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Factors Impacting Audit Quality

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CERTIFICATE OF AUTHORSHIP/ORIGINALITY

I certify that the work in this thesis has not previously been submitted for a degree nor has it been submitted as part of requirements for a degree except as fully acknowledged within the text.

I also certify that the thesis has been written by me. Any help that I have received in my research work and the preparation of the thesis itself has been acknowledged. In addition, I certify that all information sources and literature used are indicated in the thesis.

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Fiona Ball

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ABSTRACT

The objective of this thesis is to evaluate the extent to which auditor-client relations and discounting on initial audit engagements undermine audit quality. While it has been claimed that close auditor-client relations undermine auditor independence and erodes audit quality, I find no evidence of this. This suggests that controls implemented by regulators, the profession and audit firms are operating effectively and the regulation prescribing auditor rotation is likely unnecessary. In relation to the concern that discounting on initial audit engagements erodes audit quality, I find that there are fee increases in periods subsequent to initial audit engagements and this suggests concerns that price pressure arising from discounting undermines audit quality are overstated. These results suggest that many of the concerns expressed about the threats to audit quality are misdirected.

Chapter One
Introduction and Overview

1.1 Introduction

Financial reports are an important tool prepared and used by managers of the firm to communicate financial information to investors and stakeholders, while simultaneously reducing the level of information asymmetry that exists between owners and managers (Antle & Nalebuff, 1991). Subjecting financial statements to external verification and assurance is a mechanism through which managers can add credibility to the reports, enhance and improve the quality of financial information, while increasing the reliance placed upon them (Jensen & Meckling, 1976; Watts & Zimmerman, 1986). That is, financial statements are representations by management and the external audit function is placed over the top of these representations to assess if the statements present a 'true and fair view'.

The audit process is one that substantiates as well as tests the control systems which produce financial statements and determines if the underlying controls are effective at assuring the assertions, while also taking a more holistic view to ensure the application of accounting policies is appropriate (DeAngelo, 1981a). Thus, the financial statements should be read as a joint statement from management and the auditor (DeAngelo, 1981a; Antle & Nalebuff, 1991). Ultimately, the ability of the auditor to enhance the credibility of financial reporting quality, and therefore provide a high level of audit quality, is dependent on two key attributes: auditor competence and auditor reporting behaviour (DeAngelo, 1981b; Johnson, Khurana & Reynolds, 2002). Auditor competence (also known as auditor expertise) specifically refers to the likelihood the auditor will detect a material misstatement, while auditor reporting behaviour (also known as auditor independence) is the auditor's willingness to report detected financial misstatements or errors (DeAngelo, 1981a). Combined, these two attributes assist to determine audit quality,

which is often described as the market assessed joint probability that an auditor will detect and report material misstatements (DeAngelo, 1981a).

Audit quality is improved if material misstatements are detected and reported (or corrected). A failure to detect or report (or correct) a material misstatement or errors in the financial report before issuing an unqualified audit report impairs audit quality. In recent years a number of threats to audit quality have been identified. This includes the concern that close relations between the auditor and the client undermine auditor independence and this lead to the prescription of auditor rotation. Concerns have also been expressed about audit pricing, and in particular the practice of discounting. Accordingly, the objective of this thesis is to provide empirical evidence of whether the limits on auditor tenure and discounting adversely impacts audit quality.

1.2 Motivation

While there is the general motivation of understanding the factors impacting audit quality, there are particular concerns which dictate the specific focus of this thesis. First, in response to anecdotal evidence that a lack of audit independence contributed to corporate failures, many countries adopted regulation that prescribed auditor rotation. In Australia that regulation was the Corporate Law Economic Reform Program (*Audit Reform & Corporate Disclosure Act, 2004* (CLERP 9, 2004). Accordingly, a motivation for this thesis is to provide empirical evidence of any association between audit quality and auditor tenure which would support auditor rotation being prescribed. In this instance, audit quality is assessed in the period when Australian firms were transitioning to *International Financial Reporting Standards* (IFRS) and is measured as the errors arising in the initial implementation of the new standards. This

provides a unique context in which to evaluate the impact of audit quality on financial reporting outcomes. Second, there is a significant body of literature evaluating initial audit engagement fees and the practice of discounting to secure new audit clients. This practice is of concern if the discounting of audit fees results in audit effort being curtailed and there is the increased likelihood of a material misstatement in the financial statements not being discovered. These concerns may be ameliorated if there are material fee increases in subsequent years. Accordingly, another motivation for this thesis is to evaluate audit fee changes subsequent to initial audit engagements to determine if there are fee increases subsequent to initial audit fees and whether concerns over the consequences of discounting are overstated. Consideration is also given to whether the ability to recover discounts on initial audit engagements is affected by *Audit Partner/CEO tenure*, which recognises relationships between the lead audit partner and the CEO of the client firm. The concern is that these relationships limit the ability to increase audit fees and lead to constraints on audit effort and thus quality. This would provide empirical support for the prescription of auditor rotation which is now mandated in many countries.

1.3 Design

Attention is first directed at the evaluation of the impact of audit tenure on audit quality (Chapter 2). This is assessed in the period when Australian firms were transitioning to *International Financial Reporting Standards* (IFRS) and audit quality is measured as the errors arising in the initial implementation of the new standards. The impact of audit tenure on audit quality is assessed having regard to the length of the relation between the audit firm and the client firm which is labelled the 'professional relation' (*Audit_Firm_Tenure*), and the length of the relationship between the individual audit partner and a specific CEO which is labelled the

'person-to-person relationship' (*Partner/CEO_Tenure*). This distinction endeavours to distinguish between the competing effects of learning and impairment of independence on audit quality.

Attention is then directed to the issue of whether there are increases in audit fees in periods subsequent to initial audit engagements (Chapter 3). The primary concern is with changes in audit fees over time and therefore to evaluate audit fees, a lagged audit fee model is adopted, rather than the more traditional cross sectional approach which is common in many studies of audit fees. Changes in audit fees are then evaluated with controls for the initial audit engagement, the period after the initial audit engagement and that corresponds to the likely period of the first audit contract, and longer term audit fees.

1.4 Results

The key findings of this thesis are as follows: In chapter 2 there is no evidence of a significant association between IFRS adoption errors and person-to-person relationships between the audit partner and the CEO of the client firm. This would suggest that auditors do not have person-to-person relationships which undermine audit quality. While it might be expected that increased familiarity between the audit partner and senior executives might undermine audit quality, there are a range of controls to address this including; engagement reviews at the firm, profession and regulator level. The results are consistent with these measures being effective. In contrast, a significant negative association is found between certain IFRS adoption errors and professional relations between the audit firm and the client. Audit quality improves as audit firm tenure increases. These results are robust to a range of sensitivity tests including examination of

a sub sample of June year-end firms, alternative IFRS error variations and total accruals measures as alternatives for audit quality.

In chapter three, evidence is provided of audit fee increases in years subsequent to the initial audit engagement. The increases are greatest in the two years immediately subsequent to an initial audit engagement, which likely correspond with the term of initial audit contracts. Increases are in the order of 8% p.a. and are materially greater than likely cost increases experienced by audit firms. This suggests there is an increase in audit fees in the periods after initial audit engagements and concerns that discounting might result in poorer quality audits are likely misplaced. As audit tenure extends, there is evidence of a decline in the rate of increase in audit fees, and after three years the rate of increase slows to about 3% p.a. This is broadly consistent with cost changes and suggests there are significant competitive pressures which constrain audit fee increases. Accordingly, there is no support for auditor rotation due to concerns that extended tenure inhibits audit fee increases and reduces audit quality.

1.5 Contribution

This thesis contributes to academic debate about the factors impacting audit quality, while providing evidence to regulators and policy makers in the following ways. First, this thesis adopts a novel approach to the examination and measurement of auditor tenure. It provides a new approach in examining the multidimensional nature and differing aspects of audit relations by examining auditor tenure from the perspective of a person-to-person relationship (*Partner/CEO tenure*). Regard is given to both the person-to-person relationships and professional relations that exist between the audit firm and client, with these having potentially differing impacts on audit

quality. Personal relationships are measured as the period where the same lead audit partner and CEO combination worked together in preparing that firm's audited financial statements. While professional relations are measured as the duration of the relation between the audit firm and client firm.

Second, this thesis extends the literature by considering the relation between audit tenure and audit quality, using a new measure, *IFRS adoption errors*, which is not subject to the same limitations of other measures of audit quality. The introduction of IFRS in Australia presents a valuable opportunity to exploit regulatory change and investigate the quality of financial reporting in Australian companies. The change to IFRS represented a major shift in the Australian reporting environment and were viewed as having the potential to cause significant disruptions to market information flows. Recognising this, the Australian Securities and Investment Commission (ASIC) issued warnings that firms should make every effort to ensure disclosures were as accurate as possible, suggesting the ASIC would be investigating poor quality reporting (ASIC, 2005).

Finally, this is one of the few current Australian studies, of which I am aware, that evaluates audit fee changes overtime utilising a lagged audit fee model. Traditionally, prior research examining audit fee changes has relied on cross-sectional models, with relatively little attention directed towards changes in audit fees. While cross-sectional models have been valuable in evaluating variations across firms, the results of these studies could be unreliable if audit contracts are set on a multi-year basis with under-pricing in year one being offset by over-pricing in subsequent years with audit fees in one year characterised by firm characteristics in a different year. This thesis contributes to the debate surrounding discounts on initial audit engagements and provides new insights into audit pricing in the Australian market.

The remainder of this thesis is organized as follows. Chapter 2 provides empirical evidence of the association between audit quality and auditor tenure which would support auditor rotation being prescribed in Australia. Chapter 3 provides evidence on the association between changes in audit fees over the audit engagement and the professional relations and person-to-person relationships in Australia while Chapter 4 draws the conclusions and reviews the limitations of this thesis.

Chapter Two

The impact of audit tenure on audit quality: The case for auditor rotation.

The objective of this chapter is to provide empirical evidence of any association between auditor tenure and audit quality which would support auditor rotation being prescribed. Based on a sample of Australian publicly listed companies and using three main variations (measures) of audit quality, (absolute IFRS adoption errors, signed IFRS adoption errors and ranked IFRS errors)[1] I find no significant association between IFRS adoption errors and the length of the rotation between audit partner and the CEO of the client firm. As such there is no support for the assumption that person-to-person relationships undermine audit quality. On the contrary, there is a significant negative association between the measures of audit quality and length of audit firm tenure. Accordingly, I find no empirical evidence that longer auditor tenure undermines audit quality and that would support regulation prescribing auditor rotation.

[1] It is explicitly noted that the three categories of IFRS errors identified in this thesis are variation of the one measurement mechanism.

2.1 Introduction

In response to anecdotal evidence that a lack of auditor independence contributed to corporate failures, many countries adopted regulation that prescribed auditor rotation. In Australia that regulation was the Corporate Law Economic Reform Program (*Audit Reform & Corporate Disclosure Act 2004* (CLERP 9, 2004). The objective of this study is to provide empirical evidence of any association between audit quality and auditor tenure which would support auditor rotation being prescribed. Audit quality is assessed in the period when Australian firms were transitioning to International Financial Reporting Standards (IFRS) and is measured as the errors arising in the initial implementation of the new standards. Auditor tenure is measured having regard to both the person-to-person relationships and professional relations that exist between the audit firm and client firm, with these having potentially differing impacts on audit quality. Person-to-person relationships are measured as the period where the same lead audit partner and chief executive officer (CEO) combination worked together in preparing that firm's audited financial statements, and would be considered more relevant to the determination of auditor independence. Evidence that person-to-person relationships adversely impact audit quality would support auditor rotation being prescribed. Professional relations are measured as the duration of the relation between the audit firm and client firm, and this is a control for the development of engagement specific audit expertise.

The motivation for this study is twofold. First, the issue of auditor independence and its implications for audit quality has been the focus of much debate by regulators, professional bodies and academics. These debates have typically focussed on high profile corporate failures in Australia (e.g. HIH Insurance, Allco Finance, Westpoint, Centro, ABC Learning) and internationally (e.g. Enron, WorldCom, Parmalat, Madoff Investments), and typically involve

claims that they arose as a consequence of an aspect of the audit engagement which undermined auditor independence and impaired audit quality.[2] The following comment is typical;

> *"By receiving significant audit and non-audit fees, yet rarely seeming to blow the whistle on problems, auditors' independence and value are cast into serious doubt - exemplified by the collapses of ABC Learning, MFS, Allco, Centro and Bill Express. And the clamour is growing for solutions - such as having the external audit function run by a government authority, similar to the Auditor-General, or that in future, ASIC, rather than a company's board, select and appoint the auditors from an approved panel."*
>
> (Schwab, 2009, p. B1)

In particular, there is the claim that longer auditor tenure reduces audit quality. In response to anecdotal evidence, audit-partner rotation was debated, and is now mandated in Australia.[3] A motivation for this paper is to provide empirical evidence of the association of the impact of auditor tenure on audit quality which would support auditor rotation. Second, the introduction of IFRS in Australia presents a valuable opportunity to exploit regulatory change to identify differences in audit quality. With transition to IFRS, financial reports were required to include IFRS compliant income numbers in the year prior to transition, and re-estimates of these numbers in the subsequent year. As with any change in accounting standards, the complexity of accounting rules leads to errors in accounting measurement (at least temporarily) and audit quality is measured as the differences in these two estimates of income (Loyeung, Matolcsy, Weber & Wells, 2011).[4] This provides an ideal setting in which to examine audit quality as the

[2] For examples, see discussion by Gettler (2010), Treasury (2010), Kruger (2009), Schwab (2009), Washington (2009), Main (2008) and Bartholomeusz (2006).

[3] The *Corporate Law Economic Report Program (Audit Reform & Corporate Disclosure) Act 2004* (CLERP 9, 2004) for the first time required audit partner rotation after five years. Some audit firms in Australia may have been rotating their audit partners on a voluntary basis since 1997.

[4] An inherent assumption of this study is that of technical auditor competence in awareness and understanding of new accounting standards. Accountants and auditors in particular have a professional obligation to maintain up-to-date knowledge regarding accounting changes. The introduction of IFRS in Australia is reflective of an instance where accountants have to learn new accounting standards, with firms emphasizing the learning engagement for IFRS adoption (e.g. popular press and large accounting firms publicized the extensive learning and development

errors produced are less likely to be contaminated by the requirements for the incidence and identification of fraud, regulator intervention or financial report restatement which are common in many studies examining audit and financial reporting quality.

This chapter builds on an extensive literature that considers the association of auditor tenure with audit quality, and attempts to distinguish the arguments supporting shorter (longer) auditor tenure. In the literature there is evidence that shorter auditor tenure enhances auditor independence and improves audit quality. This is attributed to factors such as bringing 'fresh-eyes' to the audit which results in the identification of issues that have been previously overlooked, while simultaneously increasing investor confidence in the auditing profession (Lee, Mande & Son, 2009). It is also consistent with the notion that auditor vigilance declines as auditor tenure increases through over-familiarity with the client (Mautz & Sharaf, 1961). However, there is conflicting evidence that longer auditor tenure enhances audit quality. This is commonly attributed to the existence of a 'learning curve', with Lim & Tan (2010) noting that while longer tenure may be associated with reduced vigilance, this effect may be offset by greater auditor expertise. It is also consistent with comments by Treasury (2010) in relation to mandatory auditor rotation *"...the five-year rotation period was insufficient to build up adequate knowledge of the client"* (p. 17) and *"...organisations that are large in size or are particularly complex or operate in highly regulated and therefore complex industry are those that might command longer periods of audit tenure compared with other organizations"* (p. 17).

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employed in the IFRS adoption process, while the corporate regulator, the Australian Securities and Investment Commission (ASIC) emphasized the need to avoid disruptions to market information flows and took pre-emptive action to encourage accurate disclosure, with ASIC clearly indicating their intention to investigate poor quality reporting (ASIC, 2006; Ernest & Young, 2006; ASIC, 2005)). That is, I assume all practicing auditors have a basic level of competence in understanding IFRS adoption in Australia. Quality differences will therefore be evident in the application of these standards to a client. That is, longer tenure, and increased learning effects associated with longer tenure will assist in a superior application of the new IFRS accounting standards to a client.

This chapter adds to this literature by developing alternate measures of audit tenure which reflect person-to-person relationships and professional relations to distinguish the competing impacts of auditor tenure on audit quality. It is generally maintained that the problems of longer auditor tenure arise as a consequence of closer person-to-person relationships between those involved in the management of the audit (the audit partner and the client senior executives) and evidence of this would support the prescription of auditor rotation. Reflecting this, person-to-person relationships are measured as the period where the same lead audit partner and chief executive officer (CEO) combination have worked together in preparing that firm's audited financial statements.[5] In contrast, audit expertise is built within the audit team as a result of repeated experience in the audit of the client firm. Accordingly, I control for professional relations between the audit firm and the client, which are measured as the tenure of the audit firm as auditor of the client firm.

Based on a sample of 151 firms listed on the Australian S&P/ASX Top 500, evidence is provided of how auditor tenure is associated with audit and financial report quality. No evidence is found of a significant association between IFRS adoption errors and person-to-person relationships between the audit partner and the CEO of the client firm. This would suggest that auditors do not have person-to-person relationships which undermine audit quality. In contrast, a significant negative association is found between different categories of IFRS adoption errors (i.e. absolute IFRS errors, signed IFRS errors and rank signed IFRS errors) and professional relations between the audit firm and the client. Audit and financial report quality improves as audit firm tenure increases. These results are robust to a range of sensitivity tests.

[5] I have focused on the CEO as they are most likely to be involved in decisions on auditor appointment. Recognising that the CFO may have a more direct involvement in the financial reporting process this is also considered as a sensitivity test.

This chapter makes a number of contributions to the literature and practice. First, it extends the literature considering the relation between audit tenure and audit quality. It uses a new measure of financial report quality, IFRS adoption errors, which is not subject to the same limitations as other measures of audit quality.[6] It also considers different aspects of audit relations (i.e., person-to-person relationships and professional relations). Second, there is no evidence that person-to-person relationships between audit partners and senior executives reduce audit quality, which is presumed in the regulation prescribing auditor rotation. While it might be expected that increased familiarity between the audit partner and senior executives might undermine audit quality, there are a range of controls to address this including engagement reviews at the firm, profession and regulator level. The results are consistent with these measures being effective. Third, it provides empirical evidence that as professional relations increase in duration there is an increase in audit quality. This is consistent with the prior literature which considers the relation between various measures of audit firm tenure and audit and financial report quality (e.g. Ghosh & Moon, 2005; Johnson, Khurana & Reynolds, 2002; Geiger & Raghunandan, 2002). Accordingly, these results question the appropriateness of regulation which prescribes auditor rotation, especially for complex audit engagements.

The remainder of this chapter is organised as follows. Section 2.2 provides a review of relevant literature and the hypothesis development. Section 2.3 describes the research design and explanatory variables. Data collection and the sample description are provided in section 2.4 while the results and relevant sensitivity analysis are described in section 2.5. Section 2.6 provides summary conclusions, research limitations and future research potential.

[6] For example, the transition to IFRS in Australia provides an opportunity to exploit a regulatory change to assess audit quality which have not previously been available to researchers who have been forced to rely upon more mechanical and statistical techniques to infer accounting quality.

2.2 Literature review and hypothesis development

2.2.1 The role of auditing in the financial reporting process

Financial reports are an important tool prepared and used by managers of the firm to communicate financial information to investors and stakeholders, and reducing the level of information asymmetry that exists between owners and managers (Antle & Nalebuff, 1991). Subjecting financial statements to external verification and assurance is a mechanism through which managers can add credibility to the reports, and enhance the reliance placed upon them (Watts & Zimmerman, 1986; Jensen & Meckling, 1976). Thus, financial statements should be read as a "joint statement" from the auditor and manager (Antle & Nalebuff, 1991, p. 31), and the effectiveness of the communication will be impacted by the quality of the audit.

Auditor reporting behaviour (also known as auditor independence) and auditor competence (also known as auditor expertise) have been identified as instrumental in determining audit quality (Johnson et al., 2002), and it was concerns about the potential impact of auditor tenure on audit independence which led to regulation in many countries prescribing auditor rotation. In Australia auditor rotation has been required since 2006 under section 324DA(1) and (2) of the *Corporations Act 2001* which states that an individual cannot play a significant role in the audit of a listed entity for more than five out of seven successive financial years (and APES 110 290.154 *Code of Ethics for Professional Accountants*). However, the empirical evidence on the relation between auditor tenure and audit quality is equivocal, with this likely reflecting complex and conflicting explanations for the relation between auditor tenure and auditor quality.

2.2.2 The auditor independence hypothesis

The auditor independence hypothesis maintains that auditor independence, and therefore audit quality, becomes impaired as the association between the auditor and the client lengthens. There are three main arguments for why increased auditor tenure adversely impacts auditor quality.[7]

First, as the auditor-client relationship lengthens the auditor may develop a 'learned confidence' or become too familiar with the client's operations. This could result in the auditor not being as creative or as vigilant with audit testing procedures, and ultimately lead to auditor entrenchment and loss of audit quality through various audit failures (Lee et al., 2009), such as financial report assertions not being tested, the auditor anticipating results, failing to recognise or observe anomalies, the employment of less rigorous audit procedures, or the use of static audit programs.[8] Therefore, it is argued that auditor rotation brings "fresh eyes" to an engagement while simultaneously increasing investor confidence in the auditing profession (Lee et al., 2009; Seidman, 2001).

Second, longer relationships between an auditor and client could lead to the development of person-to-person relationships where a bond, loyalty and/or trust can be developed.[9] These person-to-person relationships, irrespective of whether they are developed intentionally or unintentionally, can impact an auditor's objectivity and therefore independence (Carey &

[7] The primary concern of this chapter is in addressing the 'person-to-person (as opposed to the professional) relationship which may be created between the engagement partner and members of the executive team (CEO or CFO). Traditionally, prior literature examining the person-to-person relationship between the auditor and the client treats the client as static or homogenous.

[8] For a more extensive discussion refer to Azizkhani, Monroe & Shailer, 2010; Myers, Myers & Omer, 2003; Johnson et al., 2002; Shockley, 1982; and Hoyle, 1978.

[9] The 'person-to-person relationship' identified in prior literature differs to that as defined in this chapter. This study explicitly defines the 'person-to-person relationship' as the period where the same lead audit partner and the CEO combination have worked together in preparing that firm's audited financial statements; whereas prior literature defines it more generally as "personal closeness" between an audit firm and client, without specificity to any particular executive (Arel et al., 2005).

Simnett, 2006; Arel, Brody & Pany, 2005; Geiger & Raghunandan, 2002). As the length of an engagement increases, the auditor is more likely to accept client pressure or side with managers on important reporting decisions (e.g., the choice and application of accounting policies). This could create a situation where auditors support more "aggressive accounting policy choices" that push boundaries (Azizkhani et al., 2010; Myers et al., 2003; Farmer, Rittenberg & Trompeter, 1987). Ultimately, the development of close person-to-person relationships between the auditor and client may result in a failure to detect and report material fraud and or financial misstatement.

Third, as auditor tenure increases, economic considerations may increasingly impact decisions relating to the conduct of the audit. This would include decisions aimed at maintaining and profiting from the audit such as keeping clients long enough to recoup initial engagement start-up costs (e.g., Sankaraguruswamy & Whisenant, 2009; Ghosh & Lustgaren, 2006; Turpen, 1990) and recovering the costs of discounting on initial audit engagements (e.g., Ghosh & Lustgarten, 2006; Francis, 2004; Craswell & Franics, 1999; Simon & Francis, 1988; DeAngelo, 1981a). These considerations may impact the auditor's judgement and undermine independence (Azizkhani et al., 2010; Geiger & Raghunandan, 2002; DeAngelo, 1981a).

Distinguishing these arguments is difficult as they all imply a negative relation between auditor tenure and audit quality.

2.2.3 Auditor expertise hypothesis

In contrast, the auditor expertise hypothesis maintains that audit quality increases with auditor tenure as it allows client-specific knowledge and expertise to develop and increase. This hypothesis is based on the degree of information asymmetry between the auditor and the client,

which reduces over time as auditors acquire client specific knowledge (Azizkhani et al., 2010). Effective audits require a thorough understanding of the client's business and client specific knowledge, including information concerning a firm's internal control structure, operations and accounting systems, procedures and processes (e.g., Dao, Mishra & Raghunandan, 2008; Johnson et al., 2002). This knowledge, expertise and understanding is developed over repeated audits and it creates significant learning curves that last a year or more (Dao et al., 2008; Myers et al., 2003; Knapp, 1991). A lack of this knowledge in the early years of an audit engagement may result in a lower quality audit (Johnson et al., 2002).[10]

2.2.4 Distinguishing the impact of auditor tenure on audit quality.

An issue in the extant literature which has likely contributed to the equivocal findings is diversity in the operationalization of auditor tenure. Much of the early literature considered auditor tenure as the duration of the audit firm and client relation, and this was largely a consequence of data availability. These studies are more likely to find a positive relation between audit tenure and audit or financial report quality.

Johnson et al (2002) is typical of the studies considering the association between audit firm–client tenure and financial reporting quality. With financial reporting quality measured as unexpected accruals, they find some evidence of lower financial reporting quality with short audit firm tenure (two to three years). Similarly, Myers et al (2003) who proxy for audit quality with the absolute value of unexpected accruals finds that as audit firm tenure increases there are greater constraints on extreme accounting decisions by management.

[10] Johnson et al. (2002) also note that an initial lack of client specific knowledge on an engagement may not be associated with lower audit quality if it is possible to overcome the lack of knowledge by employing additional audit effort.

More recently, studies have considered the relations between financial reporting quality, audit firm tenure and other factors considered relevant to determining audit quality such as auditor independence. For example, Gul, Jaggi and Krishnan (2007) find financial reporting quality, measured as unexpected accruals, is positively associated with shorter audit firm tenure (three years or less) and negatively with the payment of non-audit fees. Stanley and DeZoort (2007) find that for shorter audit tenure, higher audit fees are associated with improved audit quality and suggest that the limitations of client firm knowledge might be addressed by additional audit effort. Consistent with this, Lim and Tan (2010) find that for firms with longer auditor tenure, audits by industry specialists are associated with higher financial reporting quality. Again this is consistent with greater audit firm expertise enhancing financial reporting quality. However, there is also evidence that the impact of tenure on financial reporting quality is moderated by auditor fee dependence.

This contrasts with studies where more information about audit engagement partners is available, and when auditor tenure is measured having regard to specific audit partners, rather than audit firms. This change in definition may be significant if specific audit expertise is accumulated by the audit team rather than the audit partner, and audit partner tenure which recognises person-to-person relationships are more relevant to the determination of audit independence. This would lead to equivocal results.

In this regard, it is notable that Chi, Huang, Liao and Xie (2005) find a positive association between audit-partner tenure and absolute, signed and working capital accruals in Taiwan. Similarly, Hamilton, Ruddock, Stokes and Taylor (2006) examined audit partner rotation in Australia and found that partner changes are associated with lower signed unexpected accruals. Carey and Simnet (2006) find a deterioration in audit quality with longer audit partner

tenure, and suggest this is a result of independence concerns associated with longer audit partner tenure. However, Manry, Mock and Turner (2008) provide evidence that audit quality is improved for small clients with partner tenure of greater than seven years.

Doubtless, a confounding factor in this literature has been the measurement of audit tenure, and the lack of consideration of how the different measures reflect different aspects of the auditor–client relation. Auditor tenure has traditionally been measured as the duration of the audit firm–client relation, and if specific audit experience is developed by the audit team this would likely be relevant for evaluating the auditor expertise hypothesis. It might also be labelled the 'professional relation' that exists between the audit firm and the client.[11]

The professional relation should be distinguished from the 'person-to-person relationship' which exists between the audit partner and the senior executives of the client firm. This dichotomy extends the prior literature as it recognises that relationships are established between individual audit engagement partners and specific senior management; and this would be more relevant to the evaluation of auditor independence. It is also consistent with anecdotal evidence that auditor independence could be 'compromised' by a close association between the engagement partner and senior executives. For example,

> *"...the independence of auditors has been called into question given they are being paid by the very people they are supposed to be monitoring .... [and in many cases] are on friendly terms with its executive team...."*
>
> (Schwab, 2009, p. 1)

The 'person-to-person relationship' would be relevant for evaluating whether declining auditor independence necessitates audit partner rotation.

[11] While it may be the audit firm that finds the errors, ultimately it is the audit partner who determines if they are material. Furthermore, it is the audit partner who is responsible for changes in the audit strategy.

The above discussion highlights the importance of auditor independence and expertise within the auditing literature, and the need to distinguish between them in evaluating impacts on audit quality. Hence, in this chapter, the impact of the person-to-person relationship on audit quality is evaluated, and a control for professional relation is included.[12]

*H_1: Audit quality is a **decreasing** function of longer person-to-person relationships between the audit partner and the client firm senior management.*

Evidence consistent with this hypothesis would be supportive of regulation prescribing audit partner rotation.[13]

2.3 Research Design

The research design in this chapter evaluates the association of audit quality with person-to-person relationships between the audit partner and the client senior management (and controls) with the following model:

$$AQ = \alpha_0 + \alpha_1 Partner/CEO\_Tenure_{it} + \alpha_2 Audit\_Firm\_Tenure_{it} + \alpha_3 Controls_{it} + \varepsilon$$

Where *AQ* is a measure of audit quality, and *Partner/CEO_Tenure* and *Audit_Firm_Tenure* are measures of the different relations between the auditor and the client.

[12] This hypothesis recognizes that the professional relation between the audit firm and the client firm will likely impact the person-to-person relationship, and therefore, the variable which accounts for the professional relation is included as a control.

[13] This chapter is focused on examining the person-to-person relationship (*Partner/CEO_Tenure*) between the lead audit partner and the chief executive officer, while the professional relation or firm tenure (*Firm_Tenure*) is treated as a control variable. Thus, H_1 focuses on the person-to-person relationship aspect.

2.3.1 Audit Quality

Extant literature shows considerable diversity in the measures used for audit quality. These include measures which focus on the audit client such as unexpected accruals (Lim & Tan, 2010; Myers et al., 2003; Johnson et al., 2002); Securities and Exchange Commission (SEC) enforcement actions and financial statement restatements (Stanley & DeZoort, 2007; Myers, Myers, Palmrose & Scholz, 2003); fraud occurrence (Carcello & Nagy, 2004); litigation risk (Stice, 1991); and going concern opinions (Knechel & Vanstraelen, 2007; Geiger & Raghunandan, 2002). Other measures focus on the auditor and in particular auditor expertise is commonly proxied as Big N auditors (Behn, Choi & Kang, 2008; Simunic, 1980) and auditor specialisation (Stein & Cadman, 2005; Ferguson & Stokes, 2002; Palmrose, 1986).

