into English) may be audited by a German accounting firm that is not considered to be independent by U.S. regulations. This study presented evidence that perceptions of auditors independence by financial statement users may have an effect on their financial decisions. Consequently,

disclosure of the independence status in the financial statements used by U.S. investors in making investment decisions would provide significant information. However, at this time there seems to be no vehicle by which this could be accomplished, since the SEC does not have the power to require such disclosure by foreign corporations in their English language financial statements.<sup>1</sup>

This study is of interest to U.S. auditors of multinational corporations since the results seem to indicate that there may be a greater likelihood of German auditors violating U.S. independence rules if the German auditors disagree with those rules. Naturally, it can be argued that U.S. auditors of U.S. multinationals instruct their foreign auditors to comply with U.S. auditing and accounting rules and probably also indicate to them what they are. Moreover, it may be true that most of the audits of U.S. multinationals are performed by the "Big Eight" accounting firms which do have offices in most Western countries and thus it is likely that the foreign subsidiaries are audited by the "Big Eight" accounting firm's own foreign offices. However, it should be noted that these "Big Eight" offices in foreign countries are largely, if not exclusively, staffed by nationals. In some cases, a German auditing firm is affiliated with a "Big Eight" firm and thus WPs belonging to that German auditing firm may belong at the same time to the "Big Eight" auditing firm. The perception of independence of these WPs may not differ significantly from those WPs not involved with audits of U.S. subsidiaries as some evidence presented in this study suggest.<sup>2</sup> Thus, instructing foreign auditors about the specific U.S. independence rules is of vital

importance.

From an international point of view it seems advisable to develop common rules for all countries. In light of the recent trend in the financial investment field to extend diversification of stock portfolios to include stocks of foreign corporations to lower the overall risk,<sup>3</sup> uniform international auditing standards would provide for better financial information to the international investor. The International Accounting Standard's Committee (IASC) is working toward this goal. However, since auditing needs and the auditing professions have developed somewhat independently within most countries and thus differ, it appears that international uniformity in the accounting profession will be a slow and strenuous process unless international standards are brought down to the lowest common denominator. The recent criticism of the accounting profession in Germany as well as in the United States would suggest that lowering auditing standards on an international level would be counterproductive.

#### Limitations

The conclusions of this study are limited to some extent due to a number of constraints concerning the research methodology and design. Several limitations are inherent in the use of a mail survey.

There is always a possibility that sample subjects misunderstand the purpose of the research or misunderstand the questions asked. However, detailed instructions were sent to each subject and the questions were kept at an easily understandable level

which suggest that this confounding variable may not have significantly altered the results.

The conclusions concerning the comparison with Lavin's findings and the comparison of WP responses to applicable U.S. rules are limited to the extent that the German translation conveys the true spirit of the word. Since the translation process was carefully reviewed by a number of people competent in both languages and in accounting matters, it appears that distortions concerning the translation may have been rather small. However, it should be noted that Lavin conducted his study in 1973. Any conclusions derived from a comparison of WPs' perceptions and CPAs' perceptions of auditors' independence are limited since CPAs' perceptions may have changed over the last four years.

Due to the sizable percentage of nonrespondents, the results of this survey can only be generalized to the WP profession at large if it is assumed that nonrespondents do not significantly differ from those who responded. Strictly speaking, the results obtained from WP respondents cannot be generalized to the profession at large. However, a test performed to detect a possible nonresponse bias seems to indicate a lack of a material nonresponse bias.

LKRs and LWPs were selected on a non-random basis. This precludes generalization of the results to a larger population. Logical but not statistical inferences, however, can still be drawn.

This research was also limited by the selection of a limited number of auditor-client relationships, the type of financial statement users chosen, and the dichotomous type of response



employed for the independence decision. Thus it should be noted that the conclusions reached apply only to those specific situations selected. Although LKRs and LWPs represent two important user groups of audited financial statements, their responses cannot be considered representative of all financial statement users.

The sample subjects were only given the choice of a dichotomous response for the independence decisions to conform with German and U.S. rules on auditors' independence. However, it is possible that some respondents consider the independence question not to be a black and white situation even though they were forced to make such a choice.

The above limitations should be kept in mind; however, they do not significantly diminish the importance of the findings of this study.

#### Suggestions for Future Research

Some of the limitations mentioned could be overcome in future research efforts. The range of auditor-client relationships could be expanded to include the various types of management advisory services (MAS) currently provided by German and U.S. auditors to their audit clients.

There is little doubt that certain types of MAS may impair the auditors' appearance of independence. A recent study by Richter revealed that a sizable portion of WPs and business journalists sampled perceived providing MAS to audit clients as incompatible with the audit function.<sup>4</sup>

Similar criticism of these activities has been raised in

the United States.<sup>5</sup> However, it appears that certain MAS activities may affect the auditors' independence status negatively whereas other MAS activities may not affect them. An outright abolishment of these services, which has been suggested by some authors may not be warranted, nor necessary.<sup>6</sup> Research needs to be done in this area to establish which MAS activities would impair Wirtschaftsprüfer's independence and consequently should be prohibited.

Another way to overcome some of the limitations of this study would be to include different user groups of audited financial statements. Even though LKRs and LWPs appear to be important user groups, perhaps an extension of this study which includes a random sample of members of the two German corporate boards, stockholders, financial analysts employed by German insurance companies, and the user group sampled by Richter, business journalists, would provide additional evidence as to the financial statement users' perceptions of auditors' independence. There is no empirical evidence that indicates the extent to which LKRs and LWPs can be considered an adequate surrogate of all users of audited financial statements.

A third way to extend this research is to expand the survey to include auditors and financial statement user groups in other Common Market countries. The Union Européenne des Experts Comptables Economiques et Financiers recently issued a statement on auditors' independence which notes the potential of auditors' independence impairment in certain types of situations most of which are included in this survey. Such an extension of this research would help to provide empirical evidence in the formulation of more specific

rules of conduct concerning auditors' independence in appearance. Such specific rules are a prerequisite to solving the auditors' independence problem.

## CHAPTER SIX--FOOTNOTES

1. Unless, of course, the German corporations register with the SEC if they plan to offer securities in the United States. See Rappaport, L. H., SEC Accounting Practice and Procedure - Third Edition (New York: The Ronald Press Company, 1972), Chapter 31.
2. To test for significant differences of perceptions concerning auditors' independence between WPs belonging to "Big Eight" accounting firms and WPs who do not belong to "Big Eight" accounting firms, the Chi Square Test was applied. However, the test results did not indicate any significant differences between the two groups.
3. See, "Has Morgan Started Something?" Forbes (April 3, 1978), pp. 114-116.
4. See Richter, M., "Die Unabhängigkeit des Wirtschaftsprüfers," Universität des Saarlandes (July, 1976).
5. See, The Commission of Auditors' Responsibilities: Report, Conclusions, and Recommendations, M. F. Cohen, Chairman (New York, 1978), pp. 94-104.
6. As Biener points out, efforts of the Common Market Commission to prohibit management consulting (Beratung) were thwarted in the beginning stages due to opposition of the accounting profession and industry. One argument was economic, noting that there is not enough audit work to keep the WP profession busy. However, Biener comments that with the proposed requirements of mandatory audits of limited liability companies (GmbHs), a possible 50,000 GmbHs may have to be audited which should provide sufficient audit work for WPs to lessen their management consulting activity. See Busse von Colbe, W., and Lutter, M. (eds), Wirtschaftsprüfung Heute: Entwicklung oder Reform? Ein Bochumer Symposium (Wiesbaden: Verlag Dr. Th. Gabler, 1977), pp. 127-128.

## APPENDICES

## APPENDIX A

COVER LETTER, FOLLOW-UP LETTER  
AND QUESTIONNAIRE MAILED  
TO WIRTSCHAFTSPRÜFER

## MICHIGAN STATE UNIVERSITY

GRADUATE SCHOOL OF BUSINESS ADMINISTRATION  
DEPARTMENT OF ACCOUNTING & FINANCIAL ADMINISTRATION

EAST LANSING · MICHIGAN · 48824  
November 25, 1977

Sehr geehrter Herr Wirtschaftsprüfer!

Die unabhängige und objektive Ausübung des Wirtschaftsprüferberufes ist von grosser Bedeutung für die Funktion der deutschen und internationalen Wirtschaftsgemeinschaft im allgemeinen und für den Berufsstand des Wirtschaftsprüfers im besonderen.

Die UEC-Kommission für Berufsgrundsätze veröffentlichte kürzlich den Entwurf einer Empfehlung (Nr. 10), die sich unter anderem mit einigen Situationen befasst, wo die Unabhängigkeit und Unbefangenheit der Wirtschaftsprüfer/-gesellschaft in Frage gestellt werden könnte.

Mr. Hans Jay Dykxhoorn, Certified Public Accountant and zur Zeit Doktorand an der Graduate School of Business at Michigan State University, führt im Rahmen seiner Doktorarbeit eine Studie aus, die sich mit der Unabhängigkeit und Unbefangenheit der Wirtschaftsprüfer befasst. Mr. Dykxhoorn hofft, dass seine empirische Resultate zu einem besseren Verständnis des Begriffes der Unabhängigkeit auf dem Gebiet der Wirtschaftsprüfung in Theorie und Praxis führen werden.

Der beigelegte, anonyme Fragebogen wurde in der Absicht aufgesetzt, die Ansichten von Wirtschaftsprüfern hinsichtlich des Unabhängigkeitsproblems zu ermitteln.

Ich darf Ihnen versichern, dass alle Daten und Angaben streng vertraulich behandelt werden und die Resultate nur in Tabellenform erscheinen werden. Bitte benutzen Sie den beigelegten, adressierten und frankierten Briefumschlag für die Rücksendung des ausgefüllten Fragebogens. Die Nummer auf der Rückseite dieses Briefumschlages dient der Eingangskontrolle. Falls Sie an der Zusendung des Ergebnisses dieses Forschungsvorhabens interessiert sind, bitten wir Sie um Angabe Ihrer Adresse.

Wir hoffen, dass Sie ungefähr 15-20 Min. zur Verfügung haben, da wir Ihrer Mitarbeit an dieser Studie erhebliche Bedeutung beimessen und Ihre Angaben mit grossem Interesse entgegennehmen.

Mr. Dykxhoorn hofft, während seines kurzfristigen Aufenthalts in Deutschland (vom 25. November bis 31. Dezember) die Rücksendungen der Fragebögen an die angegebene Adresse zu verfolgen. Ich bitte Sie deshalb, den angegebenen Zeitraum zu berücksichtigen.

Mit freundlichen Grüssen

Anlage

*Harold Sollenberger*  
Dr. Harold M. Sollenberger, C.P.A.  
Professor and Chairman,  
Department of Accounting and  
Financial Administration

## MICHIGAN STATE UNIVERSITY

GRADUATE SCHOOL OF BUSINESS ADMINISTRATION  
DEPARTMENT OF ACCOUNTING & FINANCIAL ADMINISTRATION

EAST LANSING • MICHIGAN • 48824

12. Dezember 1977  
mein Schreibem vom  
25. November 1977

Sehr geehrter Herr Wirtschaftsprüfer,

ich erlaube mir, Ihnen vor zwei Wochen im Rahmen einer Doktorarbeit, die die Beziehung zwischen Wirtschaftsprüfer und Klientel zum Thema hat, einen Fragebogen mit der Bitte um Rücksendung zuzusenden.

Leider konnte Ihr Beitrag bis heute noch nicht zu den bereits eingetroffenen und ausgefüllten Fragebögen gezählt werden. Ihre Mitarbeit an diesem Forschungsprojekt ist von großer Wichtigkeit, da die Qualität des Ergebnisses ohne Ihren Beitrag im Wert erheblich gemindert sein würde.

