INDEPENDENCE AND THE CERTIFIED PUBLIC ACCOUNTANT: AN EMPIRICAL ANALYSIS

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ABSTRACT

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The objective of this study was to obtain a better understanding of how various users of certified financial statements perceived the potential effect of possible changes in the CPA-client relationship. There were six possible changes that were considered. They were: 1) Mandated rotation of audit firms; 2) Required disclosure of independent auditors in a management report; 3) A prohibition on gifts and discount purchases from clients; 4) A prohibition of executive search and placement services; 5) Required handling of fees and arrangements for independent auditors by an audit committee; 6) Required selection and payment of independent auditors by the government.

A questionnaire approach was used to solicit the perceptions of Certified Public Accountants, Certified Financial Analysts, and Corporate Bar members. These perceptions were then analyzed and compared to the

recommendations of the American Institute of Certified Public Accountants Commission on Auditors' Responsibilities.

The conclusions based on the results of the analysis of the data were:

1. Although most groups felt that rotation of independent auditors would increase independence, they felt that the costs would exceed the benefits desired from the increased independence.
2. When considering disclosure of independent auditor changes in a management report, most groups felt that independence would be increased and that the costs would be exceeded by the benefits of such disclosure.
3. All groups felt that a prohibition on gifts and discount purchases from clients would increase independence and the benefits would exceed the costs.
4. There was a consensus that independence would be increased by a prohibition on executive search and placement services. There was, however, a difference of opinion regarding the relationship of costs and benefits.
5. Most respondent groups indicated that having fees and arrangements for the independent auditors handled by an audit committee would

increase independence. At the same time there was disagreement about the balance between costs and benefits.

6. There was a nearly unanimous response that government selection and payment of auditors would increase independence. Also nearly unanimous was the response that costs would be greater than the benefits.

In those instances where there seemed to be a consensus of the respondents, the position taken by the Commission on Auditors' Responsibilities was validated.

DEDICATION

To Fiesty, Muff and all the rest of God's little creatures who have helped to make this a better world to live in. Also to my dearest Patricia, who has been my whole world these past eleven years.

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When a person has spent as long achieving a degree as I have, the list of indebtedness could fill a book by itself. I would however like to mention some of the special people.

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the final copy of the dissertation. She was my everything. thank you Patricia.

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CHAPTER I

INTRODUCTION

Objectives of the Study

The purpose of this study is to examine the relationship between Certified Public Accountants (CPAs) and their clients, focusing on the issue commonly known as independence. This will be done by examining empirically indicated perceptions of various groups of users of accounting data. The issues to be investigated are raised in the American Institute of Certified Public Accountants (AICPA) sponsored report titled The Commission on Auditors' Responsibilities: Report, Conclusions and Recommendations, (Cohen Report).[1]

More specifically, the objectives of this study are to:

1. Collect and analyze (separately and collectively) the perceptions of individual users of accounting data of the effect of potential changes on the independence of CPAs.

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[1] American Institute of Certified Public Accountants, Commission on Auditors' Responsibilities, Commission on Auditors' Responsibilities: Report, Conclusions and Recommendations (New York: American Institute of Certified Public Accountants, 1978).

2. Collect and analyze the perceptions of these same individuals on whether the potential changes should be made when considering the costs and benefits to society as a whole.
3. Contrast the data in (1) and (2) with the positions taken by the Cohen Report with respect to the potential changes.

Issues to be investigated

The six potential changes in the auditor/client relationship to be investigated are:

1. Rotation of independent audit firms.
2. Disclosure of independent auditor changes in a management report accompanying the financial statements.
3. Adoption of policies on gifts and discount purchases from clients by independent auditors.
4. End executive search and placement services by independent auditors for audit clients.
5. That fees and arrangements for independent auditors to be determined by an audit committee.
6. Government selection and payment of independent auditors.

Hypotheses of the Study

General hypotheses

The general hypotheses for this study are:

1. Ho: There is consensus among AICPA members regarding their perceptions of independence.

   H_1: There is a consensus among AICPA members regarding their perceptions of independence.

2. Ho: There is no consensus among members of the Corporate Bar regarding their perceptions of independence.[2]

   H_1: There is consensus among Corporate Bar members regarding their perceptions of independence.

3. Ho: There is no consensus among members of the Institute of Chartered Financial Analysts (ICFA) regarding their perceptions of independence.

   H_1: There is consensus among ICFA members regarding their perceptions of independence.

4. Ho: There are no differences between members

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[2]Although the entire name is the Section of Corporation, Banking and Business Law of the American Bar Association, for purposes of brevity it is here shortened to Corporate Bar.

of the AICPA, Corporate Bar and ICFA, regarding independence.

H_1: There are differences between members of the AICPA, Corporate Bar and ICFA, regarding independence.

Specific hypotheses

In each of the chapters dealing with data analysis, more specific hypotheses will be given. At that point the hypotheses will be formulated in terms of the separate issues to be investigated. Another level of specialization of the hypotheses will encompass 1) effect on independence and 2) effect on costs/benefits.

Examples of the specific hypotheses follow:

1. H_o-1: There are no significant differences between members of the AICPA, Corporate Bar and ICFA, regarding their perceptions as to the effect that rotation of audit firms will have on the CPA's independence with respect to the CPA's SEC registered clients.

   H_1-1: There are significant differences between members of the AICPA, Corporate Bar and ICFA, regarding their perceptions as to the effect that rotation of audit firms will have on the CPA's independence with respect to the CPA's

SEC registered clients.

2. H_o-3: There are no significant differences between members of the AICPA, Corporate Bar and ICFA, regarding their perceptions as to the costs and benefits to society as a whole, of rotating audit firms for SEC registered firms.

H_1-3: There are significant differences between members of the AICPA, Corporate Bar and ICFA, regarding their perceptions as to the costs and benefits to society as a whole, of rotating audit firms for SEC registered firms.

Independence and the Independent Auditor

This section of the research will look at various uses of the term independence and how the term is to be used in this research. Below is an examination of various uses of the term independence, and its use in this study is made clear.

Defined

As defined by A Dictionary for Accountants, independence is:

> The property of a relation between the accountant and his client (or supervisor) such that the accountant's findings and reports will be influenced only by the "evidence" discovered and

> assembled in accord with the rules and principles of his professional discipline.[3]

Over the years many authors have expressed concern about influences, other than evidence, upon the auditor.

In their 1974 article, Goldman and Barlev analyze three conflicts that can exist to exert influence on a CPA.[4]

1. The auditor-firm conflict of interest.
2. The shareholders-management conflict of interests.
3. The self-interests-professional standards conflict.

For this research we are primarily interested in the auditor-firm conflict of interests. We also are somewhat concerned with the self-interests-professional standards conflict as defined by Goldman and Barlev, as it relates to the possible loss of audit fees.

Increasing the auditor's power

In their article on auditor-firm conflict,[5] Nichols and Price examine a set of procedures that might be used

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[3]Eric L. Kohler, A Dictionary for Accountants, Fourth ed. (Englewood Cliffs, New Jersey: Prentice Hall, Inc., 1970), p. 229.

[4]Airch Goldman and Benzion Barlev, "The Auditor--Firm Conflict of Interests: Its Implications for Independence," The Accounting Review 49 (October 1974):707-718.

[5]Donald R. Nichols and Kenneth H. Price, "The Auditor-Firm Conflict: An Analysis Using Concepts of Exchange Theory," The Accounting Review 51 (April 1976):335-46.

to increase the ability of the auditor to withstand pressure to comply with the firm's demands. The three approaches that they recommend are:

1. Increase the power of the auditor, primarily by increasing the ability of a replaced auditor to cause sanctions to be imposed on the firm resulting from unjustified replacement.
2. Increase the expected cost to the auditor and/or the firm from taking inappropriate actions.
3. Change the structure of the auditor-firm contractual relationship as a means of reducing the firm's discretionary options.

This research deals with each of these procedures at some length.

Conscious and subconscious impairment

In their work[6] Carey and Doherty address the issue of independence:

> It is most important not only that the CPA shall refuse consciously to subordinate his judgment to that of others, but that he avoid relationships which would be likely to warp his judgment even subconsciously in reporting whether or not the financial statements he has audited are in his opinion fairly presented. Independence in this sense means avoidance of situations which would tend to impair objectivity or create

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[6]John L. Carey and William O. Doherty, Ethical Standards of the Accounting Profession (New York: American Institute of Certified Public Accountants, 1966).

> personal bias which would influence delicate judgments.[7]

As can be seen from the above not only must the independent auditor worry about consciously subordinating his judgment to that of others but he must also avoid even the possibility of subconscious subordination of his judgment.

AICPA guidelines

In order to aid in the self-interest-professional standards conflict that Goldman and Barlev discussed, the AICPA has established a set of rules and guidelines to help members avoid possible impairment of their independence. Rule 101 of the Institute's Code of Professional Ethics states:

> A member or a firm of which he is a partner or shareholder shall not express an opinion on financial statements of an enterprise unless he and his firm are independent with respect to such enterprise.[8]

Rule 101 then lists a number of examples in which independence would be considered to be impaired.[9]

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[7]Ibid., p. 19.

[8]American Institute of Certified Public Accountants, Code of Professional Ethics: Concepts of Professional Ethics, Rules of Conduct, Interpretations of Rules of Conduct, March, 1974 ed. (New York: American Institute of Certified Public Accountants, 1974), p. 18.

[9]For further research on situations in which independence might be considered to be impaired see David Lavin, "Financial Statement Users' and Accountants' Perceptions of the Independence of the Auditor in Selected Client-Auditor Relationships," Ph.D. dissertation,

Dimensions of independence

Mautz and Sharaf refer to three dimensions of independence:

1. Programming independence: Freedom from control or undue influence in the selection of audit techniques and procedures and in the extent of their application.
2. Investigative independence: Freedom from control or undue influence in the selection of areas, activities, personal relationships, and managerial policies to be examined.
3. Reporting independence: Freedom from control or undue influence in the statement of facts revealed by the examination or in the expression of recommendations or opinions as a result of the examination.[10]

Impairment of any of these three dimensions of independence should not be allowed by the CPA.

Independence in appearance

Independence must be viewed as a two-fold issue. Arens and Loebbecke deal with both aspects in their

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University of Illinois at Urbana-Champaign, 1974: Ann Arbor, MI: University Microfilms, GAX75-00349, 1975; and David Lavin, "Perceptions of the Independence of the Auditor," The Accounting Review 51 (January 1976):41-50.

[10]R. K. Mautz and Hussein A. Sharaf, The Philosophy of Auditing (Evanston, Illinois: American Accounting Assocaition, 1961), p. 206.

auditing text.

> Not only is it essential that CPAs maintain an independent attitude in fulfilling their responsibility, but it is also important that the user of financial statements have confidence in that independence. These two objectives are frequently identified as independence in fact and independence in appearance. Independence in fact exists when the auditor is actually able to maintain an unbiased attitude throughout the audit whereas independence in appearance is dependent on others' interpretation of this independence.[11]

Using the perceptions of various user groups, this study will analyze the second objective, independence in appearance.

Independence and this research

For purposes of this research, auditor independence is defined as avoidance of situations which would tend to indicate to others that impairment either consciously or subconsciously of one's judgment could take place when there is a conflict or a potential conflict between the CPA and his/her client.

Historical Perspective

Early stages

Little was written about auditor independence before 1930. In 1937, the Securities and Exchange Commission's (SEC) issuance of Accounting Series Release (ASR)

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[11]Alvin A. Arens and James K. Loebbecke, Auditing: An Integrated Approach (Englewood Cliffs, New Jersey: Prentice Hall, Inc., 1976), p. 34.

No. 2[12] stated its position on independence. Although The Journal of Accountancy editorialized on the issuance of ASR No. 2 in its June, 1937 issue,[13] the accounting profession was slow to formalize its views on independence. Not until its yearbook of 1940[14] did the American Institute of Accountants take an official position on the issue of independence.

In the following years, both the SEC and the spokesbody for the accounting profession (first as the American Institute of Accountants and now as the American Institute of Certified Public Accountants) have issued many formal pronouncements and interpretations on the issue of independence.[15]

Problems with public image

A significant change regarding the issue of independence occurred in 1973. Prior to the case of Equity

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[12]United States Securities and Exchange Commission, Accounting Series Releases 1-77 (Washington, D.C.: U.S. Government Printing Office, 1956), p. 3-4.

[13]"Independence of Accountants," Editorial, The Journal of Accountancy 63 (June 1937):409-10.

[14]"Report of the Special Committee on Cooperation with Securities and Exchange Commission," The 1940 Yearbook of the American Institute of Accountants (New York: American Institute of Accountants, 1941), pp. 230-31. The Rules of Professional Conduct as revised January 6, 1941, can also be found in this yearbook on pages 533-34. Independence is briefly referred to in these rules.

[15]See ASR's No's 22, 33, 37, 62, 81, 97, 112, 123, 126, 165 and 194 for SEC positions on independence. See also American Institute of Accountants, Committee on

Funding,[16] there had never been, according to the information of the AICPA, an instance of actual lack of independence on the part of an auditor.[17] Although the entire set of circumstances that led to the demise of Equity Funding may never be known, there are many indications that the auditors did not act with complete independence.

With the issuance of its final report, the Commission on Auditors' Responsibilities cited an instance in which the auditor's independence appears to have been compromised by providing other services.[18] While the AICPA as a whole is not bound by the Commission's findings, it is significant that the Commission did consider the

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Auditing Procedure, "Reference to the Independent Accountant in Securities Registration: Statements on Auditing Procedure No. 22," Journal of Accountancy 79 (June 1945): 465-68; American Institute of Accountants, Executive Committee, "Independence of the Certified Public Accountant: A Statement by the Executive Committee of the American Institute of Accountants." Journal of Accountancy 84 (July 1947):51-53; American Institute of Certified Public Accountants, Committee on Auditing Procedures, Auditing Standards and Procedures: Statements on Auditing Procedure No. 33 (New York: American Institute of Certified Public Accountants, 1963), pp. 20-21; American Institute of Certified Public Accountants, Code of Professional Ethics, pp. 6-9, 18-19, 30-32.

[16]For background on Equity Funding see Wyndham Robertson, "Those Daring Young Men of Equity Funding," Fortune 88 (August 1973):81-85 passim; Harold S. Taylor, "No End to Equity Funding," Banker's Magazine 157 (Spring 1974):51-54.

[17]Per April 18, 1977 conversation with John Mullarkey, Director of Auditing Research for the AICPA.

[18] AICPA, Report, Conclusions and Recommendations, p. 102.

Westec case as an issue of independence.[19]

In addition to these cases, there have been many recent disclosures of illegal political contributions by businesses, and several reports of payoffs (legal and illegal) to foreign dignitaries, and other go-betweens, by multinational firms.[20] No known instances of a lack of auditor independence have been reported in these disclosures. However, since many of these contributions and payoffs were hidden by various accounting/bookkeeping techniques, and were not discovered by the independent auditors (for a number of years in some instances), there was a public outcry for better auditing techniques.[21]

In quick response to the mood of the public, three studies were commissioned, one each by the United States (U.S.) House of Representatives, the U.S. Senate, and the AICPA. Even though none of the studies were co-ordinated, reports were issued by all three groups within a six-month period.

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[19]For background on Westec, see W. Thomas Porter and John C. Burton, Auditing: A Conceptual Approach (Belmont, California: Wadsworth Publiching Company, Inc., 1971), pp. 47-52, 65-66.

[20]"Focus on Peer Review, Illegal Payments and Lawyers' Letters," Statements in Quotes, Journal of Accountancy 141 (May 1976):90-93; "Corporate Corruption What's to be Done," Economist 259 (April 3, 1976):38, 41; "Italian Oil Scandal" Big Deal," Economist 259 (April 17, 1976):86.

[21]Eugene Kozicharow, "Ford Orders Review of Corporate Bribery," Aviation Week and Space Technology 104 (February 16, 1976);15-16; John C. Perham, "Annual Meetings --Dissidents on the Attack," Dun's Review 107 (April 1976): 53-57; "SEC Officials Discuss Disclosure of Payoffs," New Report, Journal of Accountancy 140 (August 1975):14-17.

Moss Report

The House report (Moss Report) was issued in September, 1976,[22] the result of almost two years of investigation. Unlike the reports issued by the U.S. Senate and the AICPA, the Moss Report does not deal with the accounting profession as a major topic. Its main thrust is federal regulation and reform. Chapter two, on the Securities and Exchange Commission, contains the only references to the accounting profession. Generally, the SEC is praised by the report, but the accounting profession is attacked at many points. The concern for the auditor's independence can be seen in the following segment of the report:

> To restore confidence in the system of corporate accountability and to protect the public interest and public investors, the SEC should require to the maximum extent practicable uniform accounting principles and auditing standards, assure that certified public accountants are effectively independent of the corporation being audited, and enforce the corporate disclosure requirements of the federal securities laws stringently.[23] (Underlining mine.)

In reference to the Financial Accounting Standards Board (FASB), the committee said:

> The FASB has accomplished virtually nothing toward resolving fundamental accounting problems

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[22] Federal Regulation and Regulatory Reform: Report by the Subcommittee on Oversight and Investigations of the Committee on Interstate and Foreign Commerce, House of Representatives, 98th Congress, second session, by John E. Moss, Chairman (Washington, D.C.: U.S. Government Printing Office, 1976), pp. 17-54.

[23] Ibid., p. 18.

> plaguing the profession. These include the plethora of optional "generally accepted" accounting principles (GAAPs), the ambiguities inherent in many of those principles, and the manifestations of private accountants' lack of independence with respect to their corporate clients. Considering the FASB's record, the SEC's continued reliance on the private accounting profession is questionable.[24] (Underlining mine.)

In a strongly worded rebuttal letter to the Moss Report, the FASB Chairman, Marshall S. Armstrong, charged that the SEC chapter of the Subcommittee's report is misleading in several ways. Armstrong said that the FASB was not invited to testify before the Committee, but that the Committee relied almost exclusively on the testimony of Baruch College Professor Abraham J. Briloff.[25]

Although no legislation has since resulted from the Moss hearings, hearings were held and Representative Moss spoke out very loudly against the accounting profession.[26]

Metcalf report

Also issued in December, 1976 was the report from the Subcommittee on Reports, Accounting and Management of

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[24] Ibid., pp. 32-33.

[25] "Moss Report Says SEC Should Set Accounting/ Auditing Rules: FASB's Armstrong Issues Rebuttal," Journal of Accountancy 142 (December 1976):26-68.

[26] See "A Wider Public Look at What CPAs Do," Business Week, January 30, 1978, p. 71; and "Moss Hearings," Haskins & Sells: The Week in Review, March 3, 1978, pp. 2-3; "Moss Plans to Introduce Regulatory Legislation," News Report, Journal of Accountancy 145 (April 1978):7-8.

the Committee on Government Operations of the U.S. Senate (Metcalf Report).[27] The Metcalf report is one of the most damning indictments ever presented against the accounting establishment.[28] One of its major conclusions was that the Big Eight accounting firms controlled the AICPA and through that control were able to establish accounting principles.[29] In one phrase (according to the Metcalf report), it could be summarily stated that the entire accounting profession lacks independence.[30]

Reaction to the Metcalf report from the business world and the accounting profession in particular was very strong.[31] An editorial in Business Week concludes:

> Effective accounting standards can be developed only by skilled, independent professionals. There is no place in the system for the heavy

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[27]The Accounting Establishment: A Staff Study Prepared by the Subcommittee on Reports, Accounting and Management of the Committee on Government Operations, U.S. Senate, Ninety-Fifth Congress, Second Session, by Lee Metcalf, Chairman (Washington, D.C.: U.S. Government Printing Office, 1977).

[28]See "The CPAs Get Another Lashing," Accounting, Business Week, January 31, 1977, p. 76; "Why Everybody's Jumping on the Accountants These Days," Forbes, March 15, 1977, pp. 37-43.

[29]This theme pervades the entire report. For some examples see Metcalf, Accounting Establishment, pp. 4-5, 9, 11.

[30]Ibid., p. v.

[31]See for instance: "Hanson Calls Metcalf Staff Report Illogical," News Report, Journal of Accountancy 145 (April 1978):7-8.

> hand of the well-intentioned but politically minded, inexpert bureaucrat.[32]

The AICPA issued a 40 page response that was mailed to all members, giving the AICPA view on the Metcalf report.[33] In the May 1977 issue of the Journal of Accountancy, Chairman Michael N. Chetkovich of the AICPA issued a message to the profession calling the attention of all readers both to the Metcalf report and to the AICPA response to that report.[34]

The Metcalf subcommittee held hearings April-June, 1977. At the end of the hearings the subcommittee recommended that no legislation be initiated at that time. However, it was recommended that a close watch be kept on the accounting establishment to assure members of Congress that the profession was in fact policing itself.

Commission on Auditors' Responsibilities

The third major report concerning the accounting profession was issued in the spring of 1977 by the AICPA's Commission on Auditors' Responsibilities (Cohen Report).[35]

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[32]"Sledgehammer Accounting," Editorials, Business Week, January 31, 1977, p. 175.

[33]American Institute of Certified Public Accountants, The Institute Responds: An AICPA Response to a Study Prepared by the Staff of the Subcommittee on Reports, Accounting and Management of the U.S. Senate Committee on Governmental Affairs (New York: American Institute of Certified Public Accountants, 1977).

[34]Michael N. Chetkovich, "A Message to the Profession," Journal of Accountancy 143 (May 1977):5.

[35]American Institute of Certified Public Accountants, Commission on Auditors' Responsibilities, Commission on Auditors' Responsibilities: Report of Tentative Conclusions (New York: American Institute of Certified Public Accountants, 1977).

The Commission on Auditors' Responsibilities had been commissioned in October of 1974. A major portion of the Report of Tentative Conclusions dealt with the issue of independence.

The Commission solicited written comments from any interested parties and held hearings on the Report of Tentative Conclusions in Washington, D.C. in June, 1977. The Commission issued The Commission on Auditor's Responsibilities: Report, Conclusions and Recommendations in February, 1978. The findings of this research will be compared with this final report.[36]

Commission on Auditors' Responsibilities Reviewed

General comments

As stated above, The Commission on Auditors' Responsibilities: Report, Conclusions and Recommendations, is the focus for this research. The six issues to be researched were drawn from Section 9 of this report. These are not the only six issues, nor even the six most important, but rather the ones on which this researcher wishes to focus. The reasons for the inclusion of these specific items are examined in greater depth below.

It should be noted that often the Commission on Auditors' Responsibilities investigated a particular topic,

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[36]The Report of Tentative Conclusions was the original impetus for this research. Revisions in the independence section were minor.

and then deemed no recommendation necessary. Consequently, many more issues have been investigated than just those about which recommendations have been made. Where no recommendation is made the Commission has in effect decided to maintain the status quo.

As this research relates only to the issue of independence and not to the broader issues covered in other sections of the report, the remarks here will be restricted to Section 9 of the report, entitled, "Maintaining the Independence of Auditors."

Areas Not to be Researched

Other services

When dealing with other services, the Commission made three recommendations summarized below:[37]

1. When a specialist employed by an accounting firm performs original specialized services for an audit client, the need to perform comprehensive audit procedures directed at those services is not eliminated.
2. The board of directors (or its audit committee) should consider whether they wish to engage their independent auditors for other services or retain other firms for such purposes.

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[37]AICPA, Report, Conclusions and Recommendations, pp. xxviii-xxix.

3. If management fails to disclose the nature of other services provided to the company by its independent auditor, in the management report accompanying the annual financial statements, the auditor should make appropriate disclosure in his report.

Management services

It was discovered that a minority segment of financial statement users view management services as potentially reducing the auditors' independence. The lack of empirical evidence to support this contention was cited by the Commission when they made no recommendation for change in the current handling of management services.[38]

Tax services

Of greater concern than management services was the potential conflict involving tax services performed by the independent auditor. Termed "tax advocacy," this problem is very persistent in smaller non-public businesses. The Commission suggested that their guidelines in Section 10 for restructuring the Auditing Standards Division of the AICPA would provide a solution for these problems associated with smaller clients.[39]

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[38]Ibid., p. 96.

[39]Ibid., pp. 98-99.

Advice on accounting principles

The Commission also examined advice on accounting principles. The final report recommended that in all advocacy engagements, due care should be exercised to make clear to the users that the auditor's work and opinions are not presented in his capacity as an independent auditor.[40]

None of these three other services will be researched due to the volume of literature and research already available on these topics.

Appointment of directors

The Commission recommended appointment of outside directors and audit committees where appropriate.[41] Few if any guidelines were given to distinguish what was appropriate. Consequently this topic is not included in this research.

Time-budget pressures

A new concern which has not been in the literature (at least supported by empirical research), is the concept of time-budget pressures on auditors. Research done for the Commission and its report indicated many areas where time-budget pressures seemed to inhibit independence, including:

1. Deadlines for completion of audits.

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[40]Ibid., p. 100.

[41]Ibid., p. 106.

2. Excess price competition.

3. Early release of earnings information before the completion of the audit.[42]

Much of Section 9 is devoted to the issue of time-budget pressures. Although this topic is a new and exciting one, it is not included here because of the study for the Commission just completed by John Grant Rhode,[43] and a dissertation on the topic in progress. After the dissemination of Ms. Sharon Douglas' research,[44] the area will be an extremely important one for additional exploration.

Areas to be Researched

Each of the following six issues is dealt with in a separate chapter. Each chapter consists of a literature review on the topic and findings of this research compared with prior research and the Cohen Report recommendations.

The order of the following items as well as the order of chapters four through nine is consistent with the order of the questions on the final questionnaire.

Rotation of auditors/firms

Citing the high cost of mandatory rotation of audit firms and the loss of benefits that result from

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[42]Ibid., pp. 108-109.

[43]John Grant Rhode, "The Independent Auditor's Work Environment: A Survey," Commission on Auditors' Responsibilities Research Study No. 4 (New York: American Institute of Certified Public Accountants, 1978).

[44]Sharon Douglas completed a Ph.D. dissertation at The University of Oregon on this topic.

interrupting a continuing relationship, the Commission recommended that rotation of firms should not be required. The Commission recommended that an audit committee would be in the best position to inspect the personnel rotation plan of the independent auditor and decide if it would be appropriate, to rotate firms.[45] Despite much previous writing and research on this topic, its importance warrants its inclusion here.

<u>Changes in auditors</u>

When discussing changes of auditors, the Commission has determined that disclosure comparable to that required by the SEC in ASR No. 165[46] should be included in the report by management which would accompany all audited financial statements.[47] This topic also has been selected for this research.

<u>Policies on gifts and discounts</u>

Stating that the acceptance of gifts or special favors from clients is incompatible with the maintenance of an attitude of independence, the Commission recommended

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[45]AICPA, <u>Report, Conclusions and Recommendations</u>, pp. 108-109.

[46]United States Securities and Exchange Commission, "Notice of Amendments to Require Increased Disclosure of Relationships between Registrants and Their Independent Public Accountants," <u>Accounting Series Release No. 165</u> (Washington, D.C.: U.S. Government Printing Office, 1974).

[47]AICPA, <u>Report, Conclusions and Recommendations</u>, p. 108.

that all audit firms develop for their staffs carefully drawn rules on these matters. Furthermore, the Commission recommended that the AICPA should provide more definitive guidance on what amounts of client gifts or favors can be considered "token."[48] This topic is included in this research.

Executive search and placement

The Commission suggested it would be impractical to recommend that companies be prevented from hiring individuals previously employed by public accounting firms. It did suggest that firms should not engage in recruiting or placement of individuals who would be directly involved in the decision to select or retain independent auditors.[49]

Fees and arrangements for independent auditors

The Commission stated that the boards of directors and/or their audit committees should take an active enough role in total arrangements for the audit to assure that costs versus quality decisions are made in a manner that does not sacrifice audit quality. The Commission recommended that the arrangements for the auditor should be made by both management and the board of directors and that the final decision should be based on the board's

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[48] Ibid., p. 121.

[49] Ibid., pp. 100-101.

decision, not management's.[50] This research does explore this question, specifically in relation to determination of fees and arrangements for the independent auditor by an audit committee.

Government selection and payment of independent auditors

Discussing the regulation of the accounting profession, the Commission concluded that the present structure of a private profession regulated by a combination of private and governmental efforts, including the courts and the SEC, does not require drastic change. Consequently the Commission rejected proposals to improve independence that involved substantial changes in the nature of the private profession and its relationships with its audit clients such as governmental selection or payment of auditors.[51] Because of the current climate of both the House and the Senate of the U.S. Congress, this topic was included in the research to investigate, once again, the possibility of governmental selection or payment of auditors.

Limitations of Study

Since the issue of independence always rests on the perceptions of the user, the most obvious limitation

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[50] Ibid., pp. 106-107.

[51] Ibid., p. 105.

of the purposed study is the selection of the groups to represent the users. No one has yet adequately identified the "users" referred to in the official pronouncements of the various ruling bodies of the accounting establishment. However, the author believes that the groups selected for this study comprise an important segment of the users.

Another limitation is found in the use of a questionnaire. The usual cautions for a questionnaire study will apply here as well. Steps have been taken to counter the potential problems of questionnaire research. However, at some points the author must allow the reader to make his/her own evalution of the data. This step will permit the reader to make generalizations which will have practical significance within the context of her/his own experience.

Finally, although the Cohen Report makes many recommendations, and touches on many other issues upon which no recommendations are made, this study deals with only six independence issues, and more specifically almost exclusively with Chapter 9 of the Cohen Report. More research is needed in the other areas of the Cohen Report as well as follow up research to this particular study.

Organization of the Study

The study is organized into ten chapters. Chapter One introduces the objectives of the study, provides an overview of the concept of independence, by examining existing research, and sets out the reasons for the study. The Cohen Report is reviewed with respect to the issue of independence. The research methodology and accompanying strengths and limitations are discussed, and finally the hypotheses of the study are set forth.