However, there are limitations with these measures. Measures of quality using attributes of earnings are impacted by the underlying economic characteristics of the firm (Imhoff Jr., 2003; Imhoff Jr., 1992). Isolating the separate effects of economic characteristics and audit quality on the attributes of earnings is fraught with difficulties. Other measures require the identification of financial reporting irregularity, or may lack precision with quality simply being labelled high or low. To address this problem I utilise the setting of IFRS transition, and measure audit quality as errors identified by firms in their adoption of IFRS.[14]

In July 2002, the Financial Reporting Council (FRC) announced its formal support for the adoption of the Australian equivalents to International Financial Reporting Standards (referred to as IFRS). The Australian Accounting Standards Board (AASB) was responsible for the (re)issuance of the international standards in Australia and transition was required for years beginning on or after 1 January 2005 (FRC, 2002). The adoption of IFRS required firms to

[14] I gratefully acknowledge and thank the data provided by Loyeung et al, 2011, and the hard work of Dr. Anna Loyeung in hand collecting this data

change their method of accounting for particular items, such as financial instruments, income taxes, intangible assets and goodwill and there were material impacts for many firms (Ernst & Young, 2006; Waring, 2005). To mitigate uncertainty created by the adoption of international standards AASB 1047 *Disclosing the Impact of Adopting Australian Equivalents to International Financial Reporting Standards* was issued, requiring material disclosures in the period leading up to adoption. In particular, in the year prior to adoption, firms were required to include in financial reports an estimate of earnings under IFRS, and provide line-by-line disclosures of differences from reported Australian GAAP earnings. In the financial reports for the subsequent year (the first year applying IFRS), firms were required to include prior year information calculated on the basis of IFRS, and a line-by-line disclosure of differences from reported Australian GAAP information was again required (AASB 1047; AASB 101; Waring 2005). Thus, there were two estimates of earnings for the same period prepared one year apart, and disclosures of how these estimates compared to reported Australian GAAP earnings. These differences reflect problems in the determination of appropriate accounting practices and their application, and are labelled 'IFRS adoption errors'.

Doubtless contributing to these differences was the quantity of regulation and guidelines issued by regulators and industry experts to handle the transition to and adoption of IFRS. Furthermore, in Australia there was no opportunity for early adoption essentially creating a situation where senior executives and auditors did not have the opportunity to learn the new IFRS standards gradually. Errors arose in the financial reporting process because of the uncertainty as to the meaning and application of accounting regulation (IFRS) reflecting audit quality. This is consistent with statements by the Australian Securities and Investment Commission (ASIC) warning firms to make every effort to ensure disclosures were as accurate

as possible, and suggesting it would be investigating 'poor quality reporting' (ASIC, 2005), and anecdotal evidence that audit firms were concerned with the magnitude of these errors, and they were subject to review. Furthermore, there is empirical evidence of these errors having economic consequences which is consistent with these being a measure of audit quality (Loyeung et al, 2011). Critically this provides a continuous measure of quality for all firms.

The calculation of IFRS errors begins with a comparison of the line-by-line reconciliations of earnings under IFRS to Australian GAAP earnings in the period prior to transition and in the first year of adoption. Differences between the reconciling items across the disclosures are identified and the sum of the absolute differences scaled by total assets is calculated (*ABS-Error*).[15] This variation of the IFRS adoption errors measure takes into account auditor vigilance in reporting IFRS errors and ignores the fact that there would likely be greater concern with overstatements than understatements (Ilter, 2012). Therefore, I identify the differences between the reconciling items across the disclosures and use these differences scaled by total assets to derive the second variation of the IFRS adoption error (*SIGN-Error*). Finally, to mitigate the effects of the distribution of errors (outliers and skewness in the distribution), an IFRS error variation of rank IFRS errors is also considered (*RANK-Error*).[16]

2.3.2 Auditor - client relations

The primary focus of this chapter is how auditor independence is impaired by the person-to-person relationships between audit-partners and the senior management of the client firm. Attention is focussed in the first instance on the duration of the relationship between the audit

[15] It should be noted that the way in which total assets are affected themselves should be considered, but that overall this is immaterial factor and beyond the scope of consideration for this chapter.

[16] Similar results are obtained if continuous and winsorized at the 1st and 99th percentile are employed (*Appendix 2G*)

partner and the CEO, as the CEO was most likely to be involved in the selection of the auditor, and to benefit most from the financial reports being subjected to less critical scrutiny. The person-to-person relationship (*Partner/CEO Tenure)* between the CEO and lead audit engagement partner is initially defined as the number of years (up to a maximum of 8) that the same audit partner and the same CEO have been representatives of the audit firm and client at 2006.[17]

'Powerful' CEOs have previously been identified within the corporate governance literature as those CEOs having the greatest influence over the board of director's and a company's decision making (Bebchuck, Cremers & Peyer, 2011). This likely extends to control of the financial reporting process. I refine the person-to-person relationship variable to examine powerful person-to-person relationships (*Partner/CEO Tenure*[*]*)* using an approach developed by Bebchuk et al. (2011). Bebchuck et al., (2011) argue that the CEO's pay slice (*CPS*) captures the relative significance of the CEO in terms of ability, contribution or power. As such *CPS* provides a useful proxy for the relative centrality, or power, of the CEO in the senior management team. *CPS* is calculated for each firm as the CEO's total base rate compensation as a fraction of the combined total base rate compensation of the top five executives (including the CEO). For CEO's where the *CPS* is less than 30%, *Partner/CEO Tenure*[*]*,* assumes the value of 0, otherwise it has the same value as *Partner/CEO Tenure.* This limits the impact of person-to-person relationships on audit quality to those situations where there is a powerful CEO.[18]

The professional relation between the audit firm and the client firm follows the approach adopted in prior studies that consider audit firm tenure (e.g. Lim & Tan, 2010; Gunny, Krishnan

[17] Recognising that the appropriate focal point may not be the CEO, as a sensitivity attention is also directed to the relationship between the audit partner and the CFO. The CFO may be more closely associated with the day to day financial reporting decisions.

[18] As a sensitivity, alternative cut off levels for the determination of *Partner/CEO Tenure*[*] are considered.

& Zhang, 2010; Ghosh & Moon, 2005; Myers et al., 2003). Accordingly, professional relation (*Audit Firm Tenure*) is defined as the cumulative number of years the audit firm has been employed by the client-firm to perform the audit of the financial reports at 2006, with a maximum tenure of 8 years.

2.3.3 Controls

Several control variables are included in the regression model due to the likelihood of there being other determinants of IFRS adoption errors. These primarily relate to the complexity of the financial reports and decisions made in the preparation of the financial reports. Accordingly, consistent with Loyeung et al (2011), the following control variables are included:

Market Cap	=	Market capitalisation for the firm
LEV	=	Leverage, measured as the ratio of the firm's total long-term debt to market value of equity
ROA	=	Return on assets, measured as the ratio of the firm's earnings divided by total assets (also consistent with Johnson et al., 2002)
LOSS	=	To control for whether the firm experienced a loss, an indicator variable that is set to equal one in the fiscal year 2006 if net income is negative
Audit Big N	=	Indicator variable set to equal one if the firm was audited by a member of the Big 4 during the fiscal year 2006 audit, zero otherwise.

2.4 Data collection and sample description

Sample firms in this chapter correspond to those in Loyeung et al., (2011) which are chosen from the ASX/S&P Top 500 Australian firms in 2006. Firms in the financial sector (71) are excluded as these firms are subject to additional regulatory reporting requirements and supervision (e.g. compliance with AASB 132 and 139). In order to calculate CEO, audit firm and audit partner tenure, sample firms are required to be listed continuously between 1999 and 2006

and availability of annual reports. Firms with missing annual reports or data are deleted. Firms are deleted if they report in a foreign currency (or their audit report was signed in a country other than Australia) or if they changed financial year-end. This results in a final sample of 151 firms.

Table 2.1, Panel A summarises the sample selection process and Panel B provides information on GICS industry sector grouping. The *Materials* industry has the most firms (41) in the sample, while the fewest number of firms are in the *Utilities* industry (1). This is reflective of the market and I do not expect this industry distribution to introduce any bias to our results. Panel C summarises the year-end balance dates for firms within our sample and shows that 117 firms (77.5%) in our sample have a June 30 year-end, which is again reflective of the Australian reporting environment.

Table 2.2 provides descriptive statistics on the sources of IFRS adoption errors. There are significant differences in the cause of IFRS adoption errors (*ABS-Errors*) with sixteen (16) specific standards identified where three or more firms reported adoption errors. The most frequent errors arose in determining the impact of *AASB 112 Income Taxes* (90 errors). I attribute these errors to the nature of transitioning, in that if any element of the income statement was impacted by an adoption error, there is typically also a tax effect associated with the error. The second most frequent transition error category was *AASB 2 Share Based Payments* (65 errors). Conditional on having an IFRS error, the largest mean absolute value for errors (*ABS-Errors*) related to *AASB 136 Impairment* which represented a substantial change from Australian GAAP.

Table 2.2, Panel B displays the descriptive statistics for the pooled sample of independent and control variables. The mean (median) audit firm tenure (*Audit_Firm_Tenure*) is 6.583 (8.000) years, while the mean (median) CEO-audit partner association (*Partner/CEO_Tenure*) is 2.709 (2.000) years. For more powerful CEO-audit partner relationships (*Partner/CEO_Tenure**)

the mean (median) duration is 1.775 (1.000) years. The values for the last two variables are influenced by the significant number of zero observations.

Pearson and *Spearman* correlations are reported in Table 2.3. By construction there is a high correlation between *Audit_Firm_Tenure* and *Partner/CEO_Tenure* (Spearman Corr=0.215, Pearson Corr=0.268). There is also a high correlation between *Partner/CEO_Tenure* and *Partner/CEO_Tenure** (Spearman Corr=0.443, Pearson Corr=0.611). However, the correlation between *Audit_Firm_Tenure* and *Partner/CEO_Tenure** is much weaker (Spearman Corr=-0.008, Pearson Corr=0.092).

2.5 Results

2.5.1 Test results

The initial tests of the relation between audit quality and audit tenure are presented in Table 2.4. In Panel A audit quality is measured as the sum of absolute IFRS errors (*ABS-Errors*) and for the model without controls it is notable that while there is a negative and significant relation with *Audit_Firm_Tenure* (α_2=-0.005, *t-stat*=-1.611, p=0.055), the relation with *Partner/CEO_Tenure* is not significant (α_1=0.000, *t-stat*=0.112, p=0.456). However, caution must be exercised in interpreting this result as the model has poor explanatory power (adjusted r^2=0.005). For the model with controls there is an increase in model explanatory power (adjusted r^2=0.037), but the relation between *ABS-Errors* and *Partner/CEO_Tenure* is still not significant (α_1=0.002, *t-stat*=0.454, p=0.325). Not surprisingly, the greatest determinant of *ABS-Errors* was the firm being loss making (α_6=0.064, *t-stat*=2.091, p=0.019). Accordingly, in Panel A there is no support for H_1 and longer person-to-person relationships between the audit partner and the client firm CEO reducing audit quality.

In Panel B a refined measure of the person-to-person relationship between the audit partner and the CEO is considered which emphasises clients where the CEO is more powerful (*Partner/CEO_Tenure**). Again there is no evidence of this being associated with reduced audit quality, either for the model without controls (α_1=-0.060, *t-stat*=-0.734, p=0.232) or the model with controls (α_1=-0.001, *t-stat*=-0.245, p=0.404). In contrast there is some evidence of a longer firm tenure (*Audit_Firm_Tenure*) being associated with increased audit quality in the model without controls (α_2=-0.128, *t-stat*=-1.570, p=0.060). In Panel B there is still no support for H_1 and longer person-to-person relationships between the audit partner and the client firm CEO reducing audit quality.

Panel C reports a further refinement of the primary sample. Firms are ranked on the basis of *ABS-Error* and the sample is restricted to the lower and upper thirds of the primary sample. For the model without controls it is notable that while there is a negative and significant relation with *Audit_Firm_Tenure* (α_2=-0.007, *t-stat*=-1.427, p=0.079), the relation with *Partner/CEO_Tenure* is not significant (α_1=0.000, *t-stat*=-0.002, p=0.333). However, caution should be exercised in interpreting this result as the model has poor explanatory power (adjusted r^2=0.002). For the model with controls there is an increase in model explanatory power (adjusted r^2=0.040), but the relation between *ABS-Errors* and *Partner/CEO_Tenure* is still not significant (α_1=0.001, *t-stat*=0.177, p=0.430). Not surprisingly, the greatest determinant of *ABS-Errors* was again the firm being loss making (α_6=0.081, *t-stat*=1.738, p=0.043) and use of a Big N auditor (α_7=0.050 *t-stat*=1.408, p=0.081). Accordingly, in Panel C there is no support for H_1 and longer person-to-person relationships between the audit partner and the client firm CEO reducing audit quality.

Panel D examines the association between audit quality and the person-to-person relationship between the audit partner and the CEO, where the CEO is more powerful and utilises extreme observations (thirds) of absolute IFRS errors. In the model without controls it is notable that there is a negative and significant relation with *Audit_Firm_Tenure* (α_2=-0.007, *t-stat*=-1.390, p=0.084) at the 10% level. The relation with *Partner/CEO_Tenure** is not significant (α_1=-0.005, *t-stat*=-0.894, p=0.187). For the model with controls there is an increase in model explanatory power (adjusted r^2=0.041), but the relation between *ABS-Errors* and *Partner/CEO_Tenure** is not significant (α_1=-0.002, *t-stat*=-0.335, p=0.370). Once again the greatest determinants of *ABS-Errors* was the firm being loss making (α_6=0.078, *t-stat*=1.668, p=0.050) and use of a Big N auditors (α_7=0.049, *t-stat*=1.384, p=0.085). Accordingly there is no support for H_1, longer person-to-person relationships between the audit partner and the client firm CEO do not appear to reduce audit quality.

In summary, focussing on absolute IFRS adoption errors as a proxy for audit quality, there is no support for H_1 and longer person-to-person relationships between the audit partner and the client firm CEO reducing audit quality. In contrast there is some evidence of a longer professional relation increasing audit quality. The tests in Table 2.4 emphasised errors without consideration of sign. Recognising that the impact of reduced auditor independence might be more income increasing errors, Table 2.5 focuses on signed IFRS errors.

Table 2.5 reports the results for association between professional relations and person-to-person relationships and signed IFRS errors scaled by average total assets (*SIGN-Error*). Panel A shows the results for person-to-person relationship model, in the model without controls it is notable that there is a positive and significant relation with *Audit_Firm_Tenure* (α_2=0.005, *t-stat*=2.019, p=0.023), while there is a positive but not significant relation with

Partner/CEO_Tenure. For the model with controls, there is a decrease in model explanatory power (adjusted r^2=0.002), and the model is no longer significant (*F-stat*=1.053, p=0.397). The *Audit_Firm_Tenure* variable of interest remains significant at the 5% level (α_2=0.005 *t-stat*=1.904, p=0.030). However, the *person-to-person relationships (Partner/CEO_Tenure)* variable is not significant and is positive (α_1=0.001, *t-stat*=0.369, p=0.357).

In Panel B, a refined measure of person-to-person relationship between the audit partner and the CEO is considered which emphasises clients where the CEO is more powerful (*Partner/CEO_Tenure**). In the model without controls, there is a significant positive relation between *SIGN-Error* and *Audit_Firm_Tenure* (α_2=0.005, *t-stat*=2.161, p=0.016), but the relation with *Partner/CEO_Tenure** is negative and not significant (α_1=0.000, *t-stat*=-0.160, p=0.436). For the model with controls there is a decrease in model explanatory power (adjusted r^2=0.002) and the model is no longer significant (*F-stat*=1.036, p=0.409). The relation between *SIGN-Errors* and *Audit_Firm_Tenure* remains positive and significant at the 5% level (α_2=0.005, *t-stat*=2.041, p=0.022), while the relation with *Partner/CEO_Tenure**, reflecting powerful CEOs associations with an audit partner, remains negative and not significant (α_1=0.000, *t-stat*=-0.146, p=0.442). Accordingly, in Panel B there is no support for H_1 and longer person-to-person relationships between the audit partner and the client firm CEO reducing audit quality.

Panel C reports the results of the impact of person-to-person relationships *(Partner/CEO Tenure)* on audit quality using the *SIGN-Error* IFRS error variation, with a subsample of extreme observations. In the model without controls, it is notable that there is a positive and significant relation at the 5% level (α_2=0.007, *t-stat*=1.844, p=0.034) with *Audit_Firm_Tenure*. The relation with *Partner/CEO_Tenure* is positive but not significant (α_1=0.001, *t-stat*=0.233, p=0.409). For the model with controls, there is a no model explanatory power (adjusted

r^2=0.000) and no significance (*F-Stat*=1.003, p=0.434). The relation between *SIGN-Errors* and *Partner/CEO_Tenure* is not significant (α_1=0.001, *t-stat*=0.151, p=0.440). However the association with *Audit_Firm_Tenure* remains positive and significant at the 5% level (α_2=0.007, *t-stat*=1.799, p=0.038).

Panel D examines the results of the impact of *powerful person-to-person relationships* (*Partner/CEO_Tenure**) on audit quality using the *SIGN-Error* variation. For the model without controls, it is notable that while there is a positive and significant relation with *Audit_Firm_Tenure* (α_2=0.007 *t-stat*=2.012, p=0.024) at the 5% level, the relation with *Partner/CEO_Tenure** is negative and not significant (α_1=-0.001, *t-stat*=-0.341, p=0.442). However, caution must be exercised in interpreting this result as the model has poor explanatory power (adjusted r^2=0.020) and is not significant (*F-stat*=2.024, p=0.138). For the model with controls, there is a decrease in model explanatory power (adjusted r^2=0.002, *F-stat*=1.022, p=0.421), but the relation between *SIGN-Error* and *Partner/CEO_Tenure** remains negative and not significant (α_1= -0.002, *t-stat*=-0.382, p=0.352). However, *Audit_Firm_Tenure* is positive and significant at the 5% level (α_2=0.007 *t-stat*=1.915, p=0.029) and firm *leverage* appears to be a driver of this model (α_4=0.020, *t-stat*=1.384, p=0.085). Accordingly, in Panel D there is no support for H_1 and longer person-to-person relationships between the audit partner and the client firm CEO reducing audit quality.

Table 2.6 reports the results for association between professional relations and person-to-person relationships using the rank IFRS errors scaled by average total assets (*RANK-Error*) variation measure. Panel A reports the model with and without control variables. In the model without control variables it is notable that there is a positive and significant relation between *RANK-Error* and *Audit_Firm_Tenure* (α_2=3.244, *t-stat*=2.136, p=0.017), however the relation

with *Partner/CEO_Tenure* is not significant (α_1=0.146, *t-stat*=0.103, p=0.918). For the model with controls there is a decrease in model explanatory power (adjusted r^2=0.008) and the model is no longer statistically significant (*F-stat*=1.165, p=0.327). But the relation between *RANK-Error* and *Audit_Firm_Tenure* remains positive and significant (α_2=3.583, *t-stat*=2.236, p=0.014). Not surprisingly the *Partner/CEO_Tenure* relation remains positive and not significant (α_1=0.414, *t-stat*=0.237, p=0.407). Accordingly, in Panel A there is no support for H_1 and longer person-to-person relationships between the audit partner and the client firm-CEO reducing audit quality.

Panel B of Table 2.6 reports the results for the *RANK-Error* variation and the person-to-person *power relationship* measure (*Partner/CEO_Tenure**). In the model without controls, the relation with *Audit_Firm_Tenure* is positive and significant at the 5% level (α_2=3.356, *t-stat*=2.294, p=0.012), while the relation with *Partner/CEO_Tenure** is negative and not significant (α_1=-1.065, *t-stat*=-0.600, p=0.275). For the model with controls, there is a decrease in model explanatory power (adjusted r^2=0.010) and the model is no longer significant (*F-stat*=1.206, p=0.303). However, the relation between *RANK-Errors* and *Audit_Firm_Tenure* remains positive and significant (α_2=3.703, *t-stat*=2.375, p=0.010). The *Market Cap* control variable also shows statistical significance (α_3=0.001, *t-stat* = 1.481, *p* = 0.071) at the 10% level and is a driver of this model. Still, in Panel B there is no support for H_1 and longer person-to-person relationships between the audit partner and the client firm CEO reducing audit quality.

Panel C reports the results for the *person-to-person relationship* using the *RANK-Error* variation, utilising a subsample of extreme observations. In the model without controls it is notable that while there is a positive and significant relation with *Audit_Firm_Tenure* (α_2=0=4.912 *t-stat*=1.919, p=0.029) at the 5% level, the relation with *Partner/CEO_Tenure* is

negative and not significant (α_1=-0.104, *t-stat*=-0.036, p=0.486). Once again caution must be exercised in interpreting this result as the model has poor explanatory power (adjusted r^2=0.019) and the model is not significant (*F-stat*=2.001, p=0.141). For the model with controls there is a slight decrease in model explanatory power (adjusted r^2=0.006), and the relation between *RANK-Errors* and *Partner/CEO_Tenure* is still not significant (α_1=-0.088, *t-stat*=-0.029, p=0.489). However, *Audit_Firm_Tenure* remains positive and significant (α_2=4.660, *t-stat*=2.049, p=0.022) at the 5% level.

Panel D examines results for *powerful CEOs* using the *RANK-Error* variation. For the model without controls, it is notable that while there is a positive and significant relation with *Audit_Firm_Tenure* (α_2=4.272 *t-stat*=2.050, p=0.022) at the 5% level, the relation with *Partner/CEO_Tenure** is negative but not significant (α_1=-1.895, *t-stat*=-0.699, p=0.243). However, caution must be exercised in interpreting this result as the model has poor explanatory power (adjusted r^2=0.024). For the model with controls, there is a decrease in model explanatory power (adjusted r^2=0.012), but the relation between SIGN-Error and *Partner/CEO_Tenure** is still negative and not significant (α_1=-2.218, *t-stat*=-0.777, p=0.220). The *Audit_Firm_Tenure* remains significant at the 5% level (α_2=4.698 *t-stat*=2.144, p=0.018) and drives model results. Thus, in Panel D there is no support for H_1. Longer person-to-person relationships between the audit partner and the client firm CEO no not appear to reduce audit quality.

2.5.2 Sensitivity Tests

A number of sensitivity tests are conducted including alternative measures of audit quality, governance partitioning, different financial year ends, and an alternative senior executives as part of the person-to-person relationship with the auditor.

IFRS Variations (Appendix 2A)

IFRS adoption errors have been relied upon as the main measure of audit quality within this thesis. While the main results have been conducted based on absolute errors (*ABS-Error*), signed (*SIGN-Error*), and the rank of the signed (*RANK-Error*) IFRS errors, it is important to consider alternatives and I do this using the rank absolute value of IFRS errors (*RANKABS-Error*). I replicate the main reported tests in appendix A with results holding to this sensitivity test. Of particular note, in Table 2A.7 Panel A, in the model without controls it is notable that while there is a negative and significant relation with *Audit_Firm_Tenure* (α_2=-2.912, *t-stat*=-1.464, p=0.073), the relation with *Partner/CEO_Tenure* is positive and not significant (α_1=2.923, *t-stat*=1.142, p=0.128). Interestingly for the model with controls, the relation between *RANKABS-Error* and *Partner/CEO_Tenure* is positive and becomes significant at the 10% level (α_1=3.585, *t-stat*=1.370, p=0.087), while the *Audit_Firm_Tenure* variable is not significant (α_2=-2.074, *t-stat*=-0.987, p=0.163). Caution should be exercised in interpreting the result because the model has no explanatory power (adjusted r^2=-0.005).

Audit Committee Corporate Governance (Appendix 2B)

Independent audit committees are identified as a fundamental component of good corporate governance structures. The role of the audit committee is to oversee and monitor the company's audit processes while overseeing the integrity of the financial reporting process (Burke & Guy, 2002). Therefore, as a sensitivity a control variable for audit committee governance is incorporated. Following Matolcsy, Tyler and Wells (2011), a dummy variable is included which captures audit committee strength (*AC_Gov_Dummy*). This variable is calculated as 0 if the firm has established an; all non-executive and majority independent, audit committee,

and 1 otherwise. Results are for these tests are reported in Appendix 2B and overall, results are consistent and robust to this sensitivity with the *AC_Gov_Dummy* variable adding little explanatory power to the model as expected.

CFO Alternative (Appendix 2C)

Next, consideration is given to the effects of a Chief Financial Officer (CFO) – audit partner association. While the primary focus of this thesis is on the CEO, the CFO undoubtedly plays an important role in the preparation and oversight of a firm's financial statements (Feng, Ge, Luo & Shevlin, 2011). Thus I substitute the CFO for the CEO in the *Partner/CEO_Tenure* (*Partner/CFO_Tenure*) variable and re-run the basic main test results, with results reported in Appendix 2C. Overall, results are robust and consistent with the main reported results.

Accruals (Appendix 2D)

Consideration is given to alternative measures of audit quality, predominately the use of total accruals. A potential issue that could arise is that the magnitude of IFRS adoption errors could be influenced by accounting quality more generally, and this is likely to be associated with the magnitude of accruals. Consistent with prior literature, I posit that higher-quality audits mitigate extreme management reporting decisions, and accruals are commonly used to identify extreme reporting decisions (e.g. Dechow, Ge, Larson & Sloan, 2011; Francis & Wang 2008; Myers et al., 2003). While early studies focus on unexpected accruals (e.g. Myers et al., 2003; Johnson et al., 2002), there has been a trend in recent literature towards total accruals (e.g. Dechow et al., 2011; Bayley & Taylor, 2007; Carey & Simmnet, 2006). Following the work of

Bayley and Taylor (2007) and Dechow et al. (2011), this thesis also adopts total accruals (*accruals*) as a measure of audit quality, together with ranked total accruals (*RANK-TACC*). I therefore re-perform tests for the pooled sample using rank total accruals (*RANK-TACC*) (Appendix 2D.8), absolute total accruals (*ABS-TACC*) (Appendix 2D.9) and rank absolute total accruals (*RANK-ABS-TACC*) (Appendix 2D.10). Results are generally directionally consistent with our key variables of interest and lack statistical significance.

In Table 2D.8, Panel A, which employs the *RANK-TACC* measure, the model without controls it is notable that there is a positive and significant relation with *Partner/CEO_Tenure* (α_1=9.455, *t-stat*=3.870, p=0.000) at the 1% level, while the relation with *Audit_Firm_Tenure* is positive and not significant (α_2=0.262, *t-stat*=0.138, p=0.445). This model has good explanatory power (adjusted r^2=0.088) and the model is statistically significant at the 1% level (*F-stat*=8.234, p=0.000). For the model with controls there is an increase in model explanatory power (adjusted r^2=0.116), and the relation between *RANK-TACC* and *Partner/CEO_Tenure* remains positive and significant (α_1=8.457, *t-stat*=3.459, p=0.001).

In Panel B, a refined measure of the person-to-person relationship between the audit partner and CEO is considered which emphasises clients where the CEO is more powerful (*Partner/CEO_Tenure**). Interestingly, the *Partner/CEO_Tenure** variable in the model without controls is positive and significant (α_1=7.064, *t-stat*=3.161, p=0.001), while the *Audit_Firm_Tenure* variable is positive and not significant (α_2=1.692, *t-stat*=0.907, p=0.183). The model has good explanatory power (adjusted r^2=0.059) and the model is statistically significant at the 1% level (*F-stat*=5.717, p=0.004). For the model with control there is an increase in model explanatory power (adjusted r^2=0.100) and the model is statistically significant at the 1% level (*F-stat*=3.377, p=0.002). The relation between *RANK-TACC* and

Partner/CEO_Tenure remains positive and significant (α_1=6.696, *t-stat*=3.016, p=0.002). Interestingly the *Audit_Firm_Tenure* variable switches to negative and is not significant (α_2=-0.017, *t-stat*=-0.009, p=0.497).

Panel C reports a further refinement of the primary sample to test H_1 taking the upper and lower thirds of the primary sample. Interestingly, the *Partner/CEO_Tenure* variable in the model without controls is positive and significant (α_1=12.426, *t-stat*=3.696, p=0.000) at the 1% level, while the *Audit_Firm_Tenure* variable is positive and not significant (α_2=0.383, *t-stat*=0.139, p=0.445). The model has good explanatory power (adjusted r^2=0.116) and the model is statistically significant at the 1% level (*F-stat*=7.617, p=0.001). For the model with control there is an increase in model explanatory power (adjusted r^2=0.152) and the model is statistically significant at the 1% level (*F-stat*=3.595, p=0.002). The relation between *RANK-TACC* and *Partner/CEO_Tenure* remains positive and significant (α_1=11.287, *t-stat*=3.352, p=0.001). Interestingly, once again, the *Audit_Firm_Tenure* variable switches to negative and remains not significant (α_2=-3.084, *t-stat* = -1.020, p=0.256).

Panel D, examining powerful CEOs within a subsample of extreme observations provides similar results. In the model without controls, the *Partner/CEO_Tenure** variable is positive and significant (α_1=8.386, *t-stat*=2.768, p=0.004) at the 1% level, while the *Audit_Firm_Tenure* variable is positive but not significant (α_2=2.581, *t-stat*=0.944, p=0.174). The model has good explanatory power (adjusted r^2=0.066) and the model is statistically significant at the 5% level (*F-stat*=4.576, p=0.013). For the model with controls there is an increase in model explanatory power (adjusted r^2=0.109) and is once again statistically significant at the 5% level (*F-stat*=2.765, p=0.012). The relation between *RANK-TACC* and *Partner/CEO_Tenure* remains

positive and significant (α_1=7.522, *t-stat*=2.471, p=0.008). Interestingly, the *Audit_Firm_Tenure* variable switches to negative but remains insignificant (α_2=-0.918, *t-stat*= -0.303, p=0.381).

Table 2D.9 Panel A reports the results for the measure with *ABS-TACC* and without control variables it is notable that there is a negative relation with the *Audit_Firm_Tenure* variable (α_2=-0.004, *t-stat*=-0.500, p=0.309) and a positive association with *Partner/CEO_Tenure* (α_2=0.000, *t-stat*=0.000, p=0.500). Neither variable is significant, and caution should be exercised when interpreting this result as the model has poor explanatory power (adjusted r^2=-0.012). For the model with controls there is an increase in model explanatory power (adjusted r^2=0.036) and the model being statistically significant at the 10% level (*F-stat*=1.792, p=0.093). However, the relation between *ABS-TACC* and *Partner/CEO_Tenure* is positive and not significant (α_1=0.002, *t-stat*=0.183, p=0.428). Notably, the *Audit_Firm_Tenure* switches to positive and is once again not significant (α_2=0.004, *t-stat*=0.400, p=0.345).

In Panel B, a refined measure of the person-to-person relationship between the audit partner and CEO is considered which emphasises clients where the CEO is more powerful (*Partner/CEO_Tenure**). Interestingly, the *Partner/CEO_Tenure** variable in the model without controls is negative and significant (α_1=-0.015, *t-stat*=-1.506, p=0.067), while the *Audit_Firm_Tenure* variable is also negative but not significant (α_2=-0.003, *t-stat*=-0.382, p=0.352). However, caution should be exercised when interpreting this result as the model has poor explanatory power (adjusted r^2=0.004). For the model with controls there is an increase in model explanatory power (adjusted r^2=0.043) and the model is statistically significant at the 10% level (*F-stat*=1.953, p=0.066). The relation between *ABS-TACC* and *Partner/CEO_Tenure* remains negative but is no longer significant (α_1=-0.010, *t-stat*=-1.033, p=0.152). Interestingly,

the *Audit_Firm_Tenure* variable switches to positive and remains insignificant (α_2=0.004, *t-stat*=0.505, p=0.307). Not surprisingly, the greatest determinant of *ABS-TACC* was the firm being loss making (α_6=0.236, *t-stat*=3.067, p=0.002). Accordingly, in Panels A and B, there is no support for H_1 and longer person-to-person relationships between the audit partner and the client firm CEO reducing audit quality. Overall, this result is consistent with the poor specification or fit and explanatory power of accruals models (Dechow, Sloan & Sweeney, 1995).

