AUDITOR-CLIENT NEGOTIATIONS OVER ACCOUNTING ISSUES - FIELD EVIDENCE

Ellen M. Kulset

The Norwegian School of Economics

ABSTRACT

This study investigates the relationship of each of four variables to the auditorôs combined use of the contending and the conceding strategy in auditor-client negotiations over accounting issues. These variables are the precision of accounting regulation, the audit partnerôs general level of experience, the clientôs accounting expertise, and the auditor-client relationship. Based on a survey of 79 auditor-client negotiations conducted in one of the big-four audit firms, I find that as hypothesized the precision of accounting regulation is positively related to the auditorôs choice of negotiation strategy (i.e. the more precisely regulated the accounting issue is, the more contending is the auditorôs overall negotiation strategy) and that the clientôs accounting expertise and the quality of the auditor-client relationship are negatively related to the auditorôs combined use of the contending and the conceding negotiation strategy (i.e. the higher the clientôs accounting expertise, the less contending is the auditorôs overall negotiation strategy and the more positive the auditor-client relationship, the less contending is the auditorôs overall negotiation strategy). The partnerôs experience is found to be positively related to the auditorôs combined use of the contending and the conceding negotiation strategy (i.e. the more experience the partner has, the more contending is the auditorôs overall negotiation strategy). Further findings indicate that the precision of accounting regulation is by far the most important independent variable. The study also investigates the importance of the variablesð the precision of accounting regulation, the audit partnerôs general level of experience, the clientôs accounting expertise, the auditor-client relationship and the auditorôs combined use of the contending and the conceding negotiation strategyð in predicting accounting outcomes of auditor-client negotiations over accounting issues. I find that the most important variable in predicting the accounting outcome is the precision of accounting regulation, but the auditorôs choice of negotiation strategy and the audit partnerôs general level of experience also seem to have effects, as does audit risk as a control variable.

ACKNOWLEDGEMENTS

Finally, the day has arrived when I write the acknowledgement section, and I think about everyone I need to thank for help and encouragement during the years I have spent writing this thesis.

First of all I want to thank the three members of my committee: Professor Iris Stuart, Professor Kjell Grønhaug and Professor William F. Messier. Iris became my main supervisor when my project needed a restart, and I thank her for always giving me prompt and thorough feedback and for being a lot more interested in my project than I could ever have expected. I thank her for inspiring discussions and helpful suggestions relating to my project but also for interesting conversations about everything from international politics to perennials. I thank Kjell for invaluable help, in particular for helping me to see how I could structure my research and my writing but also for his constant reminder that I was making good progress and just needed to keep on working. I thank Bill for suggesting that I should start looking at the auditor-client negotiation literature and for helping me to get in touch with people that had been doing research in this area previously.

There are also a number of other persons I would like to thank: Professor Aasmund Eilifsen and Professor Frøystein Gjesdal for hiring me and believing in me and my project from the very beginning. Professor Terje Lensberg for encouraging me to write a doctoral dissertation when I was still at the HAS. Dr. Bruce Stuart for giving me feedback on how to write a thesis, in particular for helping me to improve my English grammar. I also want to thank Professor Trond Bjørnenak and Professor Katarina Kaarbøe for administrative and moral support.

I have received helpful feedback on proposals and draft versions, comments, inspiration and other types of help from a number of persons: Professor Steven Salterio, Professor Stuart Turley, Professor Robert Knechel, Assistant Professor Don Cram, Professor Emeritus Steinar Ekern, Professor Atle Johnsen, participants at the EARNet 2011 Conference and FIBE 2012 Conference and Magne Ludvigsen at the IT-help desk. I also want to thank Elisabeth Stiegler for nice chats about all and nothing and Hilde Kinserdal for listening to my many frustrations about how it can possibly be so difficult to write a thesis.

I am grateful to all employees at the Department of Accounting, Auditing and Law and to former lecturers and colleagues at NHH for encouraging support, to NHH for funding my project and to the Big 4 audit firm which agreed to participate in my study.

I am thankful also to my parents for support and encouragement, for teaching me to love books and appreciate academic work.

Finally, I want to thank my husband, Vegar and our five children: Kristian, Sindre, Magnus, Johannes and Eline. Thank you for your constant love and support! I promise that I will spend less time in front of the computer in the evenings from now on!

TABLE OF CONTENTS

LIST OF TABLES

LIST OF FIGURES

1.0. INTRODUCTION

During an audit, an auditor may discover a number of accounting treatments that he questions, including misstatements and the need for disclosures of different types. The client and the auditor may have different preferences regarding the desired recording of these issues; but because both clients and auditors normally prefer audit opinions without qualifications, they have to reach agreement before the issuance of a clean audit opinion.

The final outcome that resolves the disagreement may equal the initial preferences of one of the two parties, be somewhere between the original positions of the two parties, or be generated as a new solution. Whatever the case, the outcome is related to the judgments and decisions made by the auditor *and* the client in the negotiation process.

The resolution process may lead to an ñunder-optimalò solution that is due to client-pressure[1] or the auditorõs being over-confident about his own abilities to pick the right solution. Any such resolution has an effect on the flow of information to the users of the financial statements (Burgstahler and Dichev 1997), and the process can result in poor information value and even lead to economic losses for stakeholders relying on the reported financial information.[2]

Prior empirical research in auditor-client conflicts seeks primarily to reveal which variables seem to have an impact on the outcome of auditor-client conflicts. Most studies research the effects of variables related to the risks and rewards faced by the auditor and show that variables such as accounting regulation, engagement risk and provision of non-audit services are related to the accounting outcome of the conflict (e.g. Knapp 1985; Lindsay 1990; Trompeter 1994; Hackenbrack and Nelson 1996). A handful of studies investigate factors related to auditor characteristics such as the auditorõs locus of control and ethical reasoning (Tsui and Gul 1995) and the auditorõs identification with the client (Bamber and Iyer 2007). A

---

[1] According to DeAngelo (1981), the value of an audit to financial statement users is based on the auditorõs ability to detect errors *and* withstand pressures from the client to selectively report detected errors.

[2] According to Barron and Stice (2001, p. 450) costs may also be imposed on stakeholders if understatement errors are left uncorrected and can, for instance, have an effect if a banker ñrefuses a profitable loan on the basis of understated financial performance.ò

more comprehensive presentation of auditor-client conflict research will be given in section 2.4.6.