Chapter Two examines in-depth the empirical studies of the issue of independence. Although in each case, a brief overview of the entire study is provided, particular emphasis is placed on the aspects of the studies that relate directly to this research.

Chapter Three discusses the data gathering instrument. The development of the mail questionnaire is reviewed, and results of the field testing presented. Populations in general, the samples selected, and the method of sample selection, are discussed. Last, the details of administering the final questionnaires are reviewed.

Chapters Four through Nine summarize and analyze the results of the questionnaire responses and contrast them with the studies discussed in Chapter Two and the Cohen Report, as well as other pertinent literature, which is reviewed in each chapter. Each question is studied individually and both raw data and statistical analyses are presented.

Chapter Ten presents a summary of the findings and draws conclusions based on the research data presented in the study. Suggestions for future research are also included.

CHAPTER II

EMPIRICAL STUDIES OF INDEPENDENCE

Introduction

The purpose of this chapter is to review the literature on empirical studies of the issue of independence in order to aid the reader's understanding of what has been done recently in the area. Whenever a particular investigation examines any of the six issues under specific study in this research, its findings on that particular question will be analyzed for later comparison with the recommendation, or lack of recommendation, of the Commission on Auditors' Responsibilities, and with the findings of this research. With the exception of the Rosenbaum dissertation, all of these studies reviewed have been summarized at least once in public pronouncements or accounting journals.

John Grant Rhode

The most recent empirical study under review was done by John Grant Rhode of the University of California at Berkley,[1] a survey done at the request of the Commission

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[1]John Grant Rhode, "The Independent Auditors' Work Environment: A Survey," Commission on Auditors' Responsibilities Research Study No. 4 (New York: American Institute of Certified Public Accountants, 1978).

on Auditors' Responsibilities.

Primary research issues

Rhode's work was designed to see whether the auditor's pressures from time budgets and worries about advancement and survival on the job was affecting the integrity and objectivity of auditors. If this were happening, then the CPA's independence must be impaired.

Although many areas of the auditor's work environment are investigated by Rhode, those relevant to this research study the understanding of auditor's responsibilities, adequacy of the scope of audits, quality control and personnel policies (including the issue of gifts and discount purchases from the client to the CPA), and non-auditing services.

Research methodology

Rhode used a questionnaire with a prescreening to limit the nonresponses, and to assure that the samples had the desired ratio of long-time workers to new workers. The samples were selected from the membership rolls of the AICPA.

Major findings related to this research

A substantial majority of the subjects do not believe that consulting work performed by CPA firms affects the independence of auditors by contributing to substandard audit performance. However, a very low number of the subjects state that there is pressure from supervisors to accept the representations by former members of their CPA firm now employed by the client, or from those individuals placed with the client following an executive search by their firms.[2]

Another area of concern is the acceptance of gifts from clients and purchase of client products at discounts not available to the general public. Whether or not such activities cause an actual loss of independence, it is likely that such activities may lead others to believe that independence has decreased. A majority of the respondents feel that the acceptance of gifts affects an auditor's ability to resist pressures to subordinate professional judgment. Seventy-six percent of the respondents agree either that there is always an effect, or that there is an effect depending upon the scale of the gift. A majority of the respondents (57 percent) also believe that purchases at discounts not available to the public adversely affect an auditor's ability to resist pressure to subordinate his or her judgment.[3]

Although many other findings relate to the issue of independence in the Rhode research, time and space do not allow for a presentation of all of them here. The findings cited above are those most relevant to this

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[2]Ibid., pp. 299-300.

[3]Ibid., pp. 99-102.

research.

Wai P. Lam

At Michigan State University in 1974, Wai P. Lam completed work for his dissertation concerning corporate audit committees in Ontario, Canada.[4] Lam's research was designed to investigate corporate audit committees which had come to be required of Ontario corporations.

Research methodology

With a questionnaire, four populations were queried about corporate audit committees. The first two populations include chief executive officers and audit committee members of 178 companies listed on the Toronto Stock Exchange and required to have audit committees. The third population consists of practicing chartered accountants who had had direct experience with audit committees. Last, financial analysts were selected from the 1973 Membership Directory of the Toronto Society of Financial Analysts.[5]

Major conclusions

The findings most pertinent to this research are:

1. The proportion of company officers on their own audit committees is less than 30 percent.

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[4] Wai P. Lam, "Corporate Audit Committees in Ontario, Canada: An Empirical Study" (Ph.D. dissertation, Michigan State University, 1974).

[5] Ibid., pp. 52-61.

2. The majority of all four sets of respondents feel that management representation on audit committees was desirable.

3. Prior to 1971 (the requirement in Ontario for audit committees came into effect in 1972), only 6 of 101 companies reported that they had an audit committee.

4. The three most important functions of audit committees are regarded as:

   a. Review with the independent auditors on completion of the audit, their experience, any restrictions on their work, cooperation received, their findings, and their recommendations.

   b. Review with the independent auditors of their evaluation of the company's internal control systems.

   c. Review of the corporate annual financial statements before their submission to the Board of Directors for approval.

5. The three functions ranked as the most important are performed effectively by most of the audit committees.

6. The five contributing factors for an effective audit committee in their order of importance are:

   a. Competence of the audit committee members.

b. A set of well established committee objectives.

c. Full support and cooperation of corporate chief executive officer.

d. A set of well-established functions of the committee.

e. Full cooperation and support of the Board of Directors.

7. In general, the audit committee plays an important role in resolving a large number of the major disagreements between the external auditors and the management of the corporation.

8. One of the principal benefits of an effective audit committee is that it reinforces the independence of the corporation's external auditor.[6]

Relationship to current research

The respondents in the Lam study clearly feel that audit committees did work. Also clear is that they feel the committee's relationship with the external auditors is of major importance to the audit committee.

Mautz and Neumann

Published by the Bureau of Economic Research of the University of Illinois, this research investigates in

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[6]Ibid., pp. 175-180.

great depth the effectiveness of corporate audit committees and is summarized in the Harvard Business Review.[7]

Research methodology

Using both questionnaires and interviews, Mautz and Neumann sampled chief executive officers, non-officers directors, independent CPAs, and internal auditors. The questionnaires mailed to independent CPAs and internal auditors were a small portion of the total; the majority went to chief executive officers and non-officer directors. Interviews accounted for less than 5 percent of the questionnaires mailed.[8]

Major findings related to this research

Although most of the research examines the makeup of boards, the duration of their existence, and various operating approaches used, the authors do investigate the question of independence as well. Although not citing data to support their contention, the authors suggest that an audit committee adds an element of discipline salutary to a CPA's performance, an element which strengthens his status independent of management.[9]

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[7]Robert K. Mautz and F. L. Neumann, "The Effective Corporate Audit Committee," Harvard Business Review 48 (November-December 1970):57-65.

[8]Ibid., p. 58.

[9]Ibid., p. 65.

David Lavin

David Lavin's work was completed in 1974 as a part of his Ph.D. program at the University of Illinois.[10]

Primary research issue

The main thrust of the research compares the requirements of the AICPA Code of Professional Ethics with the position that the SEC took when it put into effect Accounting Series Release No. 126, released in July, 1972.

The purpose of the research is to provide empirical evidence on the existence of differences in opinion regarding the concept of independence either among accountants, or between accountants and financial statement users; and to determine whether the financial statement user's perception of the auditor's independence, or lack of it, has any effect on his/her business decision.

Research methodology

Twelve situations involving CPAs and their clients are used as the basis for a questionnaire. Each of these twelve situations is included in ASR No. 126. The questionnaire was mailed to three samples.

The first sample consists of Certified Public Accountants selected from the 1972 AICPA List of Members.

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[10] David Lavin, "Financial Statement Users' and Accountants' Perceptions of the Auditor in Selected Client--Auditor Relationships" (Ph.D. dissertation, University of Illinois at Urbana-Champaign, 1974; Ann Arbor, MI: University Microfilms, GAX75-00349, 1977).

The second sample includes banks selected from the 1972 Polk's Directory of Banks. The third sample includes brokerage houses selected from the July 1972 issue of Finance.[11]

Major Conclusions

None of the situations cited in Lavin's research are directly comparable to the seven independence issues examined in this research. Although the respondents do not concur entirely either with the AICPA or the SEC, they do seem to agree more with the AICPA than the SEC. Also noteworthy is that, with the exception of one question, the CPAs agree with the financial statement users represented by the loan officers and research financial analysts.[12]

Regarding the financial decision, the research refers to the lending decision of a loan officer and to the investment decision of research financial analysts. The study examines only one independent variable in detail: the effect a financial decision maker's perception of an auditor's independence was on his financial decision. Those respondents who perceive the auditor to be lacking in independence tend to consider that this situation would somewhat impair a financial prospect. Conversely, those respondents who perceive the auditor to

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[11]Ibid., pp. 79-81.

[12]Ibid., pp. 130-35.

be not lacking in independence tend to consider that this situation would not affect, or would somewhat improve, a financial prospect. Research Financial Analysts perceive the auditor's independence as having less of an effect on their investment decision than do loan officers.[13]

Bedingfield and Loeb

Primary research issue

This research was undertaken to investigate the reasons that firms changed independent auditors.

Research methodology

Using the period of November 1971 to February 1973, Bedingfield and Loeb analyzed 250 instances of companies changing auditors.[14] The 250 instances were gleaned from 8-K Reports and letters of the registrants and their prior auditors which were filed with the SEC, as mandated by the amendment to the Securities and Exchange Act of 1934 effective October 31, 1971.

In their analysis of the auditor changes, the authors note that more firms changed from national firms to non-national firms than from non-national firms to national ones. This does not suggest displacement of the smaller

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[13] Ibid., pp. 163-64.

[14] James P. Bedingfield and Stephen E. Loeb, "Auditor Changes an Examination," Accounting and Auditing, Journal of Accountancy 137 (March 1974):66-69.

firms to the advantage of the national firms as often suggested.[15] Using a questionnaire, the researchers attempted to discover the reasons that the companies noted changed auditors.

Major findings related to this research

The reason most often cited for change is that the prior auditor's fee was too high. Forty-seven percent of the respondents cite this as a reason for changing auditors. The reason most often cited next is dissatisfaction of the firm with the services provided by the auditors.[16] Relevant to this research despite its low frequency of occurrence is the reason given by 11 percent of the respondents: that they disagree with the auditors on certain accounting matters. Although the researchers do not discuss the issue of independence, changing auditors due to disagreement on accounting matters does relate to the issue of independence. An extremely small number (2 percent) suggest that they felt that they might get better service if they rotated auditors.

Dermer, Evans, and Pick

Done in Canada, this study investigates the compatibility of auditing and management services.[17]

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[15] Ibid., pp. 66-69.

[16] Ibid., p. 68.

[17] Jerry Dermer, Martin G. Evans, and Thomas J. Pick, "The Compatibility of Auditing and Management Services," Canadian Chartered Accountant 90 (January 1971):20-25.

Research methodology

Using the questionnaire approach, the researchers solicited the perceptions of seven groups of third parties who rely on audited statements in making investment and credit decisions. The seven groups are: (1) brokerage firms, (2) investment counselors, (3) mutual funds, (4) the government (municipal and federal), (5) trust companies, (6) insurance companies, and (7) banks. Questionnaires were sent to salesmen, portfolio managers, research analysts, underwriters and traders.[18]

Major conclusions

None of the findings of this study relate directly to the current research, but rather to other particular areas of the issue of independence.

Sixty percent of the respondents had never even considered the potential incompatibility posed by the dual practice of auditing and management consulting. A like number of the third parties respond that their confidence in audit independence would in no way be affected, while 26 percent indicate a lessening of confidence, and 14 percent remained undecided.[19]

Noting that several respondents voluntarily indicate that the size of the Chartered Accountant firm is an

[18]Ibid., pp. 20-21.

[19]Ibid., p. 23.

important factor in judging the compatibility of management services and audit independence, the authors theorize that specialization and separation of the services as done now in the larger and better-known firms in Canada may provide a protection for the professional image of the auditor.

Pierre L. Titard

In this research Titard investigates the issue of independence and management advisory services.[20]

Research methodology

Questionnaires were mailed to financial analysts and executives: banks, brokerage firms, mutual funds, closed-end investment companies, life insurance companies, and property liability insurance companies representative of the nation's largest financial institutions. The sample is not random, nor is it meant to be. It includes only the largest financial institutions in the nation.[21]

Major conclusions and relationship to this research

Of particular interest to this research is the fact that executive recruitment is mentioned on 27 percent of the respondents' surveys. This is the second highest

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[20] Pierre L. Titard, "Independence and MAS: Opinions of Financial Statement Users," Journal of Accountancy 132 (June):47-52.

[21] Ibid., p. 48.

frequency and is surpassed only by mergers and business acquisitions work.[22]

Although Titard concludes that there is no great concern over auditing and MAS, 49 percent of the respondents feel that at least one of the 33 services listed, if combined with auditing, can inhibit independence. No item receives more than 3 percent of the respondents' consideration.[23]

Other observations include:

1. It may be advisable for the AICPA to provide information to members of the financial community in order to inform them as to what the accounting profession expects of CPAs who render MAS.
2. Third parties are more concerned about some of the accounting-type services than they are about some of the nonaccounting-type services. To automatically exclude accounting-oriented services as having no potential effect on independence, as often done in the past, is erroneous.
3. Since our society, as well as our profession, is ever-changing, this should not be the final research on this topic.[24]

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[22]Ibid., p. 50.

[23]Ibid., pp. 50, 52.

[24]Ibid., p. 52.

Allan Seymour Rosenbaum

Rosenbaum's research was for his dissertation for the Ph.D. from the University of Illinois in 1968.[25]

Primary research issue

Regarding the issue of tax practice and independence, the research tests the hypothesis that the simultaneous practice of auditing and tax consulting for the same client impairs the independence of the CPA.[26]

For purposes of the research, tax practice is divided into four categories: (1) tax planning, (2) return preparation and filing, (3) investigation, and (4) litigation.[27]

Major conclusions

None of the conclusions in this study are directly related to the current research, but rather relate to other particular areas of the independence issue.

Tax planning for an audit client by a CPA is found to be compatible with maintaining independence. Return

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[25] Allan Seymour Rosenbaum, "The Implications of the Concepts of Independence and Advocacy in Tax Practice for Certified Public Accountants," (Ph.D. dissertation, University of Illinois, 1968).

[26] Allan Seymour Rosenbaum, "The Implications of the Concepts of Independence and Advocacy in Tax Practice for Certified Public Accountants," Dissertation abstracts International: Humanities and Social Sciences 30 (Ann Arbor: University Microfilms, 1969):4-A, 5-A.

[27] Ibid., p. 4-A.

preparation and filing also do not cause any problems, with the possible exception of the lack of agreement between the tax liability per audit and per tax return. Regarding tax investigation, it is determined that a CPA who represents his client in an administrative hearing becomes an advocate of his client. The researchers conclude that in order to maintain independence in the area of tax practice as far as tax investigation and litigation are concerned, the limits are set at the informal conference. Action beyond that limit is the action of a partisan advocate, not an independent objective third party.[28]

Abraham J. Briloff

This study investigates many areas of responsibility for the CPA. It is not designed to examine one area of public accounting in isolation.

Research methodology

The research consists of a questionnaire of approximately 200 questions from which 136 responses were received. The responses are approximately evenly distributed between the financial community, consisting primarily of investment analysts with the brokerage firms, banks and mutual funds and insurance companies, and the accounting profession, consisting of CPA firms of all sizes and professors of

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[28] Ibid., p. 5-A.

accounting.[29]

Major conclusions

None of the conclusions bear directly on the current research, but one area does deal with another question related to independence. It is concluded from the data that management services should not be offered by CPA firms. Briloff is careful to note that he uses the term "management services," and not "management consulting."[30]

Also of interest is the fact that if the inquiry were restricted to practitioners with "Big-Eight" firms, and excluded the users of the financial statements, as well as practitioners with other firms and professors of accountancy, respondents do believe that such services should be offered. There is a difference between the opinions of those respondents working for "Big-Eight" firms and other respondents.[31]

Arthur A. Schulte, Jr.

This study is designed to examine the opinions of representatives of user groups of accounting data on the necessity of independence, and then to investigate the relationship of management consulting and audit

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[29]Abraham J. Briloff, "Old Myths and New Realities in Accountancy," The Accounting Review 41 (July 1966): 484-495.

[30]Ibid., p. 493.

[31]Ibid., pp. 493-94.

independence.[32]

Research methodology

Using questionnaires, Schulte solicited the perceptions of four groups: (1) research and financial analysts of brokerage firms; (2) commercial loan and trust officers of banks; (3) investment officers of insurance companies (both life and fire casualty); and (4) investment officers of domestic mutual funds.

In setting up his various groups, Schulte randomly selected banks and brokerage houses. In addition, the largest banks and largest brokerage houses were represented in a non-random fashion.

Major conclusions

None of the conclusions in this study are directly related to the current research, but rather relate to other particular areas of the issue of independence.

Studying the issue of independence, Schulte first determines that a large majority of the respondents feel that independence is absolutely necessary. His second set of findings draws conclusions about the relationship of management consulting and audit independence.

His analysis shows that those respondents from the largest banks and brokerage houses are much less concerned

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[32] Arthur A. Schulte, Jr., "Compatibility of Management Consulting and Auditing," The Accounting Review 40 (July 1965):587-93.

with the effect of management consulting on independence than are the randomly selected respondents. This difference is explained by the fact that the respondents from the largest banks and brokerage houses tend to deal with the larger CPA firms where auditing and management services are performed by separate staffs.[33]

Generally, Schulte finds that the large CPA firms can afford a special, qualified, separate staff for their management services function, and are less likely to impair the independent auditor status than are the smaller firms in which such specialization is neither possible nor feasible.[34]

Summary

As can be seen from the chapter, although there has been much study of independence, very little is directly relevant to this research. Because so many areas of accounting are connected to the issue of independence, it will take time to establish a substantial and inclusive body of empirical research.

Perhaps the intangibility of the issue of independence discourages attempts at investigation because of the time and inconclusiveness involved. However, the foregoing review of the literature shows the real need not only for this study but for others like it.

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[33]Ibid., p. 591.

[34]Ibid.

CHAPTER III

DATA: SOURCES, CHARACTERISTICS AND PROCEDURES FOR GATHERING

Introduction

This chapter discusses the populations in general and the samples selected in particular. Second, the administration and results of the pilot study are discussed. Third, the completed questionnaire is reviewed. Finally, the procedures used to mail the final questionnaires are presented with a breakdown of respondents.

Populations

In selecting the population for this study, several important considerations were taken into account:

1. The members of the populations should be familiar with the work of CPAs as auditors, and with their relationships with clients.
2. The populations should be clearly definable.
3. The researcher must be able to obtain a complete listing of each of the populations to be used.

All three populations selected (CPAs, Corporate Bar Members, CFAs) meet the above criteria.

The first population selected consisted of AICPA members. The population is listed in the 1976 Directory of Members.[1]

Since the study deals with CPAs, they are, properly, one of the populations queried as to perceptions of auditor independence. The AICPA has been referred to as the major standard-setting body for accounting[2] and the most important private group affecting the practice of accounting.[3] For these reasons the AICPA membership directory is regarded as a fair representation of the CPA population.

The second population is composed of CFAs who are members of the ICFA. This population is listed in the Twelfth Directory of the ICFA[4] and the 1975[5] and 1976-1977[6] supplements to the 1976 membership directory.

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[1]American Institute of Certified Public Accountants, _1976 Directory_ (New York: American Institute of Certified Public Accountants, 1976).

[2]_Federal Regulation and Regulatory Reform_, Moss, p. 31.

[3]_Accounting Establishment_, Metcalf, p. 9.

[4]The Institute of Chartered Financial Analysts, _Twelfth Directory of Members_ (Charlottesville, Virginia: The Institute of Chartered Financial Analysts, 1975).

[5]The Institute of Chartered Financial Analysts, _1975 Membership Directory Supplement_ (Charlottesville, Virginia: The Institute of Chartered Financial Analysts, 1975).

[6]The Institute of Chartered Financial Analysts, _1976-77 Supplement of 1975 Membership Directory_ (Charlottesville, Virginia: The Institute of Chartered Financial Analysts, 1976).

The CFA population was slightly more difficult to contact since its 1975 directory has not been kept up-to-date. The supplements included only additions to and not deletions from the membership listing after the 1975 Directory was issued. Address corrections for members listed in the 1975 Directory were maintained by the ICFA but were not published in the supplements. Although this was not a significant problem, it did increase the percentage of questionnaires returned as undeliverable.

The third and final population consisted of members of the Section of Corporation, Banking and Business Law of the American Bar Association drawn from their 1974-1975 Membership Directory.[7] Although the Directory is titled 1974-1975, the data are from 1974. Consequently, this population had the largest number of returns due to invalid addresses.[8]

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[7]Section of Corporation, Banking and Business Law of the American Bar Association, 1974-1975 Directory (Chicago: Illinois: Section of Corporation, Banking and Business Law of the American Bar Association, 1974).

[8]It should be noted at this point that some members of the Corporate Bar do not meet criterion 1 as well as do most CPAs and CFAs. The reason lies in the procedure by which an individual becomes a member of the Corporate Bar. Any individual who is a member of the American Bar Association can become a member of the Corporate Bar simply by submitting a fee and requesting to be included in the Corporate Bar membership. As a result, many lawyers who do not practice in the financial world may be members of the Corporate Bar for purposes of trying to keep in touch to some degree with the business world, either for themselves or for their firms. Consequently, a lawyer may have little or no contact with the financial world but still be a member of the Corporate Bar. In contrast to

Although the members' addresses from the Corporate Bar appear to be less than current, it was felt that this population should be used. The reason for using a 1974-1975 directory, was that no more recent directory has been published. After contacting the Section of Corporation, Banking and Business Law, it was discovered that the Section ceased publishing the directory. Due to increasing costs, the Section of Corporation, Banking and Business Law has cased publishing the directory, so that listings more recent than 1974-1975 are not available. In addition, those in charge of the membership rolls of the Section indicate that a future directory is unlikely. The decision of the Section not to publish directories makes the sample even more important than it was first thought, since, as years pass, unbiased sampling of the population will become more difficult as address listings grow increasingly obsolete.

Samples for the Study

From each of the three populations, a randomly selected sample of 200 subjects was drawn, using a Touche Ross Timesharing Program.[9] Each sample was reviewed for

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this situation, most CFAs and CPAs are very much involved in the financial world. This matter was of some concern to the researcher. However, review of the returned questionnaires showed that, for the most part, the responding Corporate Bar members were in touch with the issue at hand.

[9]Touche Ross & Co., Statistical Sampling Timesharing Programs (New York: Touche Ross & Co., 1975), pp. 1-16.

any noticeable bias. No indicators were noted that might suggest a non-random sample in any of the three populations.

Data was available to compile a breakdown of CPAs over the various firm size categories (national, regional, local firms and other categories). Since the Metcalf report referred continually to the "Big Eight," and the next seven largest firms,[10] an important part of the research would be to contrast responses from those who are employed by the "Big Fifteen" and those who work for other CPA firms.[11]

A recent marger has reduced the "Big Fifteen" to the "Big Fourteen."[12] This study deals with the distribution of firms as it existed when the data were collected. The distribution of the sample of CPAs did not vary markedly from the distribution of CPAs throughout the AICPA membership regarding firm size. A distribution of the sample is presented in Table III-1.

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[10]The largest eight ("Big Eight") are: Arthur Andersen & Co.; Arthur Young and Company; Coopers and Lybrand; Ernst & Ernst; Haskins & Sells; Peat, Marwick, Mitchell & Co.; Price Waterhouse & Co.; and Touche Ross & Co. The next seven largest are: Alexander Grant & Co.; Hurdman and Cranstoun; J. K. Lasser & Co.; Laventhol & Horwath; S. D. Leidesdorf & Co.; Main Lafrentz & Co.; and Seidman and Seidman.

[11]For some examples of references to the "Big Fifteen," see: Accounting Establishment, Metcalf, pp. 29, 84, 85.

[12]"Merger of Lasser and Touche Ross is Announced," The Wall Street Journal (August 23, 1977), p. 4.

TABLE III-1

SAMPLE BREAKDOWN OF CPAS BY FIRM SIZE

	Sample		Membership[a]	
	#	%	#	%
"Big Eight"	35	17.5	17,400	15
"Next Seven"	8	4.0	9,254[b]	8[b]
Other	157	78.5	91,041	77
Total	200	100.0	117,695	100

[a]These numbers are estimates by the Metcalf Committee. See: Accounting Establishment, Metcalf, pp. 85-86.

[b]As these numbers are for firms 9-25 in size, one might extrapolate that approximately one-half would be accounted for by the "Next Seven," or firms 9-15 in size.

The CFA sample was segmented by industry representation using ICFA classification codes. A comparison of the percentages of the two columns shown in Table III-2 show them to be similar. The large portion of the sample living in New York City, New Jersey, Boston, Chicago and Los Angeles was consistent with the residence profile of the entire membership listing.

Due to the nature of the membership directory for the Section on Corporation, Banking and Business Law, no analysis of job classifications was possible.

TABLE III-2

BREAKDOWN OF CFA SAMPLE AND POPULATION[a]

ICFA Industry Classification	CFA Sample		CFA Population	
	#	%	#	%
Brokerage & Investment Banker	64	32.0	1190	28.67
Investment Company	15	7.5	269	6.48
Investment Counselor	27	13.5	807	19.45
Trust Company or Trust Department of Commercial Bank	39	19.5	881	21.23
Insurance Company	15	7.5	456	10.99
Pension Fund	12	6.0	180	4.34
Other	28	14.0	367	8.84
Total	200	100.0	4150	100.00

[a]Source: The Institute of Chartered Financial Analysts 1976-77 Supplement to 1975 Membership Directory (Charlottesville, Virginia: The Institute of Chartered Financial Analysts, 1976), p. 25.

Field Testing the Questionnaire

The sample used for field testing the questionnaire was arbitrarily selected from a circle of friends and acquaintances. Each was chosen for his individual expertise in a specific area or areas such as accounting, grammar, questionnaire structure, data collection and analysis, and general readability. The sample of thirty-five selected for the field testing included CPAs, CFAs, Lawyers, and faculty members from several universities.[13]

The cover letter of the field questionnaire requested as many comments as possible; two lined pages were supplied to encourage these comments. Readers were also requested to edit the questionnaire as they deemed appropriate. Thirty-five questionnaires were mailed out for field testing; twenty-five were returned. The poorest return rate was from CFAs and CPAs. However, this problem was lessened greatly by the many faculty members responding who were either CPAs or CFAs, since they gave valuable comments specifically related to the two populations.

The questionnaire was revised in light of the comments and suggestions from the field testing. Although many changes were made from the field questionnaire to the finished questionnaire, most major changes affected the descriptive or factual information requested from the respondent rather than the attitudinal questions. Due to the responses to the field testing, all open-ended questions were dropped, with the exception of a full page set aside for comment by the respondent on any part of the questionnaire. Most important, because of the well-known comments on the issue of independence made in the Report

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[13]Faculty members represented The University of California at Berkeley, Miami University, Michigan State University, New York University and The University of Texas at Austin.

of the Commission on Auditors' Responsibilities, all references to the Commission were dropped from the final questionnaire to avoid bias. The descriptive questions were arranged differently; for easier reading, wording was adjusted. Only minor changes in wording, for the sake of clarity, were made in the attitudinal portion of the questionnaire (one page in length). With the above changes, the final questionnaire was considered satisfactory to provide data for the research goals. Copies are included as Appendix A.

The Final Questionnaire

The final questionnaire was developed with several considerations in mind: a strong desire to keep to a manageable length both the number of pages and the number and length of the responses required.

The final questionnaire had three pages, since, probably, this length would be most likely to elicit response upon receipt. CPAs, CFAs, or Corporate Bar members, respectively, received different versions of page one. The second and third pages were the same in all questionnaires. Page three was simply an open-ended request for comments on any of the subjects in the questionnaire.

It was likewise felt that the responses required should be kept to a reasonable number. Fifty responses, or fewer, was the goal for the number of responses, with a maximum of seven non-attitudinal questions. The latter included on page three, a question asking the respondent if he wished to receive a summary of the research. Twenty-eight responses were requested regarding perceptions of CPA independence and the costs/benefits of independence. The respondent recorded these on the second page of the questionnaire by circling a specific number.

It was estimated that completion of the questionnaire would require five to fifteen minutes depending upon whether an individual read it carefully and/or responded to the open-ended portion of the questionnaire.

Mailing of the Final Questionnaire

The first mailing of the questionnaire was accompanied with a cover letter from Dr. Harold H. Sollenberger, Chairman of the Department of Accounting and Financial Administration, at Michigan State University. This letter explained the purpose of the questionnaire and the technique to be used to record questionnaire responses to avoid traceability of respondents, and requested prompt participation. A copy of the cover letter is shown in Appendix B.

The mailing consisted of the cover letter, the questionnaire, and a postage paid return envelope. Returns for the first mailing included 54.0 percent for the CPAs; 35.5 percent for the CFAs; and 32.0 percent for the Corporate Bar members.[14]

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[14]These numbers do not reflect adjustment for any inappropriate subjects, so the effective rate of return is higher.

As the return envelopes allowed the researcher to note if the return was from the first or second mailing, it was possible to arrive at exact figures for the returns of each mailing. It should be noted, however, that there is a possibility that some of the responses to the first mailing were prompted by receipt of the second mailing.

Questionnaires returned as undeliverable were acted upon in one of two ways. Alternative procedures for securing an updated address were used and the questionnaire was remailed to the updated address. If no such address could be obtained, the subject was reclassified as an "inappropriate subject unlocatable." Inappropriate subjects were not replaced.

With the CPA sample the only alternative procedure used was a telephone directory to search for a possible new address in the same locale. This procedure was successful as Table III-3 shows.