Auditor Specialization (Appendix 2E)

Consideration is also directed to auditor industry specialization. Reflecting developments in prior literature, that industry specialist auditors provide 'quality' auditing services (see e.g. Stein & Cadman, 2005; Craswell, Francis & Taylor, 2005) it is necessary to consider the implications for 'quality' audits in this context. Craswell et al., (1995) contend that industry specialists offer higher quality audits given their enhanced knowledge compared to non-experts which is created by greater industry experience, facilitating a better understanding of accounting rules and reporting requirements, an efficient identification of certain industry risks and ultimately a more accurate audit judgement for that industry (Li & Stokes, 2007; Solomon, Shields & Wittington, 1999; Owhoso, Messier & Lynch, 2002). The extant literature identifies industry specialist auditors using various measures such as market share based on; client size (Palmrose, 1986), client assets (Hogan & Jeter, 1999), number of client (Craswell & Guest, 2002) and audit fees (various levels) (Ferguson & Stokes, 2002; Carson, Simnett, Soo & Wright, 2002).

Following Ferguson, Francis and Stokes (2006), Ferguson, Francis & Stokes (2003) and Francis, Stokes & Anderson (1999) a city level (as opposed to national) industry specialisation

indicator is adopted. This is based on the premise that individual audit engagements are administered through office level engagement partners and that those partners will typically be located in the same city as a client's headquarters', where an investment in industry specialisation is derived through an investment in the human capital of professional staff which reside in specific offices (Li & Stokes, 2007; Ferguson et al., 2003; Reynolds & Francis, 2001). Therefore I introduced an industry specialist dummy variable using market share of audit fees at the city level approach (*Dummy_Spec_City_Fee*), classifying an auditor as an industry specialist if they are the industry leader at the city level. A one indicates the use of an industry specialist at the city level and zero otherwise. Additionally, for robustness, following Craswell and Guest (2002) I also test an alternative industry specialist dummy variable, identifying specialists based number of clients at the city level (*Dummy_Spec_No_Clients*), using one to indicate a specialist and zero otherwise. Results for the main audit quality metrics are reported in Appendix 2E. The results are robust to the introduction of a control for industry specialist auditors is with the key variables of interest remaining consistent with prior results.

June Year End Sub Sample (Appendix 2F)

Finally, I examine whether our results are sensitive to a sub-sample of firms with a June year-end reporting date. The impact and implication of transiting to IFRS, and the majority of academic research, has predominately focused on firms with June year-end reporting dates (Hamilton & Thomas, 2007; Goodwin, Ahmed & Heaney, 2006; Rankin, 2006; Newman, 2005). While this thesis has focused on a pooled sample of firms, it is important to consider the June year-end sample as these firms which account for the majority of ASX listed firms. Therefore a sub-sample of 117 firms are examined. I reproduce the main tests and above sensitivities on this

sample and these results are reported with and without control variables in Appendix F. The results are robust and generally consistent with minimal changes across the sample.

In Table 2F.4 Panel A, audit quality is measured as *ABS-Errors* and for the model without controls it is notable that while there is a negative and significant relation with *Audit_Firm_Tenure* (α_2=-0.009, *t-stat*=-2.280, p=0.012), the relation with *Partner/CEO_Tenure* is not significant (α_1=0.004, *t-stat*=0.929, p=0.178). However, caution must be exercised in interpreting this result as the model has poor explanatory power (adjusted r^2=0.027). For the model with controls, there is an increase in model explanatory power (adjusted r^2=0.105), and the relation between *ABS-Errors* and *Partner/CEO_Tenure* becomes significant (α_1=0.006, *t-stat*=1.392, p=0.084) and *Audit_Firm_Tenure* remains negative and significant (α_2=-0.006, *t-stat*=-1.586, p=0.058) at the 10% level. Once again the loss-making firms are a significant determinant of ABS-Errors (α_6=0.094, *t-stat*=2.860, p=0.003). Accordingly, in Panel A, there is initial support for H_1 and longer person-to-person relationships between the audit partner and the client firm CEO reducing audit quality.

In Panel B a refined variation of the person-to-person relationship measure between the audit partner and the CEO is considered which emphasises clients where the CEO is more powerful (*Partner/CEO_Tenure**). In the model without controls, it is notable that while there is a negative and significant relation with *Audit_Firm_Tenure* (α_2=-0.008, *t-stat*=-2.040, p=0.022), with the *Partner/CEO_Tenure** being negative and not significant (α_1=-0.002, *t-stat*=0.371, p=0.356). In contrast there is no evidence of a longer *Audit_Firm_Tenure* being associated with increased audit quality in the model with controls (α_2=-0.005, *t-stat*=-1.270, p=0.104). Overall, in Panel B there is still no support for H_1 and longer person-to-person relationships between the audit partner and the client firm CEO reducing audit quality.

Panel C reports a further refinement of the primary sample. After ranking the *ABS-Errors* from lowest to highest and taking the lower and upper thirds of the primary sample, I arrive at a sample of 102 extreme observations and re-conduct the tests from panel A and B. For the model without controls it is notable that while there is a negative and significant relation with *Audit_Firm_Tenure* (α_2=-0.013, *t-stat*=-2.204, p=0.016), the relation with *Partner/CEO_Tenure* is positive and not significant (α_1=0.004, *t-stat*=0.591, p=0.278). The model has poor explanatory power (adjusted r^2=0.036) but is statistically significant at the 10% level (*F-Stat*=2.431, p=0.095). For the model with controls there is an increase in model explanatory power (adjusted r^2=0.103), however the relation between *ABS-Errors* and *Partner/CEO_Tenure* is still not significant (α_1=0.006, *t-stat*=0.941, p=0.175). Not surprisingly, the greatest determinant of *ABS-Errors* was the firm being loss making (α_6=0.113, *t-stat*=2.378, p=0.010) and use of a Big N auditor (α_7=0.053 *t-stat*=1.349, p=0.091). Accordingly, in Panel C there is no support for H_1 and longer person-to-person relationships between the audit partner and the client firm CEO reducing audit quality.

Panel D presents the results for the association between audit quality and the person-to-person relationship between the audit partner and the CEO, where the CEO is more powerful and utilises extreme (thirds) observations. In the model without controls it is notable that there is a negative and significant relation with *Audit_Firm_Tenure* (α_2=-0.011, *t-stat*=-2.0320, p=0.023) and is significant at the 5% level. The relation with *Partner/CEO_Tenure** is not significant and negative (α_1=-0.003, *t-stat*=-0.626, p=0.267). This result should be interpreted with caution as the model has poor explanatory power (adjusted r^2=0.036), but is statistically significant at the 10% level (*F-Stat*=2.453, p=0.093). For the model with controls there is an increase in model explanatory power (adjusted r^2=0.091), but the relation between *ABS-Errors*

and *Partner/CEO_Tenure** is not significant (α_1=-0.000, *t-stat*=0.063, p=0.475). Once again the greatest determinants of *ABS-Errors* was the firm being loss making (α_6=0.114, *t-stat*=2.380, p=0.010) and use of a Big N auditors (α_7=0.053, *t-stat*=1.317, p=0.096). Accordingly there is no support for H_1 and longer person-to-person relationships between the audit partner and the client firm CEO reducing audit quality.

The above sensitivity testing generally confirms our initial findings and provides further support for the fact that auditors do not appear to have person-to-person relationships which undermine audit quality and further emphasise the negative association between various measures of audit quality tests and the professional relations between audit firm and the client firm.

2.6 Conclusions, Limitations and Future Research

In response to anecdotal evidence that a lack of audit independence contributed to corporate failures, many countries adopted regulation that prescribed auditor rotation. The objective of this chapter was to provide empirical evidence of any association between audit quality and auditor tenure which would support auditor rotation being prescribed. This chapter assesses audit quality as the errors arising in the initial transition to IFRS in Australia. Auditor tenure is measured having regard to both the person-to-person relationships and professional relations that exist between the audit firm and client firm, with these having potentially differing impacts on audit quality. Using three main proxies for audit quality, *ABS-Errors*, *SIGN-Errors* and *RANK-Errors* I do not find a significant association between IFRS adoption errors and length of the person-to-person relationships between audit partners and the CEO of the client firm. This would suggest that auditors do not have person-to-person relationships which

undermine audit quality. In contrast, I find some evidence of a significant negative association between various categories of IFRS adoption errors and professional relations between the audit firm and the client. Ultimately, audit and financial report quality improves as audit firm tenure increases. This result is robust to a range of sensitivity tests and alternative measures of audit quality and the auditor-client tenure.

Overall, using IFRS adoption errors as a proxy for audit quality, the reported results suggest support for longer professional relations (*Firm-Tenure*) reducing IFRS errors, providing no support for auditors having person-to-person relationships with CEOs, which undermines audit Quality. I attribute this level of maintained professionalism between audit partners and CEOs to three key factors;

First, audit partner's represent one member of a broader audit team. While the audit partner takes ultimate responsibility for an engagement, normal turnover in audit staff and client management appear to reduce the importance in the development of person-to-person relationships (Davis, Soo & Trompeter, 2002). Second, internal and external audit review appears to play an important role in aiding professional scepticism and promoting auditor independence. Internal review or peer review provide a 'second look' at firms' work (Davis et al., 2002). Furthermore, firms following quality review programs which ensure compliance with professional standards (e.g. APESs) should aid professional scepticism and promote independence (Davis et al., 2002; Gay & Simnet, 2010). External reviews conducted by the ASIC such as the Surveillance and Audit and Inspection program (King, 2011a; Niven, 2010) and an *Auditing Inspection Program* would doubtlessly have an impact on the reported results. Third, auditors face increased litigation risk and public scrutiny when they develop closer

person-to-person relationships with CEOs (Dye, 1993).[19] Given the above checks and balances it is not surprising our results are consistent with a view that audit firms use supplementary mechanisms to protect audit quality and person-to-person relationships do not develop in a way that impact audit quality.

This chapter makes a number of contributions to literature and practice. First it extends the literature considering the relation between audit tenure and audit and financial report quality. Second, it uses a new measure of audit quality, IFRS adoption errors, which is not subject to some of the limitations of other measures of audit quality. Third, it considers different aspects of audit relations (i.e. person-to-person relationships and professional relations). Fourth, it also provides empirical evidence that as professional relations increase in duration there is an increase in audit quality. This chapter shows that there is no evidence of person-to-person relationships between audit partners and senior executives reducing audit quality, which provides insights to the ineffectiveness and presumptions the regulation prescribing auditor rotation was based upon.

This chapter has a number of limitations. First, the proxy of person-to-person relationships (*Partner/CEO_Tenure*) is a noisy one and does not directly capture the traditional notion of 'relationship' presented in research in other disciplines. However, I am limited by data and utilise the best available information to gain initial insights into this measure. Furthermore, I note that *person-to-person relationship* is a subset of the control variable *professional relation* (*Audit_Firm_Tenure*), which further compounds the above issue. The *person-to-person* relationship also has a maximum value of eight placed on the measure. This is reflective of the timeframe partner information began to be disclosed in Australia up until IFRS transition date, but represents a clear limitation of this chapter. Second, this thesis utilises a non-traditional

[19] For example, Centro Properties A$200m payout is a prime example of this (Hume, 2012).

measure of audit quality (IFRS Errors). While IFRS errors is a valuable measure as it overcomes some of the limitations of other measures of audit quality, it has relatively little examination in extant literature. Third, the limited sample size restricts the ability to test for industry fixed effects and due to limitations surrounding data availability, testing of auditor industry expertise have not been tested and could add to our understanding of rotation issues. Fourth, this chapter adopted a total accruals measure as a proxy for audit quality. However, I note that there are alternative methods to classifying accrual measures which are not considered in this study. Adopting alternative measures could assist in overcoming these limitations and provide an opportunity for future research.

Ultimately, this research raises questions about the regulatory change which has occurred in Australia, and provides evidence to suggest more research should be directed towards developing more appropriate alternatives to audit partner rotation as a means of maintaining auditor independence and expertise.

Table 2.1
Sample Selection and Industry Breakdown

Panel A: Sample Process	
Firms in the S&P/ASX Top 500	500
Less:	
Financial Firms	71
Firms missing CEO details	82
Firms using non AUS GAAP	26
Firms changed FYE	4
Firms without annual reports for 2005	47
Firms with other missing data	119
TOTAL FINAL SAMPLE	**151**

Panel B: GICS Sector Breakdown		
Sector	**Number**	**Percentage**
10: Energy	15	9.93%
15: Material	41	27.15%
20: Industrials	22	14.57%
25: Consumer Discretionary	33	21.85%
30: Consumer Staples	14	9.27%
35: Health Care	15	9.93%
45: information Technology	7	4.64%
50: Telecommunication	3	1.99%
55: Utilities	1	0.66%
TOTAL	**151**	**100%**

Panel C: Sample Firm Balance Dates	
Balance Date	**Number of Firms**
31 December	22
28 Feb	1
31 March	1
30 April	1
31 May	1
30 June	117
31 July	3
31 August	1
30 September	4
TOTAL	**151**

Table 2.2

Descriptive Statistics

Panel A: Accounting Standards that Led to Errors and the Size of the Errors		
Accounting Standards	**# of Firms with an Error**	**Sum of Absolute Value of Errors $M**
AASB 2: Share Based Payments	65	68.417
AASB 5: Assets held for Sale	8	50.523
AASB 6: Exploration Transition	1	5.017
AASB 112: Income Tax	90	660.904
AASB 116: Property, Plant and Equipment	34	79.211
AASB 117: Lease	20	44.497
AASB 118: Revenue	27	179.227
AASB 119: Employee Benefits Transition	21	113.948
AASB 121: Functional Currency	20	99.604
AASB 123: Borrowings	6	42.926
AASB 128: Investments in Associates	24	42.091
AAS 132 and 139: Financial Instruments	11	35.537
AAS 136: Impairment Transition	22	260.956
AASB 137: Provisions, Contingent Liabilities and Assets	26	45.670
AASB 138: Intangible Assets	25	73.745
AASB 140: Investment Property	6	52.772
Other Standards	52	317.14

Table 2.2 (continued)
Descriptive Statistics

Panel B: Independent and Experiential Variables				
	Mean (Median)	**Std. Deviation**	**Minimum**	**Maximum**
Partner/CEO_Tenure	2.709 (2.000)	1.832	1	8
Audit_Firm_Tenure	6.583 (8.000)	2.356	1	8
Partner/CEO_Tenure*	1.775 (1.000)	1.967	1	8
Market Cap	2074.188 (334.188)	5873.984	20.990	62961.960
Leverage	1.923 (1.829)	0.686	1.030	4.950
ROA	0.039 (0.068)	0.155	-0.810	0.390
Loss	0.166 (0.000)	0.373	0	1
Audit_Big_N	0.868 (1.000)	0.340	0	1

Where:

Partner/CEO_Tenure	:	The length of time as measured in years (up to a maximum of 8) that the same audit partner and the same CEO combination have worked together in preparing the firm's financial statements at 2006.
Audit_Firm_Tenure	:	The duration of the relation between the audit firm and client firm in years at 2006.
Partner/CEO_Tenure*	:	Partner/CEO_Tenure variable times by the dummy variable of the CEO pay slice.
Market Cap	:	The market capitalisation of the firm in 2006, scaled by average total assets.
LEV	:	Leverage, measured as the ratio of the firm's total long-term debt to market value of equity.
ROA	:	Return on assets, measured as the ratio of the firm's earnings divided by total assets (also consistent with Johnson et al., 2002)
LOSS	:	To control for whether the firm experienced a loss, an indicator variable that is set to equal one in the fiscal year 2006 if net income is negative.
Audit_Big_N	:	Indicator variable set to equal one if the firm was audited by a member of the Big 4 during the fiscal year 2006 audit, zero otherwise.

Table 2.3
Correlation Matrix

	Partner/CEO_Tenure	*Audit_ Firm_Tenure*	*Partner/CEO_Tenure**
Partner/CEO_Tenure	1.000	**0.268****	**0.443****
		0.000	**0.000**
Audit_Firm_Tenure	**0.215****	1.000	-0.008
	0.004		0.460
*Partner/CEO_Tenure**	**0.611****	0.092	1.000
	0.000	0.131	

Pearson correlations are below diagonal and Spearman correlations are above diagonal.
All variables as previously defined
All results are one-tailed tests
** correlation is significant at the 0.001 level
* correlation is significant at the 0.005 level

Table 2.4

Tests of association between absolute IFRS errors and tenure

This table presents the results of tests of association of pooled absolute IFRS errors and various measures of auditor tenure. Panel A presents the results for the full sample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for subsample of firms, taking the lower and upper thirds of absolute IFRS errors using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of absolute IFRS errors for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Absolute IFRS Errors

n=151	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	0.072	3.033	0.002	***	0.023	0.506	0.307	
Partner/CEO_Tenure	0.000	0.112	0.456		0.002	0.454	0.325	
Audit_Firm_Tenure	-0.005	-1.611	0.055	*	-0.003	-0.841	0.201	
Market Cap					0.000	-0.581	0.281	
LEV					-0.001	-0.045	0.482	
ROA					0.007	0.096	0.462	
LOSS					0.064	2.091	0.019	**
Audit Big N					0.023	0.968	0.167	
Adjusted R^2	0.005				0.037			
F-stat	1.354		0.261		1.814		0.089	*

Panel B: Absolute IFRS Errors with restricted definition of Partner/CEO Tenure

n=151	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	0.076	3.248	0.001	***	0.029	0.637	0.263	
Partner/CEO_Tenure*	-0.060	-0.734	0.232		-0.001	-0.245	0.404	
Audit_Firm_Tenure	-0.128	-1.570	0.060	*	-0.003	-0.745	0.229	
Market Cap					0.000	-0.583	0.281	
LEV					-0.001	-0.067	0.474	
ROA					0.011	0.149	0.441	
LOSS					0.063	2.042	0.022	**
Audit Big N					0.022	0.913	0.182	
Adjusted R^2	0.008				0.036			
F-stat	1.621		0.201		1.791		0.093	*

Table 2.4 (continued)
Tests of association between absolute IFRS errors and tenure

Panel C: Absolute IFRS Errors (Ranked Thirds)								
n=102	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	0.095	2.819	0.003	***	-0.011	-0.174	0.432	
Partner/CEO_Tenure	0.000	-0.002	0.333		0.001	0.177	0.43	
Audit_Firm_Tenure	-0.007	-1.427	0.079	*	-0.001	-0.281	0.39	
Market Cap					0.000	-0.654	0.258	
LEV					0.008	0.453	0.326	
ROA					-0.017	-0.148	0.441	
LOSS					0.081	1.738	0.043	**
Audit Big N					0.050	1.408	0.081	*
Adjusted R^2	0.002				0.040			
F-stat	1.079		0.344		1.600		0.145	

Panel D: Absolute IFRS Errors (Ranked, thirds)								
n=102	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	0.101	3.071	0.002	***	-0.005	-0.08	0.468	
Partner/CEO_Tenure*	-0.005	-0.894	0.187		-0.002	-0.335	0.37	
Audit_Firm_Tenure	-0.007	-1.39	0.084	*	-0.001	-0.251	0.402	
Market Cap					0.000	-0.662	0.255	
LEV					0.009	0.458	0.324	
ROA					-0.016	-0.146	0.443	
LOSS					0.078	1.668	0.05	**
Audit Big N					0.049	1.384	0.085	*
Adjusted R^2	0.010				0.041			
F-stat	1.487		0.231		1.613		0.141	

All variables as previously defined and reported as one-tailed
*** : Denotes significance at the 1% level
** : Denotes significance at the 5% level
* : Denotes significance at the 10% level

Table 2.5

Tests of association between signed IFRS errors and tenure

This table presents the results of tests of association of pooled signed IFRS errors and various measures of auditor tenure. Panel A presents the results for the full sample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for subsample of firms, taking the lower and upper thirds of signed IFRS errors using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of signed IFRS errors for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Signed IFRS errors

n=151	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	-0.045	-2.538	0.006	***	-0.07	-2.056	0.021	**
Partner/CEO_Tenure	0.001	0.214	0.416		0.001	0.369	0.357	
Audit_Firm_Tenure	0.005	2.019	0.023	**	0.005	1.904	0.03	**
Market Cap					0	0.516	0.304	
LEV					0.011	1.209	0.115	
ROA					-0.043	-0.799	0.213	
LOSS					-0.003	-0.113	0.455	
Audit Big N					0.004	0.225	0.411	
Adjusted R^2	0.018				0.002			
F-stat	2.345		0.099	*	1.053		0.397	

Panel B: Signed IFRS Errors

n=151	*SIGN-Error*				*SIGN-Error*			
	Co-efficient	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	-0.043	-2.471	0.008	***	-0.067	-1.945	0.027	**
Partner/CEO_Tenure*	0.000	-0.160	0.436		0.000	-0.146	0.442	
Audit_Firm_Tenure	0.005	2.161	0.016	**	0.005	2.041	0.022	**
Market Cap					0.000	0.511	0.305	
LEV					0.011	1.192	0.118	
ROA					-0.041	-0.761	0.224	
LOSS					-0.003	-0.131	0.448	
Audit Big N					0.003	0.187	0.426	
Adjusted R^2	0.017				0.002			
F-stat	2.335		0.1	*	1.036		0.409	

Table 2.5 (continued)
Tests of association between signed IFRS errors and tenure

Panel C: Signed IFRS errors (ranked thirds)								
n=102	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	-0.059	-2.417	0.009	***	-0.096	-1.896	0.032	**
Partner/CEO_Tenure	0.001	0.233	0.409		0.001	0.151	0.440	
Audit_Firm_Tenure	0.007	1.844	0.034	**	0.007	1.799	0.038	**
Market Cap					0.000	0.562	0.288	
LEV					0.019	1.352	0.009	
ROA					-0.059	-0.773	0.221	
LOSS					-0.011	-0.327	0.372	
Audit Big N					0.004	0.123	0.451	
Adjusted R^2	0.020				0.000			
F-stat	2.040		0.135		1.003		0.434	

Panel D: Signed IFRS Errors (Ranked Thirds)								
n=102	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	-0.057	-2.674	0.011	**	-0.09	-1.735	0.043	**
Partner/CEO_Tenure*	-0.001	-0.341	0.442		-0.002	-0.382	0.352	
Audit_Firm_Tenure	0.007	2.012	0.024	**	0.007	1.915	0.029	**
Market Cap					0.000	0.672	0.285	
LEV					0.020	1.384	0.085	*
ROA					-0.061	-0.793	0.217	
LOSS					-0.014	-0.396	0.347	
Audit Big N					0.000	0.14	0.495	
Adjusted R^2	0.02				0.002			
F-stat	2.024		0.138		1.022		0.421	

All variables as previously defined and reported as one-tailed
*** : Denotes significance at the 1% level
** : Denotes significance at the 5% level
* : Denotes significance at the 10% level

Table 2.6

Tests of association between ranked signed IFRS Errors and tenure

This table presents the results of tests of association of rank signed IFRS errors and various measures of auditor tenure. Panel A presents the results for the full sample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for subsample of firms, taking the lower and upper thirds of rank signed IFRS errors using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of rank signed IFRS errors for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Rank Signed IFRS Errors

n=151	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	54.247	4.942	0.000	***	36.329	1.705	0.045	**
Partner/CEO_Tenure	0.146	0.103	0.918		0.414	0.237	0.407	
Audit_Firm_Tenure	3.244	2.136	0.017	**	3.583	2.236	0.014	**
Market Cap					0.001	1.466	0.073	
LEV					3.396	0.601	0.275	
ROA					-10.492	-0.325	0.373	
LOSS					3.305	0.267	0.395	
Audit Big N					7.315	0.584	0.28	
Adjusted R^2	0.020				0.008			
F-stat	2.527		0.083	*	1.165		0.327	

Panel B: Ranked Signed IFRS Errors

n=151	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	55.796	5.142	0.000	***	39.648	1.861	0.033	**
Partner/CEO_Tenure*	-1.065	-0.600	0.275		-1.045	-0.572	0.284	
Audit_Firm_Tenure	3.356	2.294	0.012	**	3.703	2.375	0.010	***
Market Cap					0.001	1.481	0.071	*
LEV					3.213	0.569	0.285	
ROA					-10.133	-0.313	0.378	
LOSS					2.267	0.193	0.424	
Audit Big N					6.573	0.514	0.304	
Adjusted R^2	0.022				0.01			
F-stat	2.708		0.07	*	1.206		0.303	

Table 2.6 (continued)
Tests of association between ranked signed IFRS Errors and tenure

Panel C: Ranked Signed IFRS Errors (Ranked thirds)								
n=102	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	49.044	3.277	0.001	***	17.307	0.56	0.289	
Partner/CEO_Tenure	-0.104	-0.036	0.486		-0.088	-0.029	0.489	
Audit_Firm_Tenure	4.912	1.919	0.029	**	4.660	2.049	0.022	**
Market Cap					0.001	1.392	0.084	*
LEV					9.114	1.047	0.149	
ROA					-14.261	-0.305	0.381	
LOSS					2.639	0.126	0.45	
Audit Big N					10.39	0.570	0.285	
Adjusted R^2	0.019				0.006			
F-stat	2.001		0.141		1.085		0.379	

Panel D: Rank Signed IFRS Errors (Ranked Thirds)								
n=102	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	51.503	3.452	0.001	***	23.515	0.749	0.228	
Partner/CEO_Tenure*	-1.895	-0.699	0.243		-2.218	-0.777	0.22	
Audit_Firm_Tenure	4.272	2.050	0.022	**	4.698	2.144	0.018	**
Market Cap					0.001	1.424	0.079	*
LEV					9.372	1.083	0.141	
ROA					-17.529	-0.377	0.354	
LOSS					-0.185	-0.009	0.497	
Audit Big N					7.237	0.392	0.348	
Adjusted R^2	0.024				0.012			
F-stat	2.254		0.11		1.178		0.323	

All variables as previously defined and reported as one-tailed
*** : Denotes significance at the 1% level
** : Denotes significance at the 5% level
* : Denotes significance at the 10% level

Chapter Three
Audit fee changes subsequent to initial audit engagements

The objective of this chapter is to provide empirical evidence of changes in audit fees subsequent to initial audit engagements. Evidence is provided of audit fees increasing by almost 8% p.a. in the years immediately following an initial audit engagement. This rate of increase declines to 3% p.a. in subsequent years. Furthermore, there is no evidence that a close relation between the audit partner and the CEO limits audit fee increases. This suggests that concerns expressed by regulators and others about discounting undermining audit quality are largely misplaced and the impacts of discounts on initial audit engagements are likely to be ameliorated by subsequent audit fee increases.

3.1 Introduction

The objective of this chapter is to provide empirical evidence of changes in audit fees subsequent to initial audit engagements. Concerns have been expressed by regulators and others that discounting on initial audit engagements potentially undermines audit quality. However these concerns may be ameliorated if there are audit fee increases in subsequent years. Accordingly, I evaluate audit fee changes subsequent to initial audit engagements to determine if there is an increase in audit fees and whether concerns over the consequences of discounting are misplaced. Consideration is also given to whether the ability to increase discounts in audit fees subsequent to initial audit engagements is affected by *audit partner/CEO tenure,* which recognises relationships between the lead audit partner and the CEO of the client firm. The concern is that these relationships limit the ability to increase audit fees and constraints audit effort. This would provide empirical support for auditor rotation which is now mandated in many countries.

There is a significant body of literature evaluating initial audit engagement fees and the practice of discounting or lowballing to secure new audit clients (e.g. Huang, Raghunandan & Rama, 2009; Craswell & Francis, 1999; Dye, 1991; Ettredge & Greenberg, 1990; Simon & Francis, 1988; DeAngelo, 1981b). Motivating much of this literature, and an issue for regulators, is the concern that this practice results in audit effort being curtailed and an increased likelihood of material misstatements in the financial statements not being discovered (see e.g., King, 2011a; King, 2011b; Niven, 2010). One manifestation of this was the *Australian Securities and Investment Commission* (ASIC) investigating audit tenders from 14 of the largest accounting firms (Niven, 2010). It was claimed this was in response to complaints of Big N audit firms discounting or lowballing by as much as 25-30 percent to 'pick up' consulting work (King,

2011a; Niven, 2010). Similar concerns were expressed by King (2011a) that the audit quality in Australia has deteriorated in recent years because of "significant fee reductions" by audit firms (p. 46). The common concern is pressure on audit fees, starting with initial audit engagements, is resulting in audit effort being curtailed and thus undermining audit quality. While there is some empirical evidence of discounting on initial audit engagements, little is known about subsequent period audit fees. This is considered particularly salient as audit contracts generally extend beyond the initial engagement year, and audit fee increases in subsequent periods would ameliorate concerns that discounting on initial audit engagement is undermining audit quality.

There are two motivations for this chapter. First, while much attention has been directed towards fees on initial audit engagements and in particular the phenomena of discounting, relatively little is known about subsequent changes in audit fees. Doubtless contributing to this is an emphasis in the discounting literature on the costs faced by audit firms, and little consideration of the switching costs faced by audit clients. The auditing standards specifically acknowledge the need to get to know the business, and this requires significant work on both the part of the auditor and the client to establish sufficient understanding of the business and its environment in order to accept the engagement (*ASA 315: Understanding the Entity and its Environment*[20]). Therefore, it is beneficial for both the audit firm and the client to maintain auditor-client relationships. This raises the question of whether there is a increase in audit fees subsequent to initial audit engagements that would ameliorate concerns that discounting adversely impacts audit effort and undermines audit quality?

Second, considerable attention has been directed at the impact of partner/CEO tenure on audit quality, and in particular whether this relation undermines auditor independence (see

[20] AUS 304: *Knowledge of the Business*, and AUS 402: *Risk Assessments and Internal Controls* (both withdrawn April 2009) and were replaced with *ASA 315: Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement*.

chapter 2). It is also possible that a closer person-to-person relationship between the audit partner and the CEO affects the ability to recover discounts on initial audit engagements, and this may result in audit effort being curtailed.

Based on a sample of 688 firms listed on the Australian Securities Exchange (ASX) between 2005 – 2009 (3440 observations), evidence is provided of audit fee increases in years subsequent to the initial audit engagement, and these are greatest in the years immediately following a switch which likely correspond with the term of initial audit contracts. Documented increases are in the order of 8% p.a. and are materially greater than the likely cost increases experienced by audit firms. Overall, the results from this chapter suggest there are increases in audit fees in years subsequent to initial audit engagements and concerns that discounting might result in poorer quality audits are likely overstated. As audit tenure extends there is evidence of a decline in the rate of increase in audit fees, and after three years the rate of increase slows to about 3% p.a. This is broadly consistent with price level changes and suggests that there are significant competitive pressures which constrain audit fee increases. Interestingly, this thesis provides no evidence of longer partner/CEO tenure inhibiting audit fee increases. However, there is some evidence of greater audit fee increases after the period of initial audit contracts and this would suggest there may be over-servicing clients. Accordingly, there is no support for auditor rotation due to concerns that extended tenure inhibits audit fee increases and reduces audit quality.