Over the years, there has been a growing awareness that auditors and clients *negotiate* when they resolve disputed financial reporting issues. Antle and Nalebuff (1991, p. 31) focus on the negotiated character of the financial statements and assert:

> The statement becomes a joint-venture if the auditor is unwilling to provide an unqualified opinion on managementôs stated representations. At that point, the auditor and client begin negotiations in which the auditor may offer a revised statement. The client may threaten to dismiss him and find one more accepting of his views. Or they may decide to extend the audit to obtain more facts. In the end, compromises are usually found, statements are revised, and the auditor issues an unqualified opinion on the revised statements.

Following this awareness, we have seen a renewed interest in the study of auditor-client conflicts and that a line of research investigating auditor-client negotiations using negotiation theory has emerged. This line of research differs from the studies labeled ñauditor-client conflict studiesò, in that such research often has a focus on auditorsô behavior in auditor-client negotiations and thus contributes to our knowledge of the audit process which still is often described as a ñblack boxò[3] (Gendron et al. 2004), i.e. we know what results from the process but we do not know *how* the judgment or decision is made. More knowledge on how an audit is conducted is particularly valuable as it constitutes an important first step to change or improve the processes underlying the audit. Because we seldom know whether the accounting outcome of the audit process is good or bad, the knowledge of what auditors do is a good starting point for such improvements.[4]

Findings from previous audit negotiation studies indicate that auditors behave differently depending upon the negotiation issue and/or context (e.g. Goodwin 2002; Hatfield et al. 2008; Brown and Johnstone 2009). A more comprehensive presentation of these studies is given in

---

[3] Gendron et al. (2004) study ñpractices in effective audit committeesò and define the ñblack boxò approach as ñthe examination of the relationship between *externally observable features* of audit committees and indicators of effectivenessò (Gendron et al.2004, p. 155).

[4] Bonner (1999) suggests that one should distinguish between practical and theoretical reasons to understand the motivation behind studies of auditors´ judgments and decisions. From a practical perspective we know that auditors make important decisions, but we also know that these decisions are not necessarily high-quality decisions. Consequently it is interesting to know more about *how* these decisions are made. From a theoretical point-of-view, research in auditors´ judgments and decisions are interesting because the ñaccounting settings have unique features for which theories in underlying disciplines are not well developedò (Bonner 1999, p. 387).

section 2.4.6.4. Prior research also indicates that negotiatorsô choice of negotiation strategy is dependent both upon the negotiatorôs personal characteristics and the negotiation situation (e.g. Graziano et al. 1996; Friedman et al. 2000).

The purpose of my thesis is to describe what happens inside the ñblack-boxò of auditor-client negotiations and more specifically to first study the relationship between four different contextual variables (the precision of accounting regulation, the audit partnerôs experience, the clientôs accounting expertise and the auditor-client relationship), the negotiation process and accounting negotiation outcomes. These contextual variables relate either to the negotiation situation or the negotiator and Gibbins et al. (2007) suggest (but do not test) that these are the most important variables in auditor-client negotiations over accounting issues.

Second, I investigate the relationship between auditorsô choice of negotiation strategies and tactics and the accounting negotiation outcomes and construct a model that can be used to predict accounting outcomes in auditor-client negotiations. The third aim of my thesis is to investigate the relative importance of the contextual factors listed above in auditor-client negotiations over accounting issues.

Prior research shows that the precision of the accounting regulation has an effect on accounting outcomes in auditor-client conflicts (e.g. Knapp 1985 and Ng and Tan 2003) , and my study will contribute to this volume of prior research by examining the relationship between the precision of accounting regulation and a direct measure of the auditorôs negotiation strategy choice as well as contribute to the understanding of the relative importance of the precision of accounting regulation compared to other contextual variables.

The effects or the importance of the clientôs accounting expertise in auditor-client negotiations or auditor-client conflicts has, to my knowledge, not yet been studied.

Gibbins et al. (2010) study the effect of auditor-client relationship in an experimental study and find that the quality of the relationship has an effect on auditorsô use of the conceding negotiation strategy but not on the use of the contending negotiation strategy. This finding is not in line with findings in prior generic negotiation studies. In my dissertation I extend this research by using another research method as well as another measure for auditor-client relationship (a one-dimensional measure using a five-point scale).

Prior findings on the effects of (auditor) experience on auditor negotiation behavior are also mixed and more research is needed to understand the effect of auditor experience in negotiations. I will in my study examine whether newly appointed partners behave differently than more experienced partners and, if there is a difference, to determine *when* the new partners seem to have acquired enough experience to behave as experienced partners.

Second my study is, due to its design, likely to include many different types of auditor-client negotiations over accounting issues and in this way extend prior research. As follows from the presentation of relevant empirical research in section 2.4.6.4 (see Table 3), *all* previous theory-testing studies on auditorsô choice of negotiation strategies are conducted using experimental research methods. In these studies a limited number of types of negotiations are studied (see section 2.4.3 for an overview of which types of negotiations that are previously studied).

Third, my study uses field data to study auditor-client negotiations. In my thesis, I study auditor behavior in auditor-client negotiations over accounting issues in a sample of 79 audit engagements. Data on auditor behavior is collected through the use of a questionnaire in which auditors self-report their own behavior. My approach consequently seeks to measure auditorsô self-perception of their negotiation behavior. Compared to the experimental method that study how auditors think they would behave if they were to conduct an audit as described in the written experimental material, I study how auditors think they conducted a negotiation that recently occurred. Auditor behavior is measured by the use of measures developed in generic negotiation theory on negotiation strategies and tactics, and these measures have been used previously in auditing research in studies by Goodwin (2002), Gibbins et al. (2010) and McCracken et al. (2011).

Prior auditor-client negotiation research examines different negotiation strategies one at a time. As auditors often use elements from several different strategies when they negotiate, I will also contribute to prior research by using a measure that investigates the combined use of two of the strategies; the contending and the conceding negotiation strategies. Finally, my research design will allow me not only to study whether independent variables are important but also to contribute to an understanding of the magnitude of impact of each variable.