Ich nehme an, daß der Fragebogen nicht in Ihre Hände gelangt ist. Aus diesem Grunde übersende ich Ihnen in der Anlage noch einmal ein Exemplar dieses Fragebogens mit der freundlichen Bitte, diesen beantwortet zurückzusenden. Ein adressierter Briefumschlag ist beigelegt.

Schon heute möchte ich Ihnen für Ihre wertvolle Mitarbeit herzlich danken.

Mit freundlichen Grüßen



Hans Jay Dykxhoorn, C.P.A.  
Michigan State University  
z.Zt. Körner Straße 10  
4250 Bottrop  
Deutschland

Anlage





Doctoral Dissertation Research  
Michigan State University  
Return Questionnaire to:  
c/o Hans Jay Dykxhoorn, C.P.A.  
z.Z. Koernerstrasse 10  
4250 Bottrop  
West Germany

### Eine Studie der Wirtschaftsprüfer/-gesellschaft-Klientel

#### Beziehungen

Jede der folgenden Situationen beschreibt ein bestimmtes Verhältnis zwischen einer Wirtschaftsprüfungsgesellschaft und einem ihrer Jahresabschlussklienten. Bitte überprüfen Sie jede einzelne Situation, um zu entscheiden, ob Sie glauben, dass eine Wirtschaftsprüfungsgesellschaft in jedem Fall unabhängig und unbefangen oder nicht unabhängig und nicht unbefangen ist, besonders im Hinblick auf die Jahresabschlussprüfung.

Bitte beachten Sie, dass die Unabhängigkeit und Unbefangenheit eines Wirtschaftsprüfers sich nicht nur auf die Fähigkeit bezieht, objektive und unvoreingenommene Entscheidungen in Verbindung mit der Abschlussprüfung zu treffen, sondern auch darauf, wie es die Wirtschaftsprüferkammer in ihren Richtlinien vorschreibt, das kein sachlich vernünftiger Grund besteht, aus dem die Besorgnis der Befangenheit abgeleitet werden kann.

Bitte stellen Sie sich vor, dass in jeder der folgenden Situationen die genannte Wirtschaftsprüfungsgesellschaft der Wirtschaftsprüfungsfirma gleicht, mit der Sie im Augenblick zusammenarbeiten (entweder als Angestellter oder Gesellschafter) und dass der erwähnte Klient einer Ihrer Klientenfirmen von mittlerer Grösse gleicht. Bitte beurteilen Sie jede der folgenden Situationen, welche auf den nächsten drei Seiten dieses Fragebogens beschrieben sind, für sich getrennt.

Sample: German Certified Public Accountants - (Wirtschaftsprüfer)

		Unabhängigkeitsentscheidung (Bitte kreisen Sie eine Nummer ein für Ihre Beurteilung der Situation)	
		<u>Unabhängig</u> und <u>unbefangen</u>	<u>Nicht unabhängig</u> und nicht <u>unbefangen</u>
A.			
1.	Das Büro einer Wirtschaftsprüfungsgesellschaft befand sich in einem Gebäude, das einer Klientenfirma gehörte. Die Wirtschaftsprüfungsgesellschaft verfügte über ungefähr 25 Prozent des vorhandenen Büroraumes im Gebäude und der Klient benutzte den restlichen Büroraum.....	1	2
2.	Eine Wirtschaftsprüfungsgesellschaft führte für einen Klienten nicht nur die Prüfung des Jahresabschlusses durch, sondern übte auch weitere Dienstleistungen aus, einschliesslich allgemeiner Führung der Journale und Hauptbücher, Abschlussbuchungen und Anfertigung der Jahresbilanz.....	1	2
3.	Zwecks Handhabung vertraulicher Informationen beauftragte eine Klientenfirma eine Wirtschaftsprüfungsgesellschaft nicht nur für die Jahresabschlussprüfung, sondern auch für die folgenden Dienste: (a) monatliche Gehaltsbuchführung der geschäftsführenden Angestellten (b) Führung bestimmter Konten in einem privaten Buchführungsjournal.....	1	2
4.	Ein Angestellter in einer Wirtschaftsprüfungsgesellschaft mit fünf Jahren Prüfungserfahrung verwaltete persönlich ein Gebäude, das einem ihrer Jahresabschlussprüfungsklienten gehörte.....	1	2
5.	Die Angestellten eines Klienten fertigten von verschiedenen Journalen (Büchern) Computerlochstreifen an, welche mit einem Optical Scanner gelesen werden konnten, und schickten diese Lochstreifen zum Büro ihrer Abschlussprüfer. Die Wirtschaftsprüfungsgesellschaft sandte die Lochstreifen in unveränderter Form weiter zu einem Computer Service. Die Wirtschaftsprüfungsgesellschaft erhielt die gedruckten Ergebnisse des Jahresabschlusses und Auszüge der Hauptbücher von dem Computer Service zurück und schickte sie zu ihrem Klienten. Die Wirtschaftsprüfungsgesellschaft verrichtete diese Arbeit zusätzlich zu der Jahresabschlussprüfung.....	1	2
6.	Gemäss eines Umschuldungsplanes wurden die Schulden der Klientenfirma durch Schuldscheine unterlegt, die nach fünf Jahren fällig werden sollten. Die Wirtschaftsprüfungsgesellschaft erhielt ebenfalls Schuldscheine für ihre Jahresabschlussprüfungsarbeiten.....	1	2

	<u>Unabhängig und unbefangen</u>	<u>Nicht unabhängig und nicht unbefangen</u>
7. A war der Controller der Firma Z. Er war ein Firmenangestellter und nicht von Aktionären der Firma zu seinem Posten gewählt. A's Bruder, B, war ein Wirtschaftsprüfer der Jahresabschlussprüfungsgesellschaft der Firma Z, aber B persönlich war in keiner Weise mit der Jahresabschlussprüfung der Firma Z verbunden.....	1	2
8. Ein Wirtschaftsprüfer einer Wirtschaftsprüfungsgesellschaft hatte einen Schwager in leitender Position in der Verkaufsabteilung einer neuen Klientenfirma. Der Schwager war nicht an finanziellen Entscheidungen seiner Firma beteiligt. Der Wirtschaftsprüfer selbst hatte persönlich nichts mit der Jahresabschlussprüfung zu tun.....	1	2
9. Eine Wirtschaftsprüfungsgesellschaft vermietete "block time" ihres Computers an einen Klienten, als der Computer des Klienten überfordert war. Die Wirtschaftsprüfungsgesellschaft war zugleich die Abschlussprüfungsfirma des Klienten.....	1	2
10. Der Klient einer Wirtschaftsprüfungsgesellschaft verkaufte Konzessionen (franchises). Zwei Wirtschaftsprüfer der Wirtschaftsprüfungsgesellschaft legten ungefähr fünf Prozent ihres Vermögens an fünfzig Prozent der Aktien der Firma K an. Die Firma K hatte eine Konzession von dem Klienten erworben. Mit Ausnahme der Auszahlung eines bestimmten Prozentsatzes vom Umsatz an den Klienten arbeitete die Firma K selbstständig und unabhängig.....	1	2
11. Ein Wirtschaftsprüfer einer Wirtschaftsprüfungsgesellschaft besass ein Prozent der Aktien der Firma B, deren Tochtergesellschaft A ein künftiger Klient der Wirtschaftsprüfungsgesellschaft werden soll. Der Wirtschaftsprüfer, dem diese Aktien gehörten, ist in keiner Weise an den Abschlussprüfungsarbeiten beteiligt.....	1	2
12. Ein Wirtschaftsprüfer einer Wirtschaftsprüfungsgesellschaft besass ein Prozent der Aktien der Firma B, deren Tochtergesellschaft A ein künftiger Klient der Wirtschaftsprüfungsgesellschaft werden soll. Der Wirtschaftsprüfer, dem diese Aktien gehörten, wird als der Prüfungsleiter der Abschlussprüfung der Tochtergesellschaft A fungieren.....	1	2
13. Ein Wirtschaftsprüfer einer Wirtschaftsprüfungsgesellschaft war ebenfalls als Rechtsanwalt für einen Klienten tätig, genauer gesagt, er vertrat den Klienten in allen Rechtsangelegenheiten. Für diesen Dienst erhielt er Gebühren von dem Klienten. Ebenfalls erhielt er von der Wirtschaftsprüfungsgesellschaft Gebühren für die Jahresabschlussprüfung, da die Wirtschaftsprüfungsgesellschaft der Abschlussprüfer der Klientenfirma war.....	1	2

	Unabhängig und unbefangen	Nicht unabhängig und nicht unbefangen
14. Ein Wirtschaftsprüfer einer Wirtschaftsprüfungsgesellschaft besass Aktien einer künftigen Klientenfirma. Seine Wirtschaftsprüfungsgesellschaft soll die Jahresabschlussprüfung durchführen. Bitte beurteilen Sie die folgenden Situationen <u>für sich getrennt</u> .		
<u>Situation A.</u> Der Wirtschaftsprüfer besass nur sehr wenige Aktien der Klientenfirma (weniger als ein Prozent seines Vermögens).....	1	2
<u>Situation B.</u> Der Wirtschaftsprüfer besass drei Prozent der Aktien der Klientenfirma (ungefähr zehn Prozent seines Vermögens).....	1	2
<u>Situation C.</u> Der Wirtschaftsprüfer besass zehn Prozent der Aktien der Klientenfirma (ungefähr zehn Prozent seines Vermögens).....	1	2
15. Eine Bank erwarb einen bedeutenden Teil der Aktien der Firma S, genügend um einen erheblichen Einfluss auf die Geschäftsführung auszuüben. Die Bank besass ausserdem Aktien einer Wirtschaftsprüfungsgesellschaft, welche damit beauftragt war, die Jahresabschlussprüfung der Firma S durchzuführen. Bitte beurteilen Sie die folgenden Situationen <u>für sich getrennt</u> .		
<u>Situation A.</u> Die Bank besass ungefähr 10 Prozent der Aktien der Wirtschaftsprüfungsgesellschaft.....	1	2
<u>Situation B.</u> Die Bank besass zwischen 11 und 24 Prozent der Aktien der Wirtschaftsprüfungsgesellschaft.....	1	2
<u>Situation C.</u> Die Bank besass zwischen 25 und 49 Prozent der Aktien der Wirtschaftsprüfungsgesellschaft.....	1	2
<u>Situation D.</u> Die Bank besass genau 50 Prozent der Aktien der Wirtschaftsprüfungsgesellschaft.....	1	2
<u>Situation E.</u> Die Bank besass mehr als 50 Prozent der Aktien der Wirtschaftsprüfungsgesellschaft.....	1	2
16. Ein Wirtschaftsprüfer einer Wirtschaftsprüfungsgesellschaft war ein Mitglied des Aufsichtsrats der Firma L. Die Firma L war eine der grössten Lieferanten der Firma M. Die Wirtschaftsprüfungsgesellschaft war beauftragt, die Jahresabschlussprüfung der Firma M durchzuführen. ....	1	2
17. Ein gewisser Teil der Einnahmen einer Wirtschaftsprüfungsgesellschaft bestand aus Abschlussprüfungsgebühren einer einzelnen Klientenfirma. Bitte beurteilen Sie die folgenden Situationen <u>für sich getrennt</u> . Die Gebühren von der einzelnen Klientenfirma betrugen von den Gesamteinnahmen den folgenden Prozentsatz:		
<u>Situation A:</u> ungefähr 5 Prozent der Gesamteinnahmen.....	1	2
<u>Situation B:</u> ungefähr 10 Prozent der Gesamteinnahmen.....	1	2
<u>Situation C:</u> ungefähr 25 Prozent der Gesamteinnahmen.....	1	2
<u>Situation D:</u> ungefähr 50 Prozent der Gesamteinnahmen.....	1	2
<u>Situation E:</u> ungefähr 75 Prozent der Gesamteinnahmen.....	1	2

## B.

1. Führt Ihre Wirtschaftsprüfungsgesellschaft auch Jahresabschlussprüfungen von amerikanischen (U.S.) Tochtergesellschaften durch? Ja    Nein
  
2. Wie viele Jahre Prüfungserfahrung haben Sie? \_\_\_\_\_ Jahre  
(Bitte runden Sie ab)
  
3. Wo liegt das Schwergewicht Ihrer beruflichen Tätigkeit und Erfahrung? (Bitte Kreisen Sie eine Nummer oder mehr als eine Nummer ein, falls zutreffend)

Abschlussprüfungsarbeiten..... 1

Steuerberatung..... 2

Management Consulting..... 3

Sonstiges (Bitte erläutern Sie) \_\_\_\_\_ 4

Raum für zusätzliche Bemerkungen \_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

Falls Sie an der Zusendung des Ergebnisses dieses Forschungsvorhabens interessiert sind, bitte ich Sie um Angabe Ihrer Adresse.