This thesis makes a number of important contributions to both the literature and practice. First, it extends the literature on audit pricing by ameliorating concerns from practitioners, regulators and academics on initial audit engagement fee discounting leading to reduced audit effort and audit quality. Furthermore, it provides valuable information on audit pricing, and to

some extent competition, in an Australian context over a period which is characterised by limited rigorous academic research and increasing uncertainty concerning audit pricing in Australia (King, 2011a; Niven, 2010).

Second, this research contributes to the regulatory debate surrounding mandatory auditor rotation within Australia. This chapter finds no support for mandatory auditor rotation based on concerns that extended tenure inhibits audit fee increases and therefore reducing audit quality. This research should lead to a more informed debate on mandatory auditor rotation in Australia, while also providing international insights to rotation policy based on Australian experiences.

Finally, this chapter evaluates audit fee changes overtime using a lagged audit fee approach. Traditionally, prior research examining audit fee changes have relied upon cross-section models with relatively little attention directed towards time-series data. Cross-sectional models have provided extremely valuable information, however the results of these studies could potentially be somewhat unreliable if audit contracts are set on a multi-year basis with underpricing in the first year which is offset by over-pricing in subsequent years. Using a lagged audit fee approach provides new insights and aids our understanding of audit fee discounting on initial audit engagements.

The remainder of this chapter is organised as follows. Section 3.2 provides a review of relevant literature and the hypothesis development. Section 3.3 describes the research design and explanatory variables. Data collection and the sample description are provided in section 3.4 while the results and relevant sensitivity analysis are described in section 3.5. Section 3.6 provides summary conclusions, research limitations and future research potential.

3.2 Literature review and hypothesis development

3.2.1 Discounting on initial audit engagements

There has been extensive regulatory, academic and professional debate over the threats, to audit quality in Australia and internationally (see e.g. King, 2011a; King, 2011b; Malley, 2011; Treasury, 2010; Niven, 2010). A key concern is that audit quality is being undermined as a consequence of audit effort being curtailed due to pressure on audit fees (Malley, 2012; Treasury, 2010). This is reflected in the following comment which clearly links audit fee pressure with reduced audit effort, and hence reduced audit quality:

"*...directors should be mindful of the possible impacts on audit quality from reductions in audit fees. Where audit fee reductions occur, auditors have a responsibility to maintain audit quality*" (King, 2011a, p. 46)

There is some support for these concerns in the academic literature evaluating audit quality generally. For example, there is evidence of differences in audit effort across firms (e.g. Francis & Yu, 2009), and differences in audit quality (e.g. Caramanis & Lennox, 2008; Seetharaman, Gul & Lynn, 2002; O'Keefe, King & Gaver, 1994; Davis, Ricchiute & Trompeter, 1993).

Attention has also been focussed on initial audit engagements as the audit contract is clearly being renegotiated, and there is an economic incentive to reduce audit fees to attract new business. The concern is that reductions in the level of audit fees on initial audit engagements, commonly labelled 'price cutting' and 'discounting', lead to a reduction in audit effort and hence audit quality. In these contexts, price cutting on initial audit engagements is defined as the 'difference between the first-year audit fee and either the prior auditor's fee or an estimated fee based on a cross-sectional model' (Magee & Tseng, 1990, p.316). Lowballing is a market phenomenon and is defined as 'setting audit fees below total current costs on initial audit

engagements' (DeAngelo, 1981b, p.113), while price cutting and discounting behaviours are related, without information on audit costs they are difficult to distinguish (e.g. Simunic & Stein, 1995; Jensen & Payne, 2003). Accordingly, for the purposes of this chapter, price cutting will be treated as a variation of discounting.[21]

While audit fee discounting is a complicated issue, a number of factors have been suggested to drive discounting. DeAngelo (1981b) provides evidence of discounting and characterises the phenomenon as setting an initial engagement audit fee significantly below costs, with the expectation that this will be recovered on subsequent audits. Underpinning this strategy are the assumptions that auditors compete for initial audits via their pricing strategies, and hence discounts are necessary to obtain the new audit client; competing auditors possess the same audit technology, and competitive advantage cannot be achieved by reducing costs and lower audit fees are a result of discounting; initial audits cause start-up costs additional to the regular audit costs; and clients will face transaction costs in case of an auditor change which imposes switching cost and allows cost increases. These assumptions are integral, but limiting to the interpretation of discounting.

A number of researchers have extended the work of DeAngelo. For example, Magee and Tseng (1990) report similar findings to DeAngelo, using a model which relaxes the assumption that auditors are homogeneous and that only certain auditors could suffer from independence issues (Simons, 2007). Conversely, Dye (1991) argues that information asymmetries between the incumbent auditor and client cause initial audit fee discounts. While a discounting phenomenon is observed in the pricing of audit services, discounting is achieved by "encouraging auditors to attest to more favourable financial reports (than they would in the absence of lowballing)" (Dye,

[21] The focus of this chapter is on auditor expertise, rather than auditor independence. While audit-partner/CEO familiarity may impact auditor independence, independence issues represent a sunk cost of the engagement and therefore greater value can be gained from examining expertise.

1991, p. 363). Furthermore, discounting is a necessary practice for audit firms in order to offset investor expectations that auditors have agreed to attest to 'boosted' financial statements and is eliminated with the public disclosure of audit fees (Dye, 1991).

A feature of these studies is that they generally rely on cross sectional models to evaluate audit fees, and it is likely a consequence of this that they consider audit fees on initial engagements only. Problematically, these results may be unreliable if audit contracts relate to multiple years and under-pricing in one year is offset by over-pricing in subsequent years. This suggests the use of a lagged audit fee model in evaluating audit fees has received relatively little attention in the literature (exceptions include Zhang, de Villiers & Hay, 2012; Goodwin, 2011; Ferguson, Lennox & Taylor, 2005).

3.2.2 Fee increases subsequent to initial audit engagements

An important question in evaluating the impact of audit fees, and in particular discounts on initial audit engagements, on audit quality is whether there is an increase in audit fees in subsequent years. If auditors maintain clients long enough to recoup initial start-up costs of the engagement, then the impacts of discounting are relatively benign. However, if discounting creates an economic dependency with the audit client, the threat of dismissal in the early years of the initial engagement could significantly impair the auditor's professional judgment (Azizkhani, et al., 2010; Geiger & Raghunandan, 2002; and DeAngelo, 1981b). Economic dependency may also induce auditors to engage in competitive pricing (i.e. further discounting) in order to maintain clients. In these circumstances audit quality could be adversely impacted. Whether this occurs will be determined by the nature of audit markets and factors such as whether audit markets are perfectly competitive each period, or if there are switching costs or other costs which make the audit market less competitive in subsequent periods.

Central to the literature evaluating audit fees is the audit price model developed by Simunic (1980). Critically, this assumes a competitive market for audit services, and argues that the audit costs and audit fees are a function of client characteristics (e.g., size, complexity, and client-specific risk), auditor characteristics (e.g., brand name, industry expertise) and the auditor's total expected cost of providing assurance to stakeholders, that management's financial statements present a true and fair view (Stanley, 2011). While the audit pricing model is fundamental to our understanding of audit pricing, an issue is that the model is cross-sectional; there is no time series dimension to the model. Furthermore, the model assumes the market for audit pricing is competitive each year and there are no start-up costs for the auditor or the client. However, initial audit contracts are typically entered into for three year periods, and a competitive market equilibrium is only applicable when the audit contract is negotiated (i.e., year one), and then likely diverges from a competitive equilibrium in subsequent periods (i.e., year two, three). Nor does it consider the start-up costs to both the client and auditor of a new engagement.

The extant literature provides evidence of switching costs being significant (Arrunada & Paz-Ares, 1997; DeAngelo, 1981b). They act as a deterrent to switching (Beattie & Fearnley, 1995) by requiring a significant initial investment by both auditors and clients in the new auditor's first year (Hennes, Lorne & Miller, 2010). Critically, some switching costs are borne by the client firm in "breaking-in" a new auditor as the client must dedicate additional managerial time to the new auditor for training and review or re-audit of prior year works (Hennes et al., 2010; Beattie & Fearnley, 1995). Moreover, Villalonga and Amit (2006) and Leone and Liu (2010) note that firm-specific human capital possessed by executives, is less irreplaceable than the auditor's firm specific knowledge and experience (Hennes et al., 2010). Thus switching away

from an incumbent auditor is costly to clients as it involves sacrificing firm-specific expertise and efficiencies developed by the incumbent auditor (Myers, Myers & Omer, 2003; De Martinis, Moroney & Sigjali, 2009; Hennes et al., 2010).

This has implications for the setting of audit fees over time. In the presence of switching costs it can be expected that discounting will occur in the first period to win the client (Simons, 2007) and to provide the client with a 'buffer' against subsequent audit fee increases. In subsequent periods, to the extent that there are switching costs, audit fees may exceed audit costs and there will be audit fee increases subsequent to initial audit engagements. If this occurs, concerns that discounting of fees on initial audit engagements leads to reduced audit effort is likely misplaced. This is reflected in the following hypothesis;

H_1: Subsequent to initial audit engagements there is a significant increase in audit fees

3.2.3 Fee increases subsequent to initial audit engagements and partner/CEO tenure

If fee increases subsequent to initial audits is necessary to ensure that sufficient effort is applied to the conduct of an audit, any impediments to audit fee increases in subsequent periods will be of concern. There is a considerable literature evaluating the impact of auditor-client tenure (between the audit firm and the client firm) on audit quality focusing on the impact of auditor independence and the potential for compromise by a longer relation between the auditor and the client. It is argued that as the length of association increases, the auditor may develop a closer identification with the interests of the client (Dopuch, King & Schwartz, 2003).

Mautz and Sharaf (1961) were one of the first to suggest that longer auditor-client associations could create auditor independence issues, and they further note that *"...the greatest*

threat to [the auditor's] independence is a slow, gradual, almost casual erosion of his 'honest disinterestedness.'" (p. 208). Extended associations between the auditor and client can therefore foster the development of 'person-to-person relationships' whereby a bond, loyalty and/or trust can be developed. It is argued that these relationships, no matter whether they are developed intentionally or unintentionally can impact an auditor's objectivity, and therefore audit quality more broadly (Carey & Simnett, 2006; Arel, et al., 2005; Geiger & Raghunandan, 2002).

If closer partner/CEO tenure associations between the auditor and the client are also salient to the determination of audit fees, and in particular fee increases subsequent to initial audit engagements, this may also impact audit effort and hence audit quality. Accordingly, an issue requiring address is whether the audit fee increase subsequent to initial audit engagements is adversely impacted by the tenure of the relation between the auditor and the client and this would provide additional support for regulation mandating auditor rotation. This is reflected in the following hypothesis;

H_2: *As audit partner/CEO tenure increases, there is a reduction in the ability to recover discounts subsequent to initial audit engagements.*

3.3 Research Design

The basic research design evaluates audit fee changes overtime, with controls for discounts on initial audit engagements and audit tenure. This is reflected in the following model which will be used to test the hypotheses;[22]

[22] The following hypothesis implies a fixed effect.

$$AuditFee_{it} = \alpha_0 + \alpha_1 First_{it} + \alpha_2 First_{it} \times AuditFee_{it-1} + \alpha_3 AuditFee_{it-1} + \alpha_4 Audit\_Firm\_Tenure_{it} + \alpha_5 [Audit\_Firm\_Tenure_{it} \times AuditFee_{it-1}] + \alpha_6 Partner/CEO\_Tenure_{it} + \alpha_7 [Partner/CEO\_Tenure_{it} \times AuditFee_{it-1}] + \varepsilon_{it}$$

Where:

$AuditFee_{it}$	:	Audit fee is the fee reported in the financial statements for the conduct of the audit by firm i in year t.
$First_{it}$	:	A dummy variable that has the value 1 if this is the initial engagement year by the auditor, otherwise 0.
$Audit\_Firm\_Tenure_{it}$	:	The number of years the current audit firm has conducted the audit of firm i up to year t.
$Partner/CEO\_Tenure_{it}$	:	The number of years the CEO of firm i and lead audit partner have worked together on preparing that firm's financial reports up to year t.

This is a model in which the prior period audit fee is used as an estimate of next period audit fees. The emphasis is on subsequent period audit fees as these are likely the starting point for the negotiation of audit fees in the subsequent year (rather than audit fees scaled by total assets). $First_{it}$ is included to capture the extent to which discounts on initial audit engagements are determined in terms of dollars and the co-efficient on this variable is expected to be negative. Lagged audit fees are interacted with an indicator variable for initial audit engagements ($First_{it} \times AuditFee_{it-1}$) to capture the extent to which discounting of initial audit engagements represents a proportional reduction in audit fees. The co-efficient on this variable is also expected to be negative. The extent of subsequent audit fee increases is captured by the co-efficient on lagged audit fees ($AuditFee_{it-1}$). If there are fee increases subsequent to initial audit engagements as predicted by H_1 the co-efficient on this variable is expected to be positive. If the increases in audit fees are greatest in the early years of the audit engagement, and the rate of increase slows as audit tenure increases this will be captured by the interaction between lagged audit fee and audit tenure ($Audit\_Firm\_Tenure \times AuditFee_{it-1}$). If the rate of audit fee increases is greatest in

the early years, the co-efficient on this variable will be negative and this would be consistent with the early fee increases subsequent to initial audit engagements. If partner/CEO tenure impacts audit fees, this will be captured by the $Partner/CEO\_Tenure_{it}$ variable if there is a fixed dollar effect and by $Partner/CEO\_Tenure_{it} \times AuditFee_{it-1}$ if there is a proportional (percentage change in audit fees) impact on audit fees.

3.3.1 Tenure variables (Audit Firm Tenure and Partner/CEO Tenure)

Consistent with prior studies (e.g., Lim & Tan, 2010; Gunny, et al., 2010; Ghosh & Moon, 2005; Myers, Myers & Omer, 2003) the cumulative number of years where the audit firm has undertaken the audit of the financial statements of the client firm is determined. This recognises that investment in client firms occurs at the audit firm level. Recognising that contracts for audit engagements are typically for periods of 3 years, and our concern with fee increases during the first audit contract, I measure *Audit Firm Tenure* as a dichotomous variable with the value of 1 if audit tenure is greater than 3 years, and 0 otherwise. The concern here is that discounts should be recoverable in the initial contract period, and that fee increases are less necessary in subsequent periods.

However, *Audit Firm Tenure* is unlikely to capture the closeness of the relationship between the audit staff and client staff. I focus on the relationship between the specific audit engagement partner and the CEO as the most senior executives for the audit firm and the client firm, and who likely have the greatest potential impact on the negotiation of the audit contract. The partner/CEO tenure *(Partner/CEO Tenure)* is measured as the number of years where the

same lead audit partner and the CEO combination have worked together in preparing that firm's audited financial statements.[23]

3.4 Data Collection and Sample Description

The sample firms are identified in the first instance from the *UTS Auditing Database* which contains audit specific information for ASX listed firms (e.g. firm, partner, fees, opinions). To ensure there is sufficient information to determine tenure, firms are required to be listed from 2000 – 2009 inclusive, and information available for each year.[24] This information is matched to the *UTS Who Governs Australia Corporate Governance Database* to obtain CEO details.[25] Firms are deleted if CEO details or audit partner details are missing or cannot be obtained.[26] This identifies a final sample of 688 firms or 3440 firm year observations for the test period which covers the years 2005 - 2009. Details of the sample selection process are outlined in Table 3.1, Panel A. The distribution of firms across two-digit GICS industry sectors is presented in Panel B. The *Materials* sector has the most observations (183 or 26.6%) in the sample, while the fewest number of observations are in the *Utilities* industry (6 or 0.9%). This is reflective of the market and I do not expect this industry distribution to introduce any bias to our results. Panel C summarises the year-end balance dates for firms within our sample and shows

[23] The CEO is identified as per the disclosures in the firm's financial statements at year-end. If a specific CEO is not identified, but an individual holding similar responsibilities (e.g. managing director), this person is included. If no individual is identified as holding either of these roles, the firm is deleted from the sample as per Table 1. When more than one CEO appointment is disclosed during any one year, the CEO at the end of the financial year is counted, as this is the executive likely to be responsible and had control over the accounting policy choices.

[24] An inclusive model from 2000 – 2009 is used in order to more accurately ascertain CEO tenure.

[25] For firms not listed in the UTS-WGACG database, I attempt to hand collect this information from firm annual reports listed on DatAnalysis.

[26] It should be noted that while CEO data is not necessarily required for the testing of hypothesis one, this data is necessary for the testing of hypothesis two. Based on data availability for consistency, the above sample has been selected.

that 584 firms (84.9%) in our sample have a June 30 year-end which is reflective of the Australian reporting environment.

Descriptive statistics are presented in Table 3.2. The mean (median) of total audit fees is $482,748 ($85,000) highlighting the skewness in the population of firms, and audit fees. The mean (median) *Audit Firm Tenure* is 6.57 (7.00) years indicating that audit switches are not frequent. The mean (median) value of *Partner/CEO Tenure* is 1.51 (1.00) which is lower than expected and indicates significant turnover in either audit partners and/or CEO's. There are extreme values and these are relevant to the research question being asked.

Consideration is also given to the composition of auditor switching within the sample, with the results reported in Table 3.2 panels B and C.[27] Panel B reports the proportion of firms audited by Big N auditors by year. On average, 53.46% of firms within the sample are audited by Big N auditors, with the highest proportion occurring in 2006 (54.2%) and the lowest in 2005 (52.8%), and reflects the stability in our sample. Panel C reports percentage switches by year between auditors, including Big N to Big N, Big N to Non-Big N, Non-Big N to Big N and Non-Big N to Non-Big N. The mean (median) percentage of switches across the five years is 9.54% (9.2%), with switches between each grouping fairly evenly spread.

Pearson and Spearman correlations are reported in Table 3.3. By construction there is a high correlation between *Audit_Firm_Tenure* and *Partner/CEO Tenure* (Spearman Corr=0.106, Pearson Corr=0.115).

[27] It should be noted that while this study provides descriptive information on auditor switches, deeper analysis of auditor switches is beyond the scope of this study.

3.5 Results

3.5.1 Audit Fees and Audit Tenure (H_1)

The evaluation of changes in audit fees over the tenure of the audit is addressed in the first instance in Table 3.4. The model is estimated first with lagged audit fees and controls for discounts on initial audit engagements. The co-efficient on *lagged audit fees* is positive and significant (α_3=1.042, *t-stat*=188.681, p=0.000) and is consistent with annual audit fee increases after initial audit engagements of 4.2%. This is likely greater than most increases and is consistent with fee increases subsequent to initial audit engagements (H_1).

Problematically, the results for the controls for initial audit engagements are conflicting. The co-efficient on *First* is negative and significant (α_1=-55,343, *t-stat*=-1.912, p=0.056) which is consistent with discounting by a fixed dollar amount. In contrast the co-efficient on the interaction between *First* and *lagged audit fees* is positive and significant (α_2=0.197, *t-stat*=8.000, p=0.000) which is consistent with proportionately higher audit fees on initial audit engagements. The combined effect, having regard to the mean audit fees is an average increase on initial audit engagements of $29,199, which is inconsistent with discounting. This result is further evaluated below (Table 3.5).

The second column in Table 3.4 extends the analysis to include audit firm tenure. In column two with an auditor tenure variable (i.e., if audit firm tenure < 3 years, *Audit Firm Tenure*=1) the results are much stronger. Critically the co-efficient of *lagged audit fees* is positive, significant, and larger than in column one (α_3=1.079, *t-stat*=75.648, p=0.000), while the co-efficient on the interaction between *audit firm tenure* and *lagged audit fees* is negative and significant (α_5=-0.044, *t-stat*=-2.840, p=0.005). This suggests that audit fees increase more in the two years immediately subsequent to an audit change (+7.9% pa), and more modestly in the

years after that (+3.5%). This is consistent with the predictions of H_1 and discounts on initial audit engagements being recovered.

Discounting is not the focus of this paper, however further analysis was undertaken as the incidence of discounting is central to understanding fee increases subsequent to initial audit engagements. It is expected that fee changes after an auditor switch likely reflect the nature of audit firms involved (e.g., Non Big 4 to Non Big 4, Non Big 4 to Big 4, Big 4 to Non Big 4 and Big 4 to Big 4). Accordingly, the regression in column 1 of Table 3.4 is re-estimated with controls for the nature of the switch (dummy variables for nature of switch and interaction terms with lagged audit fees) and the results are reported in Table 3.5 panel A. For switches between Non Big 4 to Non Big 4 auditors the change in audit fees is captured by the co-efficient on *First* and *First* interacted with *lagged audit fees.* These coefficients (α_1=-8,117, *t-stat*=-0.204, p=0.838 and α_2=-0.385, *t-stat*=-1.497, p=0.134 respectively) are both consistent with discounting and suggest a reduced fee on initial engagements of $173,340 (based on mean lagged audit fee). For switches on Big 4 to Big 4, the combined effects co-efficients (α_4=-63,763, *t-stat*=-0.803, p=0.422 and α_5=0.590, *t-stat*=2.283, p=0.023 respectively) suggest a minimal increase in initial engagement audit fees of $16,096. For firms switching from Big 4 to Non Big 4 the combined effects on co-efficients (α_6=-13,585, *t-stat*=-0.180, p=0.857 and α_7=0.101, *t-stat*=0.317, p=0.752 respectively) suggest a material discounting of initial engagement audit fees of $143,581, while for switches from Non Big 4 to Big 4 the co-efficents (α_8=-68,481, *t-stat*=-0.937, p=0.349 and α_9=0.824, *t-stat*=7.342, p=0.000 respectively) suggest a major increase in initial engagement audit fees of $111,800. These results are generally consistent with expectation and suggest that the observation of discounting may be obscured by the confounding effect of the nature of the audit switch underlying the offsets of changes in audit quality. Further evaluation of this would

require estimation of a cross sectional audit fee model and this is beyond the scope of this paper.[28]

3.5.2 Audit Fees and Audit Tenure and Partner/CEO Tenure (H_2)

Table 3.6 reports the regression results for tests of H_2, which examines the association between the partner/CEO tenure and audit fees. This shows that the co-efficient on lagged audit fees is still significant and greater than one (α_3=1.079, *t-stat*=75.746, p=0.000). The co-efficient on *Audit Firm Tenure* interacted with lagged audit fee is negative and significant (α_5=-0.056, *t-stat*=-3.575, p=0.000). Economically, this suggests that audit fees increase by 7.9% in the first three years of an audit engagement and by only 2.3% in years thereafter. This result is again supportive of H_1. When *Partner/CEO Tenure* is interacted with lagged audit fees the coefficient is positive and significant (α_7=0.056, *t-stat*=3.909, p=0.000). This is inconsistent with H_2, and there is no evidence that longer partner/CEO tenure leads to smaller increases in audit fees. In fact the opposite occurs.

3.5.3 Sensitivity

A number of additional sensitivity tests are undertaken including, re-estimations based on annual samples, audit fee size and different lengths of audit firm tenure.

[28] Discounting is not the focus of this paper, however consideration of auditor switches is an issue which requires address. Therefore, for robustness, results for table 5 are re-estimated and reported including controls for switches individually with results reported in Table 5 panel B. Results are robust with the same key variables of interest remaining statistically significant. In column one, results are re-estimated with the control variable for auditor switches between Big 4 firms (Big 4 to Big 4), the co-efficients (α_4=-55037, *t-stat*=-0.699, p=0.484 and α_5=0.464, *t-stat*=1.794, p=0.073 respectively) are consistent with discounting and suggest a decrease fee on initial engagements.

Annualised Regressions (Appendix 3A)

To determine whether co-efficients are impacted by changes in the audit market, I re-estimate the regressions for H_1 and H_2 on an annual basis. Results are reported in Appendix 3A with results generally robust to this sensitivity. Table 3A.4 reports the annualized effects of changes in audit fees over the tenure of the audit in the first instance. Panel A reports the 2005 pooled sample, and in the first instance (Column 1) the model is estimated first with lagged audit fees and controls for discounts on initial audit engagements with results consistent with main reported results and with fee increases subsequent to initial audit engagements (H_1).

The second column in Table 3A.4 extends the analysis to include audit firm tenure. In the second column the co-efficient on lagged audit fees is positive and significant (α_3=1.455, *t-stat*=6.138, p=0.000). However, the interaction between *audit firm tenure* and *lagged audit fees* is no longer significant (α_5=-0.185, *t-stat*=-0.778, p=0.437).

Panel B reports results for the 2006 year. Interestingly, the results in column one where the model is estimated first with lagged audit fees and controls for discounts on initial audit engagements, the co-efficient on lagged audit fees remains positive and significant (α_3=1.088, *t-stat*=88.650, p=0.00) and is consistent with annual audit fee increases after initial audit engagements of 8.8%. However, the results for the controls for initial audit engagements are conflicting. The co-efficient on *First* is negative but no longer significant (α_1=-10986.803, *t-stat*=-0.167, p=0.867). In contrast the co-efficient on the interaction between *First* and *lagged audit fees* is negative and not significant (α_2=-0.275, *t-stat*=-0.859, p=0.391), which is in contrast to main reported results.

In the second column the results conflict with the main reported tests. While the *lagged audit fee* variable and the interaction of *audit firm tenure* by *lagged audit fee* are both significant at the 1% level, they are also both positive (α_3=0.929, *t-stat*=48.460, p=0.000 and α_5=0.246, *t-stat*=10.328, p=0.000). Furthermore, the interaction variable *first* by *lagged audit fee* is negative and no longer significant (α_2=-0.116, *t-stat*=-0.388, p=0.698).

Panel C results the results for the 2007 year. These are consistent with the main reported results. A similar result is documented in Panel D which accounts for the 2008 year. Once again the interaction variable *audit firm tenure* by *lagged audit fee* is negative and is statistically significant at the 1% level (α_5=-0.321, *t-stat*=-2.747, p=0.000).

Finally, Panel E reports the results for the 2009 year. In column one, the coefficient on lagged audit fees remains positive and significant (α_3=1.051, *t-stat*=161.120, p=0.000) and is consistent with annual audit fee increases after initial audit engagements of 5.1% in 2009. Interestingly, the co-efficient on the *First* variable is positive, but not significant (α_1=62740.310, *t-stat*=1.252, p=0.211), while the interaction between *First* and *lagged audit fee* is negative and significant at the 1% level (α_2=-0.567, *t-stat*=-2.811, p=0.005). The second column results show similar strength to the main results, however of particular interest is the directional change on variables *First* becoming positive (α_1=61326.001, *t-stat*=1.151, p=0.250) and a negative association on the interaction between *First* and *lagged audit fee* (α_2=-0.688, *t-stat*=-3.531, p=0.000) and *audit firm tenure* (α_4=-13,913, *t-stat*=0.000, p=1.000).

Large Versus Small Audit Fees (Appendix 3B)

As an additional sensitivity, consideration is given to audit fee size. Audit fees are split by median audit fee into 'large', above median audit fees, and 'small' below median audit fees. The results are reported in Appendix 3B, Table 3B.4.

Panel A reports the results for large audit fees over the tenure of the audit. Column one reports the model estimated first with lagged audit fees and controls for discount on initial audit engagements. The coefficient on lagged audit fees is positive and significant at the 1% level (α_3=1.036, *t-stat*=129.219, p=0.000) and is consistent with annual audit fee increases after initial audit engagements of 3.6%. This is consistent with audit fee increases subsequent to initial audit engagements (H_1) and this result suggests the discount, on average, is lower for larger firms. Interestingly, the co-efficient on the variable *First* is negative, but not significant (α_1=-102859.836, *t-stat*=-1.507, p=0.132). In contrast, the co-efficient on the interaction between *First* and *lagged audit fees* is positive and significant (α_2=0.204, *t-stat*=5.766, p=0.000) which is consistent with proportionately higher audit fees on initial audit engagements.

In the second column the results are much stronger and consistent with the main reported results. Once again, critically, the co-efficient of lagged audit fees is still positive, significant, and larger than in column one (α_3=1.076, *t-stat*=52.900, p=0.000), while the co-efficient on the interactions between *audit firm tenure* and *lagged audit fee* is negative and significant (α_5=-0.047, *t-stat*=-2.127, p=0.034). This suggests that audit fees increase more in the three years immediately subsequent to an audit change (+7.6% pa), and more modestly in the year after that (+2.9%). This is consistent with the predictions of H_1 and discounts on initial audit engagement being recovered.

Panel B reports the results for small audit fees over the tenure of the audit. Column one, once again reports the model estimated first with lagged audit fees and controls for discounts on initial audit engagements. The coefficient on lagged audit fees is positive and significant at the 1% level (α_3=0.482, *t-stat*=30.179, p=0.000) and is consistent with annual audit fee increases after initial audit engagements. Interestingly, the *First* variable is no longer significant and is positive (α_1=2996.376, *t-stat*=1.552, p=0.121), while the interaction variable between *First* and *lag audit fee* is negative and significant at the 1% level (α_2=-0.187, t stat=-4.958, p=0.000) which is consistent with proportionally lower audit fees on initial audit engagements. However, caution should be exercised in interpreting this results as the model has poor explanatory power (adjusted r^2=0.374).

Column two reports the results of the small median audit fee results incorporating the dichotomous tenure variable. Critically, the co-efficient of lagged audit fees remains positive and significant (α_3=0.560, *t-stat*=15.942, p=0.000), while the co-efficient on the interaction between *audit firm tenure* and *lagged audit fees* is negative and significant (α_5=-0.098, *t-stat*=-2.491, p=0.013). Furthermore, of particular interest for small audit fee firms, *First* variable is positive and significant at the 1% level (α_1=6417.167, *t-stat*=2.715, p=0.007), while the interaction of *First* and *lag audit fee* is negative and significant at the 1% level (α_2=-0.265, *t-stat*=-5.402, p=0.000). Once again, caution should be exercised in interpreting this result given the poor explanatory power of both models (adjusted r^2=0.374 and 0.376 respectively).

For robustness, consideration is also given to the impact of audit fee size on the association between partner/CEO tenure and audit fees. Audit fees are split by median audit fee into 'large', upper median audit fees, and 'small' lower median audit fees and results are reported in Table 3B.6. Panel A reports the results for large audit fees over the audit firm tenure

and partner/CEO tenure. Importantly, this shows that the co-efficient on *lagged audit fees* is still significant and greater than one (α_3=1.023, *t-stat*=42.846, p=0.000). The co-efficient on *audit firm tenure* interacted with *lagged audit fee* is negative and significant (α_5=-0.054, *t-stat*=-2.460, p=0.014). Economically, this suggests that audit fees increase by 2.3% in the first three years of an audit engagement and but actually decrease in the years thereafter for firms with larger audit fees. When *Partner/CEO tenure* is interacted with *lagged audit fees* the coefficient is positive and significant (α_7=0.022, *t-stat*=4.192, p=0.000).