The results of the study show that auditorӳ combined use of the contending and the conceding negotiation strategies is related to the precision of the accounting regulation, the quality of the auditor-client relationship, the audit partnerӳ general experience and the clientӳ technical accounting knowledge. The study also shows that the precision of the accounting regulation is the most important variable.

In addition, the study corroborates the importance of the precision of the accounting regulation when predicting the accounting outcome of auditor-client negotiations over accounting issues. Furthermore, the audit partnerӳ experience, the auditorӳ choice of negotiation strategy and the audit risk seem to have an impact in predicting the accounting outcome in such negotiations.

The knowledge obtained in this study provides new insights to auditors about how they perceive their negotiations with clients, and these insights can be implemented as a part of auditorsԠtraining programs to enhance auditorsԠunderstanding of how they behave when negotiating with clients.

The remainder of the dissertation is organized as follows. Chapter 2 provides the theoretical background of the study including an introduction to relevant literature and chapter 3 presents a model of the research project and hypotheses are developed in this chapter. Chapter 4 presents the research design, and chapter 5 reports the results from the empirical study. The final chapter 6 is devoted to a discussion of the major findings and implications of the study for practice and future research.

2.0. BACKGROUND

2.1. Introduction

The purpose of this chapter is to define basic negotiation concepts, to provide an overview of prior research to identify important areas that have not previously been studied and to provide the background for the theoretical arguments that will be further developed in the hypothesis sections in chapter 3.

In this chapter, I first present the definitions of negotiations that are used in prior research and discuss important characteristics of auditor-client negotiations. In section 2.3, I present different types of negotiations and in section 2.4, I present and discuss prior research that is relevant for the topic of this thesis. The summary in section 2.4.7 concludes the chapter and links the findings in the literature review to my research project. Section 2.4.7 first summarizes independent variables identified and/or found significant in prior research in auditor-client negotiations. This knowledge is used in chapter 3 and 4 to develop hypotheses and to identify possible confounding factors in my study. The section also emphasizes that all prior auditor-client negotiation studies are conducted with the experimental method and that no prior studies investigate the relative importance of different contextual variables in auditor-client negotiation. These findings provide background for my choice of research design which is further examined in chapter 4.

2.2. Auditor-client negotiations defined

A definition of negotiation often cited in auditing research is made by Murigham and Bazerman (1990, p. 642) who define negotiations as ñany context in which two or more parties with *differing preferences* jointly make decisions that affect the welfare of both (all) partiesò. Another oft-cited definition is from Pruitt and Carnevale (1993, p. 2) who define a negotiation as ña discussion between two or more parties with the apparent aim of resolving a *divergence of interest* and thus escaping social conflictò. By divergence of interest, Pruitt and Carnevale (1993) mean that the negotiation parties have incompatible preferences. From these definitions we see that while all negotiations consist of discussion, all discussions are not necessarily negotiations as discussions may also take place when parties do not have incompatible preferences.

In the accounting setting, auditors and clients engage in negotiations primarily when they disagree about different accounting issues but negotiation takes place also when they make decisions on issues such as the size of the audit fee. This thesis will investigate only negotiations over accounting issues.

Several distinct features characterize auditor-client negotiations over accounting issues and the judgments made by auditors during such processes; these features distinguish auditor-client negotiations over accounting issues from other negotiations. Firstly, both parties (auditor and client) negotiate on behalf of others (the stakeholders of the financial statements), and the interests of the negotiation parties may differ from the interests of the stakeholders. Secondly, the auditors have professional and statutory responsibilities that limit their choices, and they use their professional expertise in accounting when they negotiate. All accounting and auditing judgment tasks ñare embedded in pervasive institutional settingsò and the auditorôs judgments and decisions are made in a setting that are characterized by team-work, a strong professional society, the existence of a market for audit services, the presence of different governmental agencies (e.g. Finanstilsynet, The Financial Supervisory Authority of Norway) and possible legal sanctions (Ashton and Ashton 1995, p. 7). In this regulated environment, some solutions are preferable to others in that they better reflect the economic situation of the client company. Thirdly, the auditorï client negotiation over accounting issues takes place in an ongoing relationship which may lead the auditor to accept solutions that the client prefers in order to please the client and to avoid getting fired. Fourthly, the consequences of bad judgments can be significant for the auditor and the client, as well as for other relevant stakeholders, for instance, the owners of the client entity. Fifthly, it should be noted that agreement is not necessary in auditor-client negotiations over accounting issues because auditors will issue a modified audit opinion, if it is necessary, and they also have the possibility to resign from a client if the two parties cannot manage to agree on the financial statements.

2.3. Different negotiation types

From a theoretical perspective, some negotiations are characterized by a complete conflict of interest. Raiffa (1982) call these negotiations *distributive* bargaining. According to Raiffa: ñIn the distributive case one single issue, such as money, is under contention and the parties have almost strictly opposing interests on that issue: the more you get, the less the other party gets, and - with some exceptions and provisos ï you want as much as you can getò (Raiffa 1982, p. 33). In a distributive negotiation one of the parties wins the negotiation or the two parties agree on a compromise.

In other negotiations there are possibilities for a joint gain, meaning that a solution exists with which the negotiation parties can achieve higher joint benefits (higher collective utility) than they would achieve with a compromise. This latter negotiation type is called *integrative* bargaining (Raiffa 1982). The solution obtained is called an integrative solution and as the parties are better off with this solution than with a compromise, the negotiation parties will prefer to obtain an integrative solution. It should be noted that higher collective utility does not mean that both the negotiation parties are better off than they would have been with a win-lose outcome, but a win-lose outcome is often not feasible as the losing party will prefer a non-agreement solution instead of a win-lose solution. Distributive negotiations can be transformed into integrative bargaining, for instance, by introducing contingency payments at different time periods or by negotiating several issues at a time (Raiffa 1982).

In accounting, we want the negotiation parties to come up with the solution that is the best when it comes to reflecting the economic situation of the client company (highest possible information value). If the client company is involved in earnings management and the auditor have incentives to accept the solution the client wants, an accounting solution with high collective utility is not necessarily preferable for the stakeholders in the company. Consequently, an integrative solution is not necessarily what the negotiation parties should strive to obtain in accounting.