For the CFAs alternative procedures included:

1. Contacting the ICFA for a possible new address.
2. Contacting the individual's old firm for a possible new address.
3. Using the Federation of Financial Analysts' membership directory for a new address.[15]

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[15]The Financial Analysts Federation, <u>1976 Membership Directory</u>: Twenty-Eight Edition (New York: The Financial Analysts Federation, 1976).

TABLE III-3

ANALYSIS OF UNDELIVERABLE QUESTIONNAIRES

	CPAs	CBMs	CFAs	Total
Total Returned Questionnaires	7	31	11	49
No Updated Address was Available	3	11	3	17
Total Questionnaires Remailed	4	20	8	32
Breakdown of Remailings:				
Good Response Received	3	8	1	12
Inappropriate Response[a]	0	2	0	2
No Response	1	10	7	18
Percent of Returned Questionnaires for Which Follow-up Resulted in a Good Response	43	26	9	24

[a]See Table III-5 for the analysis of inappropriate subjects.

4. Using telephone directories to search for a possible new address in the same locale.

These alternative procedures did not prove to be fruitful, as Table III-3 indicates.

For the Corporate Bar members a set of alternative procedures was also used, which consisted of:

1. The use of the Martindale-Hubbell Law Directory for a possible new address.[16]

[16]Martindale-Hubbell, Inc., Law Directory: One Hundred and Ninth Annual Edition, 1977 (Summit, New Jersey: Martin-dale-Hubbell, Inc., 1977).

2. The use of telephone directories to search for a new address in the same locale.

It should be noted that in this case, firms of the lawyers could not be contacted because they were not listed in the directory. This time, the alternative procedures proved to be beneficial also, as is shown in Table III-3.

A second mailing was made for all subjects in the samples from which no response, or no undeliverable return was received. This second mailing also included a cover letter from Dr. Sollenberger, emphasizing the importance of the research, requesting prompt participation, and explaining that this was a second request. A copy of this letter can be found in Appendix C. This second mailing included another copy of the questionnaire, and a stamped return envelope. These were mailed sixteen days after the first mailing.

Table III-4 details the responses from both the first and second mailings from all samples. As can be seen from Table III-4 the final percentages of responses from the three samples were: CPAs 67 percent; CBMs 48 percent; CFAs 44 percent. This resulted in an overall response rate of 53 percent. These response rates were acceptable and it was not deemed necessary to follow further procedures to increase the response rate. At this point data collection was terminated.

TABLE III-4

BREAKDOWN OF RESPONSES TO BOTH MAILINGS

	CPAs	CBMs	CFAs	Total
Sample Subjects	200	200	200	600
Inappropriate Subjects[a]	7	14	7	28
Appropriate Subjects	193	186	193	572
First Mailing Responses	108	71	64	243
Second Mailing Responses	21	19	20	60
Total Responses	129	90	84	303
Response Percentage	67	48	44	53

[a]See Table III-5 for the analysis of inappropriate subjects.

TABLE III-5

ANALYSIS OF INAPPROPRIATE SUBJECTS

	CPAs	CBMs	CFAs	Total
Firm or Personal Policy to Not Respond to Surveys	2	-	1	3
Inactive CFA	-	-	2	2
No Contact With Auditing	1	-	-	1
Out of Country for Extended Period	-	-	1	1
Retired	1	-	2	3
Deceased	-	2	-	2
Unlocatable	3	12	1	16
TOTAL	7	14	7	28

Analysis of Respondents

In order to be confident that responses were proportionate over classifications consistent with the original samples selected and with the populations, the breakdown of respondents was reviewed. Table III-6 shows this breakdown for CPAs. At first glance this distribution (Table III-6) seems to be disproportionate to the distribution of the sample and the population as a whole. However, it must be remembered that this distribution includes all CPA responses, including those who no longer are practicing in public accounting. The 46 percent represented by the top fifteen firms is extremely high compared to the sample and to the population as a whole.

TABLE III-6

BREAKDOWN OF ALL CPA RESPONSES

Practiced/Practice With	Number	Percent
"Big Eight"	55	42.63
"Next Seven"	4	3.10
Other National Firms	7	5.43
Regional Firms	6	4.65
Local Firms	48	37.21
Did Not Answer	9	6.98
Total	129	100.00

An examination of the 70 respondent CPAs currently practicing public accounting shows that the distribution over the size of firms is much more consistent with the sample and with the population as a whole. Table III-7 gives this distribution, and comparing it with Table III-1 shows that the distribution is consistent with the sample and with the membership as a whole.

Table III-7

BREAKDOWN OF PRACTICING CPAs

	Number	Percent[a]
"Big Fifteen"	26	20.15
Other	44	34.11

[a]This is the percent of the total 129 responses. The remaining 59 (45.74%) is represented by those CPAs no longer practicing and those who did not answer the "currently practicing?" question. In Accounting Establishment, Metcalf, p. 85, it is noted that 40.76 percent (47,976 of 117,695 total members) are no longer practicing CPAs.

Although there is a substantial difference between the percentage of total CPAs who either currently are or have practiced with the "Big Fifteen," in contrast to those who are currently working in public accounting, this fact is consistent with the researchers' understanding of the high attrition rate of employees from "Big Fifteen" firms.

Table III-8 gives a breakdown of Corporate Bar members and the areas of law in which they are currently employed. No comparison was made to the sample or to the population as a whole, since those numbers were not available from the Section on Corporation, Banking and Business Law.

TABLE III-8

BREAKDOWN OF CORPORATE BAR MEMBER RESPONSES

	Number	Percent
Private Practice	58	64.44
Industry	20	22.22
Government	6	6.67
Education	2	2.22
Other	4	4.45
Total	90	100.00

A review of the responses of the CFAs shows that the industry classification distribution of respondents is consistent with the sample in the population as a whole. Table III-9 presents these findings, and a comparison can be made by referring to Table III-2.

The final question on the questionnaire allows the respondent to indicate by marking yes or no, whether he/she wishes to receive a summary of the research.

TABLE III-9

BREAKDOWN OF CFA RESPONSES

Industry Employed In	Number	Percent
Brokerage and Investment Banking	23	27.38
Investment Companies	3	3.57
Investment Counselor	14	16.67
Trust Companies or Trust Department of Commercial Banks	20	23.81
Insurance Companies	7	8.33
Pension Funds	5	5.95
Other	12	14.29
Total	84	100.00

Current literature does not offer any firm figures to suggest to the researcher what percentage of respondents might request such a summary. However, discussions with a number of people who have conducted survey research and have used this option suggest that the range is probably between 15 and 20 percent. If such figures are valid, an exceedingly large proportion (60 percent) of respondents requested a copy of the summary of this research. This may be due in part to the current review of the public accounting profession by many Congressional Committees, and to the large number of lawsuits involving CPAs.

Chapter Summary

This chapter has outlined the procedures for selecting the populations for this study, consisting of CPAs, Corporate Bar members, and CFAs, and the reasons for the use of these three populations. The procedures for selecting the samples and a breakdown of sample characteristics were then analyzed.

The administration of the field study was discussed, and the results of the field study analyzed, emphasizing changes made in the questionnaire. The questionnaire in its final form was then reviewed.

The procedures for both the first and second mailings of the final questionnaire were analyzed; the alternative procedures instituted in the case of undeliverable questionnaires were given. In addition to analysis of response characteristics within each sample, overall response characteristics were analyzed.

Finally, all of the responses were analyzed as to various categories of characteristics. The primary emphasis of this analysis was to confirm that the responding sample is not markedly different from the population as a whole, and the sample as a whole. This analysis has to do only with the descriptive portion of the returned questionnaires.

CHAPTER IV

ROTATION OF AUDIT FIRMS

Literature Review

A 1936 editorial in the Journal of Accountancy asks: "Is rotation of auditors any more reasonable than rotation of doctors and lawyers?"[1] Referring to a financial statement of the Southern Natural Gas Corporation, which states that the company avoids changing auditors on a whim, the editorial presents the document as an excellent model. Forty years later, the controversy on rotation of auditors continues.

Arguments for rotation

Arguing in favor of rotation, Jack Seidman, of Seidman and Seidman says that increased cost is no deterrent in the business world if it insures against far more costly risk.[2] Seidman also remarks that "there is also

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[1] "Recognition of Auditor's Importance--Auditor's Independence Clearly Defined--Reliance Upon Auditors' Report," Editorial, Journal of Accountancy 61 (February 1936):81.

[2] J. S. Seidman, "If We Fail or Falter in Calling the Accounting Shots With Unflinching Independence, the Public Will be After Us to Change Our Way of Life. One of the Changes Will be Rotation of Auditors." Letters to the Journal, Journal of Accountancy 123 (May 1967):30.

something to a new broom sweeping clean and coming up with ideas that eluded the perennial who got too close to picture."[3]

The above sentiment has been offered many times as an argument for rotation, but perhaps one of the strongest such statements is made in the Metcalf Report:

> One alternative is mandatory change of accountants after a given period of years, or after any finding by the SEC that the accounting firm failed to exercise independent action to protect investors and the public.[4]

Arguments against rotation

Often presented against the rotation of auditors is the argument that in many businesses, because there is so much to learn about the past history of the company and its operations, a client may receive less service than he would receive if he were to retain one audit firm. Another problem possible is that the start-up costs of new auditors will result in an increase of fees. Both of these arguments were offered as reasons not to rotate auditors during the McKesson and Robbins Inc. SEC proceeding in 1939.[5]

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[3]Ibid.

[4]The Accounting Establishment: A Staff Study Prepared by the Subcommittee on Reports, Accounting and Management of the Committee on Government Operations, United States Senate, Ninety-Fifth Congress, Second Session, by Lee Metcalf, Chairman (Washington, D.C.: U.S. Government Printing Office, 1977), p. 21.

[5]"The Question of Changing Auditors," Editorial, Journal of Accountancy 123 (February 1967):31-33.

A more recent argument against rotation is offered in Forbes magazine.

> It takes a great deal of knowledge about a company to perform an effective audit. In fact, many of the auditing failures of the past decade occurred because the auditors were new to the companies or industries they were auditing--not because they had become "cozy" with them.[6]

The Commission on Auditors' Responsibilities seconds this sentiment:

> More important, in the Commission's study of cases of substandard performance by auditors, several of the problem cases were first- or second-year audits. While not conclusive, this indicates the higher peril associated with new audit clients.[7]

This position is in direct contradiction to that taken by the Subcommittee on Reports, Accounting and Management of the Committee on Government Operations of the United States Senate.

Empirical studies

Since rotation is neither mandated nor practiced in the U.S., little empirical study of the topic has been done. The only study concerned with rotation is that by

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[6]"Why Everybody's Jumping on the Accountants These Days," Forbes (March 15, 1977), p. 40.

[7]American Institute of Certified Public Accountants, Commission on Auditors' Responsibilities, Commission on Auditors' Responsibilities: Report, Conclusions and Recommendations (New York: American Institute of Certified Public Accountants, 1978), p. 109. It is interesting to note that the wording here was changed from "a high percentage of the problem cases," in the Testative Report to "several of the problem cases," in the final report.

Bedingfield and Loeb, in which they find that two percent of their respondents changed auditors because they felt that they would get better service if they rotated auditors.[8]

Analysis of Data

The remaining portion of this chapter is devoted to the presentation and interpretation of the data. Each hypothesis is investigated separately, and a review and summary is presented in the section titled Data Review.

Specific hypotheses

The specific hypotheses to be tested are:

H_0-1: There are no significant differences between members of the AICPA, Corporate Bar and ICFA, regarding their perceptions as to the effect that rotation of audit firms will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_1-1: There are significant differences among members of the AICPA, Corporate Bar and ICFA, regarding their perceptions as to the effect that rotation of audit firms will have on the CPA's independence with respect to the CPA's SEC registered clients.

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[8] James P. Bedingfield and Stephen E. Loeb, "Auditor Changes and Examination," Accounting and Auditing, Journal of Accountancy 127 (March 1974):68.

H_0-2: There are no significant differences between members of the AICPA, Corporate Bar and ICFA, regarding their perceptions as to the effect that rotation of audit firms will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_1-2: There are significant differences between members of the AICPA, Corporate Bar and ICFA, regarding their perceptions as to the effect that rotation of audit firms will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_0-3: There are no significant differences between members of the AICPA, Corporate Bar and ICFA, regarding their perceptions as to the costs and benefits to society as a whole, of rotating audit firms for SEC registered firms.

H_1-3: There are significant differences between members of the AICPA, Corporate Bar and ICFA, regarding their perceptions as to the costs and benefits to society as a whole, of rotating audit firms for SEC registered firms.

H_0-4: There are no significant differences between members of the AICPA, Corporate Bar and ICFA, regarding their perceptions as to the costs and benefits to society as a whole, of rotating audit firms for non-SEC registered firms.

H_1-4: There are significant differences between members of the AICPA, Corporate Bar and ICFA, regarding their perceptions as to the costs and benefits to society as a whole, of rotating audit firms for non-SEC registered firms.

H_0-5: There are no significant differences between respondents who have experience of 0-9 years, 10-19 years, 20-29 years, and over 29 years, regarding their perceptions as to the effect that rotation of audit firms will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_1-5: There are significant differences between respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years, regarding their perceptions as to the effect that rotation of audit firms will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_0-6: There are no significant differences between respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years, regarding their perceptions as to the effect that rotation of audit firms will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_1-6: There are significant differences between respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years, regarding their perceptions as to the effect that rotation of audit firms will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_0-7: There are no significant differences between respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years, regarding their perceptions as to the costs and benefits to society as a whole of rotating audit firms for SEC registered firms.

H_1-7: There are significant differences between respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years, regarding their perceptions as to the costs and benefits to society as a whole of rotating audit firms for SEC registered firms.

H_0-8: There are no significant differences between respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years, regarding their perceptions as to the costs and benefits to society as a whole of rotating audit firms for non-SEC registered firms.

H_1-8: There are significant differences between respondents who have experience of 0-9 years, 10-19 years, 20-29 years, and over 29 years, regarding their perceptions as to the costs and benefits to society as a whole of rotating audit firms for non-SEC registered firms.

H_0-9: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions as to the effect that rotation of audit firms will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_1-9: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions as to the effect that rotation of audit firms will have on the CPA's independence, with respect to the CPA's SEC registered clients.

H_0-10: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions as to the effect that rotation of audit firms will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_1-10: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions as to the effect that rotation of audit firms will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_0-11: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions as to the costs and benefits to society as a whole, of rotating audit firms for SEC registered firms.

H_1-11: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions as to the costs and benefits to society as a whole of rotating audit firms for SEC registered firms.

H_0-12: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions as to the costs and benefits to society as a whole of rotating audit firms for non-SEC registered firms.

H_1-12: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions as to the costs and benefits to society as a whole of rotating audit firms for non-SEC registered firms.

Statistical package

The statistical analysis uses the Michigan State University CDC 6500. The Statistical Package for the Social Sciences (SPSS)[9] is the basic source of statistical analysis. Specifically, the "Subprogram Crosstabs," is used.[10] The portions of the subprogram that are used provide a contingency table of observations as well as chi-square and significance level calculations.

Collapsing of tables

When using chi-square contingency tables it is recommended that no theoretical frequency should be smaller than five.[11] The theoretical frequency for a cell can be found by calculating the product of the two marginal totals common to that cell divided by the total number of cases. In order to maintain the theoretical cell size, it is often necessary to combine more than one group of respondents (i.e., "Big Eight" and "Next Seven" for CPA's) or to combine responses of more than one column in the independence decision portion of the data.

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[9]Norman H. Nie, et al., Statistical Package for the Social Sciences, Second ed. (New York: McGraw-Hill Book Company, 1975).

[10]Ibid., pp. 218-248.

[11]Stephen Isaac and William B. Michael, Handbook in Research and Evaluation (San Diego, California: Edits Publishers, 1971), p. 135.

Usually the data, including means, is given to aid the reader in evaluation. However, whenever the theoretical cell size is too small for purposes of a chi-square, collapsing is done. When data is collapsed, a statement is made to show the reader how it is done and the chi-square and significance level are calculated on the combined data. The first analysis in Chapter IV demonstrates the collapsing technique (See Tables IV-1 and IV-2). In the data chapters the collapsed tables are not presented. When the theoretical cell size is still too small after collapsing, the data is presented with the author's remarks, but no chi-square or significance level calculations are presented as they are inappropriate.

In most cases the theoretical cell size is sufficient in analysis of the Costs/Benefits decision. When this is not the case, the raw data is presented in the same manner as the independence decision.

Calculations of means

The means in all of the tables are based on the following scales:

Independence Decisions:

1 Greatly Decrease Independence

2 Slightly Decrease Independence

3 Not Affect Independence

4 Slightly Increase Independence

5 Greatly Increase Independence

Costs/Benefits Decision:

1 If the proposed change is made, the cost to Society will exceed the benefits to Society

2 If the proposed change is made, the benefits to Society will exceed the costs to Society

Non-responses are not included in calculations.

Hypotheses in general

In each case throughout the research, the null hypotheses are stated in terms of a consensus. Should the null hypothesis not be rejected, it can then be concluded that there are no statistically significant differences among the groups analyzed as to their perceptions of the effect of the change in the auditor/client relationship. It is incorrect, however, to suggest the samples are from the same population, as only one dimension of the sample has been tested.

After acceptance of the null hypothesis, it can only be concluded that the groups perceive the effect in the same way. It is then up to the researcher and the reader to interpret the data to see in what way or ways these perceptions are distributed.

Should the null hypothesis be rejected, it can be concluded that the groups analyzed do not perceive the effect of the change in the auditor/client relationship in the same way. Again, the way in which an individual group perceives the change can be ascertained only from the data.

H_0-1: CPAs/CBMs/CFAs--Independence with SEC registered firms

In each of the data tables (Tables 1, 3-13 in Chapter IV and 1-12 in Chapters V-IX), the responses for all possible answers are given. Totals for each respondent group may not equal the total returned questionnaires as some respondents did not answer all questions.

Due to theoretical cell sizes that are too small, Table IV-1 is collapsed to arrive at Table IV-2.

As seen in Table IV-1 and Table IV-2, there is a general agreement among CPAs, CBMs and CFAs that rotation of audit firms increases the CPA's independence with respect to an SEC registered client. Only one-third of the total respondents feel it does not increase independence; the majority of that one-third feel it does not affect the CPA's independence.

H_0-2: CPAs/CBMs/CFAs--Independence with non-SEC registered firms

Table IV-3 shows that in contrast to their perceptions about SEC registered firms, the three respondent groups do not agree as to how rotation of audit firms affects the CPA's independence when the client is a non-SEC registered firm. The largest differences in perceptions exist among CPAs: 48% say that independence does

TABLE IV-1

CPAs/CBMs/CFAs--INDEPENDENCE SEC FIRMS[a]

	Greatly Decrease Indep.	Slightly Decrease Indep.	Not Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
CPAs	1	3	41	53	30	128	3.84
	.3[c]	1.0	13.6	17.6	10.0	42.5	
CBMs	5	1	24	29	31	90	3.89
	1.7	.3	8.0	9.6	10.3	29.9	
CFAs	2	3	19	36	23	83	3.90
	.7	1.0	6.3	12.0	7.6	27.6	
Total	8	7	84	118	84	301[b]	3.87
	2.7	2.3	27.9	39.2	27.9	100.0	

[a]Chi-square and significance calculations are not presented as they could be misleading due to insufficient theoretical cell size.

[b]Non-response: CPAs-1, CFAs-1.

[c]In this and all succeeding tables in Chapter IV through IX, the second row of numbers for each respondent group represents the percent of total responses on this question.

TABLE IV-2

CPAs/CBMs/CFAs--INDEPENDENCE SEC FIRMS

	Does Not[a] Increase Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
CPAs	45 15.0	53 17.6	30 10.0	128 42.6	3.84
CBMs	30 10.0	29 9.6	31 10.3	90 29.9	3.89
CFAs	24 8.0	36 12.0	23 7.6	83 27.6	3.90
Total	99 33.0	118 39.2	84 27.9	301[b] 100.0	3.87

Raw chi-square = 4.54505. Significance level = .3372

[a]The categories Greatly Decrease Independence, Slightly Decrease Independence and Not Affect Independence are combined into this column.

[b]Non-responses: CPAs-1, CFA-1.

TABLE IV-3

CPAs/CBMs/CFAs--INDEPENDENCE NON-SEC FIRMS

	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
CPAs	3	3	54	45	20	125	3.61
	1.0	1.0	18.4	15.3	6.8	42.5	
CBMs	5	1	33	18	31	88	3.78
	1.7	.3	11.2	6.1	10.5	29.9	
CFAs	3	2	26	24	26	81	3.84
	1.0	.7	8.8	8.2	8.8	27.6	
Total	11	6	113	87	77	294[b]	3.72
	3.7	2.0	38.4	29.6	26.2	100.0	

Raw chi-square = 14.04955. Significance level = .0071.

[a]For calculation purposes these columns are combined.

[b]Non-responses: CPAs-4; CBMs-2; CFAs-3.

not increase, while only 38% of the CFAs say that independence is not increased. At the same time 32% of the CFAs say that rotation of audit firms greatly increases independence (35% of the CBMs agree) while only 16% of the CPAs feel that independence greatly increases.

H_0-3: CPAs/CBMs/CFAs--Costs/Benefits with SEC registered firms

Regarding the costs and benefits of rotation of audit firms for SEC clients, the respondent groups do not agree. While the CPAs who believe that costs exceed benefits outnumber CPAs of the opposite view by a five-to-one margin, the margins (in the same direction) are only 2.3 to 1 for CFAs, and 1.6 to 1 for CBMS.

TABLE IV-4

CPAs/CBMs/CFAs--COSTS/BENEFITS SEC FIRMS

	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
CPAs	102 34.1	25 8.4	127 42.5	1.20
CBMs	55 18.4	35 11.7	90 30.1	1.39
CFAs	57 19.1	25 8.4	82 27.4	1.30
Total	214 71.6	85 28.4	299[a] 100.0	1.28

Raw chi-square = 9.78271. Significance level = .0075

[a]Non-responses: CPAs-2; CFAs-2.

H_0-4: CPAs/CBMs/CFAs--Costs/Benefits with non-SEC registered firms

When non-SEC registered firms are considered, the CPAs are even more emphatic that costs will exceed benefits than they are for SEC registered firms. A much larger portion of CBMs feel that costs will exceed benefits for non-registered firms than the portion in the same category for SEC firms, while the CFAs vary little with respect to SEC registration.

TABLE IV-5

CPAs/CBMs/CFAs--COSTS/BENEFITS NON-SEC FIRMS

	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
CPAs	111 38.3	15 5.2	126 43.4	1.12
CBMs	63 21.7	22 7.6	85 29.3	1.26
CFAs	54 18.6	25 8.6	79 27.2	1.32
Total	228 78.6	62 21.4	290[a] 100.0	1.21

Raw chi-square = 12.70812. Significance level = .0017.

[a]Non-responses: CPAs-3; CBMs-5; CFAs-5.

H_0-5: Years of experience--Independence with SEC registered firms

Although not significant at an .05 level, there is a substantial difference between the groups based on years of experience. This is best indicated by the fact that only one quarter of the respondents with 0-9 years of experience think that independence will not be increased when rotation of audit firms is mandated, while fully one half of those respondents with 30 or more years of experience answer in a like manner. The reverse is true concerning responses in the Greatly Increase Independence column, the category chosen by one-third of the 0-9 years respondents, while only one-tenth of the 30 or more years respondents make the same choice.

H_0-6: Years of experience--Independence with non-SEC firms

Although the direction of differences in responses between experience groups is the same for non-SEC registered firms as it is for SEC registered firms, those differences are not as large and are not significant.

TABLE IV-6

EXPERIENCE GROUPS--INDEPENDENCE SEC FIRMS

Years of Exper.	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
0-9	3	5	27	56	32	134	3.98
	1.0	1.7	9.0	18.6	14.3	44.5	
10-19	1	2	26	37	23	89	3.89
	.3	.7	8.6	12.3	7.6	29.6	
20-29	3	0	18	13	15	49	3.76
	1.0	0	6.0	4.3	5.0	16.3	
30-39[b]	1	0	6	8	2	17	3.59
	.3	0	2.0	2.7	.7	5.6	
40+[b]	0	0	7	4	1	12	3.50
	0	0	2.3	1.3	.3	4.0	
Total	8	7	84	118	84	301[c]	3.87
	2.7	2.3	27.9	39.2	27.9	100.0	

Raw chi-square = 12.14565. Significance level = .0588

[a]For calculation purposes these columns are combined.

[b]For calculation purposes these rows are combined.

[c]Non-responses: 10-19=2.

TABLE IV-7

EXPERIENCE GROUPS--INDEPENDENCE NON-SEC FIRMS

Years of Exper.	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
0-9	5 1.7	5 1.7	46 15.6	39 13.3	38 12.9	133 45.2	3.75
10-19	2 .7	1 .3	32 10.9	32 10.9	21 7.1	88 29.9	3.78
20-29	4 1.4	0 0	20 6.8	8 2.7	15 5.1	47 16.0	3.64
30-39[b]	0 0	0 0	7 2.4	5 1.7	3 1.0	15 5.1	3.73
40+[b]	0 0	0 0	8 2.7	3 1.0	0 0	11 3.7	3.27
Total	11 3.7	6 2.0	113 38.4	87 29.6	77 26.2	294[c] 100.0	3.72

Raw chi-square = 9.17117. Significance level = .1642.

[a]For calculation purposes these columns are combined.

[b]For calculation purposes these rows are combined.

[c]Non-responses: 0-9=1; 10-19=3; 20-29=2; 30-39=2; 40+=1.

H_0-7: Years of experience--Costs/Benefits with SEC registered firms

Study of IV-8 shows that all experience groups are fairly consistent (by an approximate three to one ratio) in their belief that the costs will exceed benefits if audit firms are rotated for SEC firms. The two most experienced groups lean more toward the opinion that costs greater than benefits will result than the other groups, but the difference is not significantly greater.

TABLE IV-8

EXPERIENCE GROUPS--COSTS/BENEFITS SEC FIRMS

Years of Exper.	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
0-9	92 30.8	40 13.4	132 44.1	1.30
10-19	66 22.1	23 7.7	89 29.8	1.26
20-29	34 11.4	15 5.0	49 16.4	1.31
30-39[a]	13 4.3	4 1.3	17 5.7	1.24
40+[a]	9 3.0	3 1.0	12 4.0	1.25
Total	214 71.6	85 28.4	299[b] 100.0	1.28

Raw chi-square = .89767. Significance level = .8260

[a]For calculation purposes these rows are combined.

[b]Non-responses: 0-9=2; 10-19=2.

H_0-8: Years of experience--Costs/Benefits with non-SEC registered firms

Table IV-9 indicates that respondents view both (SEC and non-SEC) costs/benefits decisions in the same way. There is some movement from the Benefits Exceed Costs to the Costs Exceed Benefits column for all groups.

TABLE IV-9

EXPERIENCE GROUPS--COSTS/BENEFITS NON-SEC FIRMS

Years of Exper.	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
0-9	103 35.5	27 9.3	130 44.8	1.21
10-19	67 23.1	22 7.6	89 30.7	1.25
20-29	36 12.4	10 3.4	46 15.9	1.22
30-39[a]	12 4.1	2 .7	14 4.8	1.14
40+[a]	10 3.4	1 .3	11 3.8	1.09
Total	228 78.6	62 21.4	290[b] 100.0	1.21

Raw chi-square = 1.93137. Significance level = .5868.

[a]For calculation purposes these rows are combined.

[b]Non-responses: 0-9=4; 10-19=2; 20-29=3; 30-39=3; 40+=1.

CPA Breakdown information

All CPAs were asked to indicate what size firm they either currently work for or formerly worked for. Of 129 respondents, nine do not make that indication. Table IV-10 shows the breakdown of respondents who indicate the size of their firms.

TABLE IV-10

BREAKDOWN OF CPA FIRM SIZE

Firm Size	Number	Percent
Big Eight	55	45.84
Next Seven	4	3.33
Other National	7	5.83
Regional	6	5.00
Local	48	40.00
Total	120	100.00

At the time of the questionnaire, the "Big Eight" were:

Arthur Andersen & Co.
Arthur Young and Company
Coopers & Lybrand
Ernst & Ernst
Haskins & Sells
Peat, Marwick, Mitchell & Co.
Price Waterhouse & Co.
Touche Ross & Co.

At the time of the questionnaire, the "Next Seven" were:

Alexander Grant & Co.
Hurdman and Cranstoun
J. K. Lasser & Co.
Laventhol & Horwath
S. D. Leidesdort & Co.
Main Lafrentz & Co.
Seidman & Seidman[10]

Due to the small numbers of respondents representing the three middle-size firms, the analysis that follows in this and later chapters groups all respondents (who indicate firm size) into two groups consisting of the "Big Fifteen" and all others. The presentation of data likewise consists of only two groups.

H_0-9: CPA Breakdown--Independence with SEC registered firms

Although not significant (at the .05 level), it is interesting to note that while only one-sixth of the respondents who work/worked for "Big Fifteen" firms feel rotation of firms will greatly increase independence, a full one-third of the respondents who work/worked for smaller firms think the change will greatly increase independence.

[10]These listings are taken from Accounting Establishment, Metcalf, pp. 25, 29.

TABLE IV-11

BIG FIFTEEN--INDEPENDENCE SEC FIRMS

Size of Firm	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
Big Fifteen	0 0	2 1.7	21 17.6	27 22.7	9 7.6	59 49.6	3.73
Other firms	1 .8	0 0	17 14.3	22 18.5	20 16.8	60 50.4	4.00
Total	1 .8	2 1.7	38 31.9	49 41.2	29 24.4	119[b] 100.0	3.87

Raw chi-square = 5.28434. Significance level = .0712.

[a]For calculation purposes these columns are combined.

[b]Non-responses: Other-1.