Panel B reports the results for small audit fees over the *Partner/CEO tenure*. This shows that the co-efficient on *lagged audit fees* is still significant, however it is less than one (α_3=0.546, *t-stat*=14.239, p=0.000), while the co-effiicient on *Audit Firm Tenure* interacted with *lagged audit fee* is negative and significant (α_5=-0.103, *t-stat*=-2.0587, p=0.010). When *Partner/CEO Tenure* is interacted with *lagged audit fees* the co-efficient is positive but not significant (α_7=0.005, *t-stat*=0.673, p=0.501).

Dichotomous Audit Firm Tenure Variables of Five Years (Appendix 3C)

This chapter utilised a dichotomous tenure variable where if audit firm tenure was greater than three years, *audit firm tenure* would be equal to one. While three years was selected as a basis given anecdotal evidence that audit contracts are set over a three year time horizon. However for robustness I also consider a five year alternative time horizon. Therefore, I re-estimate results for the main tests (tables 4, 6 and 7) employing a dichotomous tenure variable of 5 years, i.e. if audit firm tenure > 5 years, *audit firm tenure*=1. Results are reported in Appendix 3.C, Table 7. The first column reports results for the *audit firm tenure* model. The results are

much weaker. The co-efficient on lagged audit fees in the first instance is positive and significant (α_3=1.014, *t-stat*=98.781, p=0.000). The co-efficient on the interaction between *audit firm tenure* and *lagged audit fees* is also positive and significant (α_5=0.004, *t-stat*=3.132, p=0.000).

Column two reports results for tests of H_2, which examines the association between *Partner/CEO tenure* and audit fees, with the 5 year dichotomous variable for *audit firm* tenure. Importantly, this result shows that the co-efficient on *lagged audit fees* is still significant and greater than one (α_3=1.014, *t-stat*=98.723, p=0.000). The co-efficient on *Audit Firm Tenure* interacted with *lagged audit fee* is positive and remains significant (α_5=0.004, *t-stat*=3.119, p=0.002). Economically, this suggests that audit fees increase by 1.4% in the first five years of an audit engagement and by 1.44% in the years thereafter. This result provides some support for H_1. When *Partner/CEO Tenure* is interacted with *lagged audit fees* the coefficient is positive, but no longer significant (α_7=0.086, *t-stat*=0.417, p=0.677) which is provides no support for H_2.

3.6 Conclusion

A major concern for practitioners, regulators and academics is whether discounting of fees on initial audit engagements results in reduced audit effort and reduced audit quality. These concerns would be ameliorated if there was evidence of audit fee increases in subsequent years which would indicate fee increases. This is addressed by evaluating changes in fees subsequent to initial audit engagements in Australia over the period 2005-2009.

Evidence is provided of audit fee increases in years subsequent to the initial audit engagement and these are greatest in the three years immediately following a switch which corresponds with the typical term of initial audit contracts. These increases are in the order of

8% p.a. and are materially greater than the cost increases likely experienced by the audit firms. This suggests that there is audit fee increases subsequent to initial audit engagements and concerns that discounting might result in poorer quality audits are likely misplaced. As audit firm tenure extends there is evidence of a decline in the rate of increase in audit fees, and after three years the rate of increase slows to about 3% p.a. This is broadly consistent with price changes and suggests that there are significant competitive pressures which constrain audit fee increases.

While there is evidence of audit fee increases generally, which suggest that discounting is not problematic, there are constraints. In particular do partner/CEO relations inhibit audit fee increases? There is no evidence of longer partner/CEO tenure inhibiting audit fee increases. On the contrary, there is some evidence of greater audit fee increases after the period of the initial audit contract and this would suggest there may be over servicing of clients. Accordingly, there is no support for auditor rotation due to concerns that extended tenure inhibits audit fee increases and reduces audit quality.

This chapter is limited in four ways which also provide avenues for future research. First, this chapter does not take into consideration 'big' events which may impact the level of audit fees paid by a firm. For example, a number of significant events could impact the level of audit fees such as mergers and/or acquisitions, joint-ventures and accounting policy changes. Furthermore, the economic conditions facing firms across the sample period (e.g. the Global Financial Crisis) are not considered given the scope and data limitations of this chapter, I leave this for future research to explore. Second, this chapter does not take into account measures of auditor industry specialisation. Due to the difficulty in obtaining data relating to auditor specialisation for the sample, this is left for future research to examine. Third, the proxy for person-to-person relationship (*Partner/CEO_Tenure*) is a noisy measure and may not accurately

encompasses all facets of changes in audit fees related to person-to-person relationships, but rather contribute to our understanding by providing a 'second order effect' on audit fees. Finally, this chapter does not examine alternatives for the impact of earnings quality measures. While earnings quality is a fundamental aspect of many audit studies, addressing this issue is beyond the scope of this thesis and therefore the issue is left for future research to examine.

Table 3.1
Sample Selection and Industry Breakdown

Panel A: Sample Process	
ASX Listed Firms	990
Less:	
Firms not continuously listed over the sample period	198
Firms without annual reports for more than one year	20
Firms missing CEO or Partner Information	84
TOTAL FINAL SAMPLE	**688**

Panel B: GICS Sector Breakdown		
Sector	**Number**	**Percentage**
10: Energy	61	8.7%
15: Material	183	26.6%
20: Industrials	86	12.5%
25: Consumer Discretionary	81	11.8%
30: Consumer Staples	23	3.3%
35: Health Care	60	8.7%
40: Financials	114	16.6%
45: Information Technology	63	9.2%
50: Telecommunication	11	1.6%
55: Utilities	6	0.9%
TOTAL	**688**	**100%**

Panel C: Sample Firm Balance Dates	
Balance Date	**Number of Firms**
28 Feb	2
31 March	4
30 April	1
31 May	1
30 June	584
31 July	8
31 August	5
30 September	9
31 December	74
Total	**688**

Table 3.2
Descriptive Statistics

Panel A: Descriptive Statistics

obs=3440; n=688	**Mean (Median)**	**Std. Deviation**	**Minimum**	**Maximum**
CEO Tenure	5.26 (4.00)	3.46	1	10
Partner Tenure	2.41 (2.00)	1.33	1	10
Audit Firm Tenure	6.57 (7.00)	3.41	1	10
Partner/CEO Tenure	1.51 (1.00)	1.44	0	10
Total Audit Fees	482,748 (85,000)	1,751,198.70	0	24,947,000
Lag Total Audit Fees	429,151 (72,485)	1,593,829.12	0	24,947,000

Where:

$AuditFee_{it}$: Audit fee is the fee reported in the financial statements for the conduct of the audit by firm i in year t.

$First_{it}$: A dummy variable that has the value 1 if this is the initial engagement year by the auditor, otherwise 0.

$Audit\_Firm\_Tenure_{it}$: The number of years the current audit firm has conducted the audit of firm i up to year t.

$Partner/CEO\_Tenure_{it}$: The number of years the CEO of firm i and lead audit partner have worked together on preparing that firm's financial reports up to year t.

Table 3.2 (continued)
Descriptive Statistics

Panel B: Proportion audited by Big N Firms by Year		
n=688		
Year	**Number of firms audited by Big N Auditors**	**Percentage Audited by Big N auditors**
2005	364	52.80%
2006	372	54.20%
2007	369	53.60%
2008	369	53.80%
2009	364	52.90%

Panel C: Switches by year					
n=688	**Percentage of Switches during Year**	**No Change**	**Downgrade**	**Upgrade**	**No change**
Year		**B4 → B4 (1)**	**B4 → NB4 (2)**	**NB4 → B4 (3)**	**NB4 → NB4**
2005	8.10%	1.50%	2.80%	1.00%	2.90%
2006	10.50%	1.70%	2.00%	3.60%	3.10%
2007	12.10%	1.60%	2.30%	1.90%	6.30%
2008	9.20%	1.50%	1.00%	1.00%	5.70%
2009	7.80%	1.20%	2.30%	1.50%	2.90%

Table 3.3
Correlation Matrix – Pearson and Spearman

	Audit Firm Tenure	*Partner/CEO_Tenure*
Audit_Firm_Tenure	1.000	**0.106**** (0.000)
Partner/CEO_Tenure	**0.115**** (0.000)	1.000

Pearson correlations are below diagonal and Spearman correlations are above diagonal.
All variables as previously defined
All results are One-tailed tests
** correlation is significant at the 0.001 level
* correlation is significant at the 0.005 level

Table 3.4
Evaluating Audit Fees over Audit Tenure

obs=3440; n=688	*Dichotomous Variables 1-3years*							
	Co-efficient	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	37159.927	3.963	0.000	***	22368.866	1.104	0.270	
First	-55343.124	-1.912	0.056	*	-40554.574	-1.191	0.234	
First*AuditFee$_{t-1}$	0.197	8.000	0.000	***	0.160	5.734	0.000	***
AF$_{t-1}$	1.042	188.681	0.000	***	1.079	75.648	0.000	***
Audit_Firm_Tenure					19901.003	0.871	0.384	
Audit_Firm_Tenure * AuditFee$_{t-1}$					-0.044	-2.840	0.005	**
Adjusted R	0.918				0.918			
F-stat	12782.332		0.000	***	7684.873		0.000	***

Where:

$$AuditFee = \alpha_0 + \alpha_1 AF_{t-1} + \alpha_2 Audit\_Firm\_Tenure_{it} + \alpha_3 \left[Audit\_Firm\_Tenure \times AuditFee_{t-1} \right] + \varepsilon$$

And:

AuditFee$_{it}$: Audit fee is the fee reported in the financial statements for the conduct of the audit by firm i in year t.

First$_{it}$: A dummy variable that has the value 1 if this is the initial engagement year by the auditor, otherwise 0.

Audit_Firm_Tenure$_{it}$: 1 if the number of years the current audit firm has conducted the audit of firm i up to year t is greater than 3, 0 otherwise.

Partner/CEO_Tenure$_{it}$: The number of years the CEO of firm i and lead audit partner have worked together on preparing that firm's financial reports up to year t.

All variables as previously defined and reported as two-tailed

*** : Denotes significance at the 1% level

** : Denotes significance at the 5% level

* : Denotes significance at the 10% level

Table 3.5
Nature of Firm Switches

Panel A: Pooled Switches				
obs = 3440	*Lag Audit Fee Continuous Variable*			
	Co-efficient	**t-stat**	**p-value**	
Constant	36336.267	3.900	0.000	***
First	-8117.375	-0.204	0.838	
FIRST * $AuditFee_{t-1}$	-0.385	-1.497	0.134	
AF_{t-1}	1.040	189.625	0.000	***
Dummy B4-B4	-63763.004	-0.803	0.422	
DummyB4-B4 * AF_{t-1}	0.590	2.283	0.023	**
Dummy B4-NB4	-13585.551	-0.180	0.857	
DummyB4-NB4 * AF_{t-1}	0.101	0.317	0.752	
Dummy NB4-B4	-68481.396	-0.937	0.349	
DummyNB4-B4 * AF_{t-1}	0.824	7.342	0.000	***
Adjusted R	0.919			
F-stat	4334.237		0.000	***

Where:

$$AuditFee = \alpha_0 + \alpha_1 AF_{t-1} + \alpha_2 Audit\_Firm\_Tenure_{it} + \alpha_3 [Audit\_Firm\_Tenure \times AuditFee_{t-1}] + \alpha_4 DummyB4B4 + \alpha_5 [DummyB4B4 \times AuditFee_{t-1}] + \alpha_6 DummyB4NB4 + \alpha_7 [DummyB4NB4 \times AuditFee_{t-1}] + \alpha_8 DummyNB4B4 + \alpha_9 [DummyNB4B4 \times AuditFee_{t-1}] \varepsilon$$

Table 3.5 (continued)
Nature of Firm Switches

Panel B: Pooled Switches (Upgrades/Downgrades)

obs = 3440

	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	37248.275	3.972	0.000	***	37224.334	3.967	0.000	***	36349.704	3.903	0.000	***
First	-17385.697	-0.478	0.633		-54574.468	-1.754	0.080	*	-55638.053	-1.853	0.064	*
FIRST * $AuditFee_{t-1}$	-0.261	-1.013	0.311		0.197	7.987	0.000	***	0.198	8.096	0.000	***
AF_{t-1}	1.042	188.711	0.000	***	1.042	188.614	0.000	***	1.040	189.616	0.000	***
Dummy B4-B4	-55037.192	-0.699	0.484									
Dummy B4-B4xAF_{t-1}	0.464	1.794	0.073	*								
Dummy B4-NB4					-5549.198	-0.074	0.941					
Dummy B4-NB4xAF_{t-1}					-0.004	-0.011	0.991					
Dummy NB4-B4									-75530.992	-1.056	0.291	
Dummy NB4-B4xAF_{t-1}									0.812	7.244	0.000	***
Adjusted R	0.918				0.918				0.919			
F-stat	7672.940		0.000	***	7665.058		0.000	***	7797.850		0.000	***

Where:

DummyB4-B4 : A dummy variable that represents a switch in a prior year from a Big 4 firm to another Big 4 firm, being 1 if there is a switch and zero otherwise.

Dummy B4-B4xAF_{t-1} : Represents the *DummyB4-B4* variable times lagged audit fee

Dummy B4-NB4 : A dummy variable that represents a switch from a Big 4 auditor to a Non-Big 4 auditor, being 1 if there is a switch and zero otherwise.

Dummy B4-NB4xAF$_{t-1}$	:	Represents the *Dummy B4-NB4* variable times lagged audit fee
Dummy NB4-B4	:	A dummy variable that represents a switch from a Non-Big 4 auditor to a Big 4 auditor, being 1 if there is a switch and zero otherwise.
Dummy NB4-B4xAF$_{t-1}$	:	Represents the *Dummy NB4-B4* variable times lagged audit fee.

All variables as previously defined and reported as two-tailed

***	:	Denotes significance at the 1% level
**	:	Denotes significance at the 5% level
*	:	Denotes significance at the 10% level

Table 3.6
Association between Partner/CEO tenure and audit fees

obs=3440; n=688	*Dichotomous 1-3years*			
	Co-efficient	**t-stat**	**p-value**	
Constant	23448.993	1.157	0.247	
First	-41049.436	-1.208	0.227	
First * AuditFee$_{t-1}$	0.160	5.745	0.000	***
AF$_{t-1}$	1.079	75.786	0.000	***
Audit_Firm Tenure	25173.645	1.083	0.279	
Audit_ Firm Tenure * AuditFee$_{t-1}$	-0.056	-3.575	0.000	***
Partner/CEO Tenure	-25572.096	-1.081	0.280	
Partner/CEO Tenure * AuditFee$_{t-1}$	0.056	3.909	0.000	***
Adjusted R	0.918			
F-stat	5512.610		0.000	***

Where;

$$AuditFee_{it} = \alpha_0 + \alpha_1 First_{it} + \alpha_2 First_{it} \times AuditFee_{it-1} + \alpha_3 AuditFee_{it-1} + \alpha_4 Audit\_Firm\_Tenure_{it} + \alpha_5 [Audit\_Firm\_Tenure_{it} \times AuditFee_{it-1}] + \alpha_6 Partner/CEO\_Tenure_{it} + \alpha_7 [Partner/CEO\_Tenure_{it} \times AuditFee_{it-1}] + \varepsilon_{it}$$

AuditFee$_{it}$: Audit fee is the fee reported in the financial statements for the conduct of the audit by firm i in year t.

First$_{it}$: A dummy variable that has the value 1 if this is the initial engagement year by the auditor, otherwise 0.

Audit_Firm_Tenure$_{it}$: 1 if the number of years the current audit firm has conducted the audit of firm i up to year t is greater than 3, 0 otherwise.

Partner/CEO_Tenure$_{it}$: The number of years the CEO of firm i and lead audit partner have worked together on preparing that firm's financial reports up to year t.

All variables as previously defined and reported as two-tailed

*** : Denotes significance at the 1% level

** : Denotes significance at the 5% level

* : Denotes significance at the 10% level

Chapter 4
Conclusions

This thesis expands on current knowledge of the factors impacting audit quality by providing evidence which evaluates the extent to which auditor-client relations and discounting subsequent to initial audit engagements undermines audit quality. In response to anecdotal evidence that a lack of auditor independence contributed to corporate failures, many countries adopted regulation that prescribed auditor rotation. The objective of Chapter 2 was to provide evidence of any association between auditor tenure and audit quality which would support auditor rotation being prescribed. Auditor tenure is measured having regard to both the person-to-person relationships and professional relations which exist between the audit firm and the client firm, with these having differing impacts on audit quality. Audit quality is measured by IFRS adoption errors. Based on a sample of 151 firms during the IFRS adoption period, there was no evidence that person-to-person relationships undermine audit quality. Separately, I find no significant association between IFRS adoption errors and the length of tenure between audit partners and the CEO of the client firm were indicated. Interestingly, a significant negative association was documented between the measures of audit quality (IFRS adoption errors) and the length of audit firm tenure. Ultimately, these results present no empirical evidence for longer auditor tenure undermining audit quality and no support for regulation prescribing auditor rotation.

Concern has been raised by regulators and others that discounting reduces audit fees, which leads to constraints on audit effort. Chapter 3 seeks to provide empirical evidence of changes in audit fees subsequent to initial audit engagements. Specifically, evidence is provided of audit fees increasing by almost 8% p.a. in the years immediately following an initial audit engagement with the rate of increase declining to 3% p.a. in subsequent years. Moreover, no

evidence is provided that close relations between the audit partner and the CEO limits audit fee increases. Ultimately, this suggests that concerns by regulators and others about discounting undermining audit quality are largely misplaced and the impacts of discounting initial audit engagements are ameliorated by subsequent audit fees.

This thesis makes a number of contributions to the literature. First, this thesis contributes to the regulatory debate surrounding mandatory auditor rotation within Australia. This thesis finds no support for mandatory auditor rotation based on concerns that extended tenure inhibits audit fee increases and therefore reduces audit quality. This research should lead to a more informed debate on mandatory auditor rotation in Australia, while also providing international insights to rotation policy based on Australian experiences. Second, this thesis extends the literature on the relation between audit quality and audit pricing. It provides valuable information on audit pricing, and to some extent competition, in an Australian context over a period which is characterized by limited rigorous academic research and increasing uncertainty concerning audit pricing (King, 2011a; Niven, 2010). Third, this thesis adopts a novel approach to the examination and measurement of auditor tenure. It provides a new approach in examining the multidimensional nature and differing aspects of audit relations by examining auditor tenure from a person-to-person relationship (*Partner/CEO tenure*) perspective. Regard is given to both the person-to-person relationships and professional relations that exist between the audit firm and client firm, with these having potentially differing impacts on audit quality. Fourth, this is the only Australian research, of which I am aware, that evaluates audit fee changes overtime using a time-series approach. Traditionally, prior research examining audit fee changes has relied upon a cross-sectional model, with relatively little attention directed towards time-series data. While cross-sectional models have been a valuable source, the results of these studies could be

unreliable if audit contracts are set on a multi-year basis with under-pricing in year one which is offset by over-pricing in subsequent years. This thesis contributes to the debate surrounding discounts on initial audit engagements and provides new insights into fee discounting in the Australian market.

This thesis has a number of limitations which also present opportunities for future research. First, the proxy for person-to-person relationship is noisy and does not directly capture the traditional notion of 'relationship' presented in research in related disciplines. Furthermore, the auditor-client relation measure (*Partner/CEO Tenure*) is a subset of the control variable professional relation (*Audit Firm Tenure*), which further compounds the above issue. However, this is a consequence of data limitations and in this instance the best available information is used to gain initial insights into this measure. This presents an opportunity for future research to adopt alternative research methods to further specify the measure. Second, the reliance on IFRS errors as a proxy for audit quality in chapter two is non-traditional measure. While this IFRS errors is a valuable an innovative measure for audit quality, its limited examination in extant literature gives rise to its validity as an effective proxy for audit quality. Third, this thesis does not consider alternative specifications for earnings quality or the impact of auditor specialisation. While this thesis adopted a total accruals measure to proxy for audit quality, there are alternative methods available to classify accrual measures which have not been considered. This is also the case with examining alternatives for the impact of earnings quality. While earnings quality is a fundamental aspect of many audit studies, further addressing this issue is represents a data limitation and is beyond the scope of this thesis. However, addressing these alternatives could provide for avenues of future research. Finally, this thesis does not account for 'big' events which may impact the auditor client relationship and the level of fees paid by a firm. For

example, a number of significant events such as mergers and/or acquisitions, joint-ventures and accounting policy change could influence results. Due to data availability constraints this is left for future research to explore.

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CHAPTER TWO APPENDICIES

For continuity, the tables in the following appendices are not sequential, and instead follow the main results tables as set out in chapter two.

APPENDIX 2A: IFRS Variations

Table 2A.7

Tests of association between rank absolute IFRS errors and tenure

This table presents the results of tests of association of rank absolute IFRS errors and various measures of auditor tenure. Panel A presents the results for the full sample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for subsample of firms, taking the lower and upper thirds of rank absolute IFRS errors using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of rank absolute IFRS errors for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Ranked Absolute IFRS Errors

n=151	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	110.979	8.028	0.000	***	92.79	3.453	0.001	***
Partner/CEO_Tenure	2.923	1.142	0.128		3.585	1.370	0.087	*
Audit_Firm_Tenure	-2.912	-1.464	0.073	*	-2.074	-0.987	0.163	
Market Cap					0.000	0.172	0.432	
LEV					-2.475	-0.335	0.369	
ROA					-22.434	-0.263	0.300	
LOSS					9.490	0.519	0.302	
Audit Big N					16.902	1.183	0.120	
Adjusted R^2	0.005				-0.005			
F-stat	1.374		0.256		0.887		0.519	

Panel B: Ranked Absolute IFRS Errors with restricted definition of Partner/CEO Tenure

n=151	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	114.893	8.343	0.000	***	98.262	3.612	0.000	***
Partner/CEO_Tenure*	-0.007	-0.003	0.499		0.524	0.221	0.413	
Audit_Firm_Tenure	-2.302	-1.191	0.118		-1.458	-0.707	0.241	
Market Cap					0.000	0.126	0.450	
LEV					-2.61	-0.351	0.363	
ROA					-14.514	-0.341	0.367	
LOSS					9.989	0.539	0.296	
Audit Big N					15.979	1.109	0.135	
Adjusted R^2	-0.004				-0.018			
F-stat	0.715		0.491		0.618		0.741	

Table 2A.7 (continued)
Tests of association between rank absolute IFRS errors and tenure

Panel C: Ranked Absolute IFRS Errors (Ranked Thirds)								
n=102	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	112.949	5.711	0.000	***	86.597	2.151	0.017	**
Partner/CEO_Tenure	3.719	1.029	0.153		4.107	1.100	0.137	
Audit_Firm_Tenure	-3.462	-1.224	0.112		-2.504	-0.793	0.215	
Market Cap					0.001	0.224	0.412	
LEV					-1.685	-0.150	0.441	
ROA					-15.711	-0.222	0.412	
LOSS					-12.124	0.427	0.336	
Audit Big N					23.398	1.104	0.136	
Adjusted R^2	0.001				-0.027			
F-stat	1.042		0.356		0.616		0.742	

Panel D: Ranked Absolute IFRS Errors (Ranked Thirds) with restricted definition of Partner/CEO Tenure								
n=102	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	119.515	6.107	0.000	***	94.156	2.310	0.012	**
Partner/CEO_Tenure*	-0.655	-0.206	0.419		-0.109	-0.033	0.487	
Audit_Firm_Tenure	-2.733	-0.984	0.164	*	-1.789	-0.575	0.284	
Market Cap					0.000	0.099	0.461	
LEV					-1.852	-0.164	0.435	
ROA					-5.669	-0.080	0.468	
LOSS					12.785	0.442	0.330	
Audit Big N					22.734	1.065	0.145	
Adjusted R^2	-0.009				-0.041			
F-stat	0.529		0.591		0.438		0.876	

All variables as previously defined and reported as one-tailed
*** : Denotes significance at the 1% level
** : Denotes significance at the 5% level
* : Denotes significance at the 10% level

APPENDIX 2B: Corporate Governance

Table 2B.4

Tests of association between absolute IFRS errors, tenure and audit committee governance

This table presents the results of tests of association of absolute IFRS errors, various measures of auditor tenure and an audit committee governance dummy variable. Panel A presents the results for the full sample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for subsample of firms, taking the lower and upper thirds of absolute IFRS errors using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of absolute IFRS errors for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Absolute IFRS Errors (Corporate Governance)

n=151	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.072	3.033	0.002	***	0.019	0.430	0.334	
Partner/CEO_Tenure	0.000	0.112	0.456		0.002	0.492	0.312	
Audit_Firm_Tenure	0.005	-1.611	0.055	*	-0.003	-0.953	0.171	
Market Cap					0.000	-0.449	0.327	
LEV					0.000	0.004	0.499	
ROA					-0.001	-0.011	0.496	
LOSS					0.062	2.050	0.021	**
Audit Big N					0.023	0.951	0.172	
AC_Gov_Dummy					0.027	1.371	0.087	*
Adjusted R^2	0.005				0.042			
F-stat	1.354		0.261		1.832		0.076	*

Panel B: Absolute IFRS Errors (Corporate Governance) with restricted definition of Partner/CEO Tenure

n=151	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.076	3.248	0.001	***	0.025	0.560	0.289	
Partner/CEO_Tenure*	-0.003	-0.734	0.232		-0.001	-0.197	0.422	
Audit_Firm_Tenure	-0.005	-1.570	0.060	*	-0.003	-0.852	0.198	
Market Cap					0.000	-0.457	0.325	
LEV					0.000	-0.017	0.494	
ROA					0.003	0.049	0.481	
LOSS					0.062	2.008	0.024	**
Audit Big N					0.021	0.899	0.185	
AC_Gov_Dummy					0.027	1.349	0.090	*
Adjusted R^2	0.008				0.041			
F-stat	1.621		0.201		1.804		0.081	*

Table 2B.4 (continued)

Tests of association between absolute IFRS errors, tenure and audit committee governance

Panel C: Absolute IFRS Errors (Corporate Governance, Rank Thirds)								
n=102	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	0.095	2.814	0.003	***	-0.016	-0.248	0.402	
Partner/CEO_Tenure	0.000	0.016	0.494		0.002	0.269	0.395	
Audit_Firm_Tenure	-0.007	-1.433	0.078	*	-0.002	-0.373	0.355	
Market Cap					0.000	-0.444	0.329	
LEV					0.009	0.469	0.320	
ROA					-0.024	-0.205	0.419	
LOSS					0.080	1.724	0.044	**
Audit Big N					0.048	1.387	0.085	*
AC_Gov_Dummy					0.033	1.171	0.123	
Adjusted R^2	0.002				0.044			
F-stat	1.079		0.344		1.587		0.139	

Panel D: Absolute IFRS Errors (Corporate Governance, Rank Thirds) with restricted definition of Partner/CEO Tenure								
n=102	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	0.101	3.076	0.002	***	-0.008	-0.125	0.451	
Partner/CEO_Tenure*	-0.005	-0.912	0.182		-0.002	-0.388	0.350	
Audit_Firm_Tenure	-0.006	-1.386	0.085	*	-0.002	-0.323	0.374	
Market Cap					0.000	-0.458	0.324	
LEV					0.008	0.457	0.325	
ROA					-0.021	-0.182	0.428	
LOSS					0.078	1.657	0.051	*
Audit Big N					0.047	1.360	0.089	*
AC_Gov_Dummy					0.033	1.161	0.125	
Adjusted R^2	0.010				0.045			
F-stat	1.504		0.227		1.598		0.136	

Where:

AC_Gov_Dummy: Indicator variable set to equal zero if the firm has establish an all non-executive and majority independent, audit committee, and 1 otherwise.