Brown and Wright (2008) suggest that if the auditor and the client disagree about the use of an aggressive reporting method, this negotiation has an integrative potential (there exists an outcome with higher collective utility than the utility obtained with a compromise) as ñAn auditor may allow a client to use an aggressive reporting method as long as the client discloses the method in the footnotes to the financial statementsò (Brown and Wright 2008, p. 92). Even though this solution has the properties of an integrative solution, I claim that this solution should not be chosen unless this solution better reflects the economic situation of the firm than the solutions that have so far been considered.

Several researchers (Sanchez et al. 2007; Hatfield et al. 2008) have recently suggested, in line with the ideas in Raiffa (1982), that auditors can change negotiations over distributive issues (without value-creating potential) into integrative (value-creating) negotiations by adding immaterial issues to the list of issues to negotiate and then suggesting that the immaterial issues do not have to be corrected. The underlying idea is that the client will be more likely to record corrections suggested by the auditor when he realizes that he will not have to change the immaterial issues. Findings from these studies will be presented in section 2.4.6.4.

2.4. What we know about auditor-client negotiations ï a review of relevant literature

2.4.1. Introduction

A number of empirical research studies have been conducted that contribute to our understanding of auditor-client negotiations over accounting issues. In the rest of section 2.4, I will review theories and findings from generic negotiation research and audit research that are relevant to my research questions. Brown and Wright (2008) have reviewed this body of research previously, but because many of the auditor-client negotiation studies have been conducted in recent years, an update of the Brown and Wright review is necessary. My review differs from the Brown-Wright summary mainly in that my focus is on previously studied independent variables that are relevant to our understanding of auditor-client negotiations. The motivation behind my review is twofold: to provide the necessary background on the concepts of negotiation strategies and outcomes and to provide an overview of the independent variables that are related to auditor-client negotiation processes and outcomes as treated in previous research. This overview will constitute the necessary background to position my research in the larger body of auditor-client conflict research.

More specifically, in the following section 2.4.2 I first present a negotiation model developed by Gibbins et al. (2001 and 2007). I then use this model as a framework to elaborate on particular findings from the body of auditor-client conflict and negotiation research: In section 2.4.3, I present findings from research related to the inputs in the model, i.e. on what types of issues auditors and clients negotiate. In section 2.4.4, I present findings related to the negotiation process. In section 2.4.5, I present research findings on the outcomes of auditor-client negotiations. Section 2.4.6 is the most voluminous and presents research findings on ñthe relationship between context, process and negotiation outcomesò. This section includes findings from several different audit research streams that are of relevance for the topic of my thesis. A discussion about which streams that are relevant and which that are not is included in the introduction to section 2.4.6.

<u>2.4.2. The Gibbins et al. (2001) model of auditor-client negotiation</u>

Based on generic negotiation theory and supplemented by interviews with 18 senior practitioners, Gibbins et al. (2001) develop a three-element process model for auditor-client negotiations over accounting issues. The negotiations are modeled as ña process proceeding from triggering events through a number of stages, informed by the antecedents to that event and by expectations about consequencesò (Gibbins et al. 2007, p. 390). In the model, Gibbins et al. (2001) distinguish between the issue, the process itself and the outcome (see Figure 1 for a sketch of the model, adapted from Gibbins et al. 2001). ñThe process begins with the negotiation *issue*, which exists in the context of past negotiations and the relationships between the parties. Various choices and actions constitute the negotiation *process*. The result is the negotiation *outcome*. Each negotiation becomes an antecedent for the next one.ò (Gibbins et al. 2001, p. 537) Contextual features ñpotentially influence or are influenced by any of the three negotiation process elementsò and are divided into three groups: the role of external conditions and constraints, the interpersonal auditorïclient context and the capabilities of the parties, including accounting expertise. (Gibbins et al. 2001, p. 537)