H_0-10: CPA Breakdown--Independence with non-SEC registered firms

As is true with SEC registered firms, for non-SEC firms a larger percentage of the respondents who work/ worked with firms other than the "Big Fifteen" feel that rotation will greatly increase independence than the percentage of respondents from the "Big Fifteen." For both groups there is a sizeable movement of respondents from the Will Increase Independence categories to Will Not Increase categories when the responses for non-SEC firms are compared with those for SEC firms.

H_0-11: CPA Breakdown--Costs/Benefits with SEC registered firms

Table IV-13 indicates that in both groups a large majority of respondents feel that the costs will exceed the benefits to society. The percentage of "other" respondents is double that of the "Big Fifteen" respondents.

H_0-12: CPA Breakdown--Costs/Benefits with non-SEC registered firms

Again referring to non-SEC clients, a majority of the respondents feel that the costs will exceed the benefits, but this time in almost equal percentages for both respondent groups.

TABLE IV-12

BIG FIFTEEN--INDEPENDENCE NON-SEC FIRMS

Size of Firm	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
Big Fifteen	1 .9	1 .9	30 25.7	20 17.1	5 4.3	57 48.7	3.47
Other firms	2 1.7	0 0	23 19.7	23 19.7	12 10.3	60 51.3	3.72
Total	3 2.6	1 .9	53 45.3	43 36.8	17 14.5	117[b] 100.0	3.60

Raw chi-square = 3.87693. Significance level = .1439.

[a]For calculation purposes these columns are combined.

[b]Non-responses: Big Fifteen-2; other-1.

TABLE IV-13

BIG FIFTEEN--COSTS/BENEFITS SEC FIRMS

Size of Firms	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
Big Fifteen	52 44.1	7 5.9	59 50.0	1.12
Other firms	43 36.4	16 13.6	59 50.0	1.27
Total	95 80.5	23 19.5	118[a] 100.0	1.19

Raw chi-square = 3.45629. Significance level = .0630.

[a]Non-responses: Other-2.

TABLE IV-14

BIG FIFTEEN--COSTS/BENEFITS NON-SEC FIRMS

Size of Firms	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
Big Fifteen	53 44.9	5 4.2	58 49.2	1.09
Other firms	52 44.1	8 6.8	60 50.8	1.13
Total	105 89.0	13 11.0	118[a] 100.0	1.11

Raw chi-square = .27387. Significance level = .6007.

[a]Non-responses: Big Fifteen-1; Other-1.

Data Review

Hypotheses rejected

In reviewing the data, using an .05 alpha level of significance, the chi-square tests that reject the hypothesis of consensus are:

1. CPAs/CBMs/CFAs - Independence non-SEC firms (Table IV-3)

2. CPAs/CBMs/CFAs - Costs/Benefits SEC firms (Table IV-4)

3. CPAs/CBMs/CFAs - Costs/Benefits non-SEC firms (Table IV-5).

Closer examination shows that two other tests approach rejection of the null at an .05 level. They are:

1. Experience Group - Independence SEC firms (Table IV-6)

2. Big Fifteen - Independence SEC firms (Table IV-11)

3. Big Fifteen - Costs/Benefits SEC firms (Table IV-13).

All tests that were rejected were among the CPAs/CBMs/CFAs groupings. A further look at the tables shows that the CPAs consistently disagree with the other two groups.

Second, in review of the data of this chapter, one trend becomes obvious immediately. All groups, in all cases analyzed, feel that the required rotation of audit firms will increase the independence of the CPA with respect either to SEC registered or non-SEC registered clients.

Analysis of means of independence decisions

Using the 1 to 5 scale, it is possible to state that a group mean of below 3.0 indicates that an average response is that independence will decrease. A group mean of 3.0 indicates that an average response is that independence will not be affected; a group mean above 3.0 indicates that an average response is that independence will increase. The entire set of means falls between 3.50 and 4.00 for SEC registered firms.

Interestingly, the lowest mean involves responses for the group of respondents with the longest experience. This may be explained in part by the fact that this group has learned to live with the "as is" situation and does not see much effect on independence as a result of audit firm rotation. Also, the small number of respondents allows the mean to be greatly affected by a few responses.

TABLE IV-15

COMPARISON OF GROUP MEANS--ROTATION

Group	Independence Decision SEC	Independence Decision Non-SEC	Costs Benefits SEC	Costs Benefits Non-SEC
CPAs	3.84	3.61	1.20	1.12
CBMs	3.89	3.78	1.39	1.26
CFAs	3.90	3.86	1.30*	1.32*
0-9	3.98	3.75	1.30	1.21
10-19	3.89	3.78	1.26	1.25
20-29	3.76	3.64	1.31	1.22
30-39	3.59*	3.73*	1.24	1.14
40+	3.50	3.27	1.25	1.09
Big 15	3.73	3.27	1.25	1.09
Other CPAs	4.00	3.72	1.27	1.13
Total of All Respondents	3.87	3.72	1.28	1.21

*These are the only instances where the means seem to suggest rotation is more beneficial for non-SEC firms than for SEC firms.

At the same time the highest mean of 4.0 is for respondents who are/were with a firm not a part of the "Big Fifteen." This coincides with the prevailing opinion that if rotation is required the smaller audit firms will benefit by gaining new clients. As may be expected, the "Big Fifteen" respondents do not agree with that view. At the very least the researcher must ask, "Are they truly saying, 'it will increase independence,' or are they saying 'how will this affect my billings?'" At this point there is no way to answer that question.

When dealing with non-SEC firms, the means of the groups fall between 3.27 (again for the group with 40+ years of experience), and 3.86 (for CFAs).

Also, in ten of eleven cases (see Table IV-14) for the comparison of means), the respondent groups feel that when an SEC registered firm is involved, there will be a greater increase in independence than there will be for a non-SEC registered firm. The lone exception involves the group with 30-39 years of experience. Due to the small number of observations in this group, it is misleading to put much emphasis on the exception.

Analysis of means of costs/benefits

Considering the 1, 2 scale, it may be said that a group mean above 1.5 indicates an average response that the benefits will exceed the costs. Likewise, a group mean below 1.5 indicates an average response that the costs will exceed the benefits.

A second fact is quickly noticeable from Table IV-14. Even though all groups feel that independence will be increased by rotation of audit firms, no group feels that the benefits will exceed the costs. Also noted is that, as is true in the independence decision, with only one exception (CFAs), the groups feel that the costs/benefits ratio will increase in dealings with non-SEC firms in contrast to SEC firms.

The groups who indicate the lowest difference (highest mean--the higher the closer to benefits equalling costs) between costs and benefits are CBMs, CFAs, and the group with 20-29 years of experience. As may be expected (given the argument for small firms acquiring clients through mandated rotation), the "Big Fifteen" respondents feel most strongly that costs will exceed benefits.

Conclusions

Even though there are some statistically significant differences among various respondent groups as to the degree of effect the mandated rotation of audit firms will have on the independence of the CPA regarding a client, the majority of respondents in all groups do feel it increases independence.

At the same time, the majority of respondents in all groups feels that the costs to society will exceed the benefits to society should rotation be required. It appears that the respondents are actually saying that even though independence will be increased the costs involved will be greater than the benefits.

The findings are consistent with the recommendations of the Commission on Auditors' Responsibilities, which says that rotation of audit firms should not be required; they directly oppose the Metcalf Committee which recommends required rotation of auditors.

CHAPTER V

DISCLOSURE OF INDEPENDENT AUDITOR CHANGES

Literature Review

The Commission on Auditors' Responsibilities recommends that a report by management setting forth management representations related to the statements should accompany audited financial statements.[1] The Commission continues, "the report by management should be a useful vehicle for disclosure of auditor changes."[2]

Since the concept of the report by management is relatively new, little has been written about it to date. However, it is useful to examine what has happened with respect to reporting auditor changes in the past.

Until recently, when changing auditors, American firms have had to disclose very little to the general public. In 1974 the SEC ruled that the first auditor should be given an opportunity to explain disagreements

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[1]American Institute of Certified Public Accountants, Commission on Auditors' Responsibilities, Commission on Auditors' Responsibilities: Report, Conclusions and Recommendations (New York: American Institute of Certified Public Accountants, 1978), p. 108.

[2]Ibid.

in the last two years of its association with management that concerned accounting principles, disclosures, or the scope of the examination.[3]

Soon after ASR No. 165, the Statement on Auditing Standards No. 7 was issued by the AICPA. This pronouncement now requires that an auditor considering the acceptance of a new client consult with the previous auditor to inquire about disagreements over accounting principles, disclosures or the scope of the examination, and about any facts that might bear on the integrity of management.[4]

For a number of years, English and Canadian firms have had the opportunity to explain disagreements with management at stockholders' meetings.[5]

Currently, the SEC requires a company to disclose in its financial statements disagreements on accounting methods or disclosures if the new auditor agrees to accept a matter objected to by the preceding auditor that has a material effect on the financial statements.[6] All of the

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[3]SEC Accounting Series Release No. 165, "Notice of Amendments to Require Increased Disclosure of Relationships between Registrants and Their Independent Public Accountants," December 20, 1974.

[4]Statement on Auditing Standards No. 7, Communications Between Predecessor and Successor Auditors (October 1975) (AICPA, Professional Standards, Vol., AU section 315).

[5]For background on the English and Canadian ways of handling this matter, see Carmichael, Douglas R. "Changing Auditors and Audit Responsibilities," Journal of Accountancy 130 (November 1970), pp. 70-73.

[6]SEC Accounting Series Release No. 194, "Reporting Disagreements with Former Accountants: Adoption of Amendments of Requirements," July 28, 1976.

present pronouncements relating to disclosing auditor changes deal specifically with auditor changes when disagreements take place. It should be pointed out that this research does not refer to disclosure of independent auditor changes when there is disagreement but only when there is an auditor change. Consequently, this disclosure is a broader one than is currently required by any authoritative body.

Another important point is that all the current pronouncements require some sort of submission of materials to the SEC or to a comparable body. Again, the question dealt with by the Commission on Auditors' Responsibilities suggests that the disclosure be made in a management report. Currently this requirement does not exist.

Analysis of Data

The remaining portion of this chapter is devoted to the presentation and interpretation of the data. Each hypothesis is investigated separately; a review and summary are presented in the section titled Data Review.

Specific hypotheses

The specific hypotheses to be tested in this section are:

H_0-1: There are no significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the effect that disclosure of auditor changes in a management report will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_1-1: There are significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the effect that disclosure of auditor changes in a management report will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_0-2: There are no significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the effect that disclosure of auditor changes in a management report will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_1-2: There are significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the effect that disclosure of auditor changes in a management report will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_0-3: There are no significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the costs and benefits to society as a whole, of disclosure of auditor changes in a management report for SEC registered firms.

H_1-3: There are significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the costs and benefits to society as a whole, of disclosure of auditor changes in a management report for SEC registered firms.

H_0-4: There are no significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions as to the costs and benefits to society as a whole, of disclosure of auditor changes in a management report for non-SEC registered firms.

H_1-4: There are significant differences among members of the AICPA, Corporate Bar and ICFA, regarding their perceptions of the costs and benefits to society as a whole, of disclosure of auditor changes in a management report for non-SEC registered firms.

H_0-5: There are no significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years, and over 29 years regarding their perceptions of the effect that disclosure of auditor changes in a management report will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_1-5: There are significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years, and over 29 years regarding their perceptions of the effect that disclosure of auditor changes in a management report will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_0-6: There are no significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years, and over 29 years regarding their perceptions of the effect that disclosure of auditor changes in a management report will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_1-6: There are significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years, and over 29 years regarding their perceptions of the effect that disclosure of auditor changes in a management report will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_0-7: There are no significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-28 years, and over 29 years regarding their perceptions of the costs and benefits to society as a whole, of disclosure of auditor changes in a management report for SEC registered firms.

H_1-7: There are significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years regarding their perceptions of the costs and benefits to society as a whole, of disclosure of auditor changes in a management report for SEC registered firms.

H_0-8: There are no significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years, and over 20 years regarding their perceptions of the costs and benefits to society as a whole, of disclosure of auditor changes in a management report for non-SEC registered firms.

H_1-8: There are significant differences between respondents who have experience of 0-9 years, 10-19 years, 20-29 years, and over 29 years regarding their perceptions of the costs and benefits to society as a whole, of disclosure of auditor changes in a management report for non-SEC registered firms.

H_0-9: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms, and respondents who work/worked for other CPA firms regarding their perceptions of the effect disclosure of auditor changes in a management report will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_1-9: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the effect disclosure of auditor changes in a management report will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_0-10 There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the effect that disclosure of auditor changes in a management report will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_1-10: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the effect that disclosure of auditor changes in a management report will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_0-11: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for the other CPA firms regarding their perceptions of the costs and benefits to society as a whole, of disclosure of auditor changes in a management report for SEC registered firms.

H_1-11: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for the other CPA firms regarding their perceptions of the costs and benefits to society as a whole, of disclosure of auditor changes in a management report for SEC registered firms.

H_0-12: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for the other CPA firms regarding their perceptions of the costs and benefits to society as a whole, of disclosure of auditor changes in a management report for non-SEC registered firms.

H_1-12: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for the other CPA firms regarding their perceptions of the costs and benefits to society as a whole, of disclosure of auditor changes in a management report for non-SEC registered firms.

<u>$H_0$1: CPAs/CBMs/CFAs--Independence with SEC registered firms</u>

A look at Table V-1 shows that there is not a significant disagreement among the groups as to how disclosure

TABLE V-1

CPAs/CBMs/CFAs--INDEPENDENCE SEC FIRMS[a]

	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
CPAs	3 1.0	3 1.0	73 25.0	32 11.0	17 5.8	128 43.8	3.45
CBMs	4 1.4	4 1.4	33 11.3	22 7.5	21 7.2	84 28.8	3.62
CFAs	0 0	5 1.7	37 12.7	27 9.2	11 3.8	80 27.4	3.55
Total	7 2.4	12 4.1	143 49.0	81 27.7	49 16.8	292[b] 100.0	3.52

Raw chi-square = 7.91425. Significance level = .0948.

[a]For calculation purposes these columns are combined.

[b]Non-responses: CPAs-1, CBMs-6; CFAs-4.

of auditor changes in a management report affects the CPA's independence.[7] Only 13% of the CPAs and CFAs feel that disclosure greatly increases independence. At the same time a full 25% of the CBMs feel that disclosure greatly increases independence.

$H_0$2: CPAs/CBMs/CFAs--Independence with non-SEC registered firms

Regarding non-SEC firms, the respondent means are lower than when referring to SEC registered firms. Table V-2 shows that all of the means are lower than they are for SEC registered firms as presented in Table V-1. The two tables show that, for SEC and non-SEC registered firms, only 19 and 18 respondents, respectively, think that there is a decrease in independence.

$H_0$3: CPAs/CBMs/CFAs--Cost/Benefits with SEC registered firms

Table V-3 shows that all three respondent groups feel that the benefits to society will exceed the costs to society with respect to disclosing auditor changes in a management report. The CPAs have the lowest mean, and the CBMS have the highest; the CFAs fall exactly mid-way between these two groups.

[7]For more information on the statistical analysis, see Chapter IV.

TABLE V-2

CPAs/CBMs/CFAs--INDEPENDENCE NON-SEC FIRMS

	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
CPAs	4 1.4	5 1.7	79 27.3	24 8.3	14 4.8	126 43.6	3.31
CBMs	3 1.0	3 1.0	45 15.6	21 7.3	13 4.5	85 29.4	3.45
CFAs	0 0	3 1.0	42 14.5	24 8.3	9 3.1	78 27.0	3.50
Total	7 2.4	11 3.8	166 57.4	69 23.9	36 12.5	289[b] 100.0	3.40

Raw chi-square = 4.96379. Significance level = .2910.

[a]For calculation purposes these columns are combined.

[b]Non-responses: CPAs-3; CBMs-5; CFAs-6.

TABLE V-3

CPAs/CBMs/CFAs--COSTS/BENEFITS SEC FIRMS

	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
CPAs	46 16.7	75 27.2	121 43.8	1.62
CBMs	20 7.2	59 21.4	79 28.6	1.75
CFAs	24 8.7	52 18.8	76 27.5	1.68
Total	90 32.6	186 67.4	276[a] 100.0	1.67

Raw chi-square = 3.55859. Significance level = .1688.

[a]Non-responses: CPAs-8; CBMs-11; CFAs-8.

$H_0$4: CPAs/CBMs/CFAs--Costs/Benefits with non-SEC registered firms

Examination of the issue of disclosure of auditor changes with non-SEC registered firms indicates an apparent difference of opinion. Although the responses are not significantly different at the .05 alpha level, it is clear that there is not total agreement.

TABLE V-4

CPAs/CBMs/CFAs--COSTS/BENEFITS NON-SEC FIRMS

	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
CPAs	56 20.4	64 23.4	120 43.8	1.53
CBMs	26 9.5	53 19.3	79 28.8	1.67
CFAs	24 8.8	51 18.6	75 27.4	1.68
Total	106 38.7	168 61.3	274[a] 100.0	1.61

Raw chi-square = 5.74620. Significance level = .0565.

[a]Non-responses: CFAs-9; CBMs-11; CFAs-9.

The mean of all respondents drops from 1.69 regarding SEC registered firms, to 1.61 in reference to non-SEC registered firms. At the same time, the mean for the CFA respondents does not change. The largest drop in mean is represented by the CPA respondents; the drop in the mean of the CBMs is not significantly less than the CPAs.

H_0:5: Years of experience--Independence with SEC registered firms

Table V-5 indicates a high degree of consistency of opinion of the respondent groups divided into years of experience. All groups do feel that disclosure of auditor changes in a management report will increase independence

TABLE V-5

EXPERIENCE GROUPS--INDEPENDENCE SEC FIRMS

Years of Exper.	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
0-9	2 .7	5 1.7	62 21.2	40 13.7	21 7.2	130 44.5	3.56
10-19	1 .3	2 .7	43 14.7	26 8.9	14 4.8	86 29.5	3.58
20-29	3 1.0	4 1.4	22 7.5	10 3.4	8 2.7	47 16.1	3.34
30-39[b]	0 0	1 .3	8 2.7	3 1.0	5 1.7	17 5.8	3.71
40+[b]	1 .3	0 0	8 2.7	2 .7	1 .3	12 4.1	3.17
Total	7 2.4	12 4.1	143 49.0	81 27.7	49 16.8	292[c] 100.0	3.52

Raw chi-square - 3.54348. Significance level = .7382.

[a]For calculation purposes these columns are combined.

[b]For calculation purposes these rows are combined.

[c]Non-responses: 0-9=4; 10-19=5; 20-29=2.

on an average, and only 19 respondents in all feel that the change will decrease independence.

H_0:6: Years of experience--Independence with non-SEC registered firms

When referring to non-SEC registered firms, most of the respondent groups feel that the change will increase independence by a lesser margin than the change for SEC-registered firms. The lone exception is the group with 20-29 years of experience, whose mean goes from 3.34 to 3.35 regarding non-SEC registered firms.

It should also be noted from study of non-SEC registered firms that the groups with 40+ years of experience feel, on an average, that there will not be an effect on independence. This is represented by the mean of 3.00 in Table V-6. Again the small number of respondents in this group should make the reader wary.

H_0:7: Years of experience--Costs/Benefits with SEC registered firms

Table V-7 indicates that, regarding SEC-registered firms, all respondent groups believe that the costs to society will be smaller than benefits to society if auditor changes are disclosed in management reports.

TABLE V-6

EXPERIENCE GROUPS--INDEPENDENCE NON-SEC FIRMS

Years of Exper.	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
0-9	3	5	71	32	18	129	3.44
	1.0	1.7	24.6	11.1	6.2	44.6	
10-19	1	1	53	22	9	86	3.43
	.3	.3	18.3	7.6	3.1	29.8	
20-29	2	4	23	10	7	46	3.35
	.7	1.4	8.0	3.5	2.4	15.9	
30-39[b]	0	1	10	3	2	16	3.38
	0	.3	3.5	1.0	.7	5.5	
40+[b]	1	0	9	2	0	12	3.00
	.3	0	3.1	.7	0	4.2	
Total	7	11	166	69	36	289[c]	3.40
	2.4	3.8	57.4	23.9	12.5	100.0	

[a]For calculation purposes these columns are combined.

[b]For calculation purposes these rows are combined.

[c]Non-responses: 0-9=5; 10-19=5; 20=29=3; 30-39=1.

[d]Insufficient expected cell sizes for statistical tests.

TABLE V-7

EXPERIENCE GROUPS--COSTS/BENEFITS SEC FIRMS

Years of Exper.	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
0-9	39 14.1	87 31.5	126 45.7	1.69
10-19	24 8.7	56 20.3	80 29.0	1.70
20-29	17 6.2	27 9.8	44 15.9	1.61
30-39[a]	7 2.5	9 3.3	16 5.8	1.56
40+[a]	3 1.1	7 2.5	10 3.6	1.70
Total	90 32.6	186 67.4	276[b] 100.0	1.67

Raw chi-square = 1.53780. Significance level = .6736.

[a]For calculation purposes these rows are combined.

[b]Non-responses: 0-9=8; 10-19=11; 20-29=5; 30-39=1; 40+=2.

<u>H_0-8: Years of experience--Costs/Benefits with non-SEC registered firms</u>

Regarding non-SEC registered firms, there still seems to be a consensus that the benefits will exceed the costs if auditor changes are disclosed in management reports. The lone exception among the respondents is the group with 30-39 years of experience. As indicated in Table V-8, the mean for this group suggests that the respondents feel that the costs will exceed the benefits of this particular change.

TABLE V-8

EXPERIENCE GROUPS--COSTS/BENEFITS NON-SEC FIRMS

Years of Exper.	Costs Exceeds Benefits	Benefits Exceed Costs	Total	Mean
0-9	44 16.1	81 29.6	125 45.6	1.65
10-19	28 10.2	52 19.0	80 29.2	1.65
20-29	21 7.7	23 8.4	44 16.1	1.52
30-39[a]	10 3.6	5 1.8	15 5.5	1.33
40+[a]	3 1.1	7 2.6	10 3.6	1.70
Total	106 38.7	168 61.3	274[b] 100.0	1.61

Raw chi-square = 4.48326. Significance level = .2138.

[a]For calculation purposes these rows are combined.

[b]Non-responses: 0-9=9; 10-19=11; 20-29=5; 30-39=2; 40+=2.

This point is an interesting one: when examining the issue of independence the same respondent group has the highest mean, suggesting that, more than the others, this group thinks it will increase independence. Consequently, this group has the highest mean in reference to independence, and the lowest mean in reference to costs/ benefits. Again the small number of respondents allows a few respondents to alter the mean greatly.

H_0-9: CPA Breakdown--Independence with SEC registered firms[8]

Table V-9 shows that there is not a significant disagreement between CPA groups as to how disclosure of auditor changes in a management report will affect the CPA's independence. Examining independence with SEC registered firms, the "Big Fifteen" respondents are more likely than the CPAs from "other" firms to suggest that disclosure of auditor changes in a management report will increase independence. As Table V-9 illustrates, 44% of the "Big Fifteen" respondents feel that independence will increase, while only 30% of CPA respondents from other firms feel that independence will increase.

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[8]For more information on the distribution of CPAs, see Chapter IV, "CPA Breakdown Information."

TABLE V-9

BIG FIFTEEN--INDEPENDENCE SEC FIRMS

Size of Firm	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
Big Fifteen	1 .8	1 .8	31 26.1	17 14.3	9 7.6	59 49.6	3.54
Other Firms	2 1.7	1 .8	39 32.8	12 10.1	6 5.0	60 50.4	3.32
Total	3 2.5	2 1.7	70 58.8	29 24.4	15 12.6	119[b] 100.0	3.43

Raw chi-square = 2.53384. Significance level = .2817.

[a]For calculation purposes these columns are combined.

[b]Non-responses: Other-1.

H_0-10: CPA Breakdown--Independence with non-SEC registered firms

Regarding non-SEC registered firms, the CPAs have an even wider difference of opinion. This is indicated by the statistically significant level of .0111. As the 3.08 mean indicates, the CPAs from firms other than the "Big Fifteen" feel that independence will hardly be increased by disclosure of auditor changes in a management report.

While the "Big Fifteen" respondents who feel that independence will increase drops from 42% for SEC firms to 40% for non-SEC firms, the respondents from other firms who think that independence will increase drops from 30% for SEC firms to only 16% for non-SEC firms.

H_0-11: CPA Breakdown--Costs/Benefits with registered firms

Examination of the costs/benefits question for SEC registered firms shows that there is a statistically significant disagreement between the two respondent groups. Fully 74% of the "Big Fifteen" respondents feel that the benefits to society will exceed the costs to society when disclosure of auditor changes in a management report is mandated. At the same time barely more than half of the respondents from other firms (54%) feel that the benefits will be greater than the costs.

TABLE V-10

BIG FIFTEEN--INDEPENDENCE NON-SEC FIRMS

Size of Firm	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
Big Fifteen	1 .8	3 2.5	30 25.4	15 12.7	8 6.8	57 48.3	3.46
Other Firms	3 2.5	1 .8	47 39.8	8 6.8	2 1.7	61 51.7	3.08
Total	4 3.4	4 3.4	77 65.3	23 19.5	10 8.5	118[b] 100.0	3.26

Raw chi-square - 9.00519. Significance level = .0111.

[a]For calculation purposes these columns are combined.

[b]Non-responses: Big Fifteen-2.

TABLE V-11

BIG FIFTEEN--COSTS/BENEFITS SEC FIRMS

Size of Firm	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
Big Fifteen	14 12.5	41 36.6	55 49.1	1.75
Other firms	26 23.2	31 27.7	57 50.9	1.54
Total	40 35.7	72 64.3	112[a] 100.0	1.64

Raw chi-square = 4.11560. Significance level = .0425.

[a]Non-responses: Big Fifteen-4; Other-4.

H_0-12: CPA Breakdown--Costs/Benefits with non-SEC registered firms

As with the issue of SEC registered firms, the CPAs disagree in a statistically significant way regarding non-SEC registered firms. Table V-12 shows that the CPA respondents from "other" firms feel that the costs will exceed the benefits for disclosing auditor changes in management reports. At the same time, the "Big Fifteen" respondents, by a margin to 2 to 1, feel that the benefits will exceed the costs.

TABLE V-12

BIG FIFTEEN--COSTS/BENEFITS NON-SEC FIRMS

Size of Firm	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
Big Fifteen	17 15.2	37 33.0	54 48.2	1.69
Other firms	33 29.5	25 22.3	58 51.8	1.43
Total	50 44.6	62 55.4	112[a] 100.0	1.55

Raw chi-square = 6.31681. Significance level = .0120

[a]Non-responses: Big Fifteen-5; Other-3.

Data Review

Hypotheses rejected

Reviewing the data using an .05 alpha level of significance, the chi-square tests that reject the hypothesis of consensus are:

1. Big Fifteen - Independence Non-SEC firms (Table V-10).

2. Big Fifteen - Costs/Benefits SEC firms (Table V-11).

3. Big Fifteen - Costs/Benefits Non-SEC firms (Table V-12).

Further examination shows that two other tests approach rejection of the null at an .05 level. They are:

1. CPAs/CBMs/CFAs - Independence SEC firms (Table V-1).

2. CPAs/CBMs/CFAs - Costs/Benefits Non-SEC firms (Table V-4).

Table V-13 shows that in all but one case the respondent groups feel that disclosure of auditor changes in a management report will increase the independence of the CPA with respect either to SEC-registered or non-SEC registered clients. The one exception is the group of respondents with forty or more years of experience. On the average this group feels that the proposed change will not affect independence.

Analysis of means of independence decision

Using the 1 to 5 scale, it is possible to state that a group mean of below 3.0 indicates that an average response is that independence will decrease. A group mean of 3.0 indicates that an average response is that independence will not be affected; a group mean above 3.0 indicates that an average response is that independence will increase. The entire set of means falls between 3.17 and 3.71 for SEC registered firms.

The lowest group mean is for those respondents with the most experience, perhaps because the more experienced respondents do not want change, or because they are not convinced that there is an independence problem. Again, it should be pointed out that the limited number of respondents in this group allows a few responses to alter the mean greatly.

The second lowest mean is for the CPAs who did not/ do not work for the "Big Fifteen." Is it possible that

TABLE V-13

COMPARISON OF GROUP MEANS--DISCLOSURE

Group	Inde-pendence Decision SEC	Inde-pendence Decision Non-SEC	Costs Benefits SEC	Costs Benefits Non-SEC
CPAs	3.45	3.31	1.62	1.53
CBMs	3.62	3.45	1.75	1.67
CFAs	3.55	3.50	1.68	1.68
0-9	3.56	3.44	1.69	1.65
10-19	3.58	3.34	1.70	1.65
20-29	3.34*	3.35*	1.61	1.52
30-39	3.71	3.38	1.56	1.33
40+	3.17	3.00	1.70	1.70
Big 15	3.54	3.46	1.75	1.69
Other CPAs	3.32	3.08	1.54	1.43
Total of All Respondents	3.52	3.40	1.67	1.61

*This is the only instance in which the group mean, regarding SEC registered firms, is lower than the mean of the same group regarding non-SEC registered firms.

they feel that if management has to publish an auditor change there will be fewer changes? An extension of this argument is, then, that if there are fewer changes, small firms have fewer opportunities to acquire new clients. It should again be noted that the CPAs have a statistically significant difference of opinion on the costs and benefits of this proposed change for both SEC and non-SEC registered firms.

The highest mean is for the respondent group with 30-39 years of experience. Because of the small number of respondents, this group is also subject to large shifts in the mean due to few responses.

Regarding non-SEC firms, the means of the respondent groups are between 3.0 for the 40+ experience group and 3.5 for CFAs.

In ten of eleven cases (see Table V-13 for the comparison of means), the respondent groups feel that when an SEC-registered firm is involved there will be a greater increase in independence than there is for a non-SEC registered firm. The lone exception is the group with 20-29 years of experience.