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

Ich danke Ihnen für Ihre Mühe und Bereitschaft mich bei diesem Forschungsprojekt zu unterstützen.

\_\_\_\_\_  
Hans Jay Dykxhoorn, C.P.A.

English TranslationA STUDY OF AUDITOR-CLIENT RELATIONSHIPS

Each of the following situations involves a different relationship between an accounting firm and its client. Please evaluate each situation to determine whether you think an accounting firm would be considered independent (unbiased) or not independent (biased) with respect to a year-end audit of the client involved.

Please note that the independence of a Wirtschaftsprüfer not only deals with his ability to make objective and unbiased audit decisions but also, as the Wirtschaftsprüferkammer in its Directives mandates, that there are no circumstances that may suggest that the auditor's appearance of independence may be impaired.

Assume that the accounting firm in each of the following situations is similar to the firm with which you are now affiliated. Also, assume that the client is similar to one of your medium-size clients. Please evaluate each of the following situations described in this questionnaire separately.

Sample: German Certified Public Accountants (Wirtschaftsprüfer)

		Independence Decision (Please circle one number)	
		Independent (not biased)	Not independent (biased)
A.			
1.	An accounting firm had its office in a building which was owned by a client. The accounting firm occupied approximately 25 percent of the available office space in the building, and the client occupied the remainder.....	1	2
2.	In addition to the audit, an accounting firm provided services for the client which included maintaining the journals and ledgers, making adjusting entries and preparing financial statements.....	1	2
3.	In order to keep certain information confidential, the client had the accounting firm perform the following services in addition to the audit: (a) prepare the executive payroll (b) maintain selected general ledger accounts in a private ledger.....	1	2
4.	A partner in an accounting firm managed a building owned by an audit client.....	1	2
5.	From the books of original entry, client personnel prepared printed tapes that could be read on an optical scanner and sent the tapes to the accountant's office. The accountants forwarded the tapes to a service bureau. The accountants received the print-outs of the financial statements and general ledgers and sent them to the client. The accountants did not edit the input data prior to transmission to the service bureau. The accountants provided this service in addition to the audit.....	1	2
6.	Pursuant to a plan of recapitalization, the existing debt of the company was exchanged for five-year promissory notes. The accounting firm received the same kind of promissory notes in payment of its audit fee.....	1	2

Independence Decision (Please circle one number)		
	Independent (not biased)	Not independent (biased)
7. A was the controller of Company Z. He was not an elected officer nor did he have any stock holdings in Company Z. A's brother, B, was a partner in the public accounting firm that audits Company Z's books. However, B was not the partner in charge of the audit.....	1	2
8. A partner in a public accounting firm had a brother-in-law who was sales vice president for a recently acquired client. The brother-in-law was not directly involved in the financial affairs of the company and the partner was not connected with the audit in any way.....	1	2
9. An accounting firm rented block time on its computer to a client when the client's computer became overburdened.....	1	2
10. A client of an accounting firm was engaged in the business of selling franchises. Two partners of this accounting firm invested approximately five percent of their personal fortunes to buy one half of the stock of a corporation which held a franchise granted by this client. Except for the payment of a percentage of sales to the franchisor client, the franchise operated independently.....	1	2
11. A partner in an accounting firm whose proposed client A was a wholly owned subsidiary of corporation B, owned one percent of the stock of corporation B. The partner who owns these stocks would not in any way be involved with the year-end audit.....	1	2
12. A partner in an accounting firm whose proposed client A was a wholly owned subsidiary of corporation B, owned one percent of the stock of corporation B. The partner who owns these stocks would be in charge of the year-end audit.....	1	2
13. A partner in an accounting firm (qualified as a lawyer) also acted as general counsel for an audit client. He received fees for such legal services and, through the accounting partnership, for accounting services rendered concurrently.....	1	2



**Independence Decision**  
**(Please circle one number)**

**Independent (not biased)**      **Not independent (biased)**

- |     |   |   |   |
|-----|---|---|---|
| 14. | A partner in an accounting firm owned stocks of a proposed client for which he was engaged to do the year-end audit. Consider each of the following situations separately.  |   |   |
|     | <u>Situation A.</u> The partner owned a very small number of shares of the client amounting to less than one percent of his net worth.....  | 1 | 2 |
|     | <u>Situation B.</u> The partner owned 3 percent of the client's stock amounting to 10 percent of his net worth.....   | 1 | 2 |
|     | <u>Situation C.</u> The partner owned 10 percent of the client's stock amounting to 10 percent of his net worth.....  | 1 | 2 |
| 15. | A bank acquired a large number of shares of company S, large enough to enable the bank to significantly influence the management of company S. In addition, the same bank also owned shares of the auditing firm that was engaged to perform the year-end audit of company S. Consider each of the following situations separately. |   |   |
|     | <u>Situation A.</u> The bank owned approximately 10 percent of the outstanding stock of the auditing firm.....  | 1 | 2 |
|     | <u>Situation B.</u> The bank owned between 11 and 24 percent of the outstanding stock of the auditing firm.....   | 1 | 2 |
|     | <u>Situation C.</u> The bank owned between 25 and 49 percent of the outstanding stock of the auditing firm.....   | 1 | 2 |
|     | <u>Situation D.</u> The bank owned exactly 50 percent of the outstanding stock of the auditing firm.....  | 1 | 2 |
|     | <u>Situation E.</u> The bank owned more than 50 percent of the outstanding stock of the auditing firm.....  | 1 | 2 |
| 16. | A partner of an accounting firm was also a member of the Supervisory Board of Corporation L. Corporation L was one of the largest suppliers of Corporation M. The accounting firm was engaged to perform the year-end audit of Corporation M.....   | 1 | 2 |
| 17. | A certain portion of an accounting firm's revenue consisted of audit fees from one particular client. Consider each of the following situations separately. The fees from this particular client represented approximately:   |   |   |
|     | <u>Situation A:</u> 5 percent of total revenue.....   | 1 | 2 |
|     | <u>Situation B:</u> 10 percent of total revenue.....  | 1 | 2 |
|     | <u>Situation C:</u> 25 percent of total revenue.....  | 1 | 2 |
|     | <u>Situation D:</u> 50 percent of total revenue.....  | 1 | 2 |
|     | <u>Situation E:</u> 75 percent of total revenue.....  | 1 | 2 |

B.

1. Does your accounting firm perform annual audits of U.S. subsidiary companies? Yes No
2. To the nearest year, how many years of experience do you have in the auditing profession? \_\_\_\_\_ years
3. What is your personal area of professional emphasis?  
(You may circle more than one number if appropriate)
- Auditing..... 1
- Tax..... 2
- Management Consulting..... 3
- Other (Please specify) \_\_\_\_\_ 4

Use this space for additional comments \_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

If you would like to receive a summary of the research results, give your address below.

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

Thank you very much for your cooperation.

\_\_\_\_\_  
Hans Jay Dykxhoorn, C.P.A.

APPENDIX B

COVER LETTER, FOLLOW-UP LETTER  
AND QUESTIONNAIRE MAILED  
TO LEITER DER KREDITABTEILUNG

## MICHIGAN STATE UNIVERSITY

GRADUATE SCHOOL OF BUSINESS ADMINISTRATION  
DEPARTMENT OF ACCOUNTING & FINANCIAL ADMINISTRATION

EAST LANSING • MICHIGAN • 48824  
November 25, 1977

Sehr geehrter Herr Leiter der Kreditabteilung!

Die unabhängige und objektive Ausübung des Wirtschaftsprüferberufes ist von grosser Bedeutung für die Funktion der deutschen und internationalen Wirtschaftsgemeinschaft.

Mr. Hans Jay Dykxhoorn, Certified Public Accountant and zur Zeit Doktorand an der Graduate School of Business at Michigan State University, führt im Rahmen seiner Doktorarbeit eine Studie aus, die sich mit der Unabhängigkeit und Unbefangenheit der Wirtschaftsprüfer befasst. Mr. Dykxhoorn hofft, dass seine empirische Resultate zu einem besseren Verständnis des Begriffes der Unabhängigkeit auf dem Gebiet der Wirtschaftsprüfung in Theorie und Praxis führen werden.

Der beigegefügte, anonyme Fragebogen wurde in der Absicht aufgesetzt, nicht nur die Meinungen von Wirtschaftsprüfern, sondern auch die Ansichten von beteiligten Dritten, die mit der Handhabung von Jahresabschlüssen vertraut sind, zu ermitteln.

Ich darf Ihnen versichern, dass alle Daten und Angaben streng vertraulich behandelt werden und die Resultate nur in Tabellenform erscheinen werden. Bitte benutzen Sie den beigegefügten, adressierten und frankierten Briefumschlag für die Rücksendung des ausgefüllten Fragebogens. Die Nummer auf der Rückseite dieses Briefumschlages dient der Eingangskontrolle. Falls Sie an der Zusendung des Ergebnisses dieses Forschungsvorhabens interessiert sind, bitten wir Sie um Angabe Ihrer Adresse.

Wir hoffen, das Sie ungefähr 15-20 Min. zur Verfügung haben, da wir Ihrer Mitarbeit an dieser Studie erhebliche Bedeutung beimessen und Ihre Angaben mit grossem Interesse entgegensehen.

Mr. Dykxhoorn hofft, während seines kurzfristigen Aufenthalts in Deutschland (vom 25. November bis 31. Dezember) die Rücksendungen der Fragebögen an die angegebene Adresse zu verfolgen. Ich bitte Sie deshalb, den angegebenen Zeitraum zu berücksichtigen.

Mit freundlichen Grüssen

Anlage

*Harold Sollenberger*

Dr. Harold M. Sollenberger, C.P.A.  
Professor and Chairman,  
Department of Accounting and  
Financial Administration

## MICHIGAN STATE UNIVERSITY

GRADUATE SCHOOL OF BUSINESS ADMINISTRATION  
DEPARTMENT OF ACCOUNTING & FINANCIAL ADMINISTRATION

EAST LANSING · MICHIGAN · 48824

12. Dezember 1977

mein Schreiben vom  
25. November 1977

Sehr geehrter Herr Leiter der Kreditabteilung,

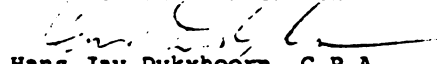
ich erlaube mir, Ihnen vor zwei Wochen im Rahmen einer Doktorarbeit, die die Beziehung zwischen Wirtschaftsprüfer und Klientel zum Thema hat, einen Fragebogen mit der Bitte um Rücksendung zuzusenden.

Leider konnte Ihr Beitrag bis heute noch nicht zu den bereits eingetroffenen und ausgefüllten Fragebögen gezählt werden. Ihre Mitarbeit an diesem Forschungsprojekt ist von großer Wichtigkeit, da die Qualität des Ergebnisses ohne Ihren Beitrag im Wert erheblich gemindert sein würde.