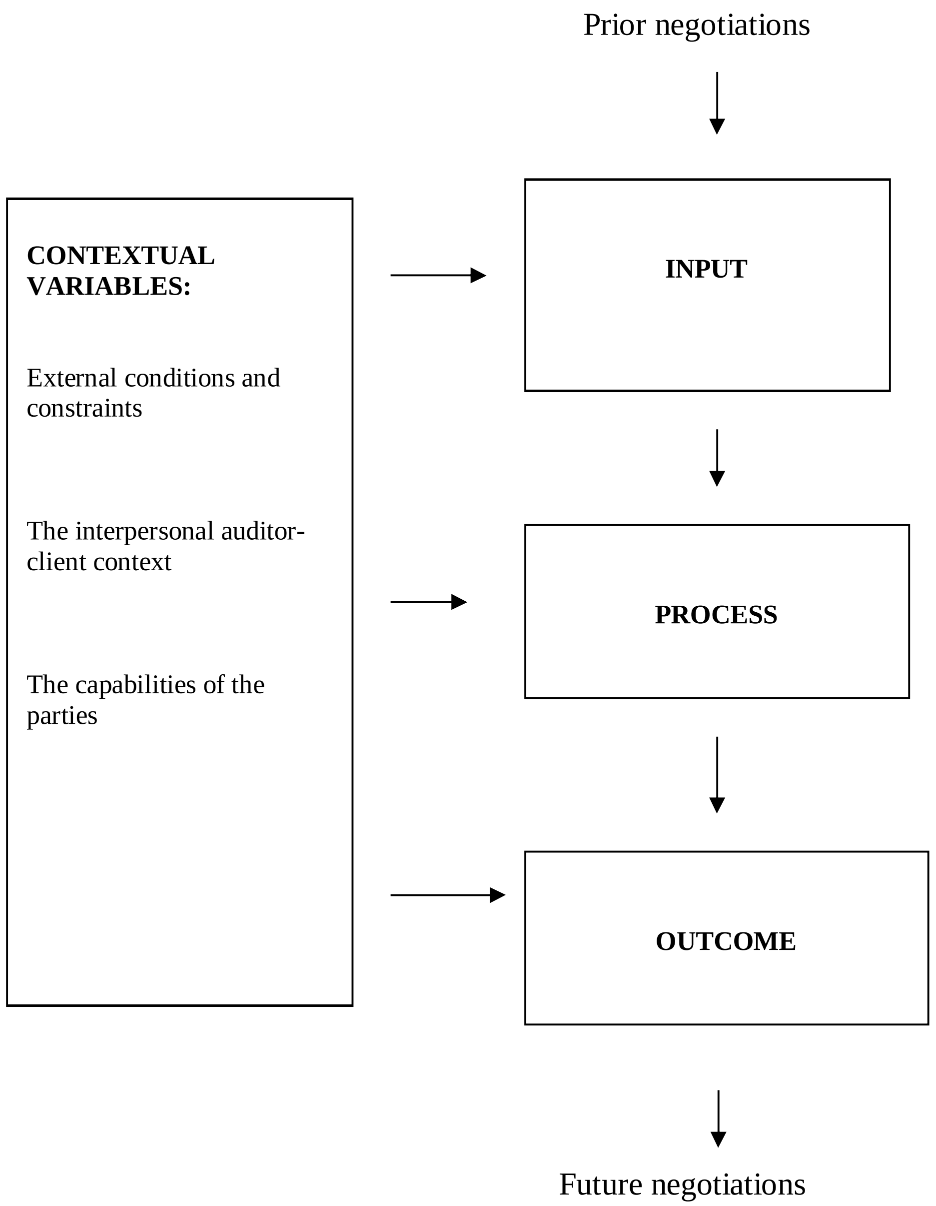


Figure 1 - Gibbins et al.ôs (2001) model of auditor-client negotiations

To describe further the elements and relationships in the model, Gibbins et al. provide audit partners from six international audit firms (Gibbins et al. 2001) and CFOs (Gibbins et al. 2007)[5] with a structured research questionnaire to describe in depth a negotiation they have conducted during the previous three years. The respondents are asked to rate the importance

[5] In Gibbins et al. (2001), 132 questionnaires were distributed, and 93 auditors responded. In Gibbins et al. (2007), 667 questionnaires were mailed, 100 CFOs responded, and 70 of these provide information about a negotiation they have experienced.

of the different process elements as well as the suggested contextual factors. Gibbins et al.ôs main findings are that: (a) accounting negotiation is context-dependent, normal (none of the auditors in the survey report, for instance, that they have never experienced an auditor-client negotiation), distributive and part of client service, (b) accounting negotiation issues are complex, (c) accounting negotiations take time and a large number of participants often take part in the negotiation, and (d) auditor expertise (related, for instance, to knowledge of GAAP or understanding the clientôs situation) is central to accounting negotiation (Gibbins et al. 2001). Gibbins et al. (2005) compare the findings in Gibbins et al. (2001) with the findings in Gibbins et al. (2007) and conclude that the recollections of the auditors and the CFOs are congruent and that the auditors´ and the clients´ mental models of negotiations (their understanding of what happens in negotiations) do not differ significantly.

2.4.3. Model input: what is negotiated?

In this section on negotiation input, I present findings from audit research on the types of issues that auditors and clients negotiate. I also summarize the types of issues that are included in prior auditor-client negotiation studies.

When auditors and clients disagree over accounting issues,[6] the disagreement may be related to assumptions underlying the financial statements (e.g. the going concern assumption), recognition of elements of the financial statements (e.g. income recognition, recognition of contingencies or deferred taxes), measurement of elements (e.g. valuation of debtors) or the choice between specific accounting principles (e.g. capital or operational lease). The parties may also disagree about how an issue should be classified (goodwill vs. other immaterial assets or short-term liabilities vs. long-term liabilities). Finally, the negotiation parties may disagree about issues that relate to the necessity and the content of disclosure, including disagreement about information in the management report.

Prior research has investigated which types of accounting issues are most frequently negotiated. From a specified list of 40 changes to the financial statements, Beattie et al. (2000) find that fair values on acquisition, reorganizing costs, stock and work-in-progress,

[6]Auditors and clients also negotiate other issues such as compliance (e.g. maintenance of proper accounting records) and other audit related matters (e.g. fee and audit scope) (Beattie et al. 2000). Such negotiations will not be studied in this thesis.

deferred taxes and liabilities and merger and acquisition accounting are the five issues negotiated most frequently. Beattie et al. (2000) suggest that the high ranking of the issues stock and work-in-progress and deferred taxes and liabilities may be due to their highly subjective nature whereas the high ranking of the issues fair values on acquisition and reorganizing costs indicate that despite the accounting regulation in place, these issues can still be ñmanagedò.

Previous audit negotiation studies have used different types of negotiations in their experiments such as valuation of inventory (Goodwin 2002; Trotman et al. 2005; Trotman et al. 2009; Hatfield et al. 2010[7]), revenue recognition (Bame-Aldred and Kida 2007; Brown and Johnstone, 2009), overstatement of income (Gibbins et al. 2010; Tan and Trotman 2010; McCracken et al. 2011) and fixed asset impairment loss (Fu et al. 2011). Sanchez et al. (2007) and Hatfield et al. (2008) include a list with different proposed audit adjustments. Sanchez et al. (2007) include consequential items that relate to sales, depreciation and warranty expense. Hatfield et al. (2008) include consequential items that relate to sales, R&D, warranty expense and goodwill.

2.4.4. Process: An introduction to negotiation strategies, tactics and styles: how is an auditor-client negotiation over accounting issues conducted?

In this section I present and discuss theory, including typologies developed in generic negotiation research, on negotiation strategies, tactics and styles. I also present findings from audit research on auditorsô use of these negotiation strategies, tactics and styles when they negotiate with their clients.

In order to obtain the preferred negotiation goals, Pruitt and Carnevale suggest that the negotiation parties choose from five different strategies[8]: problem solving, concession making, contending, withdrawal and inaction (Pruitt and Carnevale 1993). The first of these strategies is referred to as an *integrative* strategy whereas the last four strategies are labeled *distributive* strategies. Concession making, withdrawal and inaction are simple strategies (i.e.

[7] Hatfield et al. (2010) also include an immaterial, objective audit issue relating to the accrual of a service expense.
[8] ñA strategy is a plan of action, specifying broad objectives and the general approach that should be taken to achieve them.ò (Pruitt and Carnevale 1993, p. 3)

they are not implemented by use of different tactics). By contrast, problem solving and contending strategies are implemented through the use of different *tactics* (i.e. different forms) which are consistent with the overall strategy. In the following paragraphs, I define the different strategies. The definitions are based on Pruitt and Carnevale (1993).