All variables as previously defined and reported as one-tailed

*** : Denotes significance at the 1% level

** : Denotes significance at the 5% level

* : Denotes significance at the 10% level

Table 2B.5

Tests of association between signed IFRS errors, tenure and audit committee governance

This table presents the results of tests of association of signed IFRS errors, various measures of auditor tenure and an audit committee governance dummy variable. Panel A presents the results for the full sample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for subsample of firms, taking the lower and upper thirds of signed IFRS errors using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of signed IFRS errors for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Signed IFRS Errors (Corporate Governance)

n=151	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	-0.045	-2.538	0.006	***	-0.071	-2.073	0.020	**
Partner/CEO_Tenure	0.001	0.214	0.416		0.001	0.380	0.352	
Audit_Firm_Tenure	0.005	2.019	0.023	**	0.005	1.854	0.033	**
Market Cap					0.000	0.557	0.290	
LEV					0.012	1.222	0.112	
ROA					-0.045	-0.831	0.204	
LOSS					-0.003	-0.129	0.449	
Audit Big N					0.004	0.218	0.414	
Ac_Gov_Dummy					0.007	0.469	0.320	
Adjusted R^2	0.018				-0.003			
F-stat	2.345		0.099	*	0.944		0.482	

Panel B: Signed IFRS Errors (Corporate Governance) with restricted definition of Partner/CEO Tenure

n=151	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	-0.043	-2.471	0.008	***	-0.068	-1.962	0.026	**
Partner/CEO_Tenure*	0.000	-0.160	0.437		0.000	-0.129	0.449	
Audit_Firm_Tenure	0.005	2.161	0.016	**	0.005	1.993	0.024	**
Market Cap					0.000	0.549	0.292	
LEV					0.011	1.205	0.115	
ROA					-0.043	-0.790	0.216	
LOSS					-0.003	-0.144	0.443	
Audit Big N					0.003	0.181	0.428	
Ac_Gov_Dummy					0.007	0.454	0.326	
Adjusted R^2	0.017				-0.004			
F-stat	2.335		0.100	*	0.927		0.496	

Table 2B.5 (continued)

Tests of association between signed IFRS errors, tenure and audit committee governance

Panel C: Signed IFRS Errors (Corporate Governance, Rank Thirds)

n=102	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	-0.059	-2.417	0.009	***	-0.098	-1.916	0.029	**
Partner/CEO_Tenure	0.001	0.233	0.409		0.001	0.163	0.436	
Audit_Firm_Tenure	0.007	1.844	0.034	**	0.007	1.751	0.042	**
Market Cap					0.000	0.596	0.277	
LEV					0.019	1.355	0.090	*
ROA					-0.064	-0.820	0.207	
LOSS					-0.013	-0.385	0.351	
Audit Big N					0.004	0.131	0.448	
Ac_Gov_Dummy					0.012	0.524	0.301	
Adjusted R^2	0.020				-0.008			
F-stat	2.040		0.135		0.906		0.515	

Panel D: Signed IFRS Errors (Corporate Governance, Rank Thirds) with restricted definition of Partner/CEO Tenure

n=102	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	-0.057	-2.323	0.011	**	-0.092	-1.762	0.041	**
Partner/CEO_Tenure*	-0.001	-0.147	0.442		-0.002	-0.321	0.375	
Audit_Firm_Tenure	0.007	2.012	0.024	**	0.007	1.869	0.033	**
Market Cap					0.000	0.601	0.275	
LEV					0.020	1.385	0.085	*
ROA					-0.064	-0.830	0.205	
LOSS					-0.016	-0.439	0.331	
Audit Big N					0.001	0.033	0.487	
AC_Gov_Dummy					0.011	0.479	0.317	
Adjusted R^2	0.020				-0.007			
F-stat	2.024		0.138		0.916		0.507	

All variables as previously defined and reported as one-tailed

*** : Denotes significance at the 1% level

** : Denotes significance at the 5% level

* : Denotes significance at the 10% level

Table 2B.6

Tests of association between rank signed IFRS errors, tenure and audit committee governance

This table presents the results of tests of association of rank signed IFRS errors, various measures of auditor tenure and an audit committee governance dummy variable. Panel A presents the results for the full sample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for subsample of firms, taking the lower and upper thirds of rank signed IFRS errors using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of rank signed IFRS errors for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Rank Signed IFRS Errors (Corporate Governance)

n=151	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	54.247	5.008	0.000	***	32.151	1.632	0.053	*
Partner/CEO_Tenure	0.146	0.073	0.471		0.516	0.254	0.400	
Audit_Firm_Tenure	3.244	2.081	0.020	**	3.333	2.034	0.022	**
Market Cap					0.001	1.676	0.048	**
LEV					3.779	0.657	0.256	
ROA					-15.331	-0.460	0.323	
LOSS					2.416	0.170	0.433	
Audit Big N					7.024	0.632	0.264	
Ac_Gov_Dummy					17.109	1.864	0.032	**
Adjusted R^2	0.018				0.023			
F-stat	2.380		0.096	*	1.446		0.183	

Panel B: Rank Signed IFRS Errors (Corporate Governance) with restricted definition of Partner/CEO Tenure

n=151	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	55.796	5.199	0.000	***	37.397	1.777	0.039	**
Partner/CEO_Tenure*	-1.065	-0.590	0.278		-0.925	-0.506	0.307	
Audit_Firm_Tenure	3.356	2.228	0.014	**	3.469	2.170	0.016	**
Market Cap					0.001	1.686	0.047	**
LEV					3.604	0.627	0.266	
ROA					-14.633	-0.443	0.329	
LOSS					1.509	0.105	0.458	
Audit Big N					6.320	0.568	0.286	
Ac_Gov_Dummy					16.881	1.840	0.034	**
Adjusted R^2	0.020				0.025			
F-stat	2.557		0.081	*	1.472		0.173	

Table 2B.6 (continued)
Tests of association between rank signed IFRS errors, tenure and audit committee governance

Panel C: Rank Signed IFRS Errors (Corporate Governance, Rank Thirds)

n=102	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	49.044	3.277	0.001	***	14.177	0.463	0.322	
Partner/CEO_Tenure	-0.104	-0.036	0.486		0.040	0.014	0.495	
Audit_Firm_Tenure	4.192	1.919	0.029	**	4.377	1.943	0.028	**
Market Cap					0.001	1.533	0.065	*
LEV					9.375	1.090	0.140	
ROA					-22.796	-0.491	0.312	
LOSS					-1.790	-0.086	0.466	
Audit Big N					10.914	0.606	0.273	
Ac_Gov_Dummy					23.852	1.793	0.038	**
Adjusted R^2	0.019				0.029			
F-stat	2.001		0.141		1.373		0.219	

Panel D: Rank Signed IFRS Errors (Corporate Governance, Rank Thirds) with restricted definition of Partner/CEO Tenure

n=102	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	51.503	3.452	0.001	***	19.084	0.612	0.271	
Partner/CEO_Tenure*	-1.895	-0.699	0.243		-1.643	-0.577	0.283	
Audit_Firm_Tenure	4.272	2.050	0.022	**	4.436	2.041	0.022	**
Market Cap					0.001	1.552	0.062	*
LEV					9.581	1.119	0.133	
ROA					-24.745	-0.535	0.297	
LOSS					-3.747	-0.177	0.430	
Audit Big N					8.470	0.463	0.322	
AC_Gov_Dummy					22.939	1.716	0.045	**
Adjusted R^2	0.024				0.032			
F-stat	2.254		0.110		1.420		0.199	

All variables as previously defined and reported as one-tailed
*** : Denotes significance at the 1% level
** : Denotes significance at the 5% level
* : Denotes significance at the 10% level

APPENDIX 2C: CFO Person-to-Person Relationships

Table 2C.4

Tests of association between absolute IFRS errors, tenure and audit committee governance using the CFO as the key management contact in the Partner/CFO Tenure variable.

Panel A: Absolute IFRS Errors (Corporate Governance)												
n=151	*ABS-Error*				*ABS-Error*				*ABS-Error*			
	Co-efficient	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	0.075	3.252	0.001	***	0.027	0.610	0.272		0.024	0.540	0.295	
Partner/CFO_Tenure	-0.003	-0.800	0.213		-0.003	-0.998	0.160		-0.003	-1.024	0.154	
Audit_Firm_Tenure	-0.004	-1.127	0.131		-0.001	-0.271	0.393		-0.001	-0.360	0.360	
Market Cap					-0.000	-0.669	0.252		0.000	-0.541	0.295	
LEV					0.000	0.018	0.493		0.001	0.068	0.473	
ROA					0.003	0.046	0.482		-0.004	-0.059	0.477	
LOSS					0.062	2.043	0.022	**	0.061	2.001	0.024	**
Audit Big N					0.025	1.054	0.147		0.025	1.038	0.151	
AC_Gov_Dummy									0.027	1.379	0.085	*
Adjusted R^2	0.009				0.042				0.048			
F-stat	1.673		0.191		1.936		0.068	*	1.942		0.058	*

Partner/CFO_Tenure : The length of time as measured in years (up to a maximum of 8) that the same audit partner and the same CFO combination have worked together in preparing the firm's financial statements at 2006.

All variables as previously defined and reported as one-tailed

*** : Denotes significance at the 1% level

** : Denotes significance at the 5% level

* : Denotes significance at the 10% level

Table 2C.5

Tests of association between signed IFRS errors, tenure and audit committee governance using the CFO as the key management contact in the Partner/CFO Tenure variable.

Panel A: Signed IFRS Errors (Corporate Governance)												
n=151	*SIGN-Error*				*SIGN-Error*				*SIGN-Error*			
	Co-efficient	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	-0.044	-2.548	0.006	***	-0.068	-2.021	0.023	**	-0.069	-2.037	0.022	**
Partner/CFO_Tenure	0.000	0.099	0.461		-0.000	-0.001	0.500		0.000	-0.009	0.497	
Audit_Firm_Tenure	0.005	1.893	0.030	**	0.005	1.848	0.034	**	0.005	1.810	0.036	**
Market Cap					0.000	0.504	0.308		0.000	0.543	0.294	
LEV					0.011	1.198	0.117		0.011	1.210	0.114	
ROA					-0.041	-0.753	0.227		-0.043	-0.784	0.218	
LOSS					-0.003	-0.113	0.455		-0.003	-0.129	0.449	
Audit Big N					0.004	0.201	0.421		0.004	0.194	0.424	
AC_Gov_Dummy									0.007	0.459	0.324	
Adjusted R^2	0.017				0.002				-0.004			
F-stat	2.326		0.101		1.033		0.411		0.925		0.498	

All variables as previously defined and reported as one-tailed

*** : Denotes significance at the 1% level

** : Denotes significance at the 5% level

* : Denotes significance at the 10% level

Table 2C.6

Tests of association between rank signed IFRS errors, tenure and audit committee governance using the CFO as the key management contact in the Partner/CFO Tenure variable.

Panel A: Rank Signed IFRS Errors (Corporate Governance)												
n=151	*RANK-Error*				*RANK-Error*				*RANK-Error*			
	Co-efficient	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	52.817	4.983	0.000	***	36.933	1.788	0.038	**	34.975	1.705	0.045	**
Partner/CFO_Tenure	1.509	0.962	0.169		1.549	0.966	0.168		1.501	0.944	0.174	
Audit_Firm_Tenure	2.571	1.543	0.063	*	2.941	1.667	0.049	**	2.734	1.559	0.061	*
Market Cap					0.001	1.562	0.060	*	0.001	1.740	0.042	**
LEV					2.962	0.511	0.305		3.347	0.582	0.281	
ROA					-6.081	-0.183	0.428		-10.757	-0.325	0.373	
LOSS					3.998	0.279	0.390		3.098	0.218	0.414	
Audit Big N					5.909	0.526	0.300		5.626	0.505	0.307	
AC_Gov_Dummy									16.906	1.848	0.034	**
Adjusted R^2	0.024				0.012				0.029			
F-stat	2.855		0.061	*	1.271		0.269		1.558		0.143	

All variables as previously defined and reported as one-tailed

*** : Denotes significance at the 1% level
** : Denotes significance at the 5% level
* : Denotes significance at the 10% level

APPENDIX 2D: Accruals

Table 2D.8

Tests of association between rank total accruals and tenure.

This table presents the results of tests of association of rank total accruals and various measures of auditor tenure. Panel A presents the results for the full sample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for subsample of firms, taking the lower and upper thirds of rank total accruals using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of rank total accruals for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Rank Total Accruals

n=151	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	63.777	4.833	0.000	***	84.364	3.359	0.001	***
Partner/CEO_Tenure	9.455	3.870	0.000	***	8.457	3.459	0.001	***
Audit_Firm_Tenure	0.262	0.138	0.445		-1.227	-0.625	0.267	
Market Cap					-0.002	-2.038	0.022	**
LEV					-1.480	-0.214	0.416	
ROA					36.608	0.917	0.181	
LOSS					-19.793	-1.159	0.125	
Audit Big N					-0.261	-0.020	0.492	
Adjusted R^2	0.088				0.116			
F-stat	8.234		0.000	***	3.826		0.001	***

Panel B: Rank Total Accruals

n=151	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	67.434	5.073	0.000	***	84.003	3.294	0.001	***
Partner/CEO_Tenure*	7.064	3.161	0.001	***	6.696	3.016	0.002	***
Audit_Firm_Tenure	1.692	0.907	0.183		-0.017	-0.009	0.497	
Market Cap					-0.002	-2.223	0.014	**
LEV					-0.974	-0.140	0.445	
ROA					58.043	1.453	0.074	
LOSS					-13.205	-0.760	0.225	
Audit Big N					0.698	0.052	0.480	
Adjusted R^2	0.059				0.100			
F-stat	5.717		0.004	***	3.377		0.002	***

Table 2D.8 (continued)
Tests of association between rank total accruals and tenure.

Panel C: Rank Total Accruals (Ranked Thirds)

n=102	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	54.355	2.851	0.003	***	70.120	1.952	0.027	**
Partner/CEO_Tenure	12.426	3.696	0.000	***	11.287	3.352	0.001	***
Audit_Firm_Tenure	0.383	0.139	0.445		-3.084	-1.020	0.156	
Market Cap					-0.002	-1.990	0.025	**
LEV					3.443	0.379	0.353	
ROA					54.658	0.997	0.161	
LOSS					-25.866	-1.080	0.142	
Audit Big N					12.871	0.688	0.247	
Adjusted R^2	0.116				0.152			
F-stat	7.617		0.001	***	3.595		0.002	***

Panel D: Rank Total Accruals (Ranked Thirds)

n=102	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	59.456	3.052	0.002	***	74.486	2.011	0.024	**
Partner/CEO_Tenure*	8.386	2.768	0.004	***	7.522	2.471	0.008	***
Audit_Firm_Tenure	2.581	0.944	0.174		-0.918	-0.303	0.381	
Market Cap					-0.002	-2.011	0.024	**
LEV					2.890	0.311	0.379	
ROA					82.190	1.472	0.072	*
LOSS					-16.460	-0.659	0.256	
Audit Big N					10.413	0.544	0.294	
Adjusted R^2	0.066				0.109			
F-stat	4.576		0.013	**	2.765		0.012	**

Where;
RANK-TACC : Rank total accruals scaled by average total assets
All other variables as previously defined and reported as one-tailed
*** : Denotes significance at the 1% level
** : Denotes significance at the 5% level
* : Denotes significance at the 10% level

Table 2D.9

Tests of association between absolute total accruals and tenure

This table presents the results of tests of association of absolute total accruals and various measures of auditor tenure. Panel A presents the results for the full sample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for subsample of firms, taking the lower and upper thirds of absolute total accruals using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of absolute total accruals for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Absolute Total Accruals

n=151	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.122	2.051	0.021	**	-0.012	-0.108	0.457	
Partner/CEO_Tenure	0.000	0.000	0.500		0.002	0.183	0.428	
Audit_Firm_Tenure	-0.004	-0.500	0.309		0.004	0.400	0.345	
Market Cap					0.000	0.195	0.423	
LEV					-0.004	-0.127	0.450	
ROA					0.270	1.506	0.067	*
LOSS					0.246	3.212	0.001	***
Audit Big N					0.037	0.626	0.267	
Adjusted R^2	-0.012				0.036			
F-stat	0.135		0.874		1.792		0.093	*

Panel B: Absolute Total Accruals

n=151	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.141	2.405	0.009	***	0.016	0.144	0.443	
Partner/CEO_Tenure*	-0.015	-1.506	0.067	*	-0.010	-1.033	0.152	
Audit_Firm_Tenure	-0.003	-0.382	0.352		0.004	0.505	0.307	
Market Cap					0.000	0.229	0.410	
LEV					-0.006	-0.181	0.429	
ROA					0.269	1.519	0.066	*
LOSS					0.236	3.067	0.002	***
Audit Big N					0.031	0.517	0.303	
Adjusted R^2	0.004				0.043			
F-stat	1.271		0.284		1.953		0.066	*

Table 2D.9 (continued)
Tests of association between absolute total accruals and tenure

Panel C: Absolute Total Accruals (Ranked Thirds)

n=102	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.153	1.789	0.039	**	-0.032	-0.192	0.424	
Partner/CEO_Tenure	0.003	0.202	0.421		0.002	0.138	0.445	
Audit_Firm_Tenure	-0.007	-0.560	0.289		0.006	0.478	0.317	
Market Cap					0.000	0.159	0.437	
LEV					-0.010	-0.234	0.408	
ROA					0.308	1.223	0.112	
LOSS					0.302	2.860	0.003	***
Audit Big N					0.059	0.658	0.256	
Adjusted R^2	-0.017				0.032			
F-stat	0.158		0.854		1.482		0.183	

Panel D: Absolute Total Accruals (Ranked Thirds)

n=102	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.183	2.189	0.016	**	0.003	0.018	0.493	
Partner/CEO_Tenure*	-0.021	-1.445	0.076	*	-0.016	-1.104	0.136	
Audit_Firm_Tenure	-0.005	-0.394	0.347		0.008	0.609	0.272	
Market Cap					0.000	0.247	0.403	
LEV					-0.009	-0.212	0.416	
ROA					0.298	1.196	0.118	
LOSS					0.293	2.788	0.003	***
Audit Big N					0.047	0.518	0.303	
Adjusted R^2	0.004				0.045			
F-stat	1.185		0.310		1.672		0.125	

Where:
ABS-TACC : The absolute value of total accruals scaled by average total assets
All other variables as previously defined and reported as one-tailed
*** : Denotes significance at the 1% level
** : Denotes significance at the 5% level
* : Denotes significance at the 10% level

Table 2D.10

Tests of association between rank absolute total accruals and tenure

This table presents the results of tests of association of rank absolute total accruals and various measures of auditor tenure. Panel A presents the results for the full sample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for subsample of firms, taking the lower and upper thirds of rank absolute total accruals using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of rank absolute total accruals for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Rank Absolute Total Accruals

n=151	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	114.188	8.034	0.000	***	103.363	3.814	0.000	***
Partner/CEO_Tenure	-1.666	-0.633	0.264		-0.901	-0.342	0.367	
Audit_Firm_Tenure	-1.338	-0.654	0.257		0.619	0.292	0.386	
Market Cap					0.001	1.780	0.039	
LEV					-7.627	-1.023	0.154	
ROA					3.566	0.083	0.467	
LOSS					32.110	1.742	0.042	
Audit Big N					2.413	0.167	0.434	
Adjusted R^2	-0.006				0.022			
F-stat	0.566		0.569		1.491		0.175	

Panel B: Rank Absolute Total Accruals

n=151	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	116.396	8.307	0.000	***	108.788	4.011	0.000	***
Partner/CEO_Tenure*	-3.491	-1.482	0.071	*	-2.930	-1.241	0.109	
Audit_Firm_Tenure	-1.418	-0.721	0.236		0.588	0.286	0.388	
Market Cap					0.001	1.844	0.034	**
LEV					-8.016	-1.080	0.141	
ROA					0.166	0.004	0.499	
LOSS					29.211	1.580	0.058	
Audit Big N					1.037	0.072	0.472	
Adjusted R^2	0.006				0.032			
F-stat	1.468		0.234		1.709		0.111	

Table 2D.10 (continued)
Tests of association between rank absolute total accruals and tenure

Panel C: Rank Absolute Total Accruals (Ranked Thirds)

n=102	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	123.421	6.137	0.000	***	117.033	3.001	0.002	***
Partner/CEO_Tenure	-3.280	-0.814	0.209		-3.422	-0.854	0.198	
Audit_Firm_Tenure	-2.197	-0.765	0.223		1.404	0.453	0.326	
Market Cap					0.002	1.417	0.080	*
LEV					-12.971	-1.234	0.110	
ROA					7.153	0.119	0.453	
LOSS					44.136	1.759	0.041	**
Audit Big N					-4.145	-0.193	0.424	
Adjusted R^2	-0.003				0.030			
F-stat	0.849		0.431		1.453		0.194	

Panel D: Rank Absolute Total Accruals (Ranked Thirds)

n=102	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	125.718	6.383	0.000	***	121.391	3.126	0.001	***
Partner/CEO_Tenure*	-5.451	-1.568	0.060	*	-4.985	-1.431	0.078	*
Audit_Firm_Tenure	-2.415	-0.876	0.192		1.026	0.344	0.366	
Market Cap					0.002	1.504	0.068	*
LEV					-12.759	-1.222	0.113	
ROA					-2.123	-0.036	0.486	
LOSS					39.440	1.581	0.059	*
Audit Big N					-5.859	-0.275	0.392	
Adjusted R^2	0.015				0.044			
F-stat	1.756		0.178		1.660		0.128	

Where:
RANK-ABS-TACC : The rank of absolute total accruals scaled by total assets.

All variables as previously defined and reported as one-tailed
*** : Denotes significance at the 1% level
** : Denotes significance at the 5% level
* : Denotes significance at the 10% level

APPENDIX 2E: Auditor Industry Specialisation

Table 2E.4

Tests of association between absolute IFRS errors and tenure

This table presents the results of tests of association of absolute IFRS errors and various measures of auditor tenure, while also introducing a dummy variable for auditor specialization. Panel A presents the results for the full sample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for subsample of firms, taking the lower and upper thirds of absolute IFRS errors using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of absolute IFRS errors for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Absolute IFRS Errors (Auditor Specialization)

n=151	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.017	0.369	0.357		0.010	0.229	0.410	
Partner/CEO_Tenure	0.002	0.493	0.312		0.002	0.381	0.352	
Audit_Firm_Tenure	-0.003	-0.849	0.199		-0.003	-0.788	0.216	
Market Cap	0.000	-0.720	0.237		0.000	-0.887	0.188	
LEV	-0.001	-0.107	0.458		-0.004	-0.338	0.368	
ROA	0.001	0.007	0.497		0.001	0.009	0.497	
LOSS	0.065	2.133	0.018	**	0.068	2.233	0.014	**
Audit Big N	0.021	0.886	0.189		0.028	1.169	0.123	
Dummy_spec_no_clients	0.019	1.239	0.109					
Dummy_spec_city_fee					0.032	2.007	0.024	**
Adjusted R^2	0.04				0.057			
F-stat	1.785		0.085	*	2.124		0.037	**

Panel B: Absolute IFRS Errors (Auditor Specialization)

n=151	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.022	0.482	0.315		0.014	0.305	0.381	
Partner/CEO_Tenure*	0.000	-0.116	0.453		0.000	0.054	0.479	
Audit_Firm_Tenure	-0.003	-0.751	0.227		-0.002	-0.717	0.237	
Market Cap	0.000	-0.724	0.236		0.000	-0.896	0.186	
LEV	-0.002	-0.122	0.452		-0.004	-0.350	0.364	
ROA	0.005	0.071	0.472		0.004	0.057	0.477	
LOSS	0.065	2.097	0.019	**	0.067	2.206	0.015	**
Audit Big N	0.020	0.844	0.200		0.027	1.136	0.129	
Dummy_spec_no_clients	0.019	1.204	0.116					
Dummy_spec_city_fee					0.032	2.008	0.024	**
Adjusted R^2	0.039				0.056			
F-stat	1.753		0.091	*	2.104		0.039	**

Table 2E.4 (continued)
Tests of association between absolute IFRS errors and tenure

Panel C: Absolute IFRS Errors (Auditor Specialization, Rank Thirds)								
n=102	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	-0.023	-0.351	0.363		-0.025	-0.382	0.352	
Partner/CEO_Tenure	0.001	0.119	0.453		0.001	0.084	0.467	
Audit_Firm_Tenure	-0.001	-0.167	0.434		-0.001	-0.199	0.422	
Market Cap	0.000	-0.722	0.236		0.000	-0.917	0.181	
LEV	0.006	0.317	0.376		0.002	0.134	0.447	
ROA	-0.022	-0.192	0.424		-0.034	-0.294	0.385	
LOSS	0.086	1.856	0.034	**	0.083	1.786	0.039	**
Audit Big N	0.048	1.377	0.086	*	0.055	1.579	0.059	*
Dummy_spec_no_clients	0.032	1.411	0.081	*				
Dummy_spec_city_fee					0.041	1.755	0.041	**
Adjusted R^2	0.051				0.061			
F-stat	1.673		0.115		1.826		0.082	*
Panel D: Absolute IFRS Errors (Auditor Specialization, Ranked Thirds)								
n=102	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	-0.018	-0.273	0.393		-0.021	-0.309	0.379	
Partner/CEO_Tenure*	-0.001	-0.276	0.392		-0.001	-0.278	0.391	
Audit_Firm_Tenure	-0.001	-0.146	0.442		-0.001	-0.185	0.427	
Market Cap	0.000	-0.722	0.236		0.000	-0.913	0.182	
LEV	0.006	0.311	0.379		0.002	0.128	0.449	
ROA	-0.021	-0.185	0.427		-0.034	-0.293	0.385	
LOSS	0.085	1.798	0.038	**	0.081	1.730	0.044	**
Audit Big N	0.047	1.360	0.089	*	0.054	1.561	0.061	*
Dummy_spec_no_clients	0.031	1.397	0.083	*				
Dummy_spec_city_fee					0.041	1.746	0.042	**
Adjusted R^2	0.051				0.062			
F-stat	1.682		0.113		1.836		0.080	*

Where:

Dummy_Spec_No_Clients : An indicator variable set to equal one if the firm was audited by an industry specialist auditor at city level based on the number of clients and zero otherwise.

Dummy_Spec_City_Fee : An indicator variable set or equal one if the firm was audited by an industry specialist auditor at the city level based on audit fees and zero otherwise.

All variables as previously defined and reported as one-tailed

*** : Denotes significance at the 1% level

** : Denotes significance at the 5% level

* : Denotes significance at the 10% level

Table 2E.5

Tests of association between signed IFRS errors and tenure

This table presents the results of tests of association of signed IFRS errors and various measures of auditor tenure, and introduces controls for auditor specialization. Panel A presents the results for the full sample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for subsample of firms, taking the lower and upper thirds of signed IFRS errors using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of signed IFRS errors for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Signed IFRS Errors (Auditor Specialization)

n=151	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	-0.063	-1.846	0.034	**	-0.059	-1.729	0.043	**
Partner/CEO_Tenure	0.001	0.311	0.379		0.002	0.471	0.319	
Audit_Firm_Tenure	0.005	1.936	0.028	**	0.005	1.862	0.033	**
Market Cap	0.000	0.748	0.228		0.000	0.898	0.186	
LEV	0.012	1.320	0.095	*	0.015	1.578	0.059	*
ROA	-0.036	-0.663	0.255		-0.038	-0.705	0.241	
LOSS	-0.004	-0.178	0.430		-0.006	-0.268	0.395	
Audit Big N	0.006	0.359	0.360		0.000	-0.013	0.495	
Dummy_spec_no_clients	-0.023	-2.007	0.024	**				
Dummy_spec_city_fee					-0.030	-2.475	0.007	***
Adjusted R^2	0.023				0.037			
F-stat	1.445		0.183		1.720		0.098	*

Panel B: Signed IFRS Errors (Auditor Specialization)

n=151	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	-0.058	-1.694	0.046	**	-0.053	-1.544	0.063	*
Partner/CEO_Tenure*	-0.001	-0.362	0.359		-0.001	-0.385	0.351	
Audit_Firm_Tenure	0.005	2.072	0.020	**	0.005	2.033	0.022	**
Market Cap	0.000	0.758	0.225		0.000	0.902	0.185	
LEV	0.012	1.298	0.098	*	0.014	1.552	0.062	*
ROA	-0.034	-0.635	0.264		-0.035	-0.658	0.256	
LOSS	-0.005	-0.224	0.412		-0.007	-0.316	0.376	
Audit Big N	0.006	0.307	0.380		-0.001	-0.080	0.468	
Dummy_spec_no_clients	-0.024	-2.045	0.022	**				
Dummy_spec_city_fee					-0.030	-2.484	0.007	***
Adjusted R^2	0.023				0.037			
F-stat	1.449		0.181		1.710		0.101	

Table 2E.5 (continued)
Tests of association between signed IFRS errors and tenure

Panel C: Signed IFRS Errors (Auditor Specialization, Ranked Thirds)								
n=102	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	-0.097	-1.947	0.028	**	-0.085	-1.700	0.046	**
Partner/CEO_Tenure	0.002	0.335	0.369		0.002	0.489	0.313	
Audit_Firm_Tenure	0.007	1.995	0.025	**	0.006	1.741	0.043	**
Market Cap	0.000	0.926	0.179		0.000	0.988	0.163	
LEV	0.020	1.460	0.074	*	0.022	1.573	0.060	*
ROA	-0.043	-0.564	0.287		-0.052	-0.698	0.244	
LOSS	-0.003	-0.096	0.462		-0.012	-0.385	0.358	
Audit Big N	0.012	0.389	0.345		0.002	0.082	0.467	
Dummy_spec_no_clients	-0.037	-2.153	0.017	**				
Dummy_spec_city_fee					-0.042	-2.404	0.009	***
Adjusted R^2	0.039				0.050			
F-stat	1.514		0.163		1.668		0.117	

Panel D: Signed IFRS Errors (Auditor Specialization, Ranked Thirds)								
n=102	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	-0.087	-1.713	0.045	**	-0.074	-1.448	0.076	*
Partner/CEO_Tenure*	-0.002	-0.517	0.304		-0.002	-0.487	0.314	
Audit_Firm_Tenure	0.008	2.157	0.017	**	0.007	1.938	0.028	**
Market Cap	0.000	0.939	0.175		0.000	0.987	0.163	
LEV	0.021	1.508	0.068	*	0.022	1.625	0.054	*
ROA	-0.044	-0.579	0.282		-0.052	-0.699	0.243	
LOSS	-0.007	-0.203	0.420		-0.016	-0.471	0.320	
Audit Big N	0.007	0.222	0.413		-0.003	-0.098	0.461	
Dummy_spec_no_clients	-0.037	-2.167	0.017	**				
Dummy_spec_city_fee					-0.041	-2.381	0.010	***
Adjusted R^2	0.041				0.050			
F-stat	1.536		0.155		1.667		0.117	

All variables as previously defined and reported as one-tailed
*** : Denotes significance at the 1% level
** : Denotes significance at the 5% level
* : Denotes significance at the 10% level

Table 2E.6

Tests of association between rank signed IFRS errors and tenure

This table presents the results of tests of association of rank signed IFRS errors and various measures of auditor tenure, and introduces controls for auditor specialization. Panel A presents the results for the full sample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for subsample of firms, taking the lower and upper thirds of rank signed IFRS errors using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of rank signed IFRS errors for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Rank Signed IFRS Errors (Auditor Specialization)

n=151	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	32.666	1.549	0.062	*	35.262	1.652	0.051	*
Partner/CEO_Tenure	0.515	0.252	0.401		0.386	0.187	0.426	
Audit_Firm_Tenure	3.568	2.178	0.016	**	3.601	2.178	0.016	**
Market Cap	0.001	1.308	0.097	*	0.001	1.415	0.080	*
LEV	2.937	0.509	0.306	*	3.086	0.525	0.300	
ROA	-14.280	-0.428	0.335		-11.021	-0.328	0.372	
LOSS	4.024	0.282	0.389		3.627	0.252	0.401	
Audit Big N	6.145	0.550	0.292		7.712	0.683	0.248	
Dummy_spec_no_clients	11.538	1.593	0.057	*				
Dummy_spec_city_fee					2.725	0.361	0.391	***
Adjusted R^2	0.017				0.000			
F-stat	1.322		0.237		1.005		0.435	*

Panel B: Rank Signed IFRS Errors (Auditor Specialization)

n=151	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	35.558	1.674	0.048	**	38.526	1.789	0.038	**
Partner/CEO_Tenure*	-0.746	-0.404	0.344		-0.989	-0.532	0.298	
Audit_Firm_Tenure	3.393	2.309	0.011	**	3.712	2.303	0.012	**
Market Cap	0.001	1.321	0.094	*	0.001	1.437	0.077	*
LEV	2.808	0.486	0.314	*	2.951	0.502	0.308	*
ROA	-13.443	-0.406	0.343		-10.624	-0.319	0.375	
LOSS	3.259	0.227	0.411		2.606	0.179	0.429	
Audit Big N	5.579	0.499	0.310		6.962	0.615	0.270	
Dummy_spec_no_clients	11.172	1.535	0.064	*				
Dummy_spec_city_fee					2.395	0.318	0.376	
Adjusted R^2	0.018				0.002			
F-stat	1.336		0.231		1.037		0.411	

Table 2E.6 (continued)
Tests of association between rank signed IFRS errors and tenure

Panel C: Rank Signed IFRS Errors (Auditor Specialization, Ranked Thirds)								
n=102	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	16.681	0.543	0.294		15.482	0.497	0.310	
Partner/CEO_Tenure	-0.305	-0.102	0.460		-0.318	-0.105	0.459	
Audit_Firm_Tenure	4.474	1.976	0.026	**	4.720	2.067	0.021	**
Market Cap	0.001	1.171	0.122		0.001	1.266	0.105	
LEV	8.558	0.989	0.163		8.617	0.983	0.164	
ROA	-20.112	-0.432	0.334		-15.261	-0.326	0.373	
LOSS	0.336	0.016	0.494		2.968	0.141	0.444	
Audit Big N	6.822	0.373	0.355		10.509	0.574	0.284	
Dummy_spec_no_clients	15.549	1.471	0.073	*				
Dummy_spec_city_fee					6.774	0.625	0.267	***
Adjusted R^2	0.018				-0.001			
F-stat	1.231		0.290		0.992		0.448	
Panel D: Rank Signed IFRS Errors (Auditor Specialization, Ranked Thirds)								
n=102	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	21.716	0.695	0.245		21.216	0.669	0.253	
Partner/CEO_Tenure*	-1.937	-0.680	0.249		-2.147	-0.748	0.228	
Audit_Firm_Tenure	4.470	2.046	0.022	**	4.710	2.142	0.018	**
Market Cap	0.001	1.208	0.115		0.001	1.306	0.098	*
LEV	8.752	1.016	0.156		8.851	1.014	0.158	
ROA	-23.076	-0.497	0.310		-18.667	-0.400	0.345	
LOSS	-1.972	-0.093	0.463		0.286	0.013	0.495	
Audit Big N	4.388	0.238	0.407		7.639	0.412	0.341	
Dummy_spec_no_clients	14.996	1.420	0.080	*				
Dummy_spec_city_fee					6.296	0.587	0.280	***
Adjusted R^2	0.023				0.005			
F-stat	1.294		0.256		1.066		0.394	