Ich nehme an, daß der Fragebogen nicht in Ihre Hände gelangt ist. Aus diesem Grunde übersende ich Ihnen in der Anlage noch einmal ein Exemplar dieses Fragebogens mit der freundlichen Bitte, diesen beantwortet zurückzusenden. Ein adressierter Briefumschlag ist beigelegt.

Schon heute möchte ich Ihnen für Ihre wertvolle Mitarbeit herzlich danken.

Mit freundlichen Grüßen



Hans Jay Dykxhoorn, C.P.A.  
Michigan State University  
z.Zt. Körner Straße 10  
4250 Bottrop  
Deutschland

Anlage



Doctoral Dissertation Research  
Michigan State University  
Return Questionnaire to:  
c/o Hans Jay Dykxhoorn, C.P.A.  
z.z. Koernerstrasse 10  
4250 Bottrop  
West Germany

Eine Studie der Wirtschaftsprüfer/-gesellschaft-Klientel

Beziehungen

Jede der folgenden Situationen beschreibt ein bestimmtes Verhältnis zwischen einer Wirtschaftsprüfungsgesellschaft und einem ihrer Jahresabschlussklienten. Bitte überprüfen Sie jede einzelne Situation, um zu entscheiden, ob Sie glauben, dass eine Wirtschaftsprüfungsgesellschaft in jedem Fall unabhängig und unbefangen oder nicht unabhängig und nicht unbefangen ist, besonders im Hinblick auf die Jahresabschlussprüfung. Bitte markieren Sie ebenfalls, in welchem Masse Ihre Kreditentscheidung in jedem einzelnen Fall beeinflusst wäre.

Bitte beachten Sie, dass die Unabhängigkeit und Unbefangenheit eines Wirtschaftsprüfers sich nicht nur auf die Fähigkeit bezieht, objektive und unvoreingenommene Entscheidungen in Verbindung mit der Abschlussprüfung zu treffen, sondern auch darauf, wie es die Wirtschaftsprüferkammer in ihren Richtlinien vorschreibt, dass kein sachlich vernünftiger Grund besteht, aus dem die Besorgnis der Befangenheit abgeleitet werden kann.

Bitte stellen Sie sich vor, dass in jeder der folgenden Situationen, die genannte Wirtschaftsprüfungsgesellschaft eine typische Wirtschaftsprüfungsfirma darstellt, und dass der erwähnte Klient, (oder die erwähnte Klientenfirma) einen Ihrer eventuellen Kreditkunden von mittlerer Größe repräsentiert. Bitte beurteilen Sie jede der folgenden Situationen, welche auf den nächsten drei Seiten dieses Fragebogens beschrieben sind, für sich getrennt.

Sample: Directors of Loan Departments (Leiter der Kreditabteilung)

Bitte benutzen Sie diesen Schlüssel für Ihre Antworten.

Unabhängigkeitsentscheidung

- 1= Ja, ich glaube, dass in dieser Situation die Wirtschaftsprüfungsgesellschaft unabhängig und unbefangen ist.  
2= Nein, ich glaube nicht, dass in dieser Situation die Wirtschaftsprüfungsgesellschaft unabhängig und unbefangen ist.

Kreditentscheidung

- Meine Kreditentscheidung ist  
1= stark negativ beeinflusst  
2= leicht negativ beeinflusst  
3= unbeeinflusst, weder negativ noch positiv  
4= leicht positiv beeinflusst  
5= stark positiv beeinflusst

	Unabhängigkeits- entscheidung (Bitte kreisen Sie eine Nummer ein)		Kreditentscheidung (Bitte kreisen Sie eine Nummer ein)					
A.								
1.	Das Büro einer Wirtschaftsprüfungsgesellschaft befand sich in einem Gebäude, das einer Klientenfirma gehörte. Die Wirtschaftsprüfungsgesellschaft verfügte über ungefähr 25 Prozent des vorhandenen Büroraumes im Gebäude und der Klient benutzte den restlichen Büroraum.....	1	2	1	2	3	4	5
2.	Eine Wirtschaftsprüfungsgesellschaft führte für einen Klienten nicht nur die Prüfung des Jahresabschlusses durch, sondern übte auch weitere Dienstleistungen aus, einschliesslich allgemeiner Führung der Journale und Hauptbücher, Abschlussbuchungen und Anfertigung der Jahresbilanz.....	1	2	1	2	3	4	5
3.	Zwecks Handhabung vertraulicher Informationen beauftragte eine Klientenfirma eine Wirtschaftsprüfungsgesellschaft nicht nur für die Jahresabschlussprüfung, sondern auch für die folgenden Dienste: (a) monatliche Gehaltsbuchführung der geschäftsführenden Angestellten (b) Führung bestimmter Konten in einem privaten Buchführungsjournal.....	1	2	1	2	3	4	5
4.	Ein Angestellter in einer Wirtschaftsprüfungsgesellschaft mit fünf Jahren Prüfungserfahrung verwaltete persönlich ein Gebäude, das einem ihrer Jahresabschlussprüfungsklienten gehörte.....	1	2	1	2	3	4	5
5.	Die Angestellten eines Klienten fertigten von verschiedenen Journalen (Büchern) Computerlochstreifen an, welche mit einem Optical Scanner gelesen werden konnten, und schickten diese Lochstreifen zum Büro ihrer Abschlussprüfer. Die Wirtschaftsprüfungsgesellschaft sandte die Lochstreifen in unveränderter Form weiter zu einem Computer Service. Die Wirtschaftsprüfungsgesellschaft erhielt die gedruckten Ergebnisse des Jahresabschlusses und Auszüge der Hauptbücher von dem Computer Service zurück und schickte sie zu ihrem Klienten. Die Wirtschaftsprüfergesellschaft verrichtete diese Arbeit zusätzlich zu der Jahresabschlussprüfung.....	1	2	1	2	3	4	5
6.	Gemäss eines Umschuldungsplanes wurden die Schulden der Klientenfirma durch Schuldscheine unterlegt, die nach fünf Jahren fällig werden sollten. Die Wirtschaftsprüfungsgesellschaft erhielt ebenfalls Schuldscheine für ihre Jahresabschlussprüfungsarbeiten.....	1	2	1	2	3	4	5

Unabhängigkeitsentscheidung

- 1= Ja, ich glaube, dass in dieser Situation die Wirtschaftsprüfungsgesellschaft unabhängig und unbefangen ist.  
 2= Nein, ich glaube nicht, dass in dieser Situation die Wirtschaftsprüfungsgesellschaft unabhängig und unbefangen ist.

Kreditentscheidung

- Meine Kreditentscheidung ist  
 1= stark negativ beeinflusst  
 2= leicht negativ beeinflusst  
 3= unbeeinflusst, weder negativ noch positiv  
 4= leicht positiv beeinflusst  
 5= stark positiv beeinflusst

	<u>Unabhängigkeits- entscheidung (Bitte kreisen Sie eine Nummer ein)</u>		<u>Kreditentscheidung (Bitte kreisen Sie eine Nummer ein)</u>				
7. A war der Controller der Firma Z. Er war ein Firmenangestellter und nicht von Aktionären der Firma zu seinem Posten gewählt. A's Bruder, B, war ein Wirtschaftsprüfer der Jahresabschlussprüfungsgesellschaft der Firma Z, aber B persönlich war in keiner Weise mit der Jahresabschlussprüfung der Firma Z verbunden.....	1	2	1	2	3	4	5
9. Ein Wirtschaftsprüfer einer Wirtschaftsprüfungsgesellschaft hatte einen Schwager in leitender Position in der Verkaufsabteilung einer neuen Klientenfirma. Der Schwager war nicht an finanziellen Entscheidungen seiner Firma beteiligt. Der Wirtschaftsprüfer selbst hatte persönlich nichts mit der Jahresabschlussprüfung zu tun.....	1	2	1	2	3	4	5
9. Eine Wirtschaftsprüfungsgesellschaft vermietete "block time" ihres Computers an einen Klienten, als der Computer des Klienten überfordert war. Die Wirtschaftsprüfungsgesellschaft war zugleich die Abschlussprüfungsfirma des Klienten.....	1	2	1	2	3	4	5
10. Der Klient einer Wirtschaftsprüfungsgesellschaft verkaufte Konzessionen (franchises). Zwei Wirtschaftsprüfer der Wirtschaftsprüfungsgesellschaft legten ungefähr fünf Prozent ihres Vermögens an fünfzig Prozent der Aktien der Firma K an. Die Firma K hatte eine Konzession von dem Klienten erworben. Mit Ausnahme der Auszahlung eines bestimmten Prozentsatzes vom Umsatz an den Klienten arbeitete die Firma K selbstständig und unabhängig.....	1	2	1	2	3	4	5
11. Ein Wirtschaftsprüfer einer Wirtschaftsprüfungsgesellschaft besass ein Prozent der Aktien der Firma B, deren Tochtergesellschaft A ein künftiger Klient der Wirtschaftsprüfungsgesellschaft werden soll. Der Wirtschaftsprüfer, dem diese Aktien gehörten, ist in keiner Weise an den Abschlussprüfungsarbeiten beteiligt.....	1	2	1	2	3	4	5
12. Ein Wirtschaftsprüfer einer Wirtschaftsprüfungsgesellschaft besass ein Prozent der Aktien der Firma B, deren Tochtergesellschaft A ein künftiger Klient der Wirtschaftsprüfungsgesellschaft werden soll. Der Wirtschaftsprüfer, dem diese Aktien gehörten, wird als der Prüfungsleiter der Abschlussprüfung der Tochtergesellschaft A fungieren.....	1	2	1	2	3	4	5
13. Ein Wirtschaftsprüfer einer Wirtschaftsprüfungsgesellschaft war ebenfalls als Rechtsanwalt für einen Klienten tätig, genauer gesagt, er vertrat den Klienten in allen Rechtsangelegenheiten. Für diesen Dienst erhielt er Gebühren von dem Klienten. Ebenfalls erhielt er von der Wirtschaftsprüfungsgesellschaft Gebühren für die Jahresabschlussprüfung, da die Wirtschaftsprüfungsgesellschaft der Abschlussprüfer der Klientenfirma war.....	1	2	1	2	3	4	5



Unabhängigkeitsentscheidung

- 1= Ja, ich glaube, dass in dieser Situation die Wirtschaftsprüfungsgesellschaft unabhängig und unbefangen ist.  
 2= Nein, ich glaube nicht, dass in dieser Situation die Wirtschaftsprüfungsgesellschaft unabhängig und unbefangen ist.