Concession making involves reducing one's goals, demands or offers. According to Pruitt and Carnevale (1993), research shows that negotiators who resist concession making typically will receive larger outcomes than other negotiators and that some concession making may be necessary to reach an agreement. In an auditor-client negotiation over accounting issues, the auditor uses the concession making strategy if he as a part of the negotiation process is willing to move away from his initially preferred accounting outcome in order to come to an agreement with his client or if the auditor receives new information that changes the auditor's initial beliefs about the accounting solution. In the accounting setting it can therefore be fruitful to distinguish between concessions that lead to a financial statement that better reflects the underlying economic situation of the company (the client has suggested a solution that better reflects the reality than the solution the auditor has suggested) and concessions that lead to the auditor accepting an estimate other than the best estimate (the auditor is persuaded by the client). It should be noted that the client will not necessarily know that the auditor concedes because the auditor may not have told the client about his initial proposed solution.

Inaction (doing nothing or as little as possible) and *withdrawal* (dropping out of the negotiation) are normally useless strategies in auditor-client negotiations because a solution has to be found. As noted previously, in the accounting setting, finding a solution does not necessarily imply agreement as the auditor will issue a qualified audit opinion if the client does not accept the accounting that the auditor requires. If the issue that the auditor and the client disagree about is significant, the auditor may withdraw from the engagement but as inaction and withdrawal are strategies that are of relatively little use in auditing, these strategies will not be discussed any further.

The *contending strategy* is defined as a strategy in which one party tries to persuade the second party to concede. Its use also implies an effort to resist persuasive efforts by the other party. Contending tactics are tactics such as threats, harassments, persuasive arguments and positional commitments. If one of the negotiation parties uses more contentious tactics than does the other, this party is likely to win the negotiation. Yet contentious tactics may in some instances prompt the other party to intensify its own contentious tactics and thus make it difficult for the parties to reach an agreement. For example, auditors can threaten the client, telling him that he will not receive a clean audit opinion unless he accepts the accounting solution that the auditor has suggested. The auditor may adopt an alternative approach; trying to persuade the client by showing accounting precedents that support the auditorôs suggested solution.

Problem solving strategies consist of efforts to try to locate or adopt options that satisfy both partiesô goals. Problem solving tactics are tactics such as information sharing and the trading off on negotiated issues. In the auditing setting, the auditor can, for example, share information about all precedents with his client and not only the precedents that support the solution suggested by the auditor.

The *overall negotiation strategy* will often consist of elements from several different strategies. For example, concession making and contending tactics are often coupled with problem solving tactics (Pruitt and Carnevale 1993).

Some researchers study negotiatorsô *negotiation style*. A main distinction between a strategy and a style is that while a strategy represents planned or intentional behavior (Pruitt and Carnevale 1993), ñconflict style is the way a person most commonly deals with conflictò (Pruitt and Carnevale 1993, p. 105).

Building on, among others, Blake and Mouton (1964) and Thomas (1976), Rahim (1983) classify styles for handling interpersonal conflict along two axes: *concern for self* and *concern for others* (Rahim 1983). According to Pruitt and Carnevale (1993), concern for others should not be understood as due only to altruism, it may more often be caused by instrumental considerations (for example, I care about the other because I believe I have something to gain from it). According to Rahim (1995) the two dimensions ñportray the motivational orientation of a given individual during conflictò (Rahim 1995, p. 122). As auditor-client negotiations take place in an ongoing relationship, the distinction between care for self and care for others are particularly interesting as the negotiation parties are likely to care not only about the outcome that is reached in the negotiation but also about its effect on their relationship.

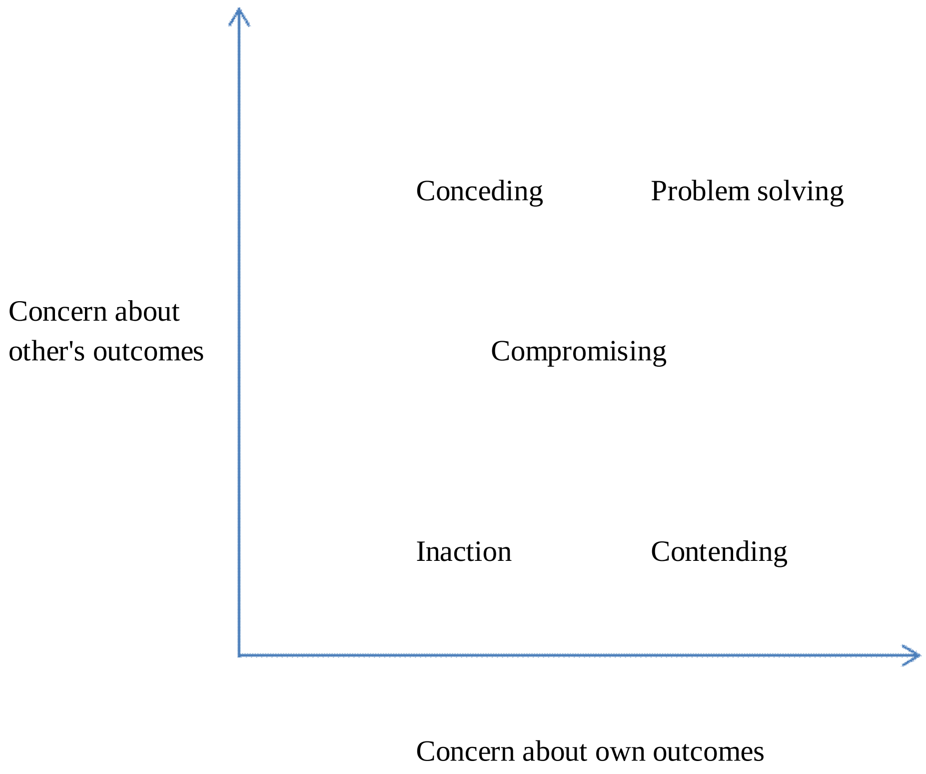


Figure 2 - The dual-concern model, building on Rahim (1983) and Pruitt and Carnevale (1993)

Negotiators who are high on both dimensions have an *integrating negotiation style*. Negotiators, who have low concern for the other negotiation party but high concern for self, typically have a *dominating (contending) negotiation style*. Low concern for self but high concern for others is labeled an obliging (conceding) style while a low score on both dimensions is labeled an *avoiding style*. Rahim (1983) also adds the *compromising negotiation style* to his typology. It should be noted that Pruitt and Carnevale (1993) claim that compromising is not a distinct strategy but a form of half-hearted integrating.