Analysis of means of costs/benefits

Considering the 1, 2 scale, it is possible to state that a group mean above 1.5 indicates an average response that the benefits will exceed the costs. Likewise, a group mean below 1.5 indicates an average response that the costs will exceed the benefits.

Two groups representing the non "Big Fifteen" CPAs and the respondents with 30-39 years of experience feel that the costs of disclosure will exceed the benefits. The means of all other groups indicate that benefits will exceed costs, although the CPAs and groups with 20-29 years of experience do not indicate this by a significant margin.

The small number of respondents in the group with 30-39 years of experience makes it unwise to interpret their results since so few responses may greatly affect the means.

Conclusions

Even though there are some significant differences among various respondent groups as to how disclosure of auditor changes in a management report will affect the independence of the CPA regarding a client, all groups except one (the group with 40+ years experience examining non-SEC firms) feel that it will increase independence.

At the same time all groups except two feel that the benefits to society will exceed the costs, should disclosure be required.

The findings are consistent with the recommendations of the Commission on Auditors' Responsibilities which states that disclosure of auditor changes should be required in a management report.

CHAPTER VI

GIFTS AND DISCOUNT PURCHASES

Literature Review

Little literature exists concerning the issue of gifts and discount purchases from clients by an independent auditor. One of the few official pronouncements concerning gifts is Ethics Ruling No. 1 which is restated in the AICPA's Code of Professional Ethics: If an employee or partner accepts more than a token gift from a client, even with the knowledge of the member's firm, the appearance of independence may be lacking.[1]

The only empirical study to date with respect to gifts and/or discount purchases from clients by independent auditors was done by John Grant Rhode.[2] Of the total respondents to Rhode's survey, 76% believe that accepting gifts from audit clients other than infrequent meals or

[1]American Institute of Certified Public Accountants, Ethics Rulings on Independence, Integrity and Objectivity, Code of Professional Standards (New York: American Institute of Certified Public Accountants, 1977), ET Section 191.002.

[2]John Grant Rhode, "The Independent Auditors' Work Environment: A Survey," Commission on Auditors' Responsibilities Research Study No. 4 (New York: American Institute of Certified Public Accountants, 1978). See Chapter II for more information on this research.

gifts with a value of less than $25.00 will affect the auditors' ability to resist pressures to subordinate professional judgment. Six percent of the respondents had at some time accepted gifts with a value of over $25.00 from an audit client. Asked the value of gifts accepted from all audit clients, fully one-third of the respondents answered that they had accepted gifts greater than $25.00 in cumulative value.

The Commission on Auditors' Responsibilities recommends that all firms should develop for their staffs carefully drawn rules on gifts and discounts, and that the AICPA should provide more definitive guidelines on amounts to be considered "token."[3]

The Metcalf Committee did not make any references to gifts or purchases at discounts.

Analysis of Data

The remaining portion of this chapter is devoted to the presentation and interpretation of the data. Each hypothesis is investigated separately; a review and summary are presented in the section titled Data Review.

Specific hypotheses

The specific hypotheses to be tested in this section are:

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[3]American Institute of Certified Public Accountants, Commission on Auditors' Responsibilities, Commission on Auditors' Responsibilities: Report, Conclusions and Recommendations (New York: American Institute of Certified Public Accountants, 1978), p. 118.

H_0-1: There are no significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the effect that adoption of policies on gifts and discounts will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_1-1: There are significant differences among members of the AICPA, Corporate Bar and ICFA regarding their perceptions of the effect that adoption of policies on gifts and discounts will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_0-2: There are no significant differences among members of the AICPA, Corporate Bar and ICFA regarding their perceptions of the effect that adoption of policies on gifts and discounts will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_1-2: There are significant differences among members of the AICPA, Corporate Bar and ICFA regarding their perceptions of the effect that adoption of policies on gifts and discounts will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_0-3: There are no significant differences among members of the AICPA, Corporate Bar and ICFA regarding their perceptions of the costs and benefits to society as a whole, of adopting policies on gifts and discounts for SEC registered firms.

H_1-3: There are significant differences among members of the AICPA, Corporate Bar and ICFA regarding their perceptions of the costs and benefits to society as a whole, of adopting policies on gifts and discounts for SEC registered firms.

H_0-4: There are no significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the costs and benefits to society as a whole, of adopting policies on gifts and discounts for non-SEC registered firms.

H_1-4: There are significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the costs and benefits to society as a whole, of adopting policies on gifts and discounts for non-SEC registered firms.

H_0-5: There are no significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years, regarding their perceptions of the effect that adoption of policies on gifts and discounts will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_1-5: There are significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years, regarding their perceptions of the effect that adoption of policies on gifts and discounts will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_0-6: There are no significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years, regarding their perceptions of the effect that adoption of policies on gifts and discounts will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_1-6: There are significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years, regarding their perceptions of the effect that adoption of policies on gifts and discounts will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_0-7: There are no significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years, regarding their perceptions as to the costs and benefits to society as a whole, of adopting policies on gifts and discounts for SEC registered firms.

H_1-7: There are significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years, regarding their perceptions of the costs and benefits to society as a whole, of adopting policies on gifts and discounts for SEC registered firms.

H_0-8: There are no significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years, regarding their perceptions of the costs and benefits to society as a whole, of adopting policies on gifts and discounts for non-SEC registered firms.

H_1-8: There are significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years, regarding their perceptions of the costs and benefits to society as a whole, of adopting policies on gifts and discounts for non-SEC registered firms.

H_0-9: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the effect that adoption of policies on gifts and discounts will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_1-9: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the effect that adoption of policies on gifts and discounts will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_0-10: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the effect that adoption of policies on gifts and discounts will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_1-10: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the effect that adoption of policies on gifts and discounts will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_0-11: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms regarding their perceptions of the costs and benefits to society as a whole, of adopting policies on gifts and discounts for SEC registered firms.

H_1-11: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other

CPA firms regarding their perceptions of the costs and benefits to society as a whole, of adopting policies on gifts and discounts for SEC registered firms.

H_0-12: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the costs and benefits to society as a whole, of adopting policies on gifts and discounts for non-SEC registered firms.

H_1-12: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions as to the costs and benefits to society as a whole, of adopting policies on gifts and discounts for non-SEC registered firms.

H_0-1: CPAs/CBMs/CFAs--Independence with SEC registered firms

As Table VI-1 shows, there is a significant disagreement at the .05 alpha level among the groups as to how adoption of policies on gifts and discounts will affect the CPA's independence.[4] While only 14% of the CPAs feel that the change will greatly increase

[4]For more information on the statistical analysis, see Chapter IV.

TABLE VI-1

CPAs/CBMs/CFAs--INDEPENDENCE SEC FIRMS

	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
CPAs	2	5	58	45	18	128	3.56
	.7	1.7	19.5	15.1	6.0	43.0	
CBMs	3	3	26	29	29	90	3.87
	1.0	1.0	8.7	9.7	9.7	30.2	
CFAs	1	2	28	33	16	80	3.76
	.3	.7	9.4	11.1	5.4	26.8	
Total	6	10	112	107	63	298[b]	3.71
	2.0	3.4	37.6	35.9	21.1	100.0	

Raw chi-square = 12.60870. Significance level = .0134

[a]For calculation purposes these columns are combined.

[b]Non-responses: CPAs-1; CFAs-4.

independence, fully one-third of the CBMs feel that independence will greatly increase, and one-fifth of the CFAs feel that independence will greatly increase.

$H_0 2$: CPAs/CBMs/CFAs--Independence with non-SEC registered firms

Table VI-2 also indicates that there is a significant disagreement among the groups as to how adoption of policies on gifts and discounts will affect the auditor's independence with respect to non-SEC clients.

Examination of the means reveals that the CBMs and CFAs have an identical mean score while the CPAs have a much lower mean. Comparison of the means with those in Table VI-1 with respect to SEC clients shows that the CPAs scores are virtually unchanged, while the CBMs have dropped the CFAs have risen so that they are equal. Again, nearly 50% of the CPAs feel that the change will not increase independence.

H_0-3: CPAs/CBMs/CFAs--Costs/Benefits with SEC registered firms

Table VI-3 shows that all three groups feel that the benefits to society will exceed the costs to society with respect to adopting policies regarding gifts and discounts to the CPA from SEC clients. Although not significant at the .05 alpha level, there is a difference of opinion on this issue: the CPAs have the lowest mean, the CBMs the highest; CFAs fall approximately midway

TABLE VI-2

CPAs/CBMs/CFAs--INDEPENDENCE NON-SEC FIRMS

	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
CPAs	4	4	53	50	16	127	3.55
	1.4	1.4	18.0	17.0	5.4	43.2	
CBMs	3	2	29	29	26	89	3.82
	1.0	.7	9.9	9.9	8.8	30.3	
CFAs	1	2	25	32	18	78	3.82
	.3	.7	8.5	10.9	6.1	26.5	
Total	8	8	107	111	60	294[b]	3.70
	2.7	2.7	36.4	37.8	20.4	100.0	

Raw chi-square = 10.49158. Significance level = .0329

[a]For calculation purposes these columns are combined.

[b]Non-responses: CPAs-2; CBMs-1, CFAs-6.

TABLE VI-3

CPAs/CBMs/CFAs--COSTS/BENEFITS SEC FIRMS

	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
CPAs	40 14.4	74 26.7	114 41.2	1.65
CBMs	17 6.1	67 24.2	84 30.3	1.80
CFAs	21 7.6	58 20.9	79 28.5	1.73
Total	78 28.2	199 71.8	277[a] 100.0	1.72

Raw chi-square = 5.40763. Significance level = .0669

[a]Non-responses: CPAs-15; CBMs-6; CFAs-5.

between the two. These responses are consistent with those regarding the increase or decrease of independence noted in Table VI-1.

$H_0$4: CPAs/CBMs/CFAs--Costs/Benefits with non-SEC registered firms

Study of responses regarding the costs/benefits decision with respect to non-SEC clients shows more agreement among the three groups. Again all three groups feel that the benefits will exceed the costs to society. CPAs are still the least convinced, but the gap between them and the most convinced (CBMs) are narrowed. On the whole, more than two-thirds of the respondents feel that the benefits to society will exceed the costs.

TABLE VI-4

CPAs/CBMs/CFAs--COSTS/BENEFITS NON-SEC FIRMS

	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
CPAs	42 15.3	72 26.3	114 41.6	1.63
CBMs	20 7.3	63 23.0	83 30.3	1.76
CFAs	20 7.3	57 20.8	77 28.1	1.74
Total	82 29.9	192 70.1	274[a] 100.0	1.70

Raw chi-square - 4.51877. Significance level = .1044.

[a]Non-response: CPAs-15; CBMs-7; CFAs-7.

H_0-5: Years of experience--Independence with SEC registered firms

Table VI-5 indicates that although there is not a statistical significance when the number of years of experience is considered, the means of the groups increase with years of experience. One point of interest is that out of the respondents that have 30 or more years of experience, only 25% feel that independence will decrease with the adoption of policies on gifts and discounts.

TABLE VI-5

EXPERIENCE GROUPS--INDEPENDENCE SEC FIRMS

Years of Exper.	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
0-9	4	6	52	46	25	133	3.62
	1.3	2.0	17.4	15.4	8.4	44.6	
10-19	0	3	34	33	18	88	3.75
	0	1.0	11.4	11.1	6.0	29.5	
20-29	1	1	20	15	12	49	3.73
	.3	.3	6.7	5.0	4.0	16.4	
30-39[b]	1	0	4	7	5	17	3.88
	.3	0	1.3	2.3	1.7	5.7	
40+[b]	0	0	2	6	3	11	4.09
	0	0	.7	2.0	1.0	3.7	
Total	6	10	112	107	63	298[c]	3.71
	2.0	3.4	37.6	35.9	21.1	100.0	

Raw chi-square = 5.30576. Significance level = .5052.

[a]For calculation purposes these columns are combined.

[b]For calculation purposes these rows are combined.

[c]Non-responses: 0-9=1, 10-19=3; 40+=1.

At the same time, each of the three groups with fewer than 30 years of experience, more than 40% of the respondents think that the adoption of policies on gifts and discounts will decrease independence.

H_0-6: Years of experience--Independence with non-SEC registered firms

Table VI-6 indicates that respondents generally do not change their responses with regard to non-SEC firms and the adoption of policies on gifts and discount purchases. In fact, the only change noted in the responses regarding SEC firms and non-SEC firms is the fact that the respondents agree more closely regarding non-SEC firms.

H_0-7: Years of experience--Costs/Benefits with SEC registered firms

When asked about the costs and benefits connected with policies on gifts and discount purchases for SEC clients, the respondent groups are again in close agreement as to the effect of these policies. Although the least experienced group has a slightly lower mean, the difference among the groups are very small.

TABLE VI-6

EXPERIENCE GROUPS--INDEPENDENCE NON-SEC FIRMS

Years of Exper.	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
0-9	6 2.0	5 1.7	47 16.0	48 16.3	26 8.8	132 44.9	3.63
10-19	0 0	2 .7	34 11.6	34 11.6	17 5.8	87 29.6	3.76
20-29	1 .3	1 .3	18 6.1	18 6.1	10 3.4	48 16.3	3.73
30-39[b]	1 .3	0 0	5 1.7	6 2.0	4 1.4	16 5.4	3.75
40+[b]	0 0	0 0	3 1.0	5 1.7	3 1.0	11 3.7	4.00
Total	8 2.7	8 2.7	107 36.4	111 37.8	60 20.4	294[c] 100.0	3.70

Raw chi-square = 1.25545. Significance level = .9741.

[a]For calculation purposes these columns are combined.

[b]For calculation purposes these rows are combined.

[c]Non-responses: 0-9=2; 10-19=4; 20-29=1; 30-39=1; 40+=1.

TABLE VI-7

EXPERIENCE GROUPS--COSTS/BENEFITS SEC FIRMS

Years of Exper.	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
0-9	38 13.7	87 31.4	125 45.1	1.70
10-19	22 7.9	62 22.4	84 30.3	1.74
20-29	12 4.3	33 11.9	45 16.2	1.73
30-39[a]	4 1.4	11 4.0	15 5.4	1.73
40+[a]	2 .7	6 2.2	8 2.9	1.75
Total	78 28.2	199 71.8	277[b] 100.0	1.72

Raw chi-square = .56958. Significance level = .9034.

[a]For calculation purposes these rows are combined.

[b]Non-responses: 0-9=9; 10-19=7; 20-29=4; 30-39=2; 40+=4.

$H_0$8: Years of experience--Costs/Benefits with non-SEC registered firms

Table VI-8 reveals that the respondents are fairly close in their views regarding the costs and benefits of policies on gifts and discount purchases. Interesting is the group with 30-39 years of experience, which has the lowest mean, and comes more closely than any of the other five groups to stating that costs will exceed benefits.

It should be noted, however, that the small number of respondents in that group allow the mean to be affected greatly by just a few responses.

TABLE VI-8

EXPERIENCE GROUPS--COSTS/BENEFITS NON-SEC FIRMS

Years of Exper.	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
0-9	40 14.6	85 31.0	125 45.6	1.68
10-19	23 8.4	60 21.9	83 30.3	1.72
20-29	12 4.4	32 11.7	44 16.1	1.73
30-39[a]	5 1.8	9 3.3	14 5.1	1.64
40+[a]	2 .7	6 2.2	8 2.9	1.75
Total	82 29.9	192 70.1	274[b] 100.0	1.70

Raw chi-square = .63588. Significance level = .8882.

[a]For calculation purposes these rows are combined.

[b]Non-responses: 0-9=9; 10-19=8; 20-29=5; 30-39=3; 40+=4.

H_0-9: CPA Breakdown--Independence with SEC registered firms[5]

Although the CPAs are in general agreement as to how policies on gifts and discount purchases will affect independence with SEC registered firms, there are some differences of opinion. This is perhaps best indicated by the fact that 62% of the "Big Fifteen" respondents feel the policies will not increase independence, while only 45% of the "Other" respondents think there will be no increase in independence.

H_0-10: CPA Breakdown--Independence with non-SEC registered firms

Regarding independence with non-SEC registered firms, the CPAs agree even more closely than they do regarding SEC registered firms. Respondents who worked for firms other than the "Big Fifteen" still believe that the proposed changes will increase independence by a greater margin than do the respondents from the "Big Fifteen" firms. However, the difference is not statistically significant.

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[5]For more information on the distribution of CPAs, see Chapter IV, "CPA Breakdown Information."

TABLE VI-9

BIG FIFTEEN--INDEPENDENCE SEC FIRMS

Size of Firm	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
Big Fifteen	2 1.7	2 1.7	33 27.7	16 13.4	6 5.0	59 49.6	3.37
Other Firms	0 0	3 2.5	24 20.2	23 19.4	10 8.4	60 50.4	3.67
Total	2 1.7	5 4.2	57 47.9	39 32.8	16 13.4	119[b] 100.0	3.52

Raw chi-square = 3.81078. Significance level = .1488.

[a]For calculation purposes these columns are combined.

[b]Non-responses: Other-1.

TABLE VI-10

BIG FIFTEEN--INDEPENDENCE NON-SEC FIRMS

Size of Firm	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
Big Fifteen	3 2.5	1 .8	28 23.5	22 18.5	4 3.4	58 48.8	3.40
Other Firms	1 .8	3 2.5	24 20.2	22 18.5	11 9.2	61 51.2	3.62
Total	4 3.4	4 3.4	52 43.7	44 37.0	15 12.6	119 100.0	3.52

Raw chi-square = 3.45990. Significance level = .1773.

[a]For calculation purposes these columns are combined.

[b]Non-responses: Big Fifteen-1.

H_0-11: CPA Breakdown--Costs/Benefits with SEC registered firms

Examination of Table VI-11 shows that both groups of respondents feel that policies on gifts and discount purchases will have more benefits than costs. There is virtually no difference among the means of the respondent groups on this question.

TABLE VI-11

BIG FIFTEEN--COSTS/BENEFITS SEC FIRMS

Size of Firm	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
Big Fifteen	19 18.1	30 28.6	49 46.7	1.61
Other Firms	19 18.1	37 35.2	56 53.3	1.66
Total	38 36.2	67 63.8	105 100.0	1.64

Raw chi-square = .09740. Significance level = .7550.

[a]Non-responses: Big Fifteen-10; Other-5.

H_0-12: CPA Breakdown--Costs/Benefits with non-SEC registered firms

When referring to non-SEC registered firms, the respondent groups again have very similar feelings. The respondents who worked for "Other" firms believe that the benefits will exceed the costs by a greater margin than do the respondents from the "Big Fifteen" firms, but the differences are very small and not statistically significant.

TABLE VI-12

BIG FIFTEEN--COSTS/BENEFITS NON-SEC FIRMS

Size of Firm	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
Big Fifteen	20 18.9	29 27.4	49 46.2	1.59
Other Firms	20 18.9	37 34.9	57 53.8	1.65
Total	40 37.7	66 62.3	106[a] 100.0	1.62

Raw chi-square = .16459. Significance level = .6850.

[a]Non-responses: Big Fifteen-10; Other-4.

Data Review

Hypotheses rejected

In a review of the data with an .05 alpha level of significance, the only chi-square tests that reject the hypothesis of consensus are:

1. CPAs/CBMs/CFAs - Independence SEC firms (Table VI-1).
2. CPAs/CBMs/CFAs - Independence non-SEC firms (Table VI-2).

Further study reveals that one other test approaches rejection of the null at an .05 level:

1. CPAs/CBMs/CFAs - Costs/Benefits SEC firms (Table VI-3).

Review of the data of this chapter makes it clear that all respondent groups feel that required adoption of rules on gifts and discount purchases will increase the independence of the CPA with respect either to SEC registered or non-SEC registered clients.

Analysis of means of independence decision

Using the 1 to 5 scale, it is possible to state that a group mean of below 3.0 indicates an average response that independence will be decreased. It is also possible to state that a group mean of 3.0 indicates an average response that independence will not be affected; a group mean above 3.0 indicates an average response that independence will be increased. The entire set of means falls between 3.37 and 4.09 for SEC registered firms and non-SEC registered firms.

The lowest mean, by a wide margin, is for the respondents who work/worked for "Big Fifteen" firms. This may be explained in part by the more elaborate rules on gifts and discount purchases that the "Big Fifteen" firms have.

At the other end of the spectrum of means are the highest means for the group of respondents with the longest experience. The question can be asked, "Have the more experienced workers seen more abuses?" Again, caution should be exercised because of the small number of respondents in this group.

In contrast to the issues of rotation and disclosure, there is no consistency among the respondents regarding the question of SEC registered versus non-SEC registered firms on this issue of gifts and discount purchases. There are some groups that feel independence will increase more for SEC firms than for non-SEC firms; some groups believe the opposite. No trend can be noted by the author.

Analysis of means of costs/benefits

Considering the 1, 2 scale, it is possible to state that a group mean above 1.5 indicates an average response that the benefits will exceed the costs. Likewise, a group mean below 1.5 indicates an average response that the costs will exceed the benefits.

Table VI-13 shows that all groups feel not only that independence will be increased by mandating policies on gifts and discount purchases, but also that the benefits of such policies will exceed the costs. Although there is more consistency regarding SEC and non-SEC registered firms (most groups feel benefits exceed costs to a greater degree for SEC firms than for non-SEC firms), still there seems to be no discernible trend.

TABLE VI-13

COMPARISON OF GROUP MEANS--GIFTS

Group	Independence Decision SEC	Independence Decision Non-SEC	Costs Benefits SEC	Costs Benefits Non-SEC
CPAs	3.56	3.55	1.65	1.63
CBMs	3.87	3.82	1.80	1.76
CFAs	3.76	3.82	1.73	1.74
0-9	3.62	3.63	1.70	1.68
10-19	3.75	3.76	1.74	1.72
20-29	3.73	3.73	1.73	1.73
30-39	3.88	3.75	1.73	1.64
40+	4.09	4.00	1.75	1.75
Big 15	3.37	3.40	1.61	1.59
Other CPAs	3.67	3.62	1.60	1.65
Total of All Respondents	3.71	3.70	1.72	1.70

The "Big Fifteen" CPAs feel the least strongly (lowest mean) about benefits exceeding costs; the CBMs have the strongest feelings (highest mean) about benefits exceeding costs.

Conclusions

Though there are some significant differences among various respondent groups as to how policies on gifts and discount purchases will affect the independence of the CPA in his/her relationship with a client, all groups do feel that such policies will increase independence.

At the same time all groups feel that the benefits to society will exceed the costs to society should these policies be required.

The findings are consistent with the recommendations of the Commission on Auditors' Responsibilities that policies on gifts and discount purchases be required.

CHAPTER VII

EXECUTIVE SEARCH AND PLACEMENT

Literature Review

The debate about auditor independence and non-auditing functions usually focuses on the issues of management advisory services and tax services. This may be due in part to the fact that these two non-auditing functions generate much more revenue for CPAs than the other non-auditing functions do.

There are, however, many other non-auditing functions performed by some or by all CPAs. Currently, one of the more talked-about of these services is the search for and placement of executives in client firms. The arguments for and against executive search and placement seem to have a common theme.

The basic argument for allowing CPAs to search for and to place executives is that there has been no instance for which it can be shown that such activities inhibited independence. The fundamental argument against executive search and placement is based on a number of surveys in which a large portion of the respondents indicated their beliefs that executive search and placement may inhibit independence. The latter argument involves the appearance of independence rather than independence in fact.

Arguments for executive search and placement

In 1969, in its final report the AICPA ad hoc committee on independence suggests that executive recruiting can be proscribed without any great harm to the profession because of the very minor part that it played in most firms.[1] The committee continues:

> In other words, a proscription of any particular service requires more than a vague visceral feeling that a particular service by a CPA "just does not look right."[2]

The committee also says that there have been no allegations that management advisory services have impaired the independence of CPAs in fact. The committee concludes by suggesting that each member of the AICPA choose the services he/she offers in the light of possible public reaction.[3]

Referring to the final report of the ad hoc committee, an editorial in the Journal of Accountancy suggests:

> In the course of its work the committee reached the conclusion that "the profession is fortunate in having achieved a remarkable reputation for integrity and independence. If this is true and if, as the committee urges, the profession continues to justify its reputation,

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[1]"Final Report of Ad Hoc Committee on Independence," Statement in Quotes, Journal of Accountancy 128 (December 1969): 54.

[2]Ibid.

[3]Ibid., p. 56.

> there seems to be little likelihood of any serious impairment of independence in fact or in appearance.[4]

Arguments against executive search and placement

In their article on audit independence, Beams and Killough say that the auditor should not provide non-audit services.[5] They also say that the auditor jeopardizes his independence if he has non-audit affiliations with a client. However, the authors do provide for an alternative: recruiting services are handled by an administrative division within a firm which has little or no contact with the audit division. The personnel between the two divisions would be mutually exclusive.[6]

Making perhaps a stronger case against executive search and placement are three research studies done in the 1970's. Each of these studies has indicated the respondents' concern about executive recruitment.

In his study of independence and MAS, Titard found that 27% of the responding financial executives and analysts think that executive recruitment may result in some loss of audit independence.[7]

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[4] "On Independence and Management Advisory Services," Editors' Notebook, Journal of Accountancy 128 (December 1969): 28.

[5] Floyd A. Beams and Larry N. Killough, Audit Independence--An Extension of the Concept," The National Public Accountant 15 (December 1970): 26.

[6] Ibid.

[7] Pierre L. Titard, "Independence and MAS--Opinions of Financial Statement Users," The Journal of Accountancy 132 (July 1971): 50.

Although very small in number, some subjects in Rhode's survey state that there was pressure from supervisors to accept the representations of former members of their firm now employed by the client or from individuals placed with the client after an executive search by the CPA firms.[8] This seems to be more of a problem of independence in fact than in appearance.

In research done for Deloitte Haskins & Sells, Reichman Research Inc. found that 41% of the responding corporate financial officers feel that executive recruitment can potentially cause a conflict of interest if offered to clients by CPA firms.[9] No other type of management service concerned the corporate financial officers as much as executive recruitment.

Committee positions

The Metcalf Report suggests that to restore public confidence in the actual independence of auditors, Federal Securities laws should promulgate and enforce strict standards of conduct for auditors.[10] Further, it is recommended that activities by auditors which impair their independence should be specifically prohibited. As an

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[8] Rhode, Auditor's Work Environment, pp. 299-300.

[9] Reichman Research, Inc., An Opinion Survey of the Accounting Profession, Sponsored by Deloitte Haskins & Sells (New York 1978), pp. 31-32.

[10] Metcalf, Accounting Establishment, p. 22.

example of such activities, the committee cites direct or indirect representation of clients' interest in performance of non-accounting management advisory services for public or private clients.

The Commission on Auditors' Responsibilities suggests that it would be impractical to recommend that companies be prevented from hiring individuals previously employed by public accounting firms. However, it does suggest that firms should not engage in recruiting or placement of individuals who would be directly involved in the decision to select or retain independent auditors.[11]

Analysis of Data

The remaining portion of this chapter is devoted to the presentation and interpretation of the data. Each hypothesis is investigated separately; a review and summary are presented in the section titled Data Review.

Specific Hypotheses

The specific hypotheses to be tested in this section are:

H_0-1: There are no significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the effect that a prohibition of executive search and placement services will

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[11] AICPA, Report, Conclusions, and Recommendations, pp. 100-101.

have on the CPA's independence with respect to the CPA's SEC registered clients.

H_1-1: There are significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the effect that a prohibition of executive search and placement services will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_0-2: There are no significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the effect that a prohibition of executive search and placement services will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_1-2: There are significant differences between members of the AICPA, Corporate Bar and ICFA regarding their perceptions of the effect that a prohibition of executive search and placement services will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_0-3: There are no significant differences between members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the costs and benefits to society as a whole, of a prohibition of executive search and placement services for SEC registered firms.

H_1-3: There are significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the costs and benefits to society as a whole, of a prohibition of executive search and placement services for SEC registered firms.

H_0-4: There are no significant differences between members of the AICPA, Corporate Bar and ICFA, regarding their perceptions of the costs and benefits to society as a whole, of a prohibition of executive search and placement services for non-SEC registered firms.

H_1-4: There are significant differences between members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the costs and benefits to society as a whole, of a prohibition of executive search and placement services for non-SEC registered firms.

H_0-5: There are no significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years, regarding their perceptions of the effect that a prohibition of executive search and placement services will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_1-5: There are significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years, and over 29 years, regarding their perceptions of the effect that a prohibition of executive search and placement services will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_0-6: There are no significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years, regarding their perceptions of the effect that a prohibition of executive search and placement services will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_1-6: There are significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years, regarding their perceptions of the effect that a prohibition of executive search and placement services will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_0-7: There are no significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years, regarding their perceptions of the costs and benefits to society as a whole, of a prohibition of executive search and placement services for SEC registered firms.

H_1-7: There are significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years, regarding their perceptions of the costs and benefits to society as a whole, of a prohibition of executive search and placement services for SEC registered firms.

H_0-8: There are no significant differences between respondents who have experience of 0-9 years, 10-19 years, 20-29 years, and over 29 years, regarding their perceptions of the costs and benefits to society as a whole, of a prohibition of executive search and placement services for non-SEC registered firms.

H_1-8: There are significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years, regarding their perceptions of the costs and benefits to society as a whole, of a prohibition of executive search and placement services for non-SEC registered firms.

H_0-9: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the effect that a prohibition of executive search and placement services will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_1-9: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the effect that a prohibition of executive search and placement services will have on the CPA's independence with respect to the CPA's SEC registered clients.

H_0-10: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the effect that a prohibition of executive search and placement services will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_1-10: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the effect that a prohibition of executive search and placement services will have on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_0-11: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the costs and benefits to society as a whole, of a prohibition of executive search and placement services for SEC registered firms.

H_1-11: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the costs and benefits to society as a whole, of a prohibition of executive search and placement services for SEC registered firms.

H_0-12: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the costs and benefits to society as a whole, of a prohibition of executive search and placement services for non-SEC registered firms.

H_1-12: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for the other CPA firms regarding their perceptions of the costs and benefits to society as a whole, of a prohibition of executive search and placement services for non-SEC registered firms.

$H_0 1$: CPAs/CBMs/CFAs--Independence with SEC registered firms

As Table VII-1 shows, there is no significant disagreement among the groups as to how regulation of executive search and placement will affect the CPA's independence with SEC registered firms.[12] Fully 50% of the CPAs do not feel the recommended change will increase independence, while only 41% of the CFAs feel that independence will not be increased.

$H_0 2$: CPAs/CBMs/CFAs--Independence with non-SEC registered firms

Table VII-2 shows that the groups agree even more closely when asked about non-SEC registered firms. More CPAs than CFAs feel that independence will not be increased, but the gap has narrowed. Also noteworthy is the fact that 52% of the total respondents feel that independence will not be increased for non-SEC registered firms.

[12]For more information on the statistical analysis, see Chapter IV.

TABLE VII-1

CPAs/CBMs/CFAs--INDEPENDENCE SEC FIRMS

	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
CPAs	2	5	57	46	17	127	3.56
	.7	1.7	19.5	15.7	5.8	43.3	
CBMs	1	3	36	28	15	83	3.64
	.3	1.0	12.3	9.6	5.1	28.3	
CFAs	2	3	29	38	11	83	3.64
	.7	1.0	9.9	13.0	3.8	28.3	
Total	5	11	122	112	43	293[b]	3.60
	1.7	3.8	41.6	38.2	14.7	100.0	

Raw chi-square = 3.69966. Significance level = .4482.

[a]For calculation purposes these columns are combined.

[b]Non-responses: CPAs-2; CBMs-7; CFAs-1.

TABLE VII-2

CPAs/CBMs/CFAs--INDEPENDENCE NON-SEC FIRMS

	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
CPAs	1	8	60	39	18	126	3.52
	.3	2.7	20.5	13.3	6.1	43.0	
CBMs	0	4	41	28	12	85	3.56
	0	1.4	14.0	9.6	4.1	29.0	
CFAs	3	3	33	29	14	82	3.59
	1.0	1.0	11.3	9.6	4.8	28.0	
Total	4	15	134	96	44	293[b]	3.55
	1.4	5.1	45.7	32.8	15.0	100.0	

Raw chi-square = 1.12320. Significance level = .8906.

[a]For calculation purposes these columns are combined.

[b]Non-responses: CPAs-3; CBMs-5; CFAs-2.

H_0-3: CPAs/CBMs/CFAs--Costs/Benefits with SEC registered firms

Regarding the costs and benefits to society, the responses of the CPAs are evenly divided as to regulations concerning executive placement and search. Both the CBMs and CFAs feel that the benefits will exceed the costs, but, on this issue as well, the responses of the CBMs approach an even division.

TABLE VII-3

CPAs/CBMs/CFAs--COSTS/BENEFITS SEC FIRMS

	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
CPAs	59 21.9	59 21.5	118 43.1	1.50
CBMs	39 14.2	42 15.3	81 29.6	1.52
CFAs	33 12.0	42 15.3	75 27.4	1.56
Total	131 47.8	143 52.2	274[a] 100.0	1.52

Raw chi-square = .66684. Significance level = .7165.

[a]Non-responses: CPAs-11; CBMs-9; CFAs-9.

H_0-4: CPAs/CBMs/CFAs--Costs/Benefits with non-SEC registered firms

Unlike the issue of independence, regarding costs and benefits, the gap between the means for CPAs and CFAs gap widens when the respondents are asked about non-SEC registered firms compared to SEC registered firms. The CPAs and CBMs are almost in agreement: 46% of each group feels that the benefits will exceed the costs. At the same time, 56% of the CFAs feel that the benefits will exceed the costs.

TABLE VII-4

CPAs/CBMs/CFAs--COSTS/BENEFITS NON-SEC FIRMS

	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
CPAs	63 23.0	55 20.1	118 43.1	1.47
CBMs	43 15.7	38 13.9	81 29.6	1.47
CFAs	33 12.0	42 15.3	75 27.4	1.56
Total	139 50.7	135 49.3	274[a] 100.0	1.49

Raw chi-square = 1.87302. Significance level = .3920.

[a]Non-responses: CPAs-11; CBMs-9; CFAs-9.

H_0-5: Years of experience--Independence with SEC registered firms

Table VII-5 indicates that there is no correlation between years of experience and feelings as to how regulations on executive search and placement will affect independence for SEC firms. The two groups with the highest percentage of respondents who believe that independence will not be increased include both the least experienced and the most experienced respondents.

H_0-6: Years of experience--Independence with non-SEC registered firms

As in the responses regarding SEC registered firms, it appears that there is no correlation between the respondent groups based on experience and their feelings about how independence will/will not be increased. However, when considering non-SEC registered firms, 52% of the total respondents feel that independence will not be increased by regulations on executive search and placement.

TABLE VII-5

EXPERIENCE GROUPS--INDEPENDENCE SEC FIRMS

Years of Exper.	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
0-9	1	8	57	48	16	130	3.54
	.3	2.7	19.5	16.4	5.5	44.4	
10-19	1	1	36	39	11	88	3.66
	.3	.3	12.3	13.3	3.8	30.0	
20-29	3	1	15	17	11	47	3.68
	1.0	.3	5.1	5.8	3.8	16.0	
30-39[b]	0	0	8	4	4	16	3.75
	0	0	2.7	1.4	1.4	5.5	
40+[b]	0	1	6	4	1	12	3.42
	0	.3	2.0	1.4	.3	4.1	
Total	5	11	122	112	43	293[c]	3.60
	1.7	3.8	41.6	38.2	14.7	100.0	

[a]For calculation purposes these columns are combined.

[b]For calculation purposes these rows are combined.

[c]Non-responses: 0-9=4; 10-19=3; 20-29=2; 30-39=1.

[d]Insufficient expected cell sizes for statistical tests.

TABLE VII-6

EXPERIENCE GROUPS--INDEPENDENCE NON-SEC FIRMS

Years of Exper.	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
0-9	1 .3	11 3.8	61 20.8	41 14.0	15 5.1	129 44.0	3.45
10-19	2 .7	1 .3	42 14.3	29 9.9	15 5.1	89 30.4	3.61
20-29	1 .3	2 .7	15 5.1	18 6.1	11 3.8	47 16.0	3.77
30-39[b]	0 0	0 0	9 3.1	4 1.4	3 1.0	16 5.5	3.63
40+[b]	0 0	1 .3	7 2.4	4 1.4	0 0	12 4.1	3.25
Total	4 1.4	15 5.1	134 45.7	96 32.8	44 15.0	293[c] 100.0	3.55

[a]For calculation purposes these columns are combined.

[b]For calculation purposes these rows are combined.

[c]Non-responses: 0-9=5; 10-19=2; 20-29=2; 30-30=1.

[d]Insufficient expected cell sizes for statistical tests.

H_0-7: Years of experience--Costs/Benefits with SEC registered firms

Table VII-7 reveals that all respondent groups, except for the most experienced (the small number of respondents in this group should be noted once again), feel that the benefits to society will exceed the costs to society. However, the numbers are extremely close to the mid-point mean or evenness in terms of percentages of those who believe that costs will exceed benefits, and those who believe benefits will exceed costs.

TABLE VII-7

EXPERIENCE GROUPS--COSTS/BENEFITS SEC FIRMS

Years of Exper.	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
0-9	59 21.5	64 23.4	123 44.9	1.52
10-19	38 13.9	45 16.4	83 30.3	1.54
20-29	21 7.7	21 7.7	42 15.3	1.50
30-39[a]	7 2.6	9 3.3	16 5.8	1.56
40+[a]	6 2.2	4 1.5	10 3.6	1.40
Total	131 47.8	143 52.2	274[b] 100.0	1.52

Raw chi-square = .26858. Significance level = .9658.

[a]For calculation purposes these rows are combined.

[b]Non-responses: 0-9=11; 10-19=8; 20-9=7; 30-39=1; 40+=2.

H_0-8: Years of experience--Costs/Benefits with non-SEC registered firms

Table VII-8 shows that, regarding non-SEC registered firms, none of the respondent groups feel that the benefits will exceed the costs. Again, the responses are very evenly divided between the two choices.

TABLE VII-8

EXPERIENCE GROUPS--COSTS/BENEFITS NON-SEC FIRMS

Years of Exper.	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
0-9	61 22.3	61 22.3	122 44.5	1.50
10-19	42 15.3	42 15.3	84 30.7	1.50
20-29	22 8.0	20 7.3	42 15.3	1.48
30-39[a]	8 2.9	8 2.9	16 5.8	1.50
40+[a]	6 2.2	4 1.5	10 3.6	1.40
Total	139 50.7	135 49.3	274[b] 100.0	1.49

Raw chi-square = .19073. Significance level = .9791.

[a]For calculation purposes these rows are combined.

[b]Non-responses: 0-9=12; 10-19=7; 20-29=7; 30-39=1; 40+=2.

H_0-9: CPA Breakdown--Independence with SEC registered firms[13]

There is a statistical significance when the responses of the two CPA groups are compared, made evident by examining the means, or by noting that 56% of the "Big Fifteen" respondents feel that independence will not be increased, while only 42% of the respondents from Other Firms think that independence will not be increased.

H_0-10: CPA Breakdown--Independence with non-SEC registered firms

Although not statistically significant, there still seems to be a difference of opinion between the two CPA groups regarding non-SEC registered firms. While each respondent group has a similar number of respondents who feel that independence will not be increased, the percentage of respondents from Other Firms who believe that independence will increase is much higher than the percentage of "Big Fifteen" respondents who feel the same way.

This chi-square test approaches rejection of the hypothesis of consensus when the .05 alpha level is used.

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[13]For more information on the distribution of CPAs, see Chapter IV, "CPA Breakdown Information."

TABLE VII-9

BIG FIFTEEN--INDEPENDENCE SEC FIRMS

Size of Firm	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
Big Fifteen	2 1.7	3 2.5	28 23.7	23 19.4	3 2.5	59 50.0	3.37
Other Firms	0 0	2 1.7	23 19.4	21 17.8	13 11.0	59 50.0	3.76
Total	2 1.7	5 4.2	51 43.2	44 37.3	16 13.6	118[b] 100.0	3.57

Raw chi-square = 7.44436. Significance level = .0242

[a]For calculation purposes these columns are combined.

[b]Non-responses: Other-2.

TABLE VII-10

BIG FIFTEEN--INDEPENDENCE NON-SEC FIRMS

Size of Firm	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
Big Fifteen	1	4	28	21	4	58	3.34
	.8	3.3	23.7	17.8	3.4	49.2	
Other Firms	0	3	28	16	13	60	3.65
	0	2.5	23.7	13.5	11.0	50.8	
Total	1	7	56	37	17	118[b]	3.53
	.8	5.9	47.5	31.4	14.4	100.0	

Raw chi-square = 5.47055. Significance level = .0649.

[a]For calculation purposes these columns are combined.

[b]Non-responses: Big Fifteen-2; Other-1.

H_0-11: CPA Breakdown--Costs/Benefits with SEC registered firms

Table VII-11 indicates that the CPA respondent groups seem to be in more agreement regarding the costs and benefits of regulations on executive search and placement. The distributions of responses for the two groups are very similar.

TABLE VII-11

BIG FIFTEEN--COSTS/BENEFITS SEC FIRMS

Size of Firms	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
Big Fifteen	26 23.9	25 22.9	51 46.8	1.49
Other Firms	26 23.9	32 29.4	58 53.2	1.55
Total	52 47.7	57 52.3	109[a] 100.0	1.52

Raw chi-square = .20210. Significance level = .6530.

[a]Non-responses: Big Fifteen-8; Other-3.

H_0-12: CPA Breakdown--Costs/Benefits with non-SEC registered firms

As in their consideration of SEC Registered firms, when asked about non-SEC registered firms, the CPA respondent groups are in agreement as to the costs and benefits of the suggested regulations. In each respondent group, more individuals feel that the costs will exceed the benefits for non-SEC registered firms than they will for SEC registered firms.

TABLE VII-12

BIG FIFTEEN--COSTS/BENEFITS NON-SEC FIRMS

Size of Firm	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
Big Fifteen	28 25.5	23 20.9	51 46.4	1.45
Other Firms	29 26.4	30 27.3	59 53.6	1.51
Total	57 51.8	53 48.2	110[a] 100.0	1.48

Raw chi-square = .16849. Significance level = .6815.

[a]Non-responses: Big Fifteen-9; Other-2.

Date Review

Hypotheses rejected

Study of the data presented earlier in the chapter shows that the only chi-square test that rejects the hypothesis of concensus at an alpha level of .05 is Big Fifteen--Independence SEC firms (Table VII-9). The only other test that approaches rejection at the .05 alpha level is Big Fifteen--Independence non-SEC firms (Table VII-10).

Table VII-13 indicates that the means of all respondent groups suggest that all groups feel the prohibition of executive search and placement services will increase the independence of the CPA with respect either to SEC registered or non-SEC registered clients.

Analysis of means of independence decision

Using the 1 to 5 scale, it is possible to state that a group mean below 3.0 indicates an average response that independence will be decreased. It is also possible to state that a group mean of 3.0 indicates an average response that independence will not be affected; a group mean above 3.0 indicates an average response that independence will be increased.

The highest means for SEC and non-SEC firms belong to the groups with 20-29 and 30-39 years of experience, and to the CPAs from Other Firms. The lowest means belong to the "Big Fifteen" CPAs and to the groups with 40+ years of experience.

TABLE VII-13

COMPARISON OF GROUP MEANS--PLACEMENT

Group	Independence Decision SEC	Independence Decision Non-SEC	Costs Benefits SEC	Costs Benefits Non-SEC
CPAs	3.56	3.52	1.50	1.47
CBMs	3.64	3.56	1.52	1.47
CFAs	3.64	3.59	1.56	1.56
0-9	3.54	3.45	1.52	1.50
10-19	3.66	3.61	1.54	1.50
20-29	3.68*	3.77*	1.50	1.48
30-39	3.75	3.63	1.56	1.50
40+	3.42	3.25	1.40	1.40
Big 15	3.37	3.34	1.49	1.45
Other CPAs	3.76	3.65	1.55	1.51
Total of All Respondents	3.60	3.55	1.52	1.49

*This is the only instance where the means seem to suggest the recommended change would be more beneficial with non-SEC firms than with SEC firms.

The extreme differences between the two CPA respondent groups appear to be consistent with the activities of the respective groups. It is evident that large CPA firms are more likely to have extensive executive search and placement services than are small firms. Perhaps "Big Fifteen" respondents are equating decrease in independence with decrease in revenue.

Another possible explanation is that the "Big Fifteen" respondents have seen good placement services work without abuses. It must be pointed out, though, that the CBMs and CFAs do believe that the prohibition will increase independence. Consequently, even if the services do not lead to abuses, the CPAs have to convince the user groups of this fact.

The other low means belonging to the group with 40+ years of experience must be analyzed with the small number of respondents taken into account.

Note that all of the above comments hold regarding either SEC registered clients or non-SEC registered clients. Only the group with 20-29 years of experience feels that there will be a larger increase for non-SEC firms than there will be for SEC firms.

<u>Analysis of means of costs/benefits</u>

Considering the 1, 2 scale, it is possible to state that a group mean above 1.5 indicates an average response that the benefits will exceed the costs. Likewise, a group mean below 1.5 indicates an average response that the costs will exceed the benefits.

Dealing with the issue of costs and benefits to society deriving from a prohibition against executive search and placement services for SEC firms, only the "Big Fifteen" CPAs and the group with 40+ years of experience feel that the costs will exceed the benefits. At the same time, all of the means appraoch 1.50 closely enough to make any conclusion unwise.

Regarding non-SEC firms, most respondent group means suggest that costs will exceed benefits. However, the closeness of most means to 1.5 again makes questionable any conclusions drawn from the means.

Conclusions

There is one statistically significant difference among various respondent groups as to how a prohibition on executive search and placement services will affect the independence of the CPA in his/her relationship with a client. But most respondents do feel that it will increase independence.

Given the data, the issue of costs and benefits of such a prohibition is clearly open to debate.

The recommendations of the Commission on Auditors' Responsibilities and the Metcalf Report are neither confirmed nor denied by this research on the prohibition of executive search and placement services.

CHAPTER VIII

FEES AND ARRANGEMENTS FOR AUDITORS

Literature Review

As a result of the McKesson and Robbins case, the New York Stock Exchange in 1939 suggested:

> Where practicable, the selection of the auditors by a special committee of the board composed of directors who are not officers of the company appears desirable.[1]

Also as a result of the McKesson and Robbins case, the SEC recommended the establishment

> of a committee to be selected from non-officer members of the board of directors which shall make all company or management nominations of auditors and shall be charged with the duty of arranging the details of the arrangement.[2]

Thus the concept of audit committees is not new. In spite of the two early recommendations cited above, a 1970 survey of publicly held companies showed that only 32% of the corporations responding had audit committees.[3]

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[1]New York Stock Exchange, "Independent Audit and Audit Procedures," Accountant, 102 (April 6, 1940):387.

[2]United States Securities and Exchange Commission, Accounting Series Releases 1-77 (Washington, D.C.: U.S. Government Printing Office, 1956), pp. 113-119.

[3]R. K. Mautz and F. L. Neumann, Corporate Audit Committees: Policies and Practices (Cleveland, Ohio: Ernst & Ernst, 1977), pp. 8-11.

A repeat survey of 1976 showed that 87% of the corporations responding had an audit committee at that time.[4]

Effective June 30, 1978, the New York Stock Exchange mandated that each domestic company with common stock listed on the Exchange must establish and maintain

> an Audit Committee comprised solely of directors independent of management and free from any relationship that, in the opinion of its Board of Directors, would interfere with the exercise of independent judgment as a committee member.[5]

The requirement of the Exchange was approved by the SEC on March 9, 1977.

In Connecticut, certain corporations of that state with at least 100 stockholders must establish audit committees. In the Canadian provinces of Ontario, Manitoba, and British Columbia, audit committees are mandatory for companies falling under the Companies Act under province statutes.

In spite of all the policies enacted and statutes listed above, little has been written regarding the duties of auditor committees. In its final report, The Commission on Auditors' Responsibilities states:

> Thus, the arrangements for the audit should be made with the auditor by both management and the Board of Directors. However, the final decisions should be based on board discussions

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[4]Ibid.

[5]New York Stock Exchange, William M. Batten letter to chief executive officers of listed companies, January 6, 1977.

> with the auditor and should not be delegated by the board to corporate officers.[6]

The Commission also says that it is difficult to outline how to order implementation of the above suggestion, but that it can be implemented voluntarily.

Analysis of Data

The remaining portion of this chapter is devoted to the presentation and interpretation of the data. Each hypothesis is investigated separately; a review and summary are presented in the section titled Data Review.

Specific hypotheses

The specific hypotheses to be tested in this section are:

H_0-1: There are no significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the effect of requirements that fees and arrangements for auditors be handled by audit committees on the CPA's independence with respect to the CPA's SEC registered clients.

H_1-1: There are significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the effect of requirements

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[6] American Institute of Certified Public Accountants, Commission on Auditors' Responsibilities, *Commission on Auditors' Responsibilities: Report, Conclusions and Recommendations* (New York: American Institute of Certified Public Accountants, 1978), p. 107.

that fees and arrangements for auditors be handled by audit committees on the CPA's independence with respect to the CPA's SEC registered clients.

H_0-2 There are no significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the effect of requirements that fees and arrangements for auditors be handled by audit committees on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_1-2: There are significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the effect of requirements that fees and arrangements for auditors be handled by audit committees on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_0-3: There are no significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the costs and benefits to society as a whole, of requirements that fees and arrangements for auditors be handled by audit committees for SEC registered firms.

H_1-3: There are significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the costs and benefits to society as a whole, of requirements that fees and arrangements for auditors be handled by audit committees for SEC registered firms.

H_0-4: There are no significant differences between members of the AICPA, Corporate Bar, and ICFA regarding their perceptions as to the costs and benefits to society as a whole, of requirements that fees and arrangements for auditors be handled by audit committees for non-SEC registered firms.

H_1-4: There are significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the costs and benefits to society as a whole, of requirements that fees and arrangements for auditors be handled by audit committees for non-SEC registered firms.

H_0-5: There are no significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years, and over 29 years regarding their perceptions as to the effect of requirements that fees and arrangements for auditors be handled by audit committees on the CPA's independence with respect to the CPA's SEC registered clients.

H_1-5: There are significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years, and over 29 years regarding their perceptions of the effect of requirements that fees and arrangements for auditors be handled by audit committees on the CPA's independence with respect to the CPA's SEC registered clients.

H_0-6: There are no significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years, and over 29 years regarding their perceptions as to the effect of requirements that fees and arrangements for auditors be handled by audit committees on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_1-6: There are significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years, and over 29 years regarding their perceptions as to the effect of requirements that fees and arrangements for auditors be handled by audit committees on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_0-7: There are no significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years, and over 29 years, regarding their perceptions of the costs and benefits to society as a whole, of requirements that fees and arrangements for auditors be handled by audit committees for SEC registered firms.

H_1-7: There are significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years, and over 29 years regarding their perceptions as to the costs and benefits to society as a whole, of requirements that fees and arrangements for auditors be handed by audit committees for SEC registered firms.

H_0-8: There are no significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years, and over 29 years regarding their perceptions of the costs and benefits to society as a whole, of requirements that fees and arrangements for auditors be handled by audit committees for non-SEC registered firms.

H_1-8: There are significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years, and over 29 years regarding their perceptions of the costs and benefits to society as a whole, of requirements that fees and arrangements for auditors be handed by audit committees for non-SEC registered firms.

H_0-9: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the effect of requirements that fees and arrangements for auditors be handled by audit committees on the CPA's independence with respect to the

CPA's SEC registered clients.

H_1-9: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the effect of requirements that fees and arrangements for auditors be handled by audit committees on the CPA's independence with respect to the CPA's SEC registered clients.

H_0-10: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the effect of requirements that fees and arrangements for auditors be handled by audit committees on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_1-10: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions as to the effect of requirements that fees and arrangements for auditors be handled by audit committees on the CPA's independence with respect to the CPA's non-SEC registered clients.

H_0-11: There are no significant differences between respondents who work/worked for the "Big Fifteen"

CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the costs and benefits to society as a whole, of requirements that fees and arrangements for auditors be handled by audit committees for SEC registered clients.

H_1-11: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the costs and benefits to society as a whole, of requirements that fees and arrangements for auditors be handled by audit committees for non-SEC registered firms.

H_0-12: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the costs and benefits to society as a whole, of requirements that fees and arrangements for auditors be handled by audit committees for non-SEC registered firms.

H_1-12: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the costs and benefits to society as a whole, of requirements that fees and arrangements for auditors be handled by audit committees for non-SEC registered firms.

H_0-1: CPAs/CBMs/CFAs--Independence with SEC registered firms

Table VIII-1 shows that there are no significant differences in the opinions of CPAs, CBMs, and CFAs as to the effect on the independence of the CPA with respect to the CPA's SEC registered clients, of requirements that fees and arrangements for auditors be handled by audit committees.[7] The CPAs feel most strong that independence will be increased; the CBMs feel the least strongly.

H_0-2: CPAs/CBMs/CFAs--Independencence with non-SEC registered firms

As they do regarding SEC registered firms, all three groups feel that the proposed requirements will increase independence with respect to non-SEC firms. Again, there is no statistically significant difference among the opinions of the groups, but there are some interesting "differences."

[7]For more information on the statistical analysis, see Chapter IV.

TABLE VIII-1

CPAs/CBMs/CFAs--INDEPENDENCE SEC FIRMS

	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
CPAs	8 2.7	3 1.0	55 18.5	35 11.7	26 8.7	127 42.6	3.54
CBMs	6 2.0	8 2.7	38 12.8	21 7.0	15 5.0	88 29.5	3.35
CFAs	3 1.0	8 2.7	36 12.1	25 8.4	11 3.7	83 27.9	3.40
Total	17 5.7	19 6.4	129 43.3	81 27.2	52 17.4	298[b] 100.0	3.44

Raw chi-square = 2.64688. Significance level = .6185.

[a]For calculation purposes these columns are combined.

[b]Non-responses: CPAs-2; CBMs-2; CFAs-1.

TABLE VIII-2

CPAs/CBMs/CFAs--INDEPENDENCE NON-SEC FIRMS

	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
CPAs	6	5	65	30	21	127	3.43
	2.0	1.7	21.9	10.1	7.1	42.8	
CBMs	7	8	43	18	12	88	3.23
	2.4	2.7	14.5	6.1	4.0	29.6	
CFAs	3	4	40	25	10	82	3.43
	1.0	1.3	13.5	8.4	3.4	27.6	
Total	16	17	148	73	43	297[b]	3.37
	5.4	5.7	49.8	24.6	14.5	100.0	

Raw chi-square = 3.08894. Significance level = .5431.

[a]For calculation purposes these columns are combined.

[b]Non-responses: CPAs-2; CBMs-2; CFAs-2.

The mean for the CPA respondent group is substantially higher than that for the CFAs regarding SEC firms. In reference to non-SEC firms, the means for the CPAs and CFAs are identical. The CBMs remain the group with the lowest mean. It is also interesting to note that the CFAs as as a group feel that a greater increase in independence will be achieved with non-SEC firms than with SEC registered firms.

H_0-3: CPAs/CBMs/CFAs--Costs/Benefits with SEC registered firms

Examining the costs and benefits of the proposed requirements in reference to SEC registered firms, all three groups agree that the benefits will exceed the costs. The CBMs have the highest group mean, the CFAs, the lowest, while the mean of the CPAs falls midway between the two.

H_0-4: CPAs/CBMs/CFAs--Costs/Benefits with non-SEC registered firms

Table VIII-4 indicates that, compared with the means for SEC registered firms, the means of all three groups drop in reference to non-SEC firms. The mean of the CPAs shows the largest drop--from 1.58 to 1.43. The mean of 1.43 suggests that on an average, CPAs feel that the costs to society will exceed the benefits to society under the adoption of the proposed requirement that fees and arrangements for auditors be handled by audit

TABLE VIII-3

CPAs/CBMs/CFAs--COSTS/BENEFITS SEC FIRMS

	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
CPAs	47 17.4	65 24.1	112 41.5	1.58
CBMs	31 11.5	49 18.1	80 29.6	1.61
CFAs	34 12.6	44 16.3	78 28.9	1.56
Total	112 41.5	158 58.5	270[a] 100.0	1.59

Raw chi-square = .39947. Significance level = .8189.

[a]Non-responses: CPAs-17; CBMs-10; CFAs-6.

TABLE VIII-4

CPAs/CBMs/CFAs--COSTS/BENEFITS NON-SEC FIRMS

	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
CPAs	66 24.2	49 17.9	115 42.1	1.43
CBMs	37 13.6	43 15.8	80 29.3	1.54
CFAs	35 12.8	43 15.8	78 28.6	1.55
Total	138 50.5	135 49.5	273[a] 100.0	1.49

Raw chi-square = 3.75104. Significance level = .1533

[a]Non-responses: CPAs-14; CBMs-10; CFAs-6.

committees. The means for CBMs and CFAs are almost identical, as is the distribution of responses for each of those two groups.

H_0-5: Years of experience--Independence with SEC registered firms

Table VIII-5 indicates that, regarding SEC firms, all respondent experience groups feel that proposed requirements will increase independence. The least experienced group has the highest mean, while the two groups with the most experience have the two lowest means.

H_0-6: Years of experience--Independence with non-SEC registered firms

Unlike respondents' feelings about SEC firms, regarding non-SEC firms, two of the respondent groups feel that the proposed requirements will not increase independence. Although both of these groups are the groups with the most experience, and are represented by a relatively small number of respondents, they are consistently lower in their indications of how much independence will be increased or decreases.

In fact, the group with 30-39 years of experience feels that independence will be decreased. The highest mean belongs to the least experienced group, which has 0-9 years of experience.

TABLE VIII-5

EXPERIENCE GROUPS--INDEPENDENCE SEC FIRMS

Years of Exper.	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
0-9	4 1.3	7 2.3	58 19.5	40 13.4	24 8.1	133 44.6	3.55
10-19	8 2.7	5 1.7	37 12.4	24 8.1	15 5.0	89 29.9	3.37
20-29	2 .7	3 1.0	23 7.7	10 3.4	9 3.0	47 15.8	3.45
30-39[b]	3 1.0	2 .7	6 2.0	2 .7	4 1.3	17 5.7	3.12
40+[b]	0 0	2 .7	5 1.7	5 1.7	0 0	12 4.0	3.25
Total	17 5.7	19 6.4	129 43.3	81 27.2	52 17.4	298[c] 100.0	3.44

Raw chi-square = 2.14635. Significance level = .9058.

[a]For calculation purposes these columns are combined.

[b]For calculation purposes these rows are combined.

[c]Non-responses: 0-9=1; 10-19=2; 20-29-2.

TABLE VIII-6

EXPERIENCE GROUPS--INDEPENDENCE NON-SEC FIRMS

Years of Exper.	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
0-9	4 1.3	7 2.4	62 20.9	36 12.1	23 7.7	132 44.4	3.51
10-19	7 2.4	3 1.0	47 15.8	22 7.4	10 3.4	89 30.0	3.20
20-29	2 .7	2 .7	25 8.4	11 3.7	8 2.7	48 16.2	3.44
30-39[b]	3 1.0	2 .7	8 2.7	1 .3	2 .7	16 5.4	2.81
40+[b]	0 0	3 1.0	6 2.0	3 1.0	0 0	12 4.0	3.00
Total	16 5.4	17 5.7	148 49.8	73 24.6	43 14.5	297[c] 100.0	3.37

[a]For calculation purposes these columns are combined.

[b]For calculation purposes these rows are combined.