Kreditentscheidung

- Meine Kreditentscheidung ist  
 1= stark negativ beeinflusst  
 2= leicht negativ beeinflusst  
 3= unbeeinflusst, weder negativ noch positiv  
 4= leicht positiv beeinflusst  
 5= stark positiv beeinflusst

Unabhängigkeits-  
entscheidung (Bitte  
kreisen Sie eine Nummer ein)

Kreditentscheidung  
(Bitte kreisen Sie  
eine Nummer ein)

14. Ein Wirtschaftsprüfer einer Wirtschaftsprüfungsgesellschaft besass Aktien einer künftigen Klientenfirma. Seine Wirtschaftsprüfungsgesellschaft soll die Jahresabschlussprüfung durchführen. Bitte beurteilen Sie die folgenden Situationen für sich getrennt.
- Situation A. Der Wirtschaftsprüfer besass nur sehr wenige Aktien der Klientenfirma (weniger als ein Prozent seines Vermögens)..... 1 2 1 2 3 4 5
- Situation B. Der Wirtschaftsprüfer besass drei Prozent der Aktien der Klientenfirma (ungefähr zehn Prozent seines Vermögens)..... 1 2 1 2 3 4 5
- Situation C. Der Wirtschaftsprüfer besass zehn Prozent der Aktien der Klientenfirma (ungefähr zehn Prozent seines Vermögens)..... 1 2 1 2 3 4 5
15. Eine Bank erwarb einen bedeutenden Teil der Aktien der Firma S, genügend um einen erheblichen Einfluss auf die Geschäftsführung auszuüben. Die Bank besass ausserdem Aktien einer WP-Gesellschaft, welche damit beauftragt war, die Jahresabschlussprüfung der Firma S durchzuführen. Bitte beurteilen Sie die folgenden Situationen für sich getrennt.
- Situation A. Die Bank besass ungefähr 10 Prozent der Aktien der Wirtschaftsprüfungsgesellschaft..... 1 2 1 2 3 4 5
- Situation B. Die Bank besass zwischen 11 und 24 Prozent der Aktien der Wirtschaftsprüfungsgesellschaft..... 1 2 1 2 3 4 5
- Situation C. Die Bank besass zwischen 25 und 49 Prozent der Aktien der Wirtschaftsprüfungsgesellschaft..... 1 2 1 2 3 4 5
- Situation D. Die Bank besass genau 50 Prozent der Aktien der Wirtschaftsprüfungsgesellschaft..... 1 2 1 2 3 4 5
- Situation E. Die Bank besass mehr als 50 Prozent der Aktien der Wirtschaftsprüfungsgesellschaft..... 1 2 1 2 3 4 5
16. Ein Wirtschaftsprüfer einer Wirtschaftsprüfungsgesellschaft war ein Mitglied des Aufsichtsrats der Firma L. Die Firma L war eine der grössten Lieferanten der Firma M. Die Wirtschaftsprüfungsgesellschaft war beauftragt, die Jahresabschlussprüfung der Firma M durchzuführen..... 1 2 1 2 3 4 5
17. Ein gewisser Teil der Einnahmen einer Wirtschaftsprüfungsgesellschaft bestand aus Abschlussprüfungsgebühren einer einzelnen Klientenfirma. Bitte beurteilen Sie die folgenden Situationen für sich getrennt. Die Gebühren von der einzelnen Klientenfirma betrugen von den Gesamteinnahmen den folgenden Prozentsatz:
- Situation A: ungefähr 5 Prozent der Gesamteinnahmen..... 1 2 1 2 3 4 5
- Situation B: ungefähr 10 Prozent der Gesamteinnahmen..... 1 2 1 2 3 4 5
- Situation C: ungefähr 25 Prozent der Gesamteinnahmen..... 1 2 1 2 3 4 5
- Situation D: ungefähr 50 Prozent der Gesamteinnahmen..... 1 2 1 2 3 4 5
- Situation E: ungefähr 75 Prozent der Gesamteinnahmen..... 1 2 1 2 3 4 5

B.

1. Wie viele Jahre Berufserfahrung haben Sie im Kreditbereich? \_\_\_\_\_ Jahre  
(Bitte runden Sie ab)

2. Wie vertraut sind Sie mit den Prüfungsaufgaben der Wirtschaftsprüfer?  
(Bitte kreisen Sie eine Nummer ein).

Nicht vertrautSehr vertraut

1

2

3

4

5

3. Welche Bedeutung messen Sie der Unabhängigkeit und Unbefangenheit der Wirtschaftsprüfer/-gesellschaft bei? (Bitte kreisen Sie eine Nummer ein).

Keine BedeutungGrosse Bedeutung

1

2

3

4

5

4. Bei ungefähr wie vielen Ihrer Kreditentscheidungen benutzen Sie testierte Jahresabschlüsse? (Bitte kreisen Sie eine Nummer ein).

0%1-25%26-50%51-75%76-100%

1

2

3

4

5

Raum für zusätzliche Bemerkungen \_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

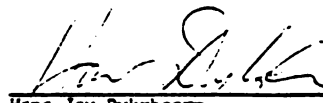
Falls Sie an der Zusendung des Ergebnisses dieses Forschungsvorhabens interessiert sind, bitte ich Sie um Angabe Ihrer Adresse.

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

Ich danke Ihnen für Ihre Mühe und Bereitschaft mich bei diesem Forschungsprojekt zu unterstützen.

  
Hans Jay Dykxhoorn  
(Certified Public Accountant)

English TranslationA STUDY OF AUDITOR-CLIENT RELATIONSHIPS

Each of the following situations involves a different relationship between an accounting firm and its client. Please evaluate each situation to determine whether you think an accounting firm would be considered independent (unbiased) or not independent (biased) with respect to a year-end audit of the client involved. Please also indicate how your lending decision would be affected.

Please note that the independence of a Wirtschaftsprüfer not only deals with his ability to make objective and unbiased audit decisions but also, as the Wirtschaftsprüferkammer in its Directives mandates, that there are no circumstances that may suggest that the auditor's appearance of independence may be impaired.

Assume that the accounting firm in each of the following situations is a typical accounting firm. Also assume that the client is one of your loan prospects. Please evaluate each of the following situations described in this questionnaire separately.

Sample: Directors of Loan Departments (Leiter der Kreditabteilung)

Please use this key for your answersIndependence Decision

- 1= Yes, I think the accounting firm is independent (unbiased) in this situation.  
 2= No, I don't think the accounting firm is independent (unbiased) in this situation.

Lending Decision

- The circumstances are such as to  
 1= greatly impair loan prospect  
 2= slightly impair loan prospect  
 3= have no effect on loan prospect  
 4= slightly improve loan prospect  
 5= greatly improve loan prospect

	<u>Independence Decision</u> <u>(Please circle one number)</u>		<u>Lending Decision</u> <u>(Please circle one number)</u>				
A.							
1.	An accounting firm had its office in a building which was owned by a client. The accounting firm occupied approximately 25 percent of the available space in the building, and the client occupied the remainder.....		1	2	1	2	3 4 5
2.	In addition to the audit, an accounting firm provided services for the client which included maintaining the journals and ledgers, making adjusting entries and preparing financial statements.....		1	2	1	2	3 4 5
3.	In order to keep certain information confidential, the client had the accounting firm perform the following services in addition to the audit: (a) prepare the executive payroll (b) maintain selected general ledger accounts in a private ledger.....		1	2	1	2	3 4 5
4.	A partner in an accounting firm managed a building owned by an audit client.....		1	2	1	2	3 4 5
5.	From the books of original entry, client personnel prepared printed tapes that could be read on an optical scanner and sent the tapes to the accountants' office. The accountants forwarded the tapes to a service bureau. The accountants received the print-outs of the financial statements and general ledgers and sent them to the client. The accountants did not edit the input data prior to transmission to the service bureau. The accountants provided this service in addition to the audit.....		1	2	1	2	3 4 5
6.	Pursuant to a plan of recapitalization, the existing debt of the company was exchanged for five-year promissory notes. The accounting firm received the same kind of promissory notes in payment of its audit fee.....		1	2	1	2	3 4 5

Independence Decision

- 1= Yes, I think the accounting firm is independent (unbiased) in this situation.  
 2= No, I don't think the accounting firm is independent (unbiased) in this situation.

Lending Decision

- 1= greatly impair loan prospect  
 2= slightly impair loan prospect  
 3= have no effect on loan prospect  
 4= slightly improve loan prospect  
 5= greatly improve loan prospect

	<u>Independence Decision</u>		<u>Lending Decision</u>				
	(Please circle one number)		(Please circle one number)				

- |  |   |   |   |   |   |   |   |
|--|---|---|---|---|---|---|---|
| 7. A was the controller of Company Z. He was not an elected officer nor did he have any stock holding in Company Z. A's brother, B, was a partner in the public accounting firm that audits Company Z's books. However, B, was not the partner in charge of the audit...   | 1 | 2 | 1 | 2 | 3 | 4 | 5 |
| 8. A partner in a public accounting firm had a brother-in-law who was sales vice president for a recently acquired client. The brother-in-law was not directly involved in the financial affairs of the company and the partner was not connected with the audit in any way.....   | 1 | 2 | 1 | 2 | 3 | 4 | 5 |
| 9. An accounting firm rented block time on its computer to a client when the client's computer became overburdened.....  | 1 | 2 | 1 | 2 | 3 | 4 | 5 |
| 10. A client of an accounting firm was engaged in the business of selling franchises. Two partners of this accounting firm invested approximately five percent of their personal fortunes to buy one half of the stock of a corporation which held a franchise granted by this client. Except for the payment of a percentage of sales to the franchisor client, the franchise operated independently..... | 1 | 2 | 1 | 2 | 3 | 4 | 5 |
| 11. A partner in an accounting firm whose proposed client A was a wholly owned subsidiary of corporation B, owned one percent of the stock of corporation B. The partner who owns these stocks would not in any way be involved with the year-end audit.....   | 1 | 2 | 1 | 2 | 3 | 4 | 5 |
| 12. A partner in an accounting firm whose proposed client A was a wholly owned subsidiary of corporation B, owned one percent of the stock of corporation B. The partner who owns these stocks would be in charge of the year-end audit.....   | 1 | 2 | 1 | 2 | 3 | 4 | 5 |
| 13. A partner in an accounting firm (qualified as a lawyer) also acted as general counsel for an audit client. He received fees for such legal services and, through the accounting partnership, for accounting services rendered concurrently.....  | 1 | 2 | 1 | 2 | 3 | 4 | 5 |

Independence Decision

- 1= Yes, I think the accounting firm is independent (unbiased) in this situation.  
 2= No, I don't think the accounting firm is independent (unbiased) in this situation.

Lending Decision

- 1= greatly impair loan prospect  
 2= slightly impair loan prospect  
 3= have no effect on loan prospect  
 4= slightly improve loan prospect  
 5= greatly improve loan prospect

Independence Decision      Lending Decision  
 (Please circle one number)      (Please circle one number)

14. A partner in an accounting firm owned stocks of a proposed client for which he was engaged to do the year-end audit. Consider each of the following situations separately.
- Situation A. The partner owned a very small number of shares of the client amounting to less than one percent of his net worth..... 1    2            1    2    3    4    5
- Situation B. The partner owned 3 percent of the client's stock amounting to 10 percent of his net worth..... 1    2            1    2    3    4    5
- Situation C. The partner owned 10 percent of the client's stock amounting to 10 percent of his net worth..... 1    2            1    2    3    4    5
15. A bank acquired a large number of shares of company S, large enough to enable the bank to significantly influence the management of company S. In addition, the same bank also owned shares of the auditing firm that was engaged to perform the year-end audit of company S. Consider each of the following situations separately.
- Situation A. The bank owned approximately 10 percent of the outstanding stock of the auditing firm..... 1    2            1    2    3    4    5
- Situation B. The bank owned between 11 and 24 percent of the outstanding stock of the auditing firm..... 1    2            1    2    3    4    5
- Situation C. The bank owned between 25 and 49 percent of the outstanding stock of the auditing firm..... 1    2            1    2    3    4    5
- Situation D. The bank owned exactly 50 percent of the outstanding stock of the auditing firm..... 1    2            1    2    3    4    5
- Situation E. The bank owned more than 50 percent of the outstanding stock of the auditing firm..... 1    2            1    2    3    4    5
16. A partner of an accounting firm was also a member of the Supervisory Board of Corporation L. Corporation L was one of the largest suppliers of Corporation M. The accounting firm was engaged to perform the year-end audit of Corporation M..... 1    2            1    2    3    4    5
17. A certain portion of an accounting firm's revenue consisted of audit fees from one particular client. Consider each of the following situations separately. The fees

from this particular client represented  
approximately:

<u>Situation A:</u>	5 percent of total revenue	1	2	1	2	3	4	5
<u>Situation B:</u>	10 percent of total revenue	1	2	1	2	3	4	5
<u>Situation C:</u>	25 percent of total revenue	1	2	1	2	3	4	5
<u>Situation D:</u>	50 percent of total revenue	1	2	1	2	3	4	5
<u>Situation E:</u>	75 percent of total revenue	1	2	1	2	3	4	5

B.