According to Pruitt and Carnevale (1993), the dual-concern model[9] discussed above is not only a model about individual differences in conflict style but also a model that can be used to predict strategic choices in negotiations. See Figure 2 for an overview of the link between the different strategies and the dual-concern framework. High concern for self and low concern

[9] Savage et al. (1989, p. 40) use the same framework but use the dimensions ñIs the substantive outcome very important to the manager? ò and ñIs the relationship outcome very important to the manager?ò to distinguish between different negotiation strategies.

for other is, for example, seen to be associated with contentious tactics (Pruitt and Carnevale 1993). In empirical audit research approximately the same statements are used to measure auditor negotiation strategy (Gibbins el al. 2010) and auditor negotiation style (Goodwin 2002).

Audit research suggests that both distributive negotiation and integrative negotiation strategies (e.g. Bame-Aldred and Kida 2007) and styles (e.g. Goodwin 2002) are used in auditor-client negotiations. Goodwin (2002) investigates what negotiation style audit partners and managers believe they normally use when resolving conflicts with clients over accounting issues. The findings show that audit partners and managers believe that the style they use most frequently is the integrating negotiation style.

A number of audit research papers discuss how negotiation strategy selection seems to be affected by different contextual variables.[10] These studies will be presented in more depth in section 2.4.6.4.

2.4.5. Negotiation outcomes

In this section I discuss typologies of outcomes in negotiations developed in generic negotiation research and present theories and findings on the relationship between negotiation strategies and outcomes. I also present findings from audit research on which outcomes are found in auditor-client negotiations.

Theoretically a negotiation can end with one of five possible outcomes: (1) and (2) victory for one of the parties or the other, (3) compromise, (4) an integrative agreement (a win-win agreement), or (5) a failure to reach an agreement. A win-win agreement is characterized as an outcome with higher joint benefit (collective utility) than the benefit received with a compromise and this is generally believed to have a number of advantages over compromises (Pruitt and Carnevale 1993). According to Thompson and Hrebec (1996, p. 396) even though "two people in an interdependent decision-making situation may have compatible interests; however, they often fail to realize this and settle on an outcome less favorable to both parties

[10] Generic studies that investigate the effect of different context variables on negotiator's choice of negotiation strategy and are of relevance for this study will be referred to in chapter 3.

than another readily available solution. People sometimes settle for less favorable outcomes even when they realize they have compatible interestsò.

Using the dual-concern model as a framework (presented in the previous chapter), prior research finds that high concern for self and high concern for others produce win-win outcomes (Pruitt and Carnevale 1993). Consequently an integrative negotiation strategy is often recommended since it is typically associated with a win-win outcome (the integrative strategy is characterized with high concern for self and high concern for others). The integrative strategy is also recommended because agreement may not be reached if the negotiators do not have a negotiation style/strategy with a relatively high concern for others.

ñAlthough the general negotiation literature advances an integrative strategy as optimal it is unclear how many opportunities are present in the auditing environment for integrative solutionsò (Brown and Wright 2008, p. 99). Brown and Wright (2008, p. 99) therefore suggest that ñperhaps rather than actually having to accomplish an integrative solution, an *integrative mindset* of both parties is sufficient to achieve high quality financial reporting where the auditor and client work toward a mutually acceptable solution and consider each otherôs interestsò. But as mentioned previously, it must be emphasized that integrative solutions are not always desirable in accounting. As a consequence, the integrative strategy is not necessarily preferable in accounting.

Several prior studies have examined the frequency of different outcomes in auditor-client negotiations over accounting issues. These studies are mainly descriptive and do not test the effect of negotiation styles, strategies or tactics or contextual variables on the reported negotiation outcomes. Findings from the studies differ considerably. Beattie et al. (2000) find that in 57 percent of the examined cases, the negotiation outcome is a change to the financial statements. In the sample of Gibbins et al. 2001 (data received from 93 auditors), 96 per cent of the negotiations result in an outcome that is a change to the financial statements. [11, 12] In the

[11] Houghton and Fogarty (1991) and Wright and Wright (1997) suggest that a large number (65 to 75 percent) of discovered misstatements be in fact waived and consequently reported in accordance with the client´s suggestions. As opposed to the research area of auditor-client negotiations, the studies of waiving or adjusting misstatements do not distinguish between proposed adjustments that are negotiated and those that are not. It can therefore be expected that the large number of waived adjustments can be explained at least partly by the immateriality of some of the proposed adjustments.

[12] The difference between the findings in Beattie et al. (2000) and Gibbins et al. (2001) on outcome can have a number of different explanations, such as a possible sample-selection bias in Gibbins et al. (2001). It can also be due to other differences in the studies such as different materiality of the issues examined or different types of

sample of Gibbins et al. 2007 (data received from 70 CFOs), 66 per cent of the outcomes are changes to the financial statement. The differences between the results in the Gibbins et al. studies (2001 and 2007) are not surprising as the respondents choose their own negotiation examples and inadvertently may have chosen to report on negotiations they experience as successes.

Studies that investigate the effect of different negotiation strategies on accounting outcomes will be presented in section 2.4.6.

2.4.6. Contextual variables: Relationship between context, process and negotiation outcomes

2.4.6.1. Introduction

In section 2.4.6 I present empirical research findings on the relationship between the negotiation process and resulting negotiation outcomes and the relationship between different context variables, the negotiation process and negotiation outcomes. The details of some research papers will be presented whereas others will only be mentioned depending upon their importance for this study.

Prior empirical research has investigated several topics related to the area of auditor-client disagreements/conflicts over accounting issues that are of interest for understanding auditor-client negotiation. In section 2.4.6 I review the most important of these studies, sorted according to the topic that is investigated. Three different research streams will be presented: The first stream studies auditorsô acceptances of client proposed accounting, and it is presented in section 2.4.6.2. The second stream investigates auditorsô decisions to book or waive proposed adjustments and is presented in section 2.4.6.3. The third stream studies auditor-client conflicts using a negotiation framework and is presented in section 2.4.6.4. A tabular overview of the studies that I present is included in Table 1, Table 2 and Table 3. A summary of the independent variables that are identified and/or found significant in auditor-client conflict research is presented in Table 4 (section 2.4.7).