All variables as previously defined and reported as one-tailed
*** : Denotes significance at the 1% level
** : Denotes significance at the 5% level
* : Denotes significance at the 10% level

APPENDIX 2F: June Year End Sample

Table 2F.4

Tests of association between absolute IFRS Errors and tenure on a sub-sample of firms

This table presents the results of tests of association of absolute IFRS errors and various measures of auditor tenure for a June year end sub-sample. Panel A presents the results for the June year end subsample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for a further refined subsample of firms, taking the lower and upper thirds of absolute IFRS errors using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of absolute IFRS errors for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Absolute IFRS Errors (June Sample)

n=117	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.080	3.032	0.002	***	0.004	0.083	0.467	
Partner/CEO_Tenure	0.004	0.929	0.178		0.006	1.392	0.084	*
Audit_Firm_Tenure	-0.009	-2.280	0.012	**	-0.006	-1.586	0.058	*
Market Cap					0.000	-0.613	0.271	
LEV					0.009	0.666	0.254	
ROA					0.026	0.343	0.366	
LOSS					0.094	2.860	0.003	***
Audit Big N					0.023	0.918	0.181	
Adjusted R^2	0.027				0.105			
F-stat	2.629		0.076	*	2.949		0.007	***

Panel B: Absolute IFRS Errors (June Sample)

n=117	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.087	3.321	0.001	***	0.013	0.268	0.395	
Partner/CEO_Tenure*	-0.002	-0.371	0.356		0.001	0.238	0.407	
Audit_Firm_Tenure	-0.008	-2.040	0.022	**	-0.005	-1.270	0.104	
Market Cap					0.000	-0.643	0.261	
LEV					0.008	0.634	0.264	
ROA					0.042	0.568	0.286	
LOSS					0.095	2.859	0.003	***
Audit Big N					0.022	0.862	0.196	
Adjusted R^2	0.021				0.090			
F-stat	2.253		0.110		2.635		0.015	**

Table 2F.4 (continued)
Tests of association between absolute IFRS Errors and tenure on a sub-sample of firms

Panel C: Absolute IFRS Errors (June Sample, Rank Thirds)

n=78	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.120	3.036	0.002	***	-0.032	-0.433	0.334	
Partner/CEO_Tenure	0.004	0.591	0.278		0.006	0.941	0.175	
Audit_Firm_Tenure	-0.013	-2.204	0.016	**	-0.007	-1.240	0.110	
Market Cap					0.000	-0.594	0.277	
LEV					0.023	1.102	0.137	
ROA					0.038	0.359	0.360	
LOSS					0.113	2.378	0.010	***
Audit Big N					0.053	1.349	0.091	*
Adjusted R^2	0.036				0.103			
F-stat	2.431		0.095	*	2.259		0.039	**

Panel D: Absolute IFRS Errors (June Sample, Rank Thirds)

n=78	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.130	3.316	0.001	***	-0.024	-0.319	0.376	
Partner/CEO_Tenure*	-0.003	-0.626	0.267		0.000	0.063	0.475	
Audit_Firm_Tenure	-0.011	-2.032	0.023	**	-0.006	-1.039	0.152	
Market Cap					0.000	-0.622	0.268	
LEV					0.024	1.146	0.128	
ROA					0.056	0.543	0.295	
LOSS					0.114	2.380	0.010	***
Audit Big N					0.053	1.317	0.096	*
Adjusted R^2	0.036				0.091			
F-stat	2.453		0.093	*	2.107		0.054	*

All variables as previously defined and reported as one-tailed
*** : Denotes significance at the 1% level
** : Denotes significance at the 5% level
* : Denotes significance at the 10% level

Table 2F.5

Tests of association between signed IFRS Errors and tenure on a sub-sample of firms

This table presents the results of tests of association of signed IFRS errors and various measures of auditor tenure for a June year end sub-sample. Panel A presents the results for the June year end subsample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for a further refined subsample of firms, taking the lower and upper thirds of signed IFRS errors using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of signed IFRS errors for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Signed IFRS Errors (June Sample)

n=117	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	-0.053	-2.684	0.004	***	-0.067	-1.788	0.039	**
Partner/CEO_Tenure	-0.002	-0.560	0.289		-0.001	-0.386	0.350	
Audit_Firm_Tenure	0.008	2.728	0.004	***	0.008	2.524	0.007	***
Market Cap					0.000	0.516	0.304	
LEV					0.006	0.639	0.262	
ROA					-0.058	-0.997	0.161	
LOSS					-0.016	-0.639	0.262	
Audit Big N					0.006	0.279	0.391	
Adjusted R^2	0.045				0.018			
F-stat	3.760		0.026	**	1.298		0.258	

Panel B: Signed IFRS Errors (June Sample)

n=117	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	-0.053	-2.726	0.004	***	-0.066	-1.739	0.043	**
Partner/CEO_Tenure*	-0.002	-0.531	0.298		-0.002	-0.566	0.287	
Audit_Firm_Tenure	0.008	2.725	0.004	***	0.008	2.543	0.006	***
Market Cap					0.000	0.540	0.295	
LEV					0.006	0.628	0.266	
ROA					-0.063	-1.082	0.141	
LOSS					-0.018	-0.709	0.240	
Audit Big N					0.005	0.254	0.400	
Adjusted R^2	0.045				0.019			
F-stat	3.744		0.027	**	1.324		0.246	

Table 2F.5 (continued)
Tests of association between signed IFRS Errors and tenure on a sub-sample of firms

Panel C: Signed IFRS Errors (June Sample, Rank Thirds)

n=78	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	-0.074	-2.616	0.006	***	-0.092	-1.631	0.054	*
Partner/CEO_Tenure	-0.003	-0.518	0.303		-0.003	-0.585	0.280	
Audit_Firm_Tenure	0.011	2.649	0.005	***	0.011	2.476	0.008	***
Market Cap					0.000	0.620	0.269	
LEV					0.014	0.879	0.191	
ROA					-0.079	-0.955	0.172	
LOSS					-0.032	-0.811	0.210	
Audit Big N					-0.001	-0.038	0.485	
Adjusted R^2	0.062				0.030			
F-stat	3.559		0.033	**	1.335		0.247	

Panel D: Signed IFRS Errors (June Sample, Rank Thirds)

n=78	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	-0.075	-2.645	0.005	***	-0.087	-1.534	0.065	*
Partner/CEO_Tenure*	-0.003	-0.533	0.298		-0.005	-0.908	0.184	
Audit_Firm_Tenure	0.011	2.652	0.005	***	0.010	2.446	0.009	***
Market Cap					0.000	0.651	0.259	
LEV					0.014	0.914	0.182	
ROA					-0.095	-1.144	0.128	
LOSS					-0.039	-0.972	0.167	
Audit Big N					-0.004	-0.120	0.453	
Adjusted R^2	0.063				0.036			
F-stat	3.568		0.033	**	1.412		0.214	

All variables as previously defined and reported as one-tailed
*** : Denotes significance at the 1% level
** : Denotes significance at the 5% level
* : Denotes significance at the 10% level

Table 2F.6

Tests of association between rank signed IFRS Errors and tenure on a sub-sample of firms

This table presents the results of tests of association of rank signed IFRS errors and various measures of auditor tenure for a June year end sub-sample. Panel A presents the results for the June year end subsample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for a further refined subsample of firms, taking the lower and upper thirds of rank signed IFRS errors using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of rank signed IFRS errors for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Rank Signed IFRS Errors (June Sample)

n=117	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	58.642	4.829	0.000	***	55.319	2.408	0.009	***
Partner/CEO_Tenure	0.543	0.257	0.399		0.710	0.322	0.374	
Audit_Firm_Tenure	2.486	1.422	0.079	*	2.710	1.455	0.074	*
Market Cap					0.001	1.436	0.077	*
LEV					0.576	0.121	0.452	
ROA					-20.130	-0.535	0.297	
LOSS					-6.812	-0.397	0.346	
Audit Big N					-0.059	-0.062	0.476	
Adjusted R^2	0.005				-0.016			
F-stat	1.274		0.284		0.731		0.646	

Panel B: Rank Signed IFRS Errors (June Sample)

n=117	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	59.872	4.972	0.000	***	58.082	2.524	0.007	***
Partner/CEO_Tenure*	-0.025	-0.272	0.393		-0.696	-0.377	0.354	
Audit_Firm_Tenure	0.149	1.595	0.057	*	2.904	1.614	0.055	*
Market Cap					0.001	1.440	0.077	*
LEV					0.443	0.099	0.461	
ROA					-18.593	-0.498	0.310	
LOSS					-7.448	-0.437	0.332	
Audit Big N					-0.448	-0.106	0.458	
Adjusted R^2	0.005				-0.016			
F-stat	1.277		0.283		0.737		0.641	

Table 2F.6 (continued)

Tests of association between rank signed IFRS Errors and tenure on a sub-sample of firms

Panel C: Rank Signed IFRS Errors (June Sample, Rank Signed)								
n=78	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	126.099	5.397	0.000	***	111.872	2.565	0.006	***
Partner/CEO_Tenure	-5.404	-1.198	0.118		-4.639	-1.028	0.154	
Audit_Firm_Tenure	-1.497	-0.443	0.330		1.307	0.364	0.359	
Market Cap					0.001	0.967	0.169	
LEV					-9.286	-0.805	0.212	
ROA					-34.859	-0.528	0.300	
LOSS					32.527	1.171	0.123	
Audit Big N					5.203	0.222	0.413	
Adjusted R^2	0.001				0.021			
F-stat	1.044		0.357		1.239		0.293	

Panel D: Rank Signed IFRS Errors (June Sample, Rank Thirds)								
n=78	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	126.639	5.559	0.000	***	115.381	2.662	0.005	***
Partner/CEO_Tenure*	-6.478	-1.707	0.046	**	-5.558	-1.451	0.076	*
Audit_Firm_Tenure	-2.044	-0.633	0.265		0.716	0.207	0.419	
Market Cap					0.001	1.015	0.157	
LEV					-9.067	-0.792	0.216	
ROA					-46.458	-0.712	0.240	
LOSS					26.608	0.960	0.171	
Audit Big N					3.747	0.161	0.437	
Adjusted R^2	0.020				0.036			
F-stat	1.790		0.174		1.405		0.217	

All variables as previously defined and reported as one-tailed

*** : Denotes significance at the 1% level

** : Denotes significance at the 5% level

* : Denotes significance at the 10% level

Table 2F.7

Tests of association between rank absolute IFRS Errors and tenure on a sub-sample of firms

This table presents the results of tests of association of rank absolute IFRS errors and various measures of auditor tenure for a June year end sub-sample. Panel A presents the results for the June year end subsample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for a further refined subsample of firms, taking the lower and upper thirds of rank absolute IFRS errors using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of rank absolute IFRS errors for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Rank Absolute IFRS Errors (June Sample)

n=117	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	97.174	6.172	0.000	***	64.804	2.174	0.016	**
Partner/CEO_Tenure	4.540	1.602	0.056	*	5.624	1.936	0.028	**
Audit_Firm_Tenure	-2.341	-1.012	0.157		-1.502	-0.619	0.269	
Market Cap					0.000	0.266	0.296	
LEV					3.039	0.380	0.353	
ROA					-49.486	-1.065	0.145	
LOSS					6.756	0.330	0.371	
Audit Big N					20.598	1.300	0.098	*
Adjusted R^2	0.007				0.001			
F-stat	1.435		0.242		1.022		0.420	

Panel B: Rank Absolute IFRS Errors (June Sample)

n=117	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	102.442	6.479	0.000	***	72.517	2.384	0.010	***
Partner/CEO_Tenure*	0.283	0.111	0.456		0.887	0.341	0.367	
Audit_Firm_Tenure	-1.240	-0.553	0.291		-0.336	-0.141	0.444	
Market Cap					0.000	0.212	0.417	
LEV					2.749	0.338	0.368	
ROA					-35.089	-0.752	0.227	
LOSS					8.102	0.387	0.350	
Audit Big N					19.576	1.213	0.114	
Adjusted R^2	-0.015				-0.032			
F-stat	0.155		0.857		0.487		0.842	

Table 2F.7 (continued)

Tests of association between rank absolute IFRS Errors and tenure on a sub-sample of firms

Panel C: Rank Absolute IFRS Errors (June Sample, Rank Thirds)								
n=78	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	94.932	3.999	0.000	***	40.403	0.861	0.196	
Partner/CEO_Tenure	5.871	1.470	0.073	*	7.456	1.781	0.040	**
Audit_Firm_Tenure	-2.507	-0.715	0.239		-1.535	-0.408	0.343	
Market Cap					0.000	0.049	0.481	
LEV					7.492	0.582	0.281	
ROA					-58.710	-0.895	0.187	
LOSS					11.081	0.373	0.356	
Audit Big N					32.207	1.294	0.100	*
Adjusted R^2	0.003				-0.015			
F-stat	1.122		0.331		0.839		0.558	

Panel D: Rank Absolute IFRS Errors (June Sample, Rank Thirds)								
n=78	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	102.761	0.432	0.000	***	48.352	0.996	0.162	***
Partner/CEO_Tenure*	0.081	0.024	0.491		1.018	0.287	0.388	
Audit_Firm_Tenure	-0.976	-0.285	0.388		0.058	0.016	0.494	
Market Cap					0.000	-0.048	0.481	
LEV					8.811	0.671	0.253	
ROA					-36.866	-0.560	0.289	
LOSS					13.715	0.448	0.328	
Audit Big N					31.660	1.241	0.110	
Adjusted R^2	-0.026				-0.060			
F-stat	0.041		0.960		0.382		0.910	

All variables as previously defined and reported as one-tailed

*** : Denotes significance at the 1% level

** : Denotes significance at the 5% level

* : Denotes significance at the 10% level

Table 2F.11

Tests of association between absolute IFRS Errors, tenure and a control variable for audit committee governance on a sub-sample of firms

This table presents the results of tests of association of absolute IFRS errors, various measures of auditor tenure and a control variable for audit committee governance for a June year end sub-sample. Panel A presents the results for the June year end subsample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for a further refined subsample of firms, taking the lower and upper thirds of absolute IFRS errors using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of absolute IFRS errors for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Absolute IFRS Errors (June Sample and Audit Committee Governance)

n=117	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.080	3.032	0.002	***	0.004	0.084	0.467	
Partner/CEO_Tenure	0.004	0.929	0.178		0.007	1.413	0.081	*
Audit_Firm_Tenure	-0.009	-2.280	0.012	**	-0.006	-1.589	0.058	*
Market Cap					0.000	-0.642	0.261	
LEV					0.009	0.686	0.247	
ROA					0.028	0.370	0.356	
LOSS					0.095	2.868	0.001	***
Audit Big N					0.024	0.926	0.178	
Ac_Gov_Dummy					-0.009	-0.370	0.356	
Adjusted R^2	0.027				0.098			
F-stat	2.629		0.076	*	2.577		0.013	**

Panel B: Absolute IFRS Errors (June Sample and Audit Committee Governance)

n=117	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.087	3.321	0.001	***	0.013	0.269	0.789	
Partner/CEO_Tenure*	-0.002	-0.371	0.356		0.001	0.249	0.402	
Audit_Firm_Tenure	-0.008	-2.040	0.022	**	-0.005	-1.266	0.208	
Market Cap					0.000	-0.662	0.255	
LEV					0.008	0.646	0.260	
ROA					0.044	0.588	0.279	
LOSS					0.096	2.859	0.003	***
Audit Big N					0.022	0.866	0.194	
Ac_Gov_Dummy					-0.006	-0.260	0.398	
Adjusted R^2	0.021				0.082			
F-stat	2.253		0.110		2.294		0.026	**

Table 2F.11 (continued)

Tests of association between absolute IFRS Errors, tenure and a control variable for audit committee governance on a sub-sample of firms

Panel C: Absolute IFRS Errors (June Sample, Audit Committee Governance, Rank Thirds)

n=78	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.120	3.036	0.002	***	-0.032	-0.429	0.335	
Partner/CEO_Tenure	0.004	0.591	0.278		0.006	0.923	0.180	
Audit_Firm_Tenure	-0.013	-2.204	0.016	**	-0.007	-1.217	0.114	
Market Cap					0.000	-0.658	0.257	
LEV					0.024	1.148	0.128	
ROA					0.046	0.436	0.332	
LOSS					0.115	2.316	0.009	***
Audit Big N					0.054	1.365	0.089	
Ac_Gov_Dummy					-0.020	-0.628	0.266	
Adjusted R^2	0.036				0.095			
F-stat	2.431		0.095	*	2.009		0.058	*

Panel D: Absolute IFRS Errors (June Sample, Audit Committee Governance, Rank Thirds)

n=78	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.130	3.316	0.001	***	-0.025	-0.326	0.373	
Partner/CEO_Tenure*	-0.003	-0.626	0.267		0.001	0.106	0.458	
Audit_Firm_Tenure	-0.011	-2.032	0.023	**	-0.006	-1.020	0.156	
Market Cap					0.000	-0.693	0.246	
LEV					0.025	1.194	0.118	
ROA					0.065	0.619	0.269	
LOSS					0.117	2.424	0.009	***
Audit Big N					0.054	1.337	0.093	*
AC_Gov_Dummy					-0.021	-0.650	0.259	
Adjusted R^2	0.036				0.084			
F-stat	2.453		0.093	*	1.881		0.077	*

All variables as previously defined and reported as one-tailed

*** : Denotes significance at the 1% level

** : Denotes significance at the 5% level

* : Denotes significance at the 10% level

Table 2F.12

Tests of association between absolute IFRS Errors, tenure and a control variable for audit committee governance on a sub-sample of firms

This table presents the results of tests of association of signed IFRS errors, various measures of auditor tenure and a control variable for audit committee governance for a June year end sub-sample. Panel A presents the results for the June year end subsample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for a further refined subsample of firms, taking the lower and upper thirds of signed IFRS errors using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of signed IFRS errors for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Absolute IFRS Errors (June Sample, Audit Committee Governance)

n=117	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	-0.053	-2.684	0.004	***	-0.067	-1.828	0.035	**
Partner/CEO_Tenure	-0.002	-0.560	0.289		-0.002	-0.585	0.280	
Audit_Firm_Tenure	0.008	2.728	0.004	***	0.008	2.633	0.050	**
Market Cap					0.000	0.730	0.234	
LEV					0.005	0.503	0.308	
ROA					-0.069	-1.196	0.117	
LOSS					-0.021	-0.825	0.206	
Audit Big N					0.004	0.207	0.418	
Ac_Gov_Dummy					0.043	2.269	0.013	**
Adjusted R^2	0.045				0.054			
F-stat	3.760		0.026	**	1.823		0.080	*

Panel B: Absolute IFRS Errors (June Sample, Audit Committee Governance)

n=117	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	-0.053	-2.726	0.004	***	-0.066	-1.790	0.038	**
Partner/CEO_Tenure*	-0.002	-0.531	0.298		-0.002	-0.687	0.247	
Audit_Firm_Tenure	0.008	2.725	0.004	***	0.008	2.610	0.005	***
Market Cap					0.000	0.760	0.225	
LEV					0.005	0.493	0.312	
ROA					-0.075	-1.314	0.096	*
LOSS					-0.023	-0.909	0.183	
Audit Big N					0.004	0.183	0.428	
Ac_Gov_Dummy					0.042	2.260	0.013	**
Adjusted R^2	0.045				0.055			
F-stat	3.744		0.027	**	1.841		0.077	*

Table 2F.12 (continued)

Tests of association between absolute IFRS Errors, tenure and a control variable for audit committee governance on a sub-sample of firms

Panel C: Absolute IFRS Errors (June Sample, Audit Committee Governance, Rank Thirds)

n=78	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	-0.074	-2.616	0.006	***	-0.085	-1.561	0.062	*
Partner/CEO_Tenure	-0.003	-0.518	0.303		-0.004	-0.751	0.228	
Audit_Firm_Tenure	0.011	2.649	0.005	***	0.012	2.717	0.004	***
Market Cap					0.000	0.807	0.211	
LEV					0.008	0.555	0.291	
ROA					-0.098	-1.219	0.114	
LOSS					-0.049	-1.278	0.103	
Audit Big N					-0.007	-0.226	0.411	
Ac_Gov_Dummy					0.073	2.530	0.007	***
Adjusted R^2	0.062				0.099			
F-stat	3.559		0.033	**	2.058		0.052	*

Panel D: Absolute IFRS Errors (June Sample, Audit Committee Governance, Rank Thirds)

n=78	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	-0.075	-2.645	0.005	***	-0.083	-1.525	0.066	*
Partner/CEO_Tenure*	-0.003	-0.533	0.298		-0.004	-0.745	0.230	
Audit_Firm_Tenure	0.011	2.652	0.005	***	0.011	2.632	0.005	***
Market Cap					0.000	0.826	0.206	
LEV					0.009	0.573	0.285	
ROA					-0.112	-1.387	0.085	*
LOSS					-0.054	-1.371	0.088	*
Audit Big N					-0.008	-0.251	0.401	
AC_Gov_Dummy					0.070	2.425	0.009	***
Adjusted R^2	0.063				0.099			
F-stat	3.568		0.033	**	2.057		0.052	*

All variables as previously defined and reported as one-tailed

*** : Denotes significance at the 1% level

** : Denotes significance at the 5% level

* : Denotes significance at the 10% level

Table 2F.13

Tests of association between rank signed IFRS Errors, tenure and a control variable for audit committee governance on a sub-sample of firms

This table presents the results of tests of association of rank signed IFRS errors, various measures of auditor tenure and a control variable for audit committee governance for a June year end sub-sample. Panel A presents the results for the June year end subsample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for a further refined subsample of firms, taking the lower and upper thirds of rank signed IFRS errors using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of rank signed IFRS errors for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Rank Signed IFRS Errors (June Sample, Audit Committee Governance)

n=117	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	58.642	4.849	0.000	***	55.119	2.470	0.008	***
Partner/CEO_Tenure	0.543	0.249	0.402		0.177	0.081	0.468	
Audit_Firm_Tenure	2.486	1.399	0.083	*	2.855	1.571	0.060	*
Market Cap					0.001	1.799	0.038	**
LEV					-0.539	-0.090	0.465	
ROA					-28.253	-0.810	0.210	
LOSS					-10.232	-0.666	0.254	
Audit Big N					-1.099	-0.093	0.463	
AC_Gov_Dummy					32.657	2.874	0.003	***
Adjusted R^2	0.004				0.048			
F-stat	1.229		0.297		1.727		0.100	*

Panel B: Rank Signed IFRS Errors (June Sample, Audit Committee Governance)

n=117	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	59.872	4.984	0.000	***	57.564	2.572	0.006	***
Partner/CEO_Tenure*	-0.472	-0.245	0.404		-0.972	-0.508	0.307	
Audit_Firm_Tenure	2.664	1.565	0.006	***	2.950	1.680	0.048	**
Market Cap					0.001	1.816	0.036	**
LEV					-0.679	-0.113	0.455	
ROA					-28.251	-0.819	0.207	
LOSS					-11.225	-0.726	0.235	
Audit Big N					-1.611	-0.136	0.446	
AC_Gov_Dummy					33.020	2.916	0.002	***
Adjusted R^2	0.004				0.050			
F-stat	1.227		0.297		1.762		0.092	*

Table 2F.13 (continued)

Tests of association between rank signed IFRS Errors, tenure and a control variable for audit committee governance on a sub-sample of firms

Panel C: Rank Signed IFRS Errors (June Sample, Audit Committee Governance, Rank Thirds)

n=78	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	126.099	5.397	0.000	***	112.455	2.566	0.006	***
Partner/CEO_Tenure	-5.404	-1.198	0.118		-4.718	-1.040	0.151	
Audit_Firm_Tenure	-1.497	-0.443	0.330		1.349	0.374	0.355	
Market Cap					0.001	0.999	0.161	
LEV					-10.084	-0.864	0.196	
ROA					-39.633	-0.593	0.278	
LOSS					30.396	1.080	0.142	
Audit Big N					4.529	0.192	0.424	
AC_Gov_Dummy					12.764	0.581	0.282	
Adjusted R^2	0.001				0.012			
F-stat	1.044		0.357		1.116		0.363	

Panel D: Rank Signed IFRS Errors (June Sample, Audit Committee Governance, Rank Thirds)

n=78	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	126.639	5.559	0.000	***	115.783	2.657	0.005	***
Partner/CEO_Tenure*	-6.478	-1.707	0.046	**	-5.548	-1.441	0.077	*
Audit_Firm_Tenure	-2.044	-0.633	0.265		0.739	0.213	0.416	
Market Cap					0.001	1.043	0.150	
LEV					-9.813	-0.846	0.200	
ROA					-51.025	-0.772	0.222	
LOSS					24.607	0.876	0.192	
Audit Big N					3.155	0.134	0.447	
AC_Gov_Dummy					11.915	0.547	0.293	
Adjusted R^2	0.020				0.026			
F-stat	1.790		0.174		1.255		0.282	

All variables as previously defined and reported as one-tailed

*** : Denotes significance at the 1% level

** : Denotes significance at the 5% level

* : Denotes significance at the 10% level

Table 2F.14

Tests of association between absolute IFRS Errors, tenure (Partner/CFO association) and a control variable for audit committee governance on a sub-sample of firms

This table presents the results of tests of association of absolute IFRS errors, various measures of auditor tenure and a control variable for audit committee governance for a June year end sub-sample. Panel A presents the results for the June year end subsample firms, results using the partner/CFO tenure measure, and the results with an audit committee governance variable introduced.

Panel A: Absolute IFRS Errors (June Sample, Audit Committee Governance)

n=117	*ABS-Error*			*ABS-Error*			*ABS-Error*			
	Co-efficient	**t-stat**	**p-value**	**Co-efficient**	**t-stat**	**p-value**	**Co-efficient**	**t-stat**	**p-value**	
Constant	0.088	3.363	0.001	0.016	0.331	0.371	0.016	0.335	0.369	
Partner/CFO_Tenure	-0.002	-0.571	0.285	-0.003	-0.794	0.215	-0.003	-0.807	0.211	
Audit_Firm_Tenure	-0.007	-1.602	0.056 *	-0.003	-0.774	0.220	-0.003	-0.765	0.223	
Market Cap				-0.000	-0.674	0.251	0.000	-0.697	0.244	
LEV				0.009	0.666	0.254	0.009	0.681	0.249	
ROA				0.035	0.473	0.319	0.037	0.495	0.311	
LOSS				0.093	2.822	0.003 ***	0.094	2.825	0.003	***
Audit Big N				0.024	0.934	0.177	0.024	0.940	0.175	
AC_Gov_Dummy							-0.007	-0.297	0.384	
Adjusted R^2	0.023			0.095			0.087			
F-stat	2.351		0.100 *	2.731		0.012 **	2.381		0.021	**

All variables as previously defined and reported as one-tailed

*** : Denotes significance at the 1% level

** : Denotes significance at the 5% level

* : Denotes significance at the 10% level

Table 2F.15

Tests of association between signed IFRS Errors, tenure (partner/CFO association) and a control variable for audit committee governance and on a sub-sample of firms

This table presents the results of tests of association of signed IFRS errors, various measures of auditor tenure and a control variable for audit committee governance for a June year end sub-sample. Panel A presents the results for the June year end subsample firms, results using the partner/CFO tenure measure, and the results with an audit committee governance variable introduced.

Panel A: Signed IFRS Errors (June Sample, Audit Committee Governance)

n=117	*SIGN-Error*				*SIGN-Error*				*SIGN-Error*			
	Co-efficient	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	-0.055	-2.821	0.003	***	-0.070	-1.875	0.032	**	-0.071	-1.948	0.027	**
Partner/CFO_Tenure	0.000	-0.126	0.450		-0.001	-0.234	0.408		0.000	-0.106	0.458	
Audit_Firm_Tenure	0.008	2.444	0.008	***	0.008	2.350	0.011	**	0.008	2.344	0.011	**
Market Cap					0.000	0.513	0.305		0.000	0.730	0.234	
LEV					0.007	0.660	0.256		0.005	0.526	0.300	
ROA					-0.063	-1.089	0.139		-0.075	-1.299	0.099	*
LOSS					-0.017	-0.652	0.258		-0.021	-0.830	0.204	
Audit Big N					0.006	0.322	0.374		0.005	0.247	0.403	
AC_Gov_Dummy									0.042	2.214	0.015	**
Adjusted R^2	0.043				0.017				0.051			
F-stat	3.602		0.030	**	1.283		0.265		1.776		0.090	*

All variables as previously defined and reported as one-tailed

*** : Denotes significance at the 1% level

** : Denotes significance at the 5% level

* : Denotes significance at the 10% level

Table 2F.16

Tests of association between rank signed IFRS Errors, tenure (partner/CFO association) and a control variable for audit committee governance and on a sub-sample of firms

This table presents the results of tests of association of rank signed IFRS errors, various measures of auditor tenure and a control variable for audit committee governance for a June year end sub-sample. Panel A presents the results for the June year end subsample firms, results using the partner/CFO tenure measure, and the results with an audit committee governance variable introduced.