1. To the nearest year, how many years of experience do you have in the credit area? \_\_\_\_\_ years

2. How familiar are you with the audit work of Wirtschaftsprüfer?  
(Please circle one number)

<u>Not familiar</u>					<u>Very familiar</u>
1	2	3	4	5	

3. What percentage of your lending decisions involve the use of audited financial statements? (Please circle one number)

<u>0%</u>	<u>1-25%</u>	<u>26-50%</u>	<u>51-75%</u>	<u>76-100%</u>
1	2	3	4	5

Space for additional comments \_\_\_\_\_

If you would like to receive a summary of the research results, please give your address below.

Thank you very much for your cooperation.

Hans Jay Dykxhoorn, C.P.A.

APPENDIX C

COVER LETTER, FOLLOW-UP LETTER  
AND QUESTIONNAIRE MAILED TO  
LEITER DER WERTPAPIERABTEILUNG



## MICHIGAN STATE UNIVERSITY

GRADUATE SCHOOL OF BUSINESS ADMINISTRATION  
DEPARTMENT OF ACCOUNTING & FINANCIAL ADMINISTRATION

EAST LANSING · MICHIGAN · 48824  
November 25, 1977

Sehr geehrter Herr Leiter der Wertpapierabteilung!

Die unabhängige und objektive Ausübung des Wirtschaftsprüferberufes ist von grosser Bedeutung für die Funktion der deutschen und internationalen Wirtschaftsgemeinschaft.

Mr. Hans Jay Dykxhoorn, Certified Public Accountant and zur Zeit Doktorand an der Graduate School of Business at Michigan State University, führt im Rahmen seiner Doktorarbeit eine Studie aus, die sich mit der Unabhängigkeit und Unbefangenheit der Wirtschaftsprüfer befasst. Mr. Dykxhoorn hofft, dass seine empirische Resultate zu einem besseren Verständnis des Begriffes der Unabhängigkeit auf dem Gebiet der Wirtschaftsprüfung in Theorie und Praxis führen werden.

Der beigelegte, anonyme Fragebogen wurde in der Absicht aufgesetzt, nicht nur die Meinungen von Wirtschaftsprüfern, sondern auch die Ansichten von beteiligten Dritten, die mit der Handhabung von Jahresabschlüssen vertraut sind, zu ermitteln.

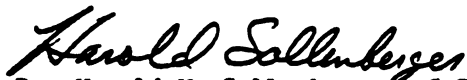
Ich darf Ihnen versichern, dass alle Daten und Angaben streng vertraulich behandelt werden und die Resultate nur in Tabellenform erscheinen werden. Bitte benutzen Sie den beigelegten, adressierten und frankierten Briefumschlag für die Rücksendung des ausgefüllten Fragebogens. Die Nummer auf der Rückseite dieses Briefumschlages dient der Eingangskontrolle. Falls Sie an der Zusendung des Ergebnisses dieses Forschungsvorhabens interessiert sind, bitten wir Sie um Angabe Ihrer Adresse.

Wir hoffen, das Sie ungefähr 15-20 Min. zur Verfügung haben, da wir Ihrer Mitarbeit an dieser Studie erhebliche Bedeutung beimessen und Ihre Angaben mit grossem Interesse entgegensehen.

Mr. Dykxhoorn hofft, während seines kurzfristigen Aufenthalts in Deutschland (vom 25. November bis 31. Dezember) die Rücksendungen der Fragebögen an die angegebene Adresse zu verfolgen. Ich bitte Sie deshalb, den angegebenen Zeitraum zu berücksichtigen.

Mit freundlichen Grüssen

Anlage



Dr. Harold M. Sollenberger, C.P.A.  
Professor and Chairman,  
Department of Accounting and  
Financial Administration

## MICHIGAN STATE UNIVERSITY

GRADUATE SCHOOL OF BUSINESS ADMINISTRATION  
DEPARTMENT OF ACCOUNTING & FINANCIAL ADMINISTRATION

EAST LANSING • MICHIGAN • 48824

12.12.1977  
mein Schreiben vom  
25.11.1977

Sehr geehrter Herr Leiter der Wertpapierabteilung,


ich erlaube mir, Ihnen vor zwei Wochen im Rahmen einer Doktorarbeit, die die Beziehung zwischen Wirtschaftsprüfer und Klientel zum Thema hat, einen Fragebogen mit der Bitte um Rücksendung zuzusenden.

Leider konnte Ihr Beitrag bis heute noch nicht zu den bereitseingetroffenen und ausgefüllten Fragebögen gezählt werden. Ihre Mitarbeit an diesem Forschungsprojekt ist von großer Wichtigkeit, da die Qualität des Ergebnisses ohne Ihren Beitrag im Wert erheblich gemindert sein würde.

Ich nehme an, daß der Fragebogen nicht in Ihre Hände gelangt ist. Aus diesem Grunde übersende ich Ihnen in der Anlage noch einmal ein Exemplar dieses Fragebogens mit der freundlichen Bitte, diesen beantwortet zurückzusenden. Ein adressierter Briefumschlag ist beigelegt.

Schon heute möchte ich Ihnen für Ihre wertvolle Mitarbeit herzlich danken.

Mit freundlichen Grüßen



Hans Jay Dykxhoorn, C.P.A.  
Michigan University  
z.Zt. Körner Straße 10  
4250 Bottrop  
Deutschland

Anlage



Doctoral Dissertation Research  
Michigan State University  
Return Questionnaire to:  
Hans Jay Dykxhoorn, C.F.A.  
1.2. Koernerstrasse 10  
4250 Bottrop  
West Germany

### Eine Studie der Wirtschaftsprüfer/-gesellschaft-Klientel

#### Beziehungen

Jede der folgenden Situationen beschreibt ein bestimmtes Verhältnis zwischen einer Wirtschaftsprüfungsgesellschaft und einem ihrer Jahresabschlussklienten. Bitte überprüfen Sie jede einzelne Situation, um zu entscheiden, ob Sie glauben, dass eine Wirtschaftsprüfungsgesellschaft in jedem Fall unabhängig und unbefangen oder nicht unabhängig und nicht unbefangen ist, besonders im Hinblick auf die Jahresabschlussprüfung. Bitte markieren Sie ebenfalls, in welchem Masse Ihre Investmententscheidung in jedem einzelnen Fall beeinflusst wäre.

Bitte beachten Sie, dass die Unabhängigkeit und Unbefangenheit eines Wirtschaftsprüfers sich nicht nur auf die Fähigkeit bezieht, objektive und unvoreingenommene Entscheidungen in Verbindung mit der Abschlussprüfung zu treffen, sondern auch darauf, wie es die Wirtschaftsprüferkammer in ihren Richtlinien vorschreibt, dass kein sachlich vernünftiger Grund besteht, aus dem die Besorgnis der Befangenheit abgeleitet werden kann.

Bitte stellen Sie sich vor, dass in jeder der folgenden Situationen die genannte Wirtschaftsprüfungsgesellschaft eine typische Wirtschaftsprüfungsfirma darstellt, und dass der erwähnte Klient, (oder die erwähnte Klientenfirma) für eine eventuelle Kapitalanlage in Frage käme. Bitte beurteilen Sie jede der folgenden Situationen, welche auf den nächsten drei Seiten dieses Fragebogens beschrieben sind, für sich getrennt.

Sample: Directors of Investment Funds (Leiter der Wertpapierabteilung)

Bitte benutzen Sie diesen Schlüssel für Ihre Antworten.

Unabhängigkeitsentscheidung

- 1= Ja, ich glaube, dass in dieser Situation die Wirtschaftsprüfungsgesellschaft unabhängig und unbefangen ist.  
2= Nein, ich glaube nicht, dass in dieser Situation die Wirtschaftsprüfungsgesellschaft unabhängig und unbefangen ist.

Investmententscheidung

- Meine Investmententscheidung ist  
1= Stark negativ beeinflusst  
2= Leicht negativ beeinflusst  
3= Unbeeinflusst, weder negativ noch positiv  
4= Leicht positiv beeinflusst  
5= Stark positiv beeinflusst

Unabhängigkeits-      Investmententscheidung  
entscheidung (Bitte      (Bitte kreisen Sie eine  
kreisen Sie eine Nummer ein)      Nummer ein)

A.

1. Das Büro einer Wirtschaftsprüfungsgesellschaft befand sich in einem Gebäude, das einer Klientenfirma gehörte. Die Wirtschaftsprüfungsgesellschaft verfügte über ungefähr 25 Prozent des vorhandenen Büroraumes im Gebäude und der Klient benutzte den restlichen Büroraum..... 1      2      1      2      3      4      5
2. Eine Wirtschaftsprüfungsgesellschaft führte für einen Klienten nicht nur die Prüfung des Jahresabschlusses durch, sondern übte auch weitere Dienstleistungen aus, einschliesslich allgemeiner Führung der Journale und Hauptbücher, Abschlussbuchungen und Anfertigung der Jahresbilanz..... 1      2      1      2      3      4      5
3. Zwecks Handhabung vertraulicher Informationen beauftragte eine Klientenfirma eine Wirtschaftsprüfungsgesellschaft nicht nur für die Jahresabschlussprüfung, sondern auch für die folgenden Dienste:  
(a) monatliche Gehaltsbuchführung der geschäftsführenden Angestellten  
(b) Führung bestimmter Konten in einem privaten Buchführungsjournal..... 1      2      1      2      3      4      5
4. Ein Angestellter in einer Wirtschaftsprüfungsgesellschaft mit fünf Jahren Prüfungserfahrung verwaltete persönlich ein Gebäude, das einem ihrer Jahresabschlussprüfungsklienten gehörte..... 1      2      1      2      3      4      5
5. Die Angestellten eines Klienten fertigten von verschiedenen Journalen (Büchern) Computerlochstreifen an, welche mit einem Optical Scanner gelesen werden konnten, und schickten diese Lochstreifen zum Büro ihrer Abschlussprüfer. Die Wirtschaftsprüfungsgesellschaft sandte die Lochstreifen in unveränderter Form weiter zu einem Computer Service. Die Wirtschaftsprüfungsgesellschaft erhielt die gedruckten Ergebnisse des Jahresabschlusses und Auszüge der Hauptbücher von dem Computer Service zurück und schickte sie zu ihrem Klienten. Die Wirtschaftsprüfungsgesellschaft verrichtete diese Arbeit zusätzlich zu der Jahresabschlussprüfung..... 1      2      1      2      3      4      5
6. Gemäss eines Umschuldungsplanes wurden die Schulden der Klientenfirma durch Schuldscheine unterlegt, die nach fünf Jahren fällig werden sollten. Die Wirtschaftsprüfungsgesellschaft erhielt ebenfalls Schuldscheine für ihre Jahresabschlussprüfungsarbeiten..... 1      2      1      2      3      4      5

Unabhängigkeitsentscheidung

- 1= Ja, ich glaube, dass in dieser Situation die Wirtschaftsprüfungsgesellschaft unabhängig und unbefangen ist.  
 2= Nein, ich glaube nicht, dass in dieser Situation die Wirtschaftsprüfungsgesellschaft unabhängig und unbefangen ist.

Investmententscheidung

- Meine Investmententscheidung ist  
 1= stark negativ beeinflusst  
 2= Leicht negativ beeinflusst  
 3= unbeeinflusst, weder negativ noch positiv  
 4= leicht positiv beeinflusst  
 5= stark positiv beeinflusst

	<u>Unabhängigkeits- entscheidung (Bitte kreisen Sie eine Nummer ein)</u>		<u>Investmententscheidung (Bitte kreisen Sie eine Nummer ein)</u>				
7. A war der Controller der Firma Z. Er war ein Firmenangestellter und nicht von Aktionären der Firma zu seinem Posten gewählt. A's Bruder, B, war ein Wirtschaftsprüfer der Jahresabschlussprüfungsgesellschaft der Firma Z, aber B persönlich war in keiner Weise mit der Jahresabschlussprüfung der Firma Z verbunden.....	1	2	1	2	3	4	5
8. Ein Wirtschaftsprüfer einer Wirtschaftsprüfungsgesellschaft hatte einen Schwager in leitender Position in der Verkaufsabteilung einer neuen Klientenfirma. Der Schwager war nicht an finanziellen Entscheidungen seiner Firma beteiligt. Der Wirtschaftsprüfer selbst hatte persönlich nichts mit der Jahresabschlussprüfung zu tun.....	1	2	1	2	3	4	5
9. Eine Wirtschaftsprüfungsgesellschaft vermietete "block time" ihres Computers an einen Klienten, als der Computer des Klienten überfordert war. Die Wirtschaftsprüfungsgesellschaft war zugleich die Abschlussprüfungsfirma des Klienten.....	1	2	1	2	3	4	5
10. Der Klient einer Wirtschaftsprüfungsgesellschaft verkaufte Konzessionen (franchises). Zwei Wirtschaftsprüfer der Wirtschaftsprüfungsgesellschaft legten ungefähr fünf Prozent ihres Vermögens an fünfzig Prozent der Aktien der Firma K an. Die Firma K hatte eine Konzession von dem Klienten erworben. Mit Ausnahme der Auszahlung eines bestimmten Prozentsatzes vom Umsatz an den Klienten arbeitete die Firma K selbstständig und unabhängig..	1	2	1	2	3	4	5
11. Ein Wirtschaftsprüfer einer Wirtschaftsprüfungsgesellschaft besass ein Prozent der Aktien der Firma B, deren Tochtergesellschaft A ein künftiger Klient der Wirtschaftsprüfungsgesellschaft werden soll. Der Wirtschaftsprüfer, dem diese Aktien gehörten, ist in keiner Weise an den Abschlussprüfungsarbeiten beteiligt.....	1	2	1	2	3	4	5
12. Ein Wirtschaftsprüfer einer Wirtschaftsprüfungsgesellschaft besass ein Prozent der Aktien der Firma B, deren Tochtergesellschaft A ein künftiger Klient der Wirtschaftsprüfungsgesellschaft werden soll. Der Wirtschaftsprüfer, dem diese Aktien gehörten, wird als der Prüfungsleiter der Abschlussprüfung der Tochtergesellschaft A fungieren.....	1	2	1	2	3	4	5
13. Ein Wirtschaftsprüfer einer Wirtschaftsprüfungsgesellschaft war ebenfalls als Rechtsanwalt für einen Klienten tätig, genauer gesagt, er vertrat den Klienten in allen Rechtsangelegenheiten. Für diesen Dienst erhielt er Gebühren von dem Klienten. Ebenfalls erhielt er von der Wirtschaftsprüfungsgesellschaft Gebühren für die Jahresabschlussprüfung, da die Wirtschaftsprüfungsgesellschaft der Abschlussprüfer der Klientenfirma war.....	1	2	1	2	3	4	5

Unabhängigkeitsentscheidung

- 1= Ja, ich glaube, dass in dieser Situation die Wirtschaftsprüfungsgesellschaft unabhängig und unbefangen ist.  
 2= Nein, ich glaube nicht, dass in dieser Situation die Wirtschaftsprüfungsgesellschaft unabhängig und unbefangen ist.

Investmententscheidung

- Meine Investmententscheidung ist  
 1= stark negativ beeinflusst  
 2= leicht negativ beeinflusst  
 3= unbeeinflusst, weder negativ noch positiv  
 4= leicht positiv beeinflusst  
 5= stark positiv beeinflusst

	<u>Unabhängigkeits-</u> <u>entscheidung (Bitte</u> <u>kreisen Sie eine Nummer ein)</u>		<u>Investmententscheidung</u> <u>(Bitte kreisen Sie</u> <u>eine Nummer ein)</u>				
14. Ein Wirtschaftsprüfer einer Wirtschaftsprüfungsgesellschaft besass Aktien einer künftigen Klientenfirma. Seine Wirtschaftsprüfungsgesellschaft soll die Jahresabschlussprüfung durchführen. Bitte beurteilen Sie die folgenden Situationen <u>für sich getrennt</u> .							
<u>Situation A.</u> Der Wirtschaftsprüfer besass nur sehr wenige Aktien der Klientenfirma (weniger als ein Prozent seines Vermögens).....	1	2	1	2	3	4	5
<u>Situation B.</u> Der Wirtschaftsprüfer besass drei Prozent der Aktien der Klientenfirma (ungefähr zehn Prozent seines Vermögens)....	1	2	1	2	3	4	5
<u>Situation C.</u> Der Wirtschaftsprüfer besass zehn Prozent der Aktien der Klientenfirma (ungefähr zehn Prozent seines Vermögens)....	1	2	1	2	3	4	5
15. Eine Bank erwarb einen bedeutenden Teil der Aktien der Firma S, genügend um einen erheblichen Einfluss auf die Geschäftsführung auszuüben. Die Bank besass ausserdem Aktien einer WP-Gesellschaft, welche damit beauftragt war, die Jahresabschlussprüfung der Firma S durchzuführen. Bitte beurteilen Sie die folgenden Situationen <u>für sich getrennt</u> .							
<u>Situation A.</u> Die Bank besass ungefähr 10 Prozent der Aktien der Wirtschaftsprüfungsgesellschaft.....	1	2	1	2	3	4	5
<u>Situation B.</u> Die Bank besass zwischen 11 und 24 Prozent der Aktien der Wirtschaftsprüfungsgesellschaft.....	1	2	1	2	3	4	5
<u>Situation C.</u> Die Bank besass zwischen 25 und 49 Prozent der Aktien der Wirtschaftsprüfungsgesellschaft.....	1	2	1	2	3	4	5
<u>Situation D.</u> Die Bank besass genau 50 Prozent der Aktien der Wirtschaftsprüfungsgesellschaft.....	1	2	1	2	3	4	5
<u>Situation E.</u> Die Bank besass mehr als 50 Prozent der Aktien der Wirtschaftsprüfungsgesellschaft.....	1	2	1	2	3	4	5
16. Ein Wirtschaftsprüfer einer Wirtschaftsprüfungsgesellschaft war ein Mitglied des Aufsichtsrats der Firma L. Die Firma L war eine der grössten Lieferanten der Firma M. Die Wirtschaftsprüfungsgesellschaft war beauftragt, die Jahresabschlussprüfung der Firma M durchzuführen.....	1	2	1	2	3	4	5
17. Ein gewisser Teil der Einnahmen einer Wirtschaftsprüfungsgesellschaft bestand aus Abschlussprüfungsgebühren einer einzelnen Klientenfirma. Bitte beurteilen Sie die folgenden Situationen <u>für sich getrennt</u> . Die Gebühren von der einzelnen Klientenfirma betrugen von den Gesamteinnahmen den folgenden Prozentsatz:							
<u>Situation A:</u> ungefähr 5 Prozent der Gesamteinnahmen.....	1	2	1	2	3	4	5
<u>Situation B:</u> ungefähr 10 Prozent der Gesamteinnahmen.....	1	2	1	2	3	4	5
<u>Situation C:</u> ungefähr 25 Prozent der Gesamteinnahmen.....	1	2	1	2	3	4	5
<u>Situation D:</u> ungefähr 50 Prozent der Gesamteinnahmen.....	1	2	1	2	3	4	5
<u>Situation E:</u> ungefähr 75 Prozent der Gesamteinnahmen.....	1	2	1	2	3	4	5

B.

1. Wie viele Jahre Berufserfahrung haben Sie im Investmentbereich?

(Bitte runden Sie ab) \_\_\_\_\_ Jahre

2. Wie vertraut sind Sie mit den Prüfungsaufgaben der Wirtschaftsprüfer?

(Bitte kreisen Sie eine Nummer ein).

Nicht vertrautSehr vertraut

1                      2                      3                      4                      5

3. Welche Bedeutung messen Sie der Unabhängigkeit und Unbefangenheit der Wirtschaftsprüfer/-gesellschaft bei?

Keine BedeutungGrosse Bedeutung

1                      2                      3                      4                      5

4. Bei ungefähr wie vielen Ihrer Investmententscheidungen benutzen Sie testierte Jahresabschlüsse? (Bitte kreisen Sie eine Nummer ein).

0%      1-25%      26-50%      51-75%      76-100%

1                      2                      3                      4                      5

Raum für zusätzliche Bemerkungen \_\_\_\_\_

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Falls Sie an der Zusendung des Ergebnisses dieses Forschungsvorhabens interessiert sind, bitte ich Sie um Angabe Ihrer Adresse.

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Ich danke Ihnen für Ihre Mühe und Bereitschaft mich bei diesem Forschungsprojekt zu unterstützen.

  
 Hans Jay Dykxhoorn, C.P.A.

English TranslationA STUDY OF AUDITOR-CLIENT RELATIONSHIPS

Each of the following situations involves a different relationship between an accounting firm and its client. Please evaluate each situation to determine whether you think an accounting firm would be considered independent (unbiased) or not independent (biased) with respect to a year-end audit of the client involved. Please also indicate how your investment decision would be affected.

Please note that the independence of a Wirtschaftsprüfer not only deals with his ability to make objective and unbiased audit decisions but also, as the Wirtschaftsprüferkammer in its Directives mandates, that there are no circumstances that may suggest that the auditor's appearance of independence may be impaired.

Assume that the accounting firm in each of the following situations is a typical accounting firm. Also assume that the client is one of your investment prospects. Please evaluate each of the following situations described in this questionnaire separately.

Sample: Directors of Investment Funds (Leiter der Wertpapierabteilung)



Please use this key for your answers

Independence Decision

- 1= Yes, I think the accounting firm is independent (unbiased) in this situation.  
2= No, I don't think the accounting firm is independent (unbiased) in this situation.

Investment Decision

- The circumstances are such as to  
1= greatly impair investment prospect  
2= slightly impair investment prospect  
3= have no effect on investment prospect  
4= slightly improve investment prospect  
5= greatly improve investment prospect

	<u>Independence Decision</u> <u>(Please circle one number)</u>		<u>Investment Decision</u> <u>(Please circle one number)</u>				
A.							
1.	An accounting firm had its office in a building which was owned by a client. The accounting firm occupied approximately 25 percent of the available space in the building, and the client occupied the remainder.....		1	2	1	2	3 4 5
2.	In addition to the audit, an accounting firm provided services for the client which included maintaining the journals and ledgers, making adjusting entries and preparing financial statements.....		1	2	1	2	3 4 5
3.	In order to keep certain information confidential, the client had the accounting firm perform the following services in addition to the audit: (a) prepare the executive payroll (b) maintain selected general ledger accounts in a private ledger.....		1	2	1	2	3 4 5
4.	A partner in an accounting firm managed a building owned by an audit client.....		1	2	1	2	3 4 5
5.	From the books of original entry, client personnel prepared printed tapes that could be read on an optical scanner and sent the tapes to the accountants' office. The accountants forwarded the tapes to a service bureau. The accountants received the print-outs of the financial statements and general ledgers and sent them to the client. The accountants did not edit the input data prior to transmission to the service bureau. The accountants provided this service in addition to the audit.....		1	2	1	2	3 4 5
6.	Pursuant to a plan of recapitalization, the existing debt of the company was exchanged for five-year promissory notes. The accounting firm received the same kind of promissory notes in payment of its audit fee.....		1	2	1	2	3 4 5

Independence Decision

- 1= Yes, I think the accounting firm is independent (unbiased) in this situation.  
 2= No, I don't think the accounting firm is independent (unbiased) in this situation.