---

issues (e.g. numerical adjustments or disagreement related to the use of accounting principles or disclosure content, contextual factors, a different negotiation definition etc.).

Studies that belong to the research streams of ñaudit qualityò and ñearnings managementò are not included in this review for a couple of reasons. First, these studies typically measure the dependent variable based on different types of discretionally/abnormal accruals, see for instance Carey and Simnett (1996) for different measures of audit quality. Second and more importantly, these studies do not necessarily imply that there is an auditor-client conflict.

2.4.6.2. Auditorôs acceptance of client-proposed accounting in situations of auditor-client conflicts

Historically, research has modeled auditor-client conflicts over accounting issues as an implicit bargaining process in which the client and the auditor each possesses a number of sources of power that have an impact on the outcome of the process. It has typically been assumed that the sources of power possessed by the auditor are insufficient to counterbalance managementôs broad power base stemming from its control over current and future audit fees (Knapp 1985).

A number of studies have examined whether client preferences influence audit judgments when auditors and clients disagree over accounting issues and if so, which factors seem to have an impact on the outcomes of such disagreements. Studies suggest that auditors are more likely to accept client preferred accounting methods if litigation risk is low (e.g. Farmer 1987), risk of client loss is high (e.g. Farmer 1987), client financial situation is sound (e.g. Knapp 1985) or engagement risk is low (e.g. Hackenbrack, 1996). In summary we see that there seems to be a tendency for auditors to be less restrictive (less conservative) if they have something to gain by doing so and if the risks are low.

Recent audit scandals as well as recent regulatory changes do, however, make it reasonable to assume that the auditor has a broader power base today than in the recent past and is less inclined to be persuaded by the client in cases of auditor-client conflicts over accounting issues.[13]

[13] Joe et al. (2011) find in a study of post-SOX data that only 24 per cent of proposed adjustments are waived as compared to the finding of 65 per cent in Wright and Wright (1997).

A clientôs ability to persuade an auditor in an auditor-client conflict over accounting issues seems to be affected by a number of different client-related as well as possibly relational variables. Whether the attempt to persuade will be successful is likely to be moderated by a number of different variables that relate to the audit, i.e. variables related to the environment that surrounds the audit and to auditor characteristics.

Prior audit conflict research investigates some of the independent variables that are included in the Gibbins et al.ôs (2001) negotiation model in order to study the relationship between these variables and auditorsô acceptance of the clientsô proposed accounting.[14] The studies included in this section are not made in an explicit ñnegotiationò context but rather include research on judgments such as auditorsô acceptance of client-preferred accounting methods and auditorsô evaluation of clientôs accounting choices. All the studies assume an auditor-client conflict/disagreement over the treatment of an accounting issue and almost all the studies use an experimental design.[15]

As emphasized, the negotiation model of Gibbins et al. (2001) does not focus particularly on client pressure or the factors that provide auditors with bargaining power, and the model is not related to the important concept of auditor independence.[16] These issues are, however, a major topic in prior research on auditorôs acceptance of client-preferred accounting. A number of studies using an experimental design investigate different variations of the question ñUnder what conditions will auditors accept a clientôs proposed (possibly aggressive) accounting principles or methods?ò An overview of the studies is given in Table 1.

An overview of the independent variables that are studied is given in Table 4. In the presentation below, the studies are grouped according to the participants in the experiments and according to which independent variables are studied.

[14] Only studies that focus on the outcome of disagreements over accounting issues are included. Research that, for instance, investigates what opinion the auditor chooses to give in a conflict situation is not included. The presentation of audit conflict studies is not meant to include *all* studies that exist in this area but rather give an idea of which types of studies are conducted and, in particular, which independent variables are found to be significant in this area of research.

[15] The research of Salterio (1996) combines an experiment with the analysis of archival data.

[16] See section 2.4.6.4 for a thorough review of the Gibbins et al.ôs (2001) study.

(1) Experiment participants: financial statement users

Knapp (1985) investigates whether the nature of the conflict, the clientôs financial condition, the auditorôs provision of management advisory services, or the degree of competition in the audit market have an effect on auditorsô ability to resist management pressure in auditor-client conflicts. 43 commercial bank senior loan officers participated in an experiment where, based on the provided case material, they were asked to indicate the perceived likelihood that management will be able to persuade the auditor to accept their suggested solution. Knappôs main findings are that auditors are perceived to be more likely to give in to management pressure if **technical standards** are vague and the **clientôs financial situation** is sound. (In both these situations, auditors have relatively little to lose but much to win if they give in). There are no conclusive findings when it comes to the effects of provision of management advisory services and the degree of competition in the audit market.

Lindsay (1989) studies the impact of four different contextual variables on auditorsô compliance with client-preferred accounting treatments in an experiment. The study finds that Australian bankers and security analysts believe that auditors are more likely to comply with a client-suggested solution if the **accounting issue is not precisely regulated**, the **audit firm** is small, the audit firm is providing **non-audit services** to the client and/or the market in which the audit firm operates is characterized by a high degree of **competition**. Lindsay (1990) replicates these findings in a study of Canadian bankers.

Gul (1991) also studies the auditorsô ability to resist management pressure in an experiment with participant bankers. Findings suggest that when the **audit fee** is large in percentage of the auditorsô total audit fees, the auditor provides **management advisory services** to the client, the **audit firm is small** and/or the **competition** in the audit market is high, financial statement users believe that auditors are less likely to resist management pressure than under other circumstances.

Iyer and Rama (2004) asked 124 CPAs employed as CEOs, CFOs, controllers and treasurers about *when* they believe they are able to persuade the auditor to accept their preferred accounting. Their findings indicate that clients that have short **auditor tenure** and **clients who perceive themselves as important to the auditor** believe they are more likely to persuade their auditors than clients with longer audit tenures and who are less important clients. Whether the respondent has previous experience as auditor or the client has purchased non-audit services from the auditor is not related to the respondentôs perception of his ability to persuade the auditor in an auditor-client conflict over accounting issues.

Table 1 - Auditorôs acceptance of (aggressive) client-proposed accounting

Author	**Research questions**	**Experiment participants**	**Main findings**
Knapp (1985)	When do auditors resist client pressure in auditