

## **Audit Quality: An Analysis**

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### **Abstract**

This paper reviews the research literature and publications relevant to audit quality. The researcher identifies three main perspectives (academic research, professional and regulatory) related to audit quality that could add to the understanding of the concepts and factors affecting audit quality in practice. For each reviewed perspective, the researcher presents and summarizes the key findings. Design/ Methodology/ Approach: This paper links academic research to publications on the topic issued by professional practitioners and regulators. Research findings: Based on the analysis, the review reveals three main findings. First, the review identifies multifaceted concepts of audit quality and the various academic research approaches that have been carried out to assess audit quality. Second, audit quality in practice is not only affected by various internal factors within the accounting firms but is also influenced by various contextual factors in which the accounting firms operate. Third, much of the prior research employs an archival approach that potentially provides limited information about the effect of the contextual setting in actual audit practices, which is important to enhance our understanding of audit quality. Theoretical contribution/ Originality: It provides some guidance for future academic research related to audit quality. Practitioner/ Policy implication: The research and reports reviewed in this paper will be useful to researchers, audit practitioners, policymakers and others who are concerned with the quality of audit services to understand the various conceptions of audit quality and the important factors affecting audit quality in practice. Research limitation/ Implications: The analysis of the audit quality from the three main perspectives provided in this study pave the way for embarking on promising and relevant future research, which is needed to further substantiate and enrich the academic understanding on concepts and factors affecting audit.

**KEYWORDS:** academic, professional, regulatory, contextual factors, audit.

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Audit quality and the factors that affect quality have been the subject of interest in academic, practitioner and regulatory debates about auditing following a series of corporate collapses. As a result, there have been considerable developments in the auditing, financial reporting and governance regimes by regulators and professional bodies in the name of enhancing audit quality. Regulators, such as the International Auditing and Assurance Standards Board (IAASB), have published a framework for audit quality, which discusses various pertinent factors affecting audit quality in practice (IAASB, 2014). Earlier, the Financial Reporting Council (FRC) released a discussion paper identifying the drivers for audit quality (FRC, 2008). In like manner, the Institute of Chartered Accountants in England and Wales (ICAEW) (2002) issued a report to frame concepts and various factors affecting audit

performance. Similarly, research in the academic domain has examined the concepts and various factors affecting quality differentiation between audit firms and auditors .

Although initiatives by regulators and professional practitioners influence the contemporary understanding concerning the concepts of audit quality, neither party have defined the term precisely. Research in the professional literature is inclined to define audit quality as conformance to the auditing standards during audit performance (Krishnan & Schauer, 2001). In comparison, various academic research approaches have conceptualized and measured audit quality in several ways including a combination of measures linking inputs (such as size of audit firm and audit fees) to audit outcomes (such as financial reporting quality and accurate audit opinion), process measures that are related to auditor performance in the audit process (Sutton, 1993; Malone & Roberts, 1996), and studies of the perceptions of the users and preparers of financial statements on audit quality . As a whole, there has been little agreement on a unified definition and measure of audit quality (Krishnan & Schauer, 2000; FRC, 2008), which might be due to the unobservable features of audit quality (Power, 1997). In addition, the definition or understanding of audit quality may be different from the perspectives of audit participants (e.g., investors, regulators and audit committees) in the audit market because of their different roles and expectations (Sutton, 1993). Consequently, audit participants employ different conceptions and approaches to its assessment. Hence, operationalizing the concepts of audit quality and the influential factors are open to further investigation (Nelson & Tan, 2005; Knechel et al., 2013).

The purpose of this paper is to review prior research and publications that are primarily drawn from the arena of regulatory policy on auditing related to audit quality from three different perspectives: academic, professional practitioners, and regulators. This paper seeks to review the literature and publications in order to develop an understanding of the multiple concepts ascribed to audit quality and provide a broader viewpoint of the various debates that affect contemporary understanding of audit quality. Primarily, it identifies and synthesizes the key research themes, thereby providing a timely summary for researchers, practitioners and regulators alike, and the research gaps that need to be addressed in future research. This paper makes a twofold contribution to the existing literature. First, it provides a greater understanding of the concepts and factors affecting audit quality from various viewpoints. Second, the analysis of academic research highlights state-of-the-art audit quality and the dominant approaches in its research. This serves as a source of reference for future research by providing an agenda for further work specific to understanding audit quality within the social and organizational context of audit practices.

The first strand of research employs the market-based data (archival) approach and focuses on the association between the proxies for ‘input’ and ‘output’ related to audit quality. The review of academic research reveals that the investigation of ‘input’ and ‘output’ is largely built around the definition of audit quality proposed by DeAngelo (1981a; 1981b). For DeAngelo, audit quality refers to the ability of the auditors to detect and report material misstatements, which reflects two key determinants of audit quality: the competence and independence of the professional auditors. Given the unobservable features of audit quality – inability to examine the

audit working papers or observe audit performance – various proxies for audit quality have been used (such as size and industry specialist of audit firms) to test the effects of the proxies on the independence and competence of the auditors. As such, ‘input’ variables (such as audit firm size, audit fees, non-audit fees, and audit tenure) and ‘output’ quality (such as quality of earnings, litigation, accurate audit opinion and regulatory sanctions) have been extensively examined to assess audit quality.

The second strand of academic research related to audit quality concentrates on examining the factors affecting audit quality including Perspectives of Audit Quality: An Analysis audit procedures, auditors’ judgment and the behaviour or task performance during the audit process. The literature has documented that the audit process can be impacted by the audit procedures used in conducting the audit. A number of studies have focused on the audit procedures by specifically examining the audit methods used in conducting the audit, the effects of the audit methods applied, as well as the decision aids applied in practice to develop new audit methods or procedures (Curtis, 2006). The different audit and decision aids used have been documented as having a different influence on the various aspects of audit performance, which, in turn, can negatively or positively influence the audit quality. For example, Wilks and Zimbelman (2004) find that the use of a holistic approach to assess the risks would result in an understatement of the fraud risk assessments compared to an approach that separately assesses the risk of fraud for different components. In all, the audit methods and decision aids are specifically adopted to direct and help an audit team conduct the audit in a systematic manner (Knechel et al., 2013).

#### Conclusions

In this paper, the researcher reviewed the academic research and publications related to audit quality. Overall, the researcher believes that the review provides wider concepts attributed to audit quality and the various contextual factors that can affect it. Hence, more research is needed to understand Audit Quality: An Analysis this issue better and to move towards a policy resolution. In addition, the researcher has identified a number of important research opportunities and hopes that auditing researchers will examine these issues to improve the knowledge about audit quality. Further, the analysis would be helpful for audit practitioners and policymakers in terms of understanding the key factors that affect audit quality, thus positioning the best strategies and policies in supporting it.

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