Investment Decision

- 1= greatly impair investment prospect  
 2= slightly impair investment prospect  
 3= have no effect on investment prospect  
 4= slightly improve investment prospect  
 5= greatly improve investment prospect

Independence Decision  
 (Please circle one number)

Investment Decision  
 (Please circle one number)

- |  |   |   |   |   |   |   |   |
|--|---|---|---|---|---|---|---|
| 7. A was the controller of Company Z. He was not an elected officer nor did he have any stock holding in Company Z. A's brother, B was a partner in the public accounting firm that audits Company Z's books. However, B, was not the partner in charge of the audit...  | 1 | 2 | 1 | 2 | 3 | 4 | 5 |
| 8. A partner in a public accounting firm had a brother-in-law who was sales vice president for a recently acquired client. The brother-in-law was not directly involved in the financial affairs of the company and the partner was not connected with the audit in any way.....   | 1 | 2 | 1 | 2 | 3 | 4 | 5 |
| 9. An accounting firm rented block time on its computer to a client when the client's computer became overburdened.....  | 1 | 2 | 1 | 2 | 3 | 4 | 5 |
| 10. A client of an accounting firm was engaged in the business of selling franchises. Two partners of this accounting firm invested approximately five percent of their personal fortunes to buy one half of the stock of a corporation which held a franchise granted by this client. Except for the payment of a percentage of sales to the franchisor client, the franchise operated independently..... | 1 | 2 | 1 | 2 | 3 | 4 | 5 |
| 11. A partner in an accounting firm whose proposed client A was a wholly owned subsidiary of corporation B, owned one percent of the stock of corporation B. The partner who owns these stocks would not in any way be involved with the year-end audit.....   | 1 | 2 | 1 | 2 | 3 | 4 | 5 |
| 12. A partner in an accounting firm whose proposed client A was a wholly owned subsidiary of corporation B, owned one percent of the stock of corporation B. The partner who owns these stocks would be in charge of the year-end audit.....   | 1 | 2 | 1 | 2 | 3 | 4 | 5 |
| 13. A partner in an accounting firm (qualified as a lawyer) also acted as general counsel for an audit client. He received fees for such legal services and, through the accounting partnership, for accounting services rendered concurrently.....  | 1 | 2 | 1 | 2 | 3 | 4 | 5 |

Independence Decision

- 1= Yes, I think the accounting firm is independent (unbiased) in this situation.  
 2= No, I don't think the accounting firm is independent (unbiased) in this situation.

Investment Decision

- 1= greatly impair investment prospect  
 2= slightly impair investment prospect  
 3= have no effect on investment prospect  
 4= slightly improve investment prospect  
 5= greatly improve investment prospect

Independence Decision      Investment Decision  
 (Please circle one number)      (Please circle one number)

14. A partner in an accounting firm owned stocks of a proposed client for which he was engaged to do the year-end audit. Consider each of the following situations separately.
- Situation A. The partner owned a very small number of shares of the client amounting to less than one percent of his net worth..... 1    2                    1    2    3    4    5
- Situation B. The partner owned 3 percent of the client's stock amounting to 10 percent of his net worth..... 1    2                    1    2    3    4    5
- Situation C. The partner owned 10 percent of the client's stock amounting to 10 percent of his net worth..... 1    2                    1    2    3    4    5
15. A bank acquired a large number of shares of company S, large enough to enable the bank to significantly influence the management of company S. In addition, the same bank also owned shares of the auditing firm that was engaged to perform the year-end audit of company S. Consider each of the following situations separately.
- Situation A. The bank owned approximately 10 percent of the outstanding stock of the auditing firm..... 1    2                    1    2    3    4    5
- Situation B. The bank owned between 11 and 24 percent of the outstanding stock of the auditing firm..... 1    2                    1    2    3    4    5
- Situation C. The bank owned between 25 and 49 percent of the outstanding stock of the auditing firm..... 1    2                    1    2    3    4    5
- Situation D. The bank owned exactly 50 percent of the outstanding stock of the auditing firm..... 1    2                    1    2    3    4    5
- Situation E. The bank owned more than 50 percent of the outstanding stock of the auditing firm..... 1    2                    1    2    3    4    5
16. A partner of an accounting firm was also a member of the Supervisory Board of Corporation L. Corporation L was one of the largest suppliers of Corporation M. The accounting firm was engaged to perform the year-end audit of Corporation M..... 1    2                    1    2    3    4    5
17. A certain portion of an accounting firm's revenue consisted of audit fees from one particular client. Consider each of the following situations separately. The fees

from this particular client represented approximately:

<u>Situation A:</u>	5 percent of total revenue...	1	2	1	2	3	4	5
<u>Situation B:</u>	10 percent of total revenue..	1	2	1	2	3	4	5
<u>Situation C:</u>	25 percent of total revenue..	1	2	1	2	3	4	5
<u>Situation D:</u>	50 percent of total revenue..	1	2	1	2	3	4	5
<u>Situation E:</u>	75 percent of total revenue..	1	2	1	2	3	4	5

B.

1. To the nearest year, how many years of experience do you have in the investment area? \_\_\_\_\_ years
2. How familiar are you with the audit work of Wirtschaftsprüfer?  
(Please circle one number)  

<u>Not familiar</u>				<u>Very familiar</u>
1	2	3	4	5
3. How important do you consider the independence of auditors to be?  
(Please circle one number)  

<u>Not important</u>				
1	2	3	4	5
4. What percentage of your investment decisions involve the use of audited financial statements? (Please circle one number)  

<u>0%</u>	<u>1-25%</u>	<u>26-50%</u>	<u>51-75%</u>	<u>76-100%</u>
1	2	3	4	5

Space for additional comments \_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

If you would like to receive a summary of the research results, please give your address below.

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

Thank you very much for your cooperation.

Hans Jay Dykxhoorn, C.P.A.

## APPENDIX D

### INTERPRETATION OF THE WIRTSCHAFTSPRÜFERKAMMER OF THE AUDITOR-CLIENT RELATIONSHIPS INVESTIGATED IN THIS STUDY

Berufsrechtliche Beurteilung der Fragen 1 - 17  
des Fragebogens der Michigan State University  
nach Maßgabe der Berufsrichtlinien in der neuesten  
Fassung

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Frage 1:

Die Konstellation ist berufsrechtlich unerheblich und begründet nicht ohne weiteres eine Befangenheit oder Besorgnis der Befangenheit.

Frage 2:

Die Führung der Bücher und die Erstellung der Bilanz ist mit der gleichzeitig Tätigkeit als Abschlußprüfer nicht vereinbar. Der Tatbestand wird in den neugefaßten Berufsrichtlinien unmittelbar angesprochen, war aber schon früher in den Richtungsweisenden Feststellungen erwähnt.

Frage 3:

Der Sachverhalt entspricht rechtlich demjenigen der Frage 2; daraus folgt die gleichartige berufsrechtliche Beurteilung, daß die dort genannten Tätigkeiten nicht gleichzeitig wahrgenommen werden können.

Frage 4:

Der Sachverhalt bietet für sich allein keinen Grund zum Ausschluß des Prüfers; die Verwaltungstätigkeit handelt sich um eine sonstige Beratungstätigkeit, die mit der Prüfung prinzipiell vereinbar ist.

Frage 5:

Im Innenverhältnis mag der Geschehensablauf unbedenklich sein, da der Abschlußprüfer hier lediglich als Adresse zwischen geprüften Unternehmen und Datenverarbeiter fungiert. Im Außenverhältnis tritt er jedoch als derjenige auf, der für die Führung der Bücher verantwortlich ist. Infolgedessen ist aus formalen Gründen die Tätigkeit als Abschlußprüfer ausgeschlossen.

Frage 6:

Die Art der Bezahlung ist für die Beurteilung, ob Abhängigkeit oder Befangenheit bzw. Besorgnis der Befangenheit gegeben ist, grundsätzlich ohne Bedeutung. Allerdings ist eine Kreditierung des geprüften Unternehmens durch Stundung des Honorars mitunter bedenklich.

Frage 7:

Der geschilderte Sachverhalt erfüllt weder den Tatbestand des § 164 AktG noch den des § 49 WPO.

Frage 8:

Die Feststellung zu Frage 7 gilt entsprechend.

Frage 9:

Die Vermietung der Datenverarbeitungsanlage an einen Mandanten, der geprüft wird, ist im Regelfall berufsrechtlich unerheblich und begründet keinen Ausschließungstatbestand für den Abschlußprüfer.

Frage 10:

Die Fragestellung ist für deutsche Verhältnisse kaum verständlich, was auch Herrn Dykxhoorn dargelegt wurde. Das aus deutscher Sicht gravierende Problem ist die Verwertung von Insider-Kenntnissen für persönliche Zwecke, was nach Abschnitt IV. Richtungsweisende Feststellungen Nr. 3 nicht zulässig ist.

Frage 11 und 12:

Hier geht es um die Beteiligung an solchen Unternehmen, die mit dem geprüften Unternehmen verbunden sind. Nach der Neufassung der Richtlinien ist zunächst nur die unmittelbare Beteiligung am geprüften Unternehmen mit der gleichzeitigen Funktion als Abschlußprüfer unvereinbar. Infolgedessen ist die Beteiligung an verbundenen Unternehmen zur Zeit berufsrechtlich nicht zu beanstanden. Für die Praxis wird der geschilderte Fall wenig Bedeutung haben, da verbundene Unternehmen meist von ein und demselben Abschlußprüfer geprüft werden, das Beteiligungsverbot also jeweils unmittelbar eingreift.

Frage 13:

Der Sachverhalt ist berufsrechtlich unbedenklich; es handelt sich um den weiten Bereich der Vereinbarkeit von Prüfung und Beratung.

Frage 14:

Nach der Neufassung der Richtlinien ist die Beteiligung am geprüften Unternehmen grundsätzlich unzulässig, so daß alle drei Alternativen rechtlich gleichmäßig zu beurteilen sind.

Frage 15:

Es handelt sich um das Problem der Verbundenheit im Sinne des Aktienrechts. Nach der derzeitigen gesetzlichen Regelung sind die Situationen von A bis D berufsrechtlich ohne Bedeutung, da eine Verbundenheit nicht vorliegt, sofern nicht besondere Umstände eine solche Verbundenheit indizieren. Es wird insoweit auf die jüngste Entscheidung des Bundesgerichtshofs in Sachen VEBA AG verwiesen; der BGH hat in diesem Urteil festgestellt, daß der Bund herrschendes Unternehmen sein kann und daß eine Konzerneigenschaft auch dann möglich ist, wenn die Beteiligung unter 50% liegt, jedoch besondere Umstände auf einen herrschenden Einfluß schließen lassen.

Frage 16:

Es handelt sich um keinen Fall des § 164 AktG oder des § 49 WPO.

Frage 17:

Das Problem des auf einen einzigen Prüfungsmandanten entfallenden Honoraranteils ist erstmalig in den Richtlinien angesprochen worden; dabei ist bewußt darauf verzichtet worden, prozentuale Grenzen festzulegen, wie dies in den angelsächsischen Ländern bzw. in Frankreich zur Zeit üblich ist. Zu berücksichtigen ist vor allem, daß es von der Lage des Falles anhängt, ob eine wirtschaftliche Abhängigkeit gegeben ist oder nicht. Der Berufsanfänger, der nur wenige Mandate hat, erzielt zwangsläufig größere prozentuale Anteile als der Inhaber einer größeren Praxis, ohne daß dies berufsrechtlich zum Vorwurf gereicht. Auch die persönlichen Vermögensverhältnisse spielen eine Rolle, wenn z.B. der Beruf z.B. als Hobby ausgeübt wird, ohne daß es auf das Honorar ankommt.



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