[c]Non-responses: 0-9=2; 10-29=2; 20-29=1; 30-39=1.

[d]Insufficient expected cell sizes for statistical tests.

H_0-7: Years of experience--Costs/Benefits with SEC registered firms

Table VIII-7 illustrates that the respondent groups are close to agreement that the benefits to society will exceed the costs to society for the proposed requirements. The two highest means belong to the most experienced groups; the lowest means belong to the middle experience groups.

TABLE VIII-7

EXPERIENCE GROUPS--COSTS/BENEFITS SEC FIRMS

Years of Exper.	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
0-9	48 17.8	77 28.5	125 46.3	1.62
10-19	36 13.3	42 15.6	78 28.9	1.54
20-29	19 7.0	22 8.1	41 15.2	1.54
30-39[a]	6 2.2	10 3.7	16 5.9	1.63
40+[a]	3 1.1	7 2.6	10 3.7	1.70
Total	112 41.5	158 58.5	270[b] 100.0	1.59

Raw chi-square = 2.09434. Significance level = .5531.

[a]For calculation purposes these rows are combined.

[b]Non-responses: 0-9=9; 10-19=13; 20-29=8; 30-39=1; 40+=2.

H_0-8: Years of experience--Costs/Benefits with non-SEC registered firms

Although not statistically significant, there is a definite difference of opinion among the respondent groups as to how the proposed requirements will affect the costs and benefits regarding non-SEC registered firms. Only the least experienced and most experienced groups feel that, on an average, the benefits will exceed the

TABLE VIII-8

EXPERIENCE GROUPS--COSTS/BENEFITS NON-SEC FIRMS

Years of Exper.	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
0-9	58 21.2	70 25.6	128 46.9	1.55
10-19	45 16.5	34 12.5	79 28.9	1.43
20-29	23 8.4	18 6.6	41 15.0	1.44
30-39[a]	9 3.3	6 2.2	15 5.5	1.40
40+[a]	3 1.1	7 2.6	10 3.7	1.70
Total	138 50.5	135 49.5	273[b] 100.0	1.49

Raw chi-square = 3.27383. Significance level = .3513.

[a]For calculation purposes these rows are combined.

[b]Non-responses: 0-9=6; 10-19=12; 20-29=8; 30-39=2; 40+=2.

costs, while the other three respondent groups feel that the costs will exceed the benefits. Again it should be noted that the most experienced group (40+), has a very small number of respondents.

H_0-9: CPA Breakdown--Independence with SEC registered firms[8]

Table VIII-9 shows that the CPA respondent groups are in agreement as to the effect of the proposed requirements that fees and arrangements for auditors be handled by audit committees. The "Big Fifteen" respondent group does have a higher mean than the group of respondents who work/worked for other firms.

H_0-10: CPA Breakdown--Independence with non-SEC registered firms

Table VIII-10 shows that there is a statistically significant difference of opinion between the two respondent groups as to how the proposed requirements will affect independence for non-SEC registered firms. Both groups do agree that independence will not be increased as much for non-SEC firms as it will be for SEC firms.

The largest disagreement is how much less the proposed requirements will affect independence for non-SEC firms. While 50% of the "Big Fifteen" respondents feel that independence will not be increased, fully 72%

[8]For more information on the distribution of CPAs, see Chapter IV, "CPA Breakdown Information."

TABLE VIII-9

BIG FIFTEEN--INDEPENDENCE SEC FIRMS

Size of Firm	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
Big Fifteen	2 1.7	1 .8	26 22.0	16 13.6	13 11.0	58 49.2	3.64
Other Firms	5 4.2	2 1.6	26 22.0	15 12.7	12 10.1	60 50.8	3.45
Total	7 5.9	3 2.5	52 44.1	31 26.3	25 21.2	118[b] 100.0	3.54

Raw chi-square = .29651. Significance level = .8622.

[a]For calculation purposes these columns are combined.

[b]Non-responses: Big Fifteen-1; Other-1.

TABLE VIII-10

BIG FIFTEEN--INDEPENDENCE NON-SEC FIRMS

Size of Firm	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
Big Fifteen	1 .8	2 1.7	26 21.8	18 15.1	11 9.2	58 48.8	3.62
Other Firms	4 3.3	3 2.5	37 31.1	8 6.6	9 7.6	61 51.2	3.25
Total	5 4.2	5 4.2	63 52.9	26 21.9	20 16.8	119[b] 100.0	3.43

Raw chi-square = 7.05720. Significance level = .0293.

[a]For calculation purposes these columns are combined.

[b]Non-responses: Big Fifteen-1.

of the respondents who work/worked for other firms feel that independence will not be increased.

H_0-11: CPA Breakdown--Costs/Benefits with SEC registered firms

Regarding the question of costs and benefits for SEC firms, both respondent groups feel that the benefits to society will exceed the costs to society with implementation of the requirements that fees and arrangements for auditors be handled by audit committees. The mean for the "Big Fifteen" respondent group is higher than the mean of the group of respondents who work/worked with other firms.

TABLE VIII-11

BIG FIFTEEN--COSTS/BENEFITS SEC FIRMS

Size of Firm	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
Big Fifteen	20 19.3	30 28.8	50 48.1	1.60
Other Firms	23 22.1	31 29.8	54 51.9	1.57
Total	43 41.3	61 58.7	104[a] 100.0	1.59

Raw chi-square = .00476. Significance level = .9450.

[a]Non-responses: Big Fifteen-9; Other firms-7.

H_0-12: CPA Breakdown--Costs/Benefits with non-SEC registered firms

In contrast to their reactions regarding SEC registered firms, both respondent groups feel that the costs will exceed the benefits if there were a requirement that fees and arrangements for auditors be handled by audit committees. Nearly 60% of the total CPA respondents feel that costs will exceed benefits.

TABLE VIII-12

BIG FIFTEEN--COSTS/BENEFITS NON-SEC FIRMS

Size of Firm	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
Big Fifteen	28 26.2	24 22.4	52 48.6	1.46
Other Firms	34 31.7	21 19.6	55 51.4	1.38
Total	62 57.9	45 42.1	107[a] 100.0	1.42

Raw chi-square = .40832. Significance level = .5228.

[a]Non-responses: Big Fifteen-7; Other firms-6.

Data Review

Hypotheses rejected

Review of the data shows that the only chi-square test that rejects the hypothesis of consensus at an alpha level of .05 is Big Fifteen - Independence Non-SEC firms

(Table VIII-10). No other tests even approach rejection at the .05 level.

Examination of the means of all groups (see Table VIII-13), shows that all respondent groups feel that a requirement that fees and arrangements for auditors be handled by audit committees will increase the independence of the CPA with respect of SEC registered clients.

Analysis of means independence decision

Using the 1 to 5 scale, it is possible to state that a group mean of below 3.0 indicates an average response that independence will be decreased. It is also possible to state that a group mean of 3.0 indicates an average response that independence will not be affected; a group mean above 3.0 indicates an average response that independence will be increased.

The lowest means (3.12 and 3.25) represent the two respondent groups with the longest experience. The highest mean (3.64) belongs to the respondents who work/worked for "Big Fifteen" firms.

Two explanations seem possible for the high mean of the "Big Fifteen" respondents. Perhaps the respondents feel more management presssure (high fees for large firms) and believe that it will be reduced when an audit committee is used. Also, it may be that the members of this group of respondents have seen more audit committees in practice (since the bigger clients are more likely to have

TABLE VIII-13

COMPARISON OF GROUP MEANS--FEES

Group	Inde-pendence Decision SEC	Inde-pendence Decision Non-SEC	Costs Benefits SEC	Costs Benefits Non-SEC
CPAs	3.54	3.43	1.58	1.43
CBMs	3.35	3.23	1.61	1.54
CFAs	3.40*	3.45*	1.56	1.55
0-9	3.55	3.51	1.62	1.55
10-19	3.37	3.28	1.54	1.43
20-29	3.45	3.44	1.54	1.44
30-39	3.12	2.81	1.63	1.40
40+	3.25	3.00	1.70	1.70
Big 15	3.64	3.62	1.60	1.46
Other CPAs	3.45	3.25	1.57	1.38
Total of All Respondents	3.44	3.37	1.59	1.49

*This is the only instance in which the means seem to suggest the recommended change would be more beneficial with Non-SEC firms than with SEC firms.

audit committees), and that they approve of what they see.

Regarding non-SEC firms, again, the two lowest means (2.81 and 3.00) belong to the two most experienced respondent groups. Neither group feels that independence will be increased. In fact, the group with 30-39 years of experience feels that the independence will be decreased. Again, because of the small number of respondents in these two groups, caution should be exercised in drawing conclusions about their willingness to accept major changes. All other respondent groups feel that independence will be increased when fees and arrangements for auditors are handled by audit committees.

Only the CFA respondent groups feels that independence will be increased more for non-SEC firms than it will be for SEC firms. All other groups feel that independence will be increased more with SEC firms than it will be with non-SEC firms.

When discussing the comparison of SEC and non-SEC firms, it should be noted that the costs for non-SEC firms is likely to be higher than for SEC firms. This is due in large part to the fact that currently many more SEC firms have audit committees than do non-SEC firms.

Analysis of means of costs/benefits

Using the 1, 2 scale, it is possible to state that a group mean above 1.5 indicates an average response that the benefits will exceed the costs. A group mean below 1.5 indicates an average response that the costs will exceed the benefits.

Further examination of Table VIII-13 shows that all respondent groups feel that the benefits to society will exceed the costs to society if SEC firms were to be required to have fees and arrangements for auditors handled by audit committees. Except for the group with 40+ years of experience, the means of all groups show a surprising closeness to one another.

Regarding non-SEC firms, the respondent groups seem to disagree as to how the proposed requirement will affect costs and benefits. The CPAs feel the costs will exceed the benefits, while the CBMs and CFAs feel that the benefits will exceed the costs. The least experienced and most experienced respondents also feel that the benefits will exceed the costs. The remaining groups feel that costs will exceed benefits.

Conclusions

There is only one statistically significant difference among respondent groups as to how requirements that fees and arrangements for auditors be handled by audit committees will affect independence. All groups feel that independence will be increased when an SEC client is involved. All but two respondent groups feel that independence will be increased for non-SEC clients.

All respondent groups feel that the benefits to society will exceed the costs to society should the requirements be ordered for SEC clients. However, the opinions of the two groups are divided regarding non-SEC clients.

The findings are consistent with the recommendations of the Commission on Auditors' Responsibilities that companies should have fees and arrangements for auditors handled by audit committees.

CHAPTER IX

GOVERNMENT SELECTION AND PAYMENT OF AUDITORS

Literature Review

Little has been written about government selection and payment of independent auditors. Even the Metcalf Report, which recommends that "The Federal Government should establish . . . auditing standards and other accounting practices in meetings open to the public,"[1] stops short of recommending government selection and payment of independent auditors.

An argument that can be offered in favor of government selection and payment is that it allows the auditor independence from the client. Although this may be true, problems are possible. As one CPA states, "You cannot be truly independent when you have to interact with the people who pay you. Government regulation of CPAs is not the answer--it would just create another government agency and lots of rules and regulations.[2]

Referring to the more general question of auditing standards and responsibilities, Forbes states:

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[1]Metcalf, Accounting Establishment, p. 23.

[2]Included in remarks to field questionnaire by James Richardson, former Ernst & Ernst manager.

> It would be a bad thing for everybody if, in punishing the accountants for sins now atoned for, the politicians were to subvert the true (if somewhat limited) functions of certified public accounting--and at the same time foist upon this country yet another maze of regulations, yet more miles of costly red tape.[3]

Referring to the issue of government selection and payment of auditors the Commission on Auditors' Responsibilities states:

> Thus, while there may be some deficiencies in the independence of public accounting firms, it is not clear that increased government involvement would be free of similar difficulties.[4]

The Commission continues:

> Some significant advantages are gained from having the auditor compensated by the company where financial statements are audited. Management is in a position to reduce the cost of auditing by establishing effective internal accounting controls and, in general, by operating a well-disciplined accounting system. Requiring companies to pay the audit fee, therefore, gives them added incentive to institute internal procedures to produce reliable financial information.[5]

Analysis of Data

The remaining portion of this chapter is devoted to the presentation and interpretation of the data. Each hypothesis is investigated separately; a review and and summary are presented in the section titled Data Review.

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[3] "Why Everybody's Jumping on the Accountants These Days," *Forbes*, March 15, 1977, p. 43.

[4] AICPA, *Report, Conclusions, and Recommendations*, p. 105.

[5] Ibid., pp. 105-106.

Specific hypotheses

The specific hypotheses to be tested in this section are:

H_0-1: There are no significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the effect that government selection and payment of auditors will have on the independence of the CPA with respect to the CPA's SEC registered clients.

H_1-1: There are significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the effect that government selection and payment of auditors will have on the independence of the CPA with respect to the CPA's SEC registered clients.

H_0-2: There are no significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the effect that government selection and payment of auditors will have on the independence of the CPA with respect to the CPA's non-SEC registered clients.

H_1-2: There are significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the effect that government selection and payment of auditors will have on the independence of the CPA with respect to the CPA's non-SEC registered clients.

H_0-3: There are no significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the costs and benefits to society as a whole of government selection and payment of auditors for SEC registered firms.

H_1-3: There are significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the costs and benefits to society as a whole of government selection and payment of auditors for SEC registered firms.

H_0-4: There are no significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions as to the costs and benefits to society as a whole of government selection and payment of auditors for non-SEC registered firms.

H_1-4: There are significant differences among members of the AICPA, Corporate Bar, and ICFA regarding their perceptions of the costs and benefits to society as a whole of government selection and payment of auditors for non-SEC registered firms.

H_0-5: There are no significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years regarding their perceptions of the effect that government selection and payment of auditors will have on the independence of the CPA with respect to the CPA's SEC registered clients.

H_1-5: There are significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years, and over 29 years regarding their perceptions of the effect that government selection and payment of auditors will have on the independence of the CPA with respect to the CPA's SEC registered clients.

H_0-6: There are no significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years regarding their perceptions of the effect that government selection and payment of auditors will have on the independence of the CPA with respect to the CPA's non-SEC registered clients.

H_1-6: There are significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years regarding their perceptions of the effect that government selection and payment of auditors will have on the independence of the CPA with respect to the CPA's non-SEC registered clients.

H_0-7: There are no significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years regarding their perceptions of the costs and benefits to society as a whole of government selection and payment of auditors for SEC registered firms.

H_1-7: There are significant differences between respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years regarding their perceptions of the costs and benefits to society as a whole of government selection and payment of auditors for SEC registered firms.

H_0-8: There are no significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years regarding their perceptions of the costs and benefits to society as a whole of government selection and payment of auditors for non-SEC registered firms.

H_1-8: There are significant differences among respondents who have experience of 0-9 years, 10-19 years, 20-29 years and over 29 years regarding their perceptions of the costs and benefits to society as a whole of government selection and payment of auditors for non-SEC registered firms.

H_0-9: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the effect that government selection and payment of auditors will have on the independence of the CPA with respect to the CPA's SEC registered clients.

H_1-9: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the effect that government selection and payment of auditors will have on the independence of the CPA with respect to the CPA's SEC registered clients.

H_0-10: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the effect that government selection and payment of auditors will have on the independence of the CPA with respect to the CPA's non-SEC registered clients.

H_1-10: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for other CPA firms regarding their perceptions of the effect that government selection and payment of auditors will have on the independence of the CPA with respect to the CPA's non-SEC registered clients.

H_0-11: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for the other CPA firms regarding their perceptions of the costs and benefits to society as a whole of government selection and payment of auditors for SEC registered firms.

H_1-11: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for the other CPA firms regarding their perceptions of the costs and benefits to society as a whole of government selection and payment of auditors for SEC registered firms.

H_0-12: There are no significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for the other CPA firms regarding their perceptions of the costs and benefits to society as a whole of government selection and payment of auditors for non-SEC registered firms.

H_1-12: There are significant differences between respondents who work/worked for the "Big Fifteen" CPA firms and respondents who work/worked for the other CPA firms regarding their perceptions of the costs and benefits to society as a whole of government selection and payment of auditors for non-SEC registered firms.

H_0-1: CPAs/CBMs/CFAs--Independence with SEC registered firms

Table IX-1 shows that there is not a statistically significant difference among the respondent groups and the effect that they feel government selection and payment of auditors will have on the independence of CPAs.[6] On the average, both the CPAs and CFAs feel that the change will decrease independence. At the same time, the CBMs seem to feel that independence will be increased.

However, it should be pointed out that the mean in all three cases approaches 3.00 closely enough to suggest that there is no clear feeling in either direction for any of the three groups.

H_0-2: CPAs/CBMs/CFAs--Indepencence with non-SEC registered firms

In reference to non-SEC registered firms, the results are essentially the same. Sixty three percent of all of the respondents do not feel that independence will be increased by the proposed change for non-SEC firms.

H_0-3: CPAs/CBMs/CFAs--Costs/Benefits with SEC registered firms

Table IX-3 indicates that the groups are basically in agreement as to their feelings about how government selection and payment of auditors will affect the

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[6]For more information on the statistical analysis, see Chapter IV.

TABLE IX-1

CPAs/CBMs/CFAs--INDEPENDENCE SEC FIRMS

	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
CPAs	31	6	46	23	17	123	2.91
	10.7	2.1	25.9	7.9	5.9	42.4	
CBMs	20	3	26	19	20	88	3.18
	6.9	1.0	9.0	6.6	6.9	30.3	
CFAs	23	7	16	18	15	79	2.94
	7.9	2.4	5.5	6.2	5.2	27.2	
Total	74	16	88	60	52	290[b]	3.00
	25.5	5.5	30.3	20.7	17.9	100.0	

Raw chi-square = 4.11348. Significance level = .3909.

[a]For calculation purposes these columns are combined.

[b]Non-responses: CPAs-6; CBMs-2; CFAs-5.

TABLE IX-2

CPAs/CBMs/CFAs--INDEPENDENCE NON-SEC FIRMS

	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
CPAs	28	7	52	19	17	123	2.92
	9.7	2.4	18.1	6.6	5.9	42.7	
CBMs	20	4	26	16	21	87	3.16
	6.9	1.4	9.0	5.6	7.3	30.2	
CFAs	23	7	15	17	16	78	2.95
	8.0	2.4	5.2	5.9	5.6	27.1	
Total	71	18	93	52	54	288[b]	3.00
	24.7	6.3	32.3	18.1	18.8	100.0	

Raw chi-square = 6.07321. Significance level = .1937

[a]For calculation purposes these columns are combined.

[b]Non-responses: CPAs-6; CBMs-3; CFAs-6.

independence of the CPA. All three groups declare overwhelmingly that government intervention will have more costs than benefits to society as a whole.

TABLE IX-3

CPAs/CBMs/CFAs--COSTS/BENEFITS SEC FIRMS

	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
CPAs	114 39.2	8 2.7	122 41.9	1.07
CBMs	82 28.2	7 2.4	89 30.6	1.08
CFAs	69 23.7	11 3.8	80 27.5	1.14
Total	265 91.1	26 8.9	291[a] 100.0	1.09

Raw chi-square = 3.25239. Significant level = .1967.

[a]Non-responses: CPAs-7; CBMs-1; CFAs-4.

Ninety one percent of all of the respondents to this question feel that the costs of the proposed change will exceed the benefits. The CPAs feel most strongly in this regard. Of the CBMs and the CFAs, 86% feel that the costs will exceed the benefits.

H_0-4: CPAs/CBMs/CFAs--Costs/Benefits with non-SEC registered firms

Regarding non-SEC registered firms, the responses of the three respondent groups are virtually the same as they are for SEC registered firms. The overall percentage of respondents who feel that costs will exceed benefits is greater than 92%.

TABLE IX-4

CPAs/CBMs/CFAs--COSTS/BENEFITS NON-SEC FIRMS

	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
CPAs	114 39.4	8 2.8	122 42.2	1.07
CBMs	82 28.4	6 2.1	88 30.5	1.07
CFAs	71 24.6	8 2.8	79 27.3	1.10
Total	267 92.4	22 7.6	289[a] 100.0	1.08

Raw chi-square = .98205. Significance level = .6120.

[a]Non-responses: CPAs-7; CBMs-2; CFAs-5.

$H_0$5: Years of experience--Independence with SEC registered firms

Table IX-5 shows that the more experience a respondent group has, the less likely that group is to feel that government selection and payment of auditors will increase independence when dealing with SEC registered firms. In fact, the group with 0-9 years of experience is the only group that feels that independence will be increased.

H_0-6: Years of experience--Independence with non-SEC registered firms

The data in Table IX-5 indicate that the correlation between years of experience and responses regarding non-SEC registered firms is the same as that for responses regarding SEC registered firms. The greater the number of years of experience, the lower the group mean. One interesting fact is that the mean for the group with 0-9 years of experience increases for non-SEC registered firms as compared to SEC registered firms. At the same time the group means for the other four groups either remain the same, or decrease when the respondents are asked about non-SEC registered firms.

TABLE IX-5

EXPERIENCE GROUPS--INDEPENDENCE SEC FIRMS

	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
0-9	26	6	41	31	25	129	3.18
	9.0	2.1	14.1	10.7	8.6	44.5	
10-19	24	6	25	16	15	86	2.91
	8.3	2.1	8.6	5.5	5.2	29.7	
20-29	13	2	16	10	6	47	2.87
	4.5	.7	5.5	3.4	2.1	16.2	
30-39[b]	7	0	4	2	4	17	2.76
	2.4	0	1.4	.7	1.4	5.9	
40+[b]	4	2	2	1	2	11	2.55
	1.4	.7	.7	.3	.7	3.8	
Total	74	16	88	60	52	290[c]	3.00
	25.5	5.5	30.3	20.7	17.9	100.0	

Raw chi-square = 4.21110. Significance level = .6481.

[a]For calculation purposes these columns are combined.

[b]For calculation purposes these rows are combined.

[c]Non-responses: 0-9=5; 10-19=5; 20-29=2; 40+=1.

TABLE IX-6

EXPERIENCE GROUPS--INDEPENDENCE NON-SEC FIRMS

Years of Exper.	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
0-9	23 8.0	7 2.4	46 16.0	24 8.3	28 9.7	128 44.4	3.21
10-19	23 8.0	8 2.8	25 8.7	15 5.2	15 5.2	86 29.9	2.90
20-29	13 4.5	2 .7	16 5.6	10 3.5	6 2.1	47 16.3	2.87
30-39[b]	7 2.4	0 0	4 1.4	2 .7	3 1.0	16 5.6	2.63
40+[b]	5 1.7	1 .3	2 .7	1 .3	2 .7	11 3.8	2.45
Total	71 24.7	18 6.3	93 32.3	52 18.1	54 18.8	288[c] 100.0	3.00

Raw chi-square = 3.30942. Significance level = .7691.

[a]For calculation purposes these columns are combined.

[b]For calculation purposes these rows are combined.

[c]Non-responses: 0-9=6; 10-19=5; 20-29=2; 30-39=1; 40+=1.

H_0-7: Years of experience--Costs/Benefits with SEC registered firms

Regarding the costs and benefits to society, the respondents, grouped by the number of years of experience, are consistent in their responses that the costs will exceed the benefits to society. Fewer than 10% of all of the respondents feel that the benefits will exceed the costs.

TABLE IX-7

EXPERIENCE GROUPS--COSTS/BENEFITS SEC FIRMS

Years of Exper.	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
0-9	121 41.6	9 3.1	130 44.7	1.07
10-19	77 26.5	9 3.1	86 29.6	1.10
20-29	42 14.4	6 2.1	48 16.5	1.13
30-39[a]	16 5.5	1 .3	17 5.8	1.06
40+[a]	9 3.1	1 .3	10 3.4	1.10
Total	265 91.1	26 8.9	291[b] 100.0	1.09

[a]For calculation purposes these rows are combined.

[b]Non-responses: 0-9=4; 10-19=5; 20-29=1; 40+=2.

[c]Insufficient expected cell sizes for statistical tests.

H_0-8: Years of experience--Costs/Benefits with non-SEC registered firms

Table IX-8 reveals that the respondent groups are again close in their responses; all groups feel that costs will exceed the benefits for non-SEC registered firms.

TABLE IX-8

EXPERIENCE GROUPS--COSTS/BENEFITS NON-SEC FIRMS

Years of Exper.	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
0-9	122 42.2	7 2.4	129 44.6	1.05
10-19	79 27.3	7 2.4	86 29.8	1.08
20-29	42 14.5	6 2.1	48 16.6	1.13
30-39[a]	15 5.2	1 .3	16 5.5	1.06
40+[a]	9 3.1	1 .3	10 3.5	1.10
Total	267 92.4	22 7.6	289[b] 100.0	1.08

[a]For calculation purposes these rows are combined.

[b]Non-responses: 0-9=5; 10-19=5; 20-29=1; 30-39-1; 40+=2.

[c]Insufficient expected cell sizes for statistical tests.

H_0-9: CPA Breakdown--Independence with SEC registered firms[7]

Both CPA respondent groups indicate that government selection of independent auditors will not increase independence. The respondents from firms other than the "Big Fifteen" indicate by their mean of 2.73 that they feel that independence will be decreased. The "Big Fifteen" mean of 3.00 indicates no clear feelings in either direction.

H_0-10: CPA Breakdown--Independence with non-SEC registered firms

Table IX-10 shows that when the CPAs examine non-SEC registered firms there is even wider divergence between the means for the two respondent groups. Although the percentage of respondents that feels independence will be decreased is about the same for both groups, the "greatly decrease" column shows that the number of respondents from other firms who indicate this category is three times that of the number of respondents from the "Big Fifteen."

[7]For more information on the distribution of CPAs, see Chapter IV, "CPA Breakdown Information."

TABLE IX-9

BIG FIFTEEN--INDEPENDENCE SEC FIRMS

Size of Firm	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
Big Fifteen	9 7.9	4 3.5	25 22.0	10 8.8	7 6.1	55 48.2	3.04
Other Firms	21 18.4	2 1.8	16 14.1	12 10.5	8 7.0	59 51.8	2.73
Total	30 26.3	6 5.3	41 36.0	22 19.3	15 13.2	114[b] 100.0	2.88

Raw chi-square = .12127. Significance level = .9412.

[a]For calculation purposes these columns are combined.

[b]Non-responses: Big Fifteen-4; Other-2.

TABLE IX-10

BIG FIFTEEN--INDEPENDENCE NON-SEC FIRMS

Size of Firm	Greatly[a] Decrease Indep.	Slightly[a] Decrease Indep.	Not[a] Affect Indep.	Slightly Increase Indep.	Greatly Increase Indep.	Total	Mean
Big Fifteen	7 6.1	5 4.4	26 22.6	9 7.8	8 7.0	55 47.8	3.11
Other Firms	21 18.3	2 1.7	21 18.3	9 7.8	7 6.1	60 52.2	2.54
Total	28 24.3	7 6.1	47 40.9	18 15.7	15 13.0	115[b] 100.0	2.87

Raw chi-square = .28885. Significance level = .8655.

[a]For calculation purposes these columns are combined.

[b]Non-responses: Big Fifteen-4; Other-1.

H_0-11: CPA Breakdown--Costs/Benefits with SEC registered firms

Considering the costs and benefits of government selection and payment of auditors, the respondent groups are remarkably similar in their opinions. As Table IX-11 reveals, both group means are extremely close as are the raw scores. More than 93% of the total respondents feel that the costs to society will exceed the benefits to society.

TABLE IX-11

BIG FIFTEEN--COSTS/BENEFITS SEC FIRMS

Size of Firm	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
Big Fifteen	53 46.9	3 2.7	56 49.6	1.05
Other Firms	53 46.9	4 3.5	57 50.4	1.07
Total	106 93.8	7 6.2	113[a] 100.0	1.06

[a]Non-responses: Big Fifteen-3; Other-4.

[b]Insufficient expected cell sizes for statistical tests.

H_0-12: CPA Breakdown--Costs/Benefits with non-SEC registered firms

The responses of the CPA groups are virtually the same for non-SEC registered firms as they are for SEC registered firms. In fact, the only difference among their responses for non-SEC registered firms is that one respondent in the category of "Other Firms" who did not answer the cost/benefit question for SEC registered firms, feels that costs will exceed benefits for non-SEC registered firms.

TABLE IX-12

BIG FIFTEEN--COSTS/BENEFITS NON-SEC FIRMS

Size of Firm	Costs Exceed Benefits	Benefits Exceed Costs	Total	Mean
Big Fifteen	53 46.5	3 2.6	56 49.1	1.05
Other Firms	54 47.4	4 3.5	58 50.9	1.07
Total	107 93.9	7 6.1	114[a] 100.0	1.06

[a]Non-responses: Big Fifteen-3; Other-3.

[b]Insufficient expected cell sizes for statistical tests.

Data Review

Hypotheses rejected

Examination of the data shows that no chi-square test even approaches rejection of the hypothesis of consensus at the alpha level of .05. This suggests that there is general agreement of all groups on all issues concerning government selection and payment of independent auditors.

No clear-cut statement can be made as to how the respondent groups feel that government selection and payment of independent auditors will affect independence either for SEC registered or non-SEC registered clients.

Analysis of means of independence decision

Using the 1 to 5 scale, it is possible to state that a group mean of below 3.0 indicates an average response that independence will be decreased. It is also possible to state that a group mean of 3.0 indicates an average response that independence will not be affected; a group mean above 3.0 indicates an average response that independence will be increased.

The highest means for SEC and non-SEC firms belong to the CBMs (3.18 and 3.16), to the group with 0-9 years of experience (3.18 and 3.21), and to the "Big Fifteen CPAs (3.04 and 3.11). The lowest means belong to the group with 30-39 years of experience (2.76 and 2.63), to the group with 40+ years of experience (2.55 and 2.45), and to the CPAs from other firms (2.73 and 2.65).

Based on many of the comments volunteered on the questionnaires, this researcher has to speculate as to what question the respondents are actually addressing. Are they honestly answering how they feel that independence will be affected? Or are they indicating how they want selection and payment of independent auditors to take place?

Analysis of means of costs/benefits

Using the 1, 2 scale, it is possible to state that a group mean above 1.5 indicates an average response that the benefits will exceed the costs. Conversely, a group mean below 1.5 indicates an average response that the costs will exceed the benefits.

Asked about the issue of costs and benefits to society when there is government selection and payment of auditors, all respondent groups clearly agree. By a very wide margin, every group mean suggests that the respondents feel that the costs to society as a whole will exceed the benefits to society as a whole. The closeness of the means makes it futile to look at differences among group means.

The data in Table IX-13 reveals that there is no correspondence between the respondent groups when their means for SEC and non-SEC registered firms are compared. Some of the group means are higher for SEC firms than for

TABLE IX-13

COMPARISON OF GROUP MEANS--GOVERNMENT

Group	Independence Decision SEC	Independence Decision Non-SEC	Costs Benefits SEC	Costs Benefits Non-SEC
CPAs	2.91	2.92	1.07	1.07
CBMs	3.18	3.16	1.08	1.07
CFAs	2.94	2.95	1.14	1.10
0-9	3.18	3.21	1.07	1.05
10-19	2.91	2.90	1.10	1.08
20-29	2.87	2.87	1.13	1.13
30-39	2.76	2.63	1.06	1.06
40+	2.55	2.45	1.10	1.10
Big 15	3.04	3.11	1.05	1.05
Other CPAs	2.73	2.65	1.07	1.07
Total of All Respondents	3.00	3.00	1.09	1.08

non-SEC firms. The reverse is true of the other groups both for the issue of independence and for the costs and benefits decisions.

Although no clear reason seems to exist for the differences of means for the CPA groups, it is possible that the respondents from smaller firms are concerned that the government is more likely to select large firms.

Conclusions

All respondent groups seem to agree on all of the research questions in this chapter. Independence will be neither increased or decreased by government selection and payment of independent auditors.

It is clear that all respondent groups feel the costs to society as a whole will far exceed the benefits to society as a whole. This was the strongest position taken by the respondents for any of the questions in this research.

The position of the Commission on Auditors' Responsibilities on government selection and payment of auditors is strongly supported by this research.

CHAPTER X

SUMMARY AND CONCLUSIONS

For many years the business community has relied on statements from Certified Public Accountants about the appropriateness of the financial statements of the CPAs' clients. This has created a vast trust for the CPA which until recently was seldom questioned. In the last few years many incidents have come to light that have cast doubt on the CPAs and the relationships that they have with their clients. In an attempt to look more closely at this problem, committees were set up in both houses of the U.S. Congress as well as within the AICPA.

The primary emphasis of this research is to examine some changes possible as a result of the report titled *The Commission on Auditors' Responsibilities: Report, Conclusions, and Recommendations*, issued by the AICPA early in 1978. Using the questionnaire approach, this study examines potential changes in the CPA/client relationships, and how various response groups view these changes.

Summary

Review of the data chapters shows that ten of the tests are significant at the .05 alpha level; another seven are significant at the .10 level. Table X-1 summarizes the results of the statistical tests.

Since the study deals with six issues, each question or set of questions is considered separately below.

Rotation of audit firms

There are a number of significant differences of opinion regarding the rotation of independent auditors, but the group means suggest that on the whole, the groups do feel that rotation will increase independence. At the same time all groups are of the opinion that rotation will be more costly than the benefits received by society.

CPAs who work/worked with firms other than the Big Fifteen are the group most in favor of rotation. The groups least in favor of rotation are the Big Fifteen CPAs and those respondents with 30 or more years of experience. It should be noted that the two groups with the most experience do have limited numbers of respondents.

One of the questions left unanswered, and one that remains unresolved by this research is what the respondents are actually saying. Possibly some of the CPA respondents are indicating how they think the possible change will affect their billings, rather than how it will affect independence. This conclusion is to some degree supported by the numbers. Those respondent groups (Big Fifteen CPAs and the older groups) most likely to have large, stable clients indicate the effect least favorable

TABLE X-1

SUMMARY OF STATISTICAL TESTS

Test	Rotation	Disclosure	Gifts/ Discounts	Placement	Fees	Government
CPAs/CBMs/CFAs - Independence SEC Firms	.337	.095**	.013*	.448	.619	.391
CPAs/CBMs/CFAs - Independence Non-SEC Firms	.007*	.291	.033*	.891	.543	.194
CPAs/CBMs/CFAs - Costs/Benefits SEC Firms	.008*	.169	.067**	.717	.819	.197
CPAs/CBMs/CFAs - Costs/Benefits Non-SEC Firms	.002*	.057**	.104	.392	.153	.612
Experience Groups - Independence SEC Firms	.059**	.738	.505	***	.906	.648
Experience Groups - Independence Non-SEC Firms	.164	***	.974	***	***	.769
Experience Groups - Costs/Benefits SEC Firms	.826	.674	.903	.966	.553	***
Experience Groups - Costs/Benefits Non-SEC Firms	.587	.214	.888	.979	.351	***
Big Fifteen - Independence SEC Firms	.071**	.282	.149	.024*	.862	.941
Big Fifteen - Independence Non-SEC Firms	.144	.011*	.177	.065**	.029*	.866
Big Fifteen - Costs/Benefits SEC Firms	.063**	.043*	.755	.653	.945	***
Big Fifteen - Costs/Benefits Non-SEC Firms	.601	.012*	.685	.682	.523	***

*Significant at .05 alpha level.
**Significant at .10 alpha level.
***Insufficient expected cell sizes for statistical tests.

to independence.

The results suggest that none of the groups feel that the benefits derived from rotation warrant mandated rotation. This finding is consistent with the recommendation made by the Commission on Auditors' Responsibilities that rotation not be required.

Disclosure of independent auditor changes

On the question of a management report containing disclosure of independent auditor changes, there are again a number of statistical differences of opinion among the respondent groups. All respondent groups feel that independence will be increased for SEC firms; all but one of the groups feel that independence will be increased with non-SEC firms if changes in independent auditors are disclosed. Regarding the issue of costs and benefits for the proposed change, all groups feel the benefits will exceed the costs for SEC firms; all but two groups feel the same way regarding non-SEC firms.

Possibly the respondents are actually saying that, while they believe the proposed change may not significantly increase independence, still the cost of implementing such a change is so low that it is worthwhile nevertheless. This explains to some degree those groups who do not feel independence will be increased significantly, yet still think that the costs will be less than the benefits.

Finally, it should be noted that, based on the comments volunteered on many questionnaires, a number of respondents do not understand the format of the suggested management report. A number of respondents think that this disclosure will appear in the "highlight" section of the current annual reports--illustrating the problems possible in communication when questionnaires are used. However, this researcher does not believe that it constitutes a major problem here.

The findings in this chapter are consistent with the recommendation of the Commission on Auditors' Responsibilities that a management report be used to disclose the changes of independent auditors.

Gifts and discount purchases

Although there are a few statistically significant differences among groups as to how prohibition of gifts and discount purchases will affect independence, the issue is the degree of the effect and not its direction. All groups feel that independence will be increased for both SEC and non-SEC firms if gifts and discount purchases from clients are prohibited. All groups feel that for SEC and non-SEC firms, the costs of such a prohibition will be less than the benefits.

The more experienced groups are consistently the most emphatic about the benefits of a prohibition. CBMs also seem to feel strongly about this issue. However, it is still useful to examine further some of the possible reasons for the groups means. Possibly the more experienced groups feel as strongly as they do because over the years they have seen more abuses. Perhaps lawyers are more likely to see the bargaining and deals that reportedly take place. It may also be true that Big Fifteen firms have so many built-in safety guidelines that few abuses occur, and consequently the need for reform is not as great in these firms. This line of reasoning has been neither supported nor refuted by research.

The findings of this research suggest that gifts and discount purchases should be prohibited. This is consistent with the recommendation of the Commission on Auditors' Responsibilities which also suggests a prohibition.

Executive search and placement

Only one significant difference exists among the respondents on this question. The difference is between the CPAs who work/worked for Big Fifteen firms (mean of 3.37) and those who work/worked for other firms (mean of 3.76). All groups feel that independence will be increased if executive search and placement service were prohibited. However, a number of groups feel that with such a prohibition, the costs to society as a whole will exceed the benefits to society as a whole.

In all but one case the respondents feel the benefits of a prohibition will be less (smaller increase of independence), for non-SEC firms than for SEC firms. Sometimes the difference was large when comparing responses for SEC vs. non-SEC firms.

It can be argued that the CPAs who work with the Big Fifteen firms have seen the usefulness of recruitment, and have seen few abuses considering the many built-in constraints of the large firms. It may be more likely that, given their larger search and placement services, the big firms have more to lose if such a prohibition is enacted. Consequently, it is necessary again to speculate as to which question the respondents are actually addressing.

Because of the mixed results on this question, it is not wise to draw any conclusions on the correctness or incorrectness of the stand taken by the Commission on Auditors' Responsibilities on the issue of executive search and placement. The data in this study gives no clear indicator as to the direction which should be taken by the profession.

Fees and arrangements for auditors

Only one test is significant on this question, one involving the two groups of CPAs. All groups feel that independence will be increased if fees and arrangements for auditors are taken care of by audit committees for SEC firms. Only the group with 30-39 years of experience feels that independence will not be increased for non-SEC firms.

The groups with the highest means (that is, those who believe independence will be increased the most) are the CPAs with the Big Fifteen firms, and the respondents with 0-9 years of experience.

One possible explanation for the findings above is the heavy pressure, due to large fees, on CPAs in large firms. Also, it is more likely that pressure is put on the new and least experienced employees. Once again the lowest means are for the two most experienced groups. In fact, neither the groups with 30-39 years of experience, nor those with 40+ years of experience feel that independence will be increased for non-SEC firms by this proposed change.

Regarding the costs and benefits for this question, all groups think that the benefits will exceed the costs for SEC firms. At the same time, a number of groups do not feel the costs will be covered by the benefits for non-SEC firms.

It should be noted that many non-SEC firms have no members of the board of directors who are not management. Consequently, for these firms, the cost of an audit committee made up of non-management people would be costly. It is likely that this is a consideration when respondents refer to non-SEC firms.

One point of misunderstanding on the questionnaire may have been due to the respondents' ignorance of the current state of audit committees in the U.S. A number of respondents suggest that this is already the law. Typically they are referring to the fact that the New York Stock Exchange requires audit committees. At the time of this questionnaire, the requirements had not spelled out any duties for these committees; they state merely that they must exist. This may have affected some respondents' evaluation of the costs and benefits of such a mandate.

The findings of this research support the position of the Commission on Auditors' Responsibilities that SEC firms should have audit committees handle fees and arrangements for independent auditors. The position of the commission on non-SEC firms has been neither supported nor refusted by this research.

Government selection and payment of auditors

On this issue there seems to be little disagreement among the various respondent groups. None of the tests are statistically significant. Regarding both SEC and non-SEC firms, only three respondent groups feel that independence will be increased by government selection and payment of auditors. All of the other groups feel that independence will be decreased.

Regarding the issue of costs and benefits, all respondents feel that the costs of government selection and payment of auditors will exceed the benefits of such action to society.

Over-all Comparisons

Table X-2 shows that the means of the CPAs are consistently lower than the means for CBMs and CFAs. Only on the issue of fees and arrangements is the mean of the CPAs higher than those of the other two groups. Consistently this indicates that the CPAs do not feel independence will be increased as much as the CBMs and CFAs.

Table X-3 indicates that for the costs/benefits decision, the means of the CPAs are again consistently lower than those of the other two groups.

Another observation that can be made based on Tables X-2 and X-3 concerns the CPAs who are with the Big Fifteen and the CPAs with other firms. Although the direction differs from question to question as to which group has the high or low mean, regarding the issue of independence, the two groups never approach agreement. There is always a large gap between the means for the two groups. Referring to the costs/benefits decision, the CPAs agree much more closely. The means for the costs/benefits decision are very close for the two groups.

TABLE X-2

COMPARISON OF MEANS--ALL INDEPENDENCE

Decision	CPAs	CBMs	CFAs	Big 15	Other CPAs	Total
Rotation - Independence SEC Firms	3.84	3.89	3.90	3.73	4.00	3.87
Rotation - Independence Non-SEC Firms	3.61	3.78	3.86	3.27	3.72	3.72
Disclosure - Independence SEC Firms	3.45	3.62	3.55	3.54	3.32	3.52
Disclosure - Independence Non-SEC Firms	3.31	3.45	3.50	3.46	3.08	3.40
Gifts/Discounts - Independence SEC Firms	3.56	3.87	3.76	3.37	3.67	3.71
Gifts/Discounts - Independence Non-SEC Firms	3.55	3.82	3.82	3.40	3.60	3.70
Placement - Independence SEC Firms	3.56	3.64	3.64	3.37	3.76	3.60
Placement - Independence Non-SEC Firms	3.52	3.56	3.59	3.34	3.65	3.55
Fees - Independence SEC Firms	3.54	3.35	3.40	3.64	3.45	3.44
Fees - Independence Non-SEC Firms	3.43	3.23	3.45	3.62	3.25	3.37
Government - Independence SEC Firms	2.91	3.18	2.94	3.04	2.73	3.00
Government - Independence Non-SEC Firms	2.92	3.16	2.95	3.11	2.65	3.00

TABLE X-3

COMPARISON OF MEANS--ALL COSTS/BENEFITS

Decision	CPAs	CBMs	CFAs	Big 15	Other CPAs	Total
Rotation - Costs/Benefits SEC Firms	1.20	1.39	1.30	1.25	1.27	1.28
Rotation - Costs/Benefits Non-SEC Firms	1.12	1.28	1.32	1.09	1.13	1.21
Disclosure - Costs/Benefits SEC Firms	1.62	1.75	1.68	1.75	1.54	1.67
Disclosure - Costs/Benefits Non-SEC Firms	1.53	1.67	1.68	1.69	1.43	1.61
Gifts/Discounts - Costs/Benefits SEC Firms	1.65	1.80	1.73	1.61	1.60	1.72
Gifts/Discounts - Costs/Benefits Non-SEC Firms	1.63	1.76	1.74	1.59	1.65	1.70
Placement - Costs/Benefits SEC Firms	1.50	1.52	1.56	1.49	1.55	1.52
Placement - Costs/Benefits Non-SEC Firms	1.47	1.47	1.56	1.45	1.51	1.49
Fees - Costs/Benefits SEC Firms	1.58	1.61	1.56	1.60	1.57	1.59
Fees - Costs/Benefits Non-SEC Firms	1.43	1.54	1.55	1.46	1.38	1.49
Government - Costs/Benefits SEC Firms	1.07	1.08	1.14	1.05	1.07	1.09
Government - Costs/Benefits Non-SEC Firms	1.07	1.07	1.10	1.05	1.07	1.08

Finally, as review of all of the means makes clear the CPAs and CBMs view the relationship of SEC and non-SEC firms differently from the CFAs. While the means for CPAs and CBMs for SEC firms are almost always higher (for both the independence and cost/benefits decisions) than for non-SEC firms, this relationship of means does not hold for CFAs. In fact, in a number of instances the mean of the CFAs for non-SEC firms is higher than the mean for SEC firms.

Possible Limitations of Research

As this research deals with the perceptions of the users of accounting data, one possible limitation is the selection of samples to represent the users. The researcher believes that the samples selected are an important segment of the users. Generalization regarding other segments of the users is difficult, but this would be true no matter which groups were chosen, unless all users were selected.

Use of a questionnaire always presents a number of problems to the researcher. This study is no different. As noted earlier in the summary, in some instances it is not clear that the respondents understand precisely what information the questions ask for. It is not believed that this is a significant problem, but it does exist to some extent.

Non-responses to the questionnaire are a possible problem in a questionnaire study. There is always some question as to bias of those subjects who do not respond.

However, the high response rate helps to diminish this concern.

Although it is not believed that a major problem exists, it should be noted that the higher response rates of the CPAs vs. the other two groups of professionals may bias the results. One way to see the possible effect is to look at the between-group comparisons for the various questions. By doing this the reader can confirm how the groups vary in responses.

Finally, it is obvious that the chi-square does note differences between groups, but in examination of more than two groups, it does not pinpoint the groups that differ. There are other tests that may be used to look further at this data for additional insight. Although the differences are not pinpointed by the chi-square, the reader can examine the raw data and the group means, and thus obtain meaningful information. In fact, the researcher finds these items of more worth for informational content than the results of the chi-square.

The limitations noted above do not diminish the significance of the results of this study; in fact, in view of the additional information presented by this study, they are minor.

Possible extensions of this research

As the analysis chapters as well as the limitations section of this chapter make clear, there are some opportunities to obtain more information from this data using additional research techniques. This researcher hopes that those opportunities will be pursued.

Included in such additional research might be a closer study of the experience groups. As the data chapters reveal, the groups with the most experience seem consistently to be less impressed with the usefulness of a change regarding independence. There also seems to be a consistency as to how the CPA groups (Big Fifteen and Other Firms) almost always disagree as to the effect that a proposed change would have on independence. Possibly additional insight can be gained by categorizing the CPAs into additional groupings, and studying them further. Limits of space and time do not allow for such analysis here.

During hearings for its final report, the Commission on Auditors' Responsibilities was concerned about small firms. The present study shows that there is a general feeling that SEC and non-SEC registered firms may benefit differently from the proposed change. Why this is so is not clear, but certainly this issue is worth further study.

Another area for additional research is the sequence of returns, and whether there is a bias connected with when the returns were received. This might be done using a time series analysis of the responses either in total, or for each major respondent group, since all returns were dated as received. This may also lead to other areas of questionnaire research such as an examination of factors that may have prompted the high response rates; this would aid further questionnaire research.

This researcher believes that one of the most important issues to be considered in this research is the costs/benefits analysis. Due to the various interpretations of costs/benefits, there is little in the returned questionnaires to suggest which factors were taken into account by the respondents. Further research has to be done to elaborate on the costs/benefits issue; perhaps models can be developed to aid organizations such as the AICPA and the SEC in establishing new rules for CPAs. The present study is thus only a first step.

Finally, a replication of this study can be undertaken to validate these results.

Conclusions

This research examines empirically a number of recommendations made in The Commission on Auditors' Responsibilities: Report, Conclusions, and Recommendations. Where there seems to be a consensus of the respondents, the position taken by the Commission is validated. Few of the proposals are accepted or rejected by all respondent groups.

It seems from this research that the Commission on

Auditors' Responsibilities is following the wishes of the users in its recommendations regarding independence. Much remains to be done regarding the problem of smaller firms, and regarding the issues raised by the costs and benefits sections of this research.

Finally, it should be noted that this research deals only with six of the many independence issues raised in the Commission's report; there are still other issues that the Commission does not deal with. The present study is merely a small first step into unexplored and exciting territory for research.

APPENDICES

APPENDIX A

FINAL QUESTIONNAIRE MAILED TO CERTIFIED PUBLIC ACCOUNTANTS

I. A. Are you currently practicing with a Certified Public Accounting (CPA) firm? (Please circle one.)

Yes No

B. Into which of the following groups would the practice with which you are(were) involved fall? (Please circle one number.)

Arthur Andersen & Co. Arthur Young and Company Coopers & Lybrand Ernst & Ernst	Haskins & Sells Peat, Marwick, Mitchell & Co. Price Waterhouse & Co. Touche Ross & Co.	1
Alexander Grant & Co. Hurdman and Cranstoun J. K. Lasser & Co. Laventhol & Horwath	S. D. Leidesdorf & Co. Main Lafrentz & Co. Seidman & Seidman	2

Other national firms . . . 3 Regional firms . . 4 Local firms. . 5

C. If you are not currently a practicing CPA, in what sort of work are you currently employed? (Please circle one number.)

Private Industry . . . . . 1 Government 2

Education . . . . 3 Retired 4

Other (Please specify)____ . . 5

D. To the nearest year, how many years experience do(did) you have in public accounting?

______

E. How would you describe your Securities and Exchange Commission experience, either directly with SEC registration or with SEC registered firms? (Please circle one number.)

Little or no experience				Considerable experience
1	2	3	4	5

II. In each of the seven situations presented on the next page a potential change in the current relationship between Certified Public Accountants (CPAs) and their audit clients is presented. Each situation is to be considered as unrelated to the other six.

In each situation please evaluate how you think the potential change would affect the independence (non-bias) of the CPAs from their clients with respect to an opinion audit on the clients' statements involved for the two categories of firms: 1) Securities and Exchange Commission (SEC) registered companies and 2) non-SEC registered companies.

Also, for each of the seven unrelated situations, please indicate how you feel the proposed changes would affect costs and benefits to society as a whole when the change would involve: 1) SEC registered companies and 2) non-SEC registered companies.

	Independence Decision	Costs/Benefits Decision
The proposed change would	1 = Greatly Decrease Independence 2 = Slightly Decrease Independence 3 = Not Affect Independence 4 = Slightly Increase Independence 5 = Greatly Increase Independence	1 = If the proposed change is made, the cost to Society will exceed the benefits to Society 2 = If the proposed change is made, the benefits to Society will exceed the costs to Society

			Independence Decision (Please circle one)					Costs/Benefits Decision (Please circle one)	
1.	Require rotation of independent audit firms	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2
2.	Require disclosure of independent auditor changes in a management report accompanying the financial statements	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2
3.	Require adoption of policies on gifts and discount purchases from clients by independent auditors	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2
4.	Prohibit executive search and placement services by independent auditors for audit clients . . .	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2
5.	Require fees and arrangements for independent auditors be determined by an audit committee . .	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2
6.	Require involvement by the independent auditor in a company's financial reporting process on a current and continuing basis. .	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2
7.	Require government selection and payment of independent auditors . . .	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2

Use this space for any additional comments on any part of this questionnaire.

Would you like to receive a summary of this research? Yes No

I am very grateful for your cooperation !

APPENDIX B

FINAL QUESTIONNAIRE MAILED TO MEMBERS OF THE SECTION OF CORPORATION, BANKING AND BUSINESS LAW OF THE AMERICAN BAR ASSOCIATION

I. A. In what area of law are you currently employed? (Please circle one number.)

Private Practice 1

Industry 2

Government 3

Education 4

Other (Please specify)________________________________ . . 5

B. To the nearest year, how many years experience do you have in your present occupation? __________

C. How would you describe your Securities and Exchange Commission experience, either directly with SEC registration or with SEC registered firms? (Please circle one number.)

Little or no experience				Considerable experience
1	2	3	4	5

D. How familiar are you with the audit work of Certified Public Accountants? (Please circle one number.)

Not familiar				Very familiar
1	2	3	4	5

E. To what extent do you believe that independence is necessary to CPAs' audit reports? (Please circle one number.)

Not necessary				Very necessary
1	2	3	4	5

II. In each of the seven situations presented on the next page a potential change in the current relationship between Certified Public Accountants (CPAs) and their audit clients is presented. Each situation is to be considered as unrelated to the other six.

In each situation please evaluate how you think the potential change would affect the independence (non-bias) of the CPAs from their clients with respect to an opinion audit on the clients' statements involved for the two categories of firms: 1) Securities and Exchange Commission (SEC) registered companies and 2) non-SEC registered companies.

Also, for each of the seven unrelated situations, please indicate how you feel the proposed changes would affect costs and benefits to society as a whole when the change would involve: 1) SEC registered companies and 2) non-SEC registered companies.

The proposed change would	Independence Decision	Costs/Benefits Decision
	1 = Greatly Decrease Independence 2 = Slightly Decrease Independence 3 = Not Affect Independence 4 = Slightly Increase Independence 5 = Greatly Increase Independence	1 = If the proposed change is made, the cost to Society will exceed the benefits to Society 2 = If the proposed change is made, the benefits to Society will exceed the costs to Society

			Independence Decision (Please circle one)					Costs/Benefits Decision (Please circle one)	
1.	Require rotation of independent audit firms	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2
2.	Require disclosure of independent auditor changes in a management report accompanying the financial statements	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2
3.	Require adoption of policies on gifts and discount purchases from clients by independent auditors	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2
4.	Prohibit executive search and placement services by independent auditors for audit clients . . .	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2
5.	Require fees and arrangements for independent auditors be determined by an audit committee . .	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2
6.	Require involvement by the independent auditor in a company's financial reporting process on a current and continuing basis. .	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2
7.	Require government selection and payment of independent auditors . . .	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2

Use this space for any additional comments on any part of this questionnaire.

Would you like to receive a summary of this research?   Yes   No

I am very grateful for your cooperation !

APPENDIX C

FINAL QUESTIONNAIRE MAILED TO
CHARTERED FINANCIAL ANALYSTS

I. A. In what industry are you currently employed? (Please circle one number.)

Brokerage and Investment Banking 1

Investment Companies 2

Investment Counselor 3

Trust Companies or Trust Departments of Commercial Banks 4

Insurance Companies 5

Pension Funds 6

Other (Please specify)____ . . 7

B. Do you currently analyze securities of individual firms? (Please circle one.)

Yes No

C. To the nearest year, how many years experience do you have in your present occupation? ________

D. How would you describe your Securities and Exchange Commission experience, either directly with SEC registration or with the securities of SEC registered firms? (Please circle one number.)

Little or no experience				Considerable experience
1	2	3	4	5

E. How familiar are you with the audit work of Certified Public Accountants? (Please circle one number.)

Not familiar				Very familiar
1	2	3	4	5

F. To what extent do you believe that independence is necessary to CPAs' audit reports? (Please circle one number.)

Not necessary				Very necessary
1	2	3	4	5

II. In each of the seven situations presented on the next page a potential change in the current relationship between Certified Public Accountants (CPAs) and their audit clients is presented. Each situation is to be considered as unrelated to the other six.

In each situation please evaluate how you think the potential change would affect the independence (non-bias) of the CPAs from their clients with respect to an opinion audit on the clients' statements involved for the two categories of firms: 1) Securities and Exchange Commission (SEC) registered companies and 2) non-SEC registered companies.

Also, for each of the seven unrelated situations, please indicate how you feel the proposed changes would affect costs and benefits to society as a whole when the change would involve: 1) SEC registered companies and 2) non-SEC registered companies.

	Independence Decision	Costs/Benefits Decision
The proposed change would	1 = Greatly Decrease Independence 2 = Slightly Decrease Independence 3 = Not Affect Independence 4 = Slightly Increase Independence 5 = Greatly Increase Independence	1 = If the proposed change is made, the cost to Society will exceed the benefits to Society 2 = If the proposed change is made, the benefits to Society will exceed the costs to Society

			Independence Decision (Please circle one)					Costs/Benefits Decision (Please circle one)	
1.	Require rotation of independent audit firms	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2
2.	Require disclosure of independent auditor changes in a management report accompanying the financial statements	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2
3.	Require adoption of policies on gifts and discount purchases from clients by independent auditors	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2
4.	Prohibit executive search and placement services by independent auditors for audit clients . . .	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2
5.	Require fees and arrangements for independent auditors be determined by an audit committee . .	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2
6.	Require involvement by the independent auditor in a company's financial reporting process on a current and continuing basis. .	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2
7.	Require government selection and payment of independent auditors . . .	a) SEC registered firms	1	2	3	4	5	1	2
		b) non-SEC firms	1	2	3	4	5	1	2

Use this space for any additional comments on any part of this questionnaire.

Would you like to receive a summary of this research? Yes No

I am very grateful for your cooperation !

APPENDIX D

COVER LETTER FOR THE FIRST MAILING

MICHIGAN STATE UNIVERSITY

GRADUATE SCHOOL OF BUSINESS ADMINISTRATION
DEPARTMENT OF ACCOUNTING & FINANCIAL ADMINISTRATION

EAST LANSING · MICHIGAN · 48824

We invite your participation in a research study which focuses on an issue of vital importance in our business society in general and to the profession of public accounting in particular.

All of your responses will be held in strict confidence with no specific identification of you or your answers to anyone. We are very conscious of your dignity and right to privacy and feel that those concerns are more important than any research study.

Mr. Duane R. Milano is a doctoral candidate in our Graduate School of Business Administration. As part of his doctoral research, he is conducting a study relating to the independence of the certified public accountant. Mr. Milano is defining independence as the ability to make an unbiased analysis of a given situation. The CPA's usefulness as an auditor is likely to be impaired by any belief on the part of a third party that he/she is lacking independence.

The enclosed short questionnaire is designed to obtain the viewpoints of third parties and CPAs. Using statistical probability methods, you were chosen to represent your profession.

It is necessary that you use the enclosed postage-paid envelope as it is the record of your response. When your reply is received, your name will be removed from our address listing for follow-up mailings. All questionnaires will be reviewed and tabulated only after all cross references to names and addresses have been destroyed.

You may learn of the results of this study by marking the appropriate response at the end of the questionnaire.

Again be assured that your responses will remain anonymous.

Thank you for your kind assistance and your cooperation.

Harold M. Sollenberger

Harold M. Sollenberger
Professor and Chairman

APPENDIX E

COVER LETTER FOR THE SECOND MAILING

MICHIGAN STATE UNIVERSITY

GRADUATE SCHOOL OF BUSINESS ADMINISTRATION
DEPARTMENT OF ACCOUNTING & FINANCIAL ADMINISTRATION

EAST LANSING • MICHIGAN • 48824

A few weeks ago you should have received a research questionnaire from Mr. Duane R. Milano, a doctoral candidate of our College. Mr. Milano's research concerns independence and the certified public accountant.

He has had good response to the questionnaire to date. However the research would be more meaningful if we could include your confidential response in the study.

Mr. Milano is defining independence as the ability to make an unbiased analysis of a given situation.

May we have the benefit of your thoughts in this important research? Please complete the enclosed questionnaire and return it in the self-addressed, numbered envelope as soon as possible. This will allow us to remove your name from future mailings requests without identifying your questionnaire.

Thank you for your cooperation in this research.

Sincerely,

Harold M. Sollenberger

Harold M. Sollenberger
Professor and Chairman

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