Panel A: Rank Signed IFRS Errors (June Sample, Audit Committee Governance)

n=117	*RANK-Error*				*RANK-Error*				*RANK-Error*			
	Co-efficient	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	57.246	4.817	0.000	***	56.179	2.486	0.007	***	89.223	2.983	0.002	***
Partner/CFO_Tenure	1.923	0.884	0.190		2.023	0.919	0.180		-2.627	-1.107	0.136	
Audit_Firm_Tenure	1.673	1.098	0.138		1.850	1.130	0.131		2.298	0.862	0.195	
Market Cap					0.001	1.547	0.063	*	0.001	1.358	0.089	*
LEV					0.174	0.028	0.489		-4.564	-0.558	0.289	
ROA					-13.903	-0.392	0.348		-36.368	-0.771	0.221	
LOSS					-5.990	-0.380	0.352		23.339	1.117	0.133	
Audit Big N					-1.702	-0.139	0.445		14.725	0.908	0.183	
AC_Gov_Dummy									7.524	0.488	0.314	
Adjusted R^2	0.014				-0.005				0.019			
F-stat	1.812		0.168		0.920		0.494		1.280		0.262	

All variables as previously defined and reported as one-tailed

*** : Denotes significance at the 1% level

** : Denotes significance at the 5% level

* : Denotes significance at the 10% level

Table 2F.8

Tests of association between rank total accruals and tenure on a sub-sample of firms

This table presents the results of tests of rank total accruals and various measures of auditor tenure for a June year end sub-sample. Panel A presents the results for the June year end subsample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for a further refined subsample of firms, taking the lower and upper thirds of rank total accruals using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of rank total accruals for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Rank Total Accruals (June Sample)

n=117	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	56.860	3.742	0.000	***	78.907	2.805	0.003	***
Partner/CEO_Tenure	9.489	3.470	0.001	***	8.026	2.926	0.002	***
Audit_Firm_Tenure	1.015	0.455	0.325		-0.269	-0.117	0.454	
Market Cap					-0.001	-1.764	0.040	**
LEV					-2.537	-0.336	0.369	
ROA					68.854	1.570	0.060	*
LOSS					-8.786	-0.455	0.325	
Audit Big N					-2.381	-0.159	0.437	
Adjusted R^2	0.098				0.131			
F-stat	7.273		0.001	***	3.507		0.002	***

Panel B: Rank Total Accruals (June Sample)

n=117	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	61.234	3.962	0.000	***	80.088	2.798	0.003	***
Partner/CEO_Tenure*	2.798	2.490	0.007	***	1.135	2.332	0.011	**
Audit_Firm_Tenure	6.179	1.277	0.102		5.704	0.505	0.307	
Market Cap					-0.001	-1.866	0.033	**
LEV					-2.423	-0.316	0.376	
ROA					90.937	2.071	0.021	**
LOSS					-2.438	-0.124	0.451	
Audit Big N					-1.761	-0.116	0.454	
Adjusted R^2	0.054				0.108			
F-stat	4.297		0.016	**	3.000		0.006	***

Table2F.8 (continued)

Tests of association between rank total accruals and tenure on a sub-sample of firms

Panel C: Rank Total Accruals (June Sample, Rank Thirds)								
n=78	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	39.136	1.699	0.047	**	55.028	1.322	0.096	*
Partner/CEO_Tenure	12.389	3.257	0.001	***	10.719	2.821	0.003	***
Audit_Firm_Tenure	2.594	0.782	0.391		-1.016	-0.276	0.392	
Market Cap					-0.002	-1.564	0.061	*
LEV					3.942	0.367	0.358	
ROA					108.952	1.809	0.038	**
LOSS					-9.117	-0.342	0.367	
Audit Big N					8.744	0.399	0.346	
Adjusted R^2	0.132				0.173			
F-stat	6.841		0.002	***	3.296		0.004	***

Panel D: Rank Total Accruals (June Sample, Rank Thirds)								
n=78	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	50.518	2.906	0.003	***	59.617	1.369	0.088	**
Partner/CEO_Tenure*	-0.218	-0.069	0.473		6.212	1.780	0.040	**
Audit_Firm_Tenure	5.704	2.279	0.013	**	1.078	0.290	0.386	
Market Cap					-0.002	-1.594	0.058	*
LEV					3.063	0.276	0.392	
ROA					136.039	2.200	0.016	**
LOSS					-0.682	-0.024	0.491	
Audit Big N					9.352	0.413	0.341	
Adjusted R^2	0.040				0.119			
F-stat	2.603		0.081	*	2.479		0.025	**

All variables as previously defined and reported as one-tailed

*** : Denotes significance at the 1% level

** : Denotes significance at the 5% level

* : Denotes significance at the 10% level

Table 2F.9

Tests of association between absolute total accruals and tenure on a sub-sample of firms

This table presents the results of tests of absolute total accruals and various measures of auditor tenure for a June year end sub-sample. Panel A presents the results for the June year end subsample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for a further refined subsample of firms, taking the lower and upper thirds of absolute total accruals using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of absolute total accruals for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Absolute Total Accruals (June Sample)

n=117	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.140	1.835	0.035	**	-0.013	-0.096	0.462	
Partner/CEO_Tenure	-0.004	-0.266	0.395		-0.002	-0.110	0.457	
Audit_Firm_Tenure	-0.004	-0.360	0.360		0.004	0.366	0.358	
Market Cap					0.000	0.110	0.456	
LEV					-0.003	-0.085	0.467	
ROA					0.322	1.470	0.072	
LOSS					0.289	3.005	0.002	***
Audit Big N					0.043	0.580	0.282	
Adjusted R^2	-0.015				0.034			
F-stat	0.143		0.867		1.587		0.147	

Panel B: Absolute Total Accruals (June Sample)

n=117	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.155	2.069	0.021	**	0.009	0.062	0.475	
Partner/CEO_Tenure*	-0.017	-1.397	0.083		-0.011	-0.932	0.176	
Audit_Firm_Tenure	-0.003	-0.318	0.376		0.005	0.409	0.342	
Market Cap					0.000	0.139	0.445	
LEV					0.000	-0.117	0.454	
ROA					0.314	1.459	0.074	
LOSS					0.278	2.877	0.003	***
Audit Big N					0.038	0.517	0.304	
Adjusted R^2	0.001				0.042			
F-stat	1.085		0.341		1.722		0.111	

Table 2F.9 (continued)

Tests of association between absolute total accruals and tenure on a sub-sample of firms

Panel C: Absolute Total Accruals (June Sample, Rank Thirds)							
n=78	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	0.177	1.601	0.057	*	-0.022	-0.106	0.458	
Partner/CEO_Tenure	-0.004	-0.176	0.431		-0.003	-0.124	0.451	
Audit_Firm_Tenure	-0.006	-0.371	0.356		0.005	0.326	0.373	
Market Cap					0.000	0.097	0.462	
LEV					-0.006	-0.120	0.453	
ROA					0.335	1.082	0.142	
LOSS					0.335	2.574	0.006	***
Audit Big N					0.066	0.599	0.276	
Adjusted R^2	-0.024				0.020			
F-stat	0.111		0.895		1.221		0.303	

Panel D: Absolute Total Accruals (June Sample, Rank Thirds)							
n=78	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	0.205	1.902	0.031	**	0.011	0.054	0.479	
Partner/CEO_Tenure*	-0.026	-1.450	0.076	*	-0.019	-1.033	0.153	
Audit_Firm_Tenure	-0.004	-0.288	0.387		0.006	0.379	0.353	
Market Cap					0.000	0.150	0.441	
LEV					-0.006	-0.105	0.458	
ROA					0.317	1.036	0.152	
LOSS					0.319	2.455	0.009	***
Audit Big N					0.056	0.511	0.306	
Adjusted R^2	0.004				0.034			
F-stat	1.150		0.322		1.389		0.224	

All variables as previously defined and reported as one-tailed

*** : Denotes significance at the 1% level

** : Denotes significance at the 5% level

* : Denotes significance at the 10% level

Table 2F.10

Tests of association between rank absolute total accruals and tenure on a sub-sample of firms

This table presents the results of tests of rank absolute total accruals and various measures of auditor tenure for a June year end sub-sample. Panel A presents the results for the June year end subsample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for a further refined subsample of firms, taking the lower and upper thirds of rank absolute total accruals using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of rank absolute total accruals for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Rank Absolute Total Accruals (June Sample)

n=117	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	115.635	7.116	0	***	92.933	3.064	0.001	***
Partner/CEO_Tenure	-0.402	-1.172	0.122		-2.28	-0.771	0.221	
Audit_Firm_Tenure	-3.428	-0.168	0.434		1.469	0.595	0.277	
Market Cap					0.001	1.355	0.089	*
LEV					-4.933	-0.606	0.273	
ROA					-22.702	-0.48	0.316	
LOSS					25.316	1.217	0.113	
Audit Big N					12.328	0.765	0.223	
Adjusted R^2	-0.003				0.019			
F-stat	0.838		0.435		1.329		0.243	

Panel B: Rank Absolute Total Accruals (June Sample)

n=117	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	116.729	7.284	0.000	***	97.225	3.215	0.001	***
Partner/CEO_Tenure*	-4.483	-1.742	0.042	**	-3.710	-1.436	0.077	*
Audit_Firm_Tenure	-0.838	-0.369	0.357		1.193	0.503	0.308	
Market Cap					0.001	1.420	0.080	*
LEV					-5.215	-0.644	0.261	
ROA					-29.698	-0.640	0.262	
LOSS					21.428	1.029	0.153	
Audit Big N					11.174	0.696	0.244	
Adjusted R^2	0.011				0.032			
F-stat	1.671		0.193		1.556		0.156	

Table 2F.10 (continued)

Tests of association between rank absolute total accruals and tenure on a sub-sample of firms

Panel C: Rank Absolute Total Accruals (June Sample, Rank Thirds)

n=78	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	126.099	5.397	0.000	***	111.872	2.565	0.006	***
Partner/CEO_Tenure	-5.404	-1.198	0.118		-4.639	-1.028	0.154	
Audit_Firm_Tenure	-1.497	-0.443	0.330		1.307	0.364	0.359	
Market Cap					0.001	0.967	0.169	
LEV					-9.286	-0.805	0.212	
ROA					-34.859	-0.528	0.300	
LOSS					32.527	1.171	0.123	
Audit Big N					5.203	0.222	0.413	
Adjusted R^2	0.001				0.021			
F-stat	1.044		0.357		1.239		0.293	

Panel D: Rank Absolute Total Accruals (June Sample, Rank Thirds)

n=78	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	126.639	5.559	0.000	***	115.381	2.662	0.005	***
Partner/CEO_Tenure*	-6.478	-1.707	0.046	**	-5.558	-1.451	0.076	*
Audit_Firm_Tenure	-2.044	-0.633	0.265		0.716	0.207	0.419	
Market Cap					0.001	1.015	0.157	
LEV					-9.067	-0.792	0.216	
ROA					-46.458	-0.712	0.240	
LOSS					26.608	0.960	0.171	
Audit Big N					3.747	0.161	0.873	
Adjusted R^2	0.020				0.036			
F-stat	1.790		0.174		1.405		0.217	

All variables as previously defined and reported as one-tailed

*** : Denotes significance at the 1% level

** : Denotes significance at the 5% level

* : Denotes significance at the 10% level

APPENDIX 2G: Winsorized Results at the 1st and 99th Percentiles

Table 2G.2
Descriptive Statistics

Panel B: Independent and Experimental Variables

	Mean (Median)	Std. Deviation	Minimum	Maximum
Partner/CEO_Tenure	2.709 (2.000)	1.832	1	8
Audit_Firm_Tenure	6.583 (8.00)	2.356	1	8
Partner/CEO_Tenure*	1.775 (1.000)	1.967	0	8
Market Cap	1773.284 (334.866)	3359.861	20.990	17525.340
Leverage	1.906 (1.829)	0.625	1.030	3.770
ROA	0.472 (0.068)	0.123	-0.340	0.390
Loss	0.166 (0.000)	0.373	0	1
Audit_Big_N	0.868 (1.000)	0.340	0	1

All variables as previously defined

Table 2G.3
Correlation Matrix (Winsorized)

	Partner/CEO_Tenure	*Audit_Firm_Tenure*	*Partner/CEO_Tenure**
Partner/CEO_Tenure	1.000	**0.215****	**0.443****
		0.004	**0.000**
Audit_Firm_Tenure	**0.268****	1.000	-0.008
	0.000		(0.460)
Partner/CEO_Tenure*	**0.611****	0.092	1.000
	0.000	0.131	

Pearson correlations are below diagonal and Spearman correlations are above diagonal.
All variables as previously defined
All results are One-tailed tests
** correlation is significant at the 0.001 level
* correlation is significant at the 0.005 level

Table 2G.4

Tests of association between absolute IFRS errors and tenure (winsorized)

This table presents the results of winsorized tests of association of pooled absolute IFRS errors and various measures of auditor tenure. Panel A presents the results for the full sample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for subsample of firms, taking the lower and upper thirds of absolute IFRS errors using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of absolute IFRS errors for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Absolute IFRS Errors (winsorized)

n=151	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.049	3.165	0.001	***	0.028	0.915	0.181	
Partner/CEO_Tenure	0.001	0.420	0.338		0.002	0.777	0.219	
Audit_Firm_Tenure	-0.003	-1.506	0.067	*	-0.001	-0.614	0.270	
Market Cap					0.000	-0.657	0.257	
LEV					-0.004	-0.479	0.317	
ROA					-0.018	-0.277	0.391	
LOSS					0.035	1.640	0.052	*
Audit Big N					0.012	0.792	0.215	
Adjusted R^2	0.002				0.040			
F-stat	1.134		0.325		1.899		0.074	*

Panel B: Absolute IFRS Errors (winsorized)

n=151	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.054	3.464	0.001	***	0.034	1.108	0.135	
Partner/CEO_Tenure*	-0.002	-0.765	0.223		-0.001	-0.315	0.377	
Audit_Firm_Tenure	-0.003	-1.372	0.086	*	-0.001	-0.435	0.332	
Market Cap					0.000	-0.683	0.248	
LEV					-0.005	-0.519	0.302	
ROA					-0.011	-0.173	0.422	
LOSS					0.035	1.598	0.056	
Audit Big N					0.011	0.708	0.240	
Adjusted R^2	0.005				0.037			
F-stat	1.341		0.265		1.820		0.088	*

Table 2G.4 (continued)
Tests of association between absolute IFRS errors and tenure (winsorized)

Panel C: Absolute IFRS Errors, Rank Thirds (winsorized)

n=102	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.066	2.935	0.002	***	0.015	0.322	0.374	
Partner/CEO_Tenure	0.001	0.353	0.363		0.002	0.545	0.294	
Audit_Firm_Tenure	-0.004	-1.374	0.086	*	-0.001	-0.264	0.396	
Market Cap					0.000	-0.669	0.253	
LEV					-0.001	-0.082	0.468	
ROA					0.003	0.029	0.489	
LOSS					0.050	1.456	0.075	*
Audit Big N					0.025	1.100	0.137	
Adjusted R^2	-0.001				0.029			
F-stat	0.945		0.392		1.438		0.199	

Panel D: Absolute IFRS Errors, Rank Thirds (winsorized)

n=102	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	0.072	3.290	0.001	***	0.023	0.488	0.314	
Partner/CEO_Tenure*	-0.003	-0.969	0.168		-0.002	-0.429	0.335	
Audit_Firm_Tenure	-0.004	-1.230	0.111		0.000	-0.143	0.444	
Market Cap					0.000	-0.708	0.240	
LEV					-0.002	-0.112	0.456	
ROA					0.013	0.138	0.446	
LOSS					0.050	1.440	0.077	*
Audit Big N					0.023	1.032	0.153	
Adjusted R^2	0.007				0.028			
F-stat	1.359		0.262		1.421		0.206	

All variables as previously defined and reported as one-tailed
*** : Denotes significance at the 1% level
** : Denotes significance at the 5% level
* : Denotes significance at the 10% level

Table 2G.5

Tests of association between signed IFRS errors and tenure (winsorized)

This table presents the results of winsorized tests of association of pooled signed IFRS errors and various measures of auditor tenure. Panel A presents the results for the full sample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for subsample of firms, taking the lower and upper thirds of signed IFRS errors using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of signed IFRS errors for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Signed IFRS Errors (winsorized)

n=151	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	-0.024	-2.641	0.003	***	-0.039	-2.616	0.016	**
Partner/CEO_Tenure	0.001	0.562	0.288		0.001	0.828	0.205	
Audit_Firm_Tenure	0.002	1.607	0.055	*	0.002	1.389	0.084	*
Market Cap					0.000	0.578	0.282	
LEV					0.009	1.642	0.052	*
ROA					-0.049	-1.316	0.095	*
LOSS					-0.008	-0.612	0.271	
Audit Big N					0.001	0.152	0.440	
Adjusted R^2	0.011				0.017			
F-stat	1.822		0.165		1.379		0.219	

Panel B: Signed IFRS Errors (winsorized)

n=151	**Co-efficient**	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	-0.023	-2.535	0.006	***	-0.037	-2.009	0.023	**
Partner/CEO_Tenure*	0.000	0.070	0.473		0.000	0.093	0.463	
Audit_Firm_Tenure	0.002	1.809	0.037	**	0.002	1.603	0.056	*
Market Cap					0.000	0.525	0.300	
LEV					0.009	1.624	0.054	*
ROA					-0.044	-1.202	0.116	
LOSS					-0.007	-0.581	0.281	
Audit Big N					0.001	0.111	0.456	
Adjusted R^2	0.009				0.013			
F-stat	1.663		0.193		1.276		0.266	

Table 2G.5 (continued)
Tests of association between signed IFRS errors and tenure (winsorized)

Panel C: Signed IFRS Errors, Ranked Thirds (winsorized)

n=102	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	-0.034	-2.650	0.005	***	-0.057	-2.134	0.018	**
Partner/CEO_Tenure	0.002	0.647	0.260		0.002	0.736	0.232	
Audit_Firm_Tenure	0.003	1.520	0.066	*	0.003	1.388	0.085	*
Market Cap					0.000	0.795	0.215	
LEV					0.013	1.671	0.049	**
ROA					-0.058	-1.099	0.138	
LOSS					-0.009	-0.514	0.305	
Audit Big N					0.003	0.182	0.428	
Adjusted R^2	0.016				0.024			
F-stat	1.815		0.168		1.353		0.235	

Panel D: Signed IFRS Errors, Ranked Thirds (winsorized)

n=102	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	-0.032	-2.513	0.007	***	-0.053	-1.937	0.028	**
Partner/CEO_Tenure*	0.000	0.001	0.500		0.000	-0.199	0.422	
Audit_Firm_Tenure	0.003	1.778	0.040	**	0.003	1.629	0.054	*
Market Cap					0.000	0.755	0.226	
LEV					0.013	1.691	0.047	**
ROA					-0.053	-1.012	0.157	
LOSS					-0.010	-0.572	0.285	
Audit Big N					0.001	0.077	0.470	
Adjusted R^2	0.012				0.019			
F-stat	1.599		0.207		1.274		0.272	

All variables as previously defined and reported as one-tailed
*** : Denotes significance at the 1% level
** : Denotes significance at the 5% level
* : Denotes significance at the 10% level

Table 2G.6

Tests of association between ranked signed IRS Errors and tenure (winsorized)

This table presents the results of winsorized tests of association of rank signed IFRS errors and various measures of auditor tenure. Panel A presents the results for the full sample firms. Panel B presents the results using the partner/CEO tenure measure. Panel C presents results for subsample of firms, taking the lower and upper thirds of rank signed IFRS errors using the partner/CEO tenure measure. Panel D reports the results for a subsample firms, taking the lower and upper third of rank signed IFRS errors for the partner/CEO tenure measure times the dummy variable of the CEO pay slice to represent powerful CEOs.

Panel A: Rank Signed IFRS Errors (winsorized)

n=151	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	54.247	5.008	0.000	***	33.723	1.545	0.063	*
Partner/CEO_Tenure	0.146	0.562	0.288		0.528	0.255	0.400	
Audit_Firm_Tenure	3.244	2.081	0.020	**	3.222	1.971	0.026	**
Market Cap					0.001	0.819	0.207	
LEV					5.927	0.920	0.180	
ROA					-18.006	-0.397	0.346	
LOSS					2.124	0.139	0.445	
Audit Big N					8.299	0.750	0.228	
Adjusted R^2	0.018				0.000			
F-stat	2.380		0.096	*	1.008		0.428	

Panel B: Rank Signed IFRS Errors (winsorized)

n=151	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	55.796	5.199	0.000	***	37.264	1.687	0.047	**
Partner/CEO_Tenure*	-1.065	-0.590	0.278		-0.934	-0.504	0.308	
Audit_Firm_Tenure	3.356	2.228	0.014	**	3.356	2.104	0.019	
Market Cap					0.001	0.831	0.204	
LEV					5.612	0.869	0.194	
ROA					-16.910	-0.377	0.354	
LOSS					1.233	0.079	0.469	
Audit Big N					7.541	0.679	0.249	
Adjusted R^2	0.020				0.002			
F-stat	2.556		0.081	*	1.036		0.409	

Table 2G.6 (continued)
Tests of association between ranked signed IRS Errors and tenure (winsorized)

Panel C: Rank Signed IFRS Errors, Ranked Thirds (winsorized)

n=102	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	49.044	3.277	0.001	***	12.438	0.395	0.347	
Partner/CEO_Tenure	-0.104	-0.036	0.486		0.118	0.039	0.485	
Audit_Firm_Tenure	4.192	1.919	0.029	**	4.177	1.869	0.033	**
Market Cap					0.002	1.031	0.153	
LEV					12.848	1.370	0.087	*
ROA					-30.790	-490.000	0.313	
LOSS					0.302	0.014	0.495	
Audit Big N					11.662	0.646	0.260	
Adjusted R^2	0.019				0.008			
F-stat	2.001		0.141		1.119		0.358	

Panel D: Rank Signed IFRS Errors, Ranked Thirds (winsorized)

n=102	Co-efficient	t-stat	p-value		Co-efficient	t-stat	p-value	
Constant	51.503	3.452	0.001	***	19.557	0.608	0.273	
Partner/CEO_Tenure*	-1.895	-0.699	0.243		-2.146	-0.752	0.227	
Audit_Firm_Tenure	4.272	2.050	0.022	**	4.256	1.978	0.026	**
Market Cap					0.002	1.074	0.143	
LEV					12.825	1.374	0.087	*
ROA					-34.705	-0.555	0.290	
LOSS					-2.650	-0.118	0.453	
Audit Big N					8.306	0.454	0.326	
Adjusted R^2	0.024				0.014			
F-stat	2.254		0.110		1.206		0.307	

All variables as previously defined and reported as one-tailed
*** : Denotes significance at the 1% level
** : Denotes significance at the 5% level
* : Denotes significance at the 10% level

CHAPTER THREE APPENDICIES

For continuity, the tables in the following appendices are not sequential, and instead follow the main results tables as set out in chapter three.

APPENDICIES 3A: Pooled Sample Split by Year

Table 3A.4
Evaluating Audit Fees over Audit Tenure
Pooled Sample Split by Year

Panel A: Pooled Sample Split by Year, 2005

obs = 688	*Dichotomous 1-3years Variable*							
	Co-efficient	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	6249.220	0.557	0.578		-5856.647	-0.190	0.849	
First	-70319.455	-1.835	0.067	*	-58213.588	-1.215	0.225	
FIRST * $AuditFee_{t-1}$	0.591	23.250	0.000	***	0.407	1.709	0.088	*
AF_{t-1}	1.271	110.153	0.000	***	1.455	6.138	0.000	***
Audit_Firm_Tenure					11638.426	0.350	0.727	
Audit_Firm_Tenure * $AuditFee_{t-1}$					-0.185	-0.778	0.437	
Adjusted R	0.965				0.965			
F-stat	6322.928		0.000	***	3786.209		0.000	***

Panel B: Pooled Sample Split by Year, 2006

obs = 688	*Dichotomous 1-3years Variable*							
	Co-efficient	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	29440.557	1.514	0.131		29516.885	0.689	0.491	
First	-10986.803	-0.167	0.867		-11063.130	-0.153	0.879	
FIRST * $AuditFee_{t-1}$	-0.275	-0.859	0.391		-0.116	-0.388	0.698	
AF_{t-1}	1.088	88.650	0.000	***	0.929	48.460	0.000	***
Audit_Firm_Tenure					-27244.125	-0.576	0.565	
Audit_Firm_Tenure * $AuditFee_{t-1}$					0.246	10.328	0.000	***
Adjusted R	0.920				0.931			
F-stat	2636.972		0.000	***	1850.034		0.000	***

Table 3A.4 (continued)
Evaluating Audit Fees over Audit Tenure
Pooled Sample Split by Year

Panel C: Pooled Sample Split by Year, 2007

obs = 688	*Dichotomous 1-3years Variable*							
	Co-efficient	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	17348.357	0.816	0.415		9806.738	0.211	0.833	
First	-80182.402	-1.293	0.196		-72640.783	-0.976	0.329	
FIRST * $AuditFee_{t-1}$	0.859	3.997	0.000	***	0.801	3.727	0.000	***
AF_{t-1}	1.130	96.045	0.000	***	1.187	49.578	0.000	***
Audit_Firm_Tenure					14718.907	0.281	0.779	
Audit_Firm_Tenure * $AuditFee_{t-1}$					-0.075	-2.744	0.006	***
Adjusted R	0.932				0.932			
F-stat	3121.264		0.000	***	1889.565		0.000	***

Panel D: Pooled Sample Split by Year, 2008

obs = 688	*Dichotomous 1-3years Variable*							
	Co-efficient	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	94279.513	3.854	0.000	***	19152.935	0.375	0.708	
First	-95172.277	-1.238	0.216		-200045.698	-0.226	0.821	
FIRST * $AuditFee_{t-1}$	0.037	0.986	0.324		-0.280	-2.304	0.022	**
AF_{t-1}	0.881	71.133	0.000	***	1.197	10.291	0.000	***
Audit_Firm_Tenure					86408.125	1.481	0.139	
Audit_Firm_Tenure * $AuditFee_{t-1}$					-0.321	-2.747	0.006	***
Adjusted R	0.893				0.894			
F-stat	1913.596		0.000	***	1159.743		0.000	***

Table 3A.4 (continued)
Evaluating Audit Fees over Audit Tenure
Pooled Sample Split by Year

Panel E: Pooled Sample Split by Year, 2009

obs = 688	*Dichotomous 1-3years*							
	Co-efficient	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	-8642.945	-0.678	0.498		-8343.706	-0.324	0.746	
First	62740.310	1.252	0.211		61326.001	1.151	0.250	
FIRST * $AuditFee_{t-1}$	-0.567	-2.811	0.005	***	-0.688	-3.531	0.000	***
AF_{t-1}	1.051	161.120	0.000	***	1.175	64.969	0.000	***
Audit_Firm_Tenure					-13.913	0.000	1.000	
Audit_Firm_Tenure * $AuditFee_{t-1}$					-0.140	-7.259	0.000	***
Adjusted R	0.974				0.976			
F-stat	8695.680		0.000	***	5636.058		0.000	***

All variables as previously defined and reported as two-tailed
*** : Denotes significance at the 1% level
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* : Denotes significance at the 10% level

APPENDIX 3B: Large versus Small Audit Fees

Table 3B.4
Evaluating Audit Fees over Audit Tenure
Pooled Sample Split by Median Audit Fees

Panel A: Pooled, Median Split by Audit Fees (Large)

obs = 1727	*Dichotomous 1-3years Variable*							
	Co-efficient	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	74822.258	3.955	0.000	***	54215.689	1.215	0.224	
First	-102859.836	-1.507	0.132		-82262.096	-1.038	0.300	
FIRST * $AuditFee_{t-1}$	0.204	5.766	0.000	***	0.165	4.113	0.000	***
AF_{t-1}	1.036	129.219	0.000	***	1.076	52.900	0.000	***
Audit_Firm_Tenure					27605.110	0.560	0.575	
Audit_Firm_Tenure * $AuditFee_{t-1}$					-0.047	-2.127	0.034	**
Adjusted R	0.913				0.913			
F-stat	6005.211		0.000	***	3609.309		0.000	***

Panel B: Pooled, Median Split by Audit Fees (Small)

obs = 1713	*Dichotomous 1-3years Variable*							
	Co-efficient	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	22944.778	31.350	0.000	***	19523.987	12.599	0.000	***
First	2996.376	1.552	0.121		6417.167	2.715	0.007	***
FIRST * $AuditFee_{t-1}$	-0.187	-4.958	0.000	***	-0.265	-5.402	0.000	***
AF_{t-1}	0.482	30.719	0.000	***	0.560	15.942	0.000	***
Audit_Firm _Tenure					4359.471	2.479	0.013	**
Audit_Firm _Tenure * $AuditFee_{t-1}$					-0.098	-2.491	0.013	**
Adjusted R	0.374				0.376			
F-stat	341.720		0.000	***	206.951		0.000	***

All variables as previously defined and reported as two-tailed
*** : Denotes significance at the 1% level
** : Denotes significance at the 5% level
* : Denotes significance at the 10% level

Table 3B.6

Association between Partner/CEO Tenure and Audit Fees
Pooled Sample Split by Median Audit Fees

Panel A: Pooled, Median Split by Audit Fees (Large)

obs=3440; n=688	*Dichotomous 1-3years*			
	Co-efficient	**t-stat**	**p-value**	
Constant	75318.195	1.454	0.146	
First	-92799.257	-1.165	0.244	
First * $AuditFee_{t-1}$	0.195	4.820	0.000	***
AF_{t-1}	1.023	42.846	0.000	***
Audit_Firm Tenure	28150.389	0.573	0.567	
Audit_Firm Tenure * $AuditFee_{t-1}$	-0.054	-2.460	0.014	**
Partner/CEO Tenure	-9856.890	-0.777	0.437	
Partner/CEO Tenure * $AuditFee_{t-1}$	0.022	4.192	0.000	***
Adjusted R	0.913			
F-stat	2604.067		0.000	***

Panel B: Pooled, Median Split by Audit Fees (Small)

obs=3440; n=688	*Dichotomous 1-3years*			
	Co-efficient	**t-stat**	**p-value**	
Constant	21245.522	12.668	0.000	***
First	5795.373	2.443	0.015	**
First * $AuditFee_{t-1}$	-0.260	-5.254	0.000	***
AF_{t-1}	0.546	14.239	0.000	***
Audit Firm Tenure	4800.049	2.719	0.007	***
Audit Firm Tenure * $AuditFee_{t-1}$	-0.103	-2.594	0.010	***
Partner/CEO Tenure	-819.783	-2.587	0.010	***
Partner/CEO Tenure * $AuditFee_{t-1}$	0.005	0.673	0.501	
Adjusted R	0.378			
F-stat	149.402		0.000	***

All variables as previously defined and reported as two-tailed
*** : Denotes significance at the 1% level
** : Denotes significance at the 5% level
* : Denotes significance at the 10% level

Appendix 3C: Dichotomous Firm Tenure, 1-5years

This appendix presents results for each of the main regression models, where audit firm tenure is reported using a dichotomous variable of one-to-five years.

Table 3C.7
Evaluating Audit Fees over Audit Tenure
Dichotomous Firm Tenure, 1-5years

Dichotomous Firm Tenure 1-5years								
obs=3440; n=688	*Dichotomous 1-5years*							
	Co-efficient	**t-stat**	**p-value**		**Co-efficient**	**t-stat**	**p-value**	
Constant	26142.108	1.682	0.093	*	26499.765	1.702	0.089	*
First	-44307.150	-1.410	0.159		-44487.985	-1.416	0.157	
First*AuditFee$_{t-1}$	0.225	8.626	0.000	***	0.225	8.628	0.000	***
AF$_{t-1}$	1.014	98.781	0.000	***	1.014	98.723	0.000	***
Audit_Firm_Tenure	16326.116	0.842	0.400		17415.369	0.893	0.372	
Audit_Firm_Tenure * AuditFee$_{t-1}$	0.004	3.132	0.002	***	0.004	3.119	0.002	***
Partner/CEO Tenure					-28666.385	-0.612	0.541	
Partner/CEO Tenure * AuditFee$_{t-1}$					0.086	0.417	0.677	
Adjusted R	0.918				0.918			
F-stat	7694.195		0.000	***	5493.346		0.000	***

All variables as previously defined and reported as two-tailed
*** : Denotes significance at the 1% level
** : Denotes significance at the 5% level
* : Denotes significance at the 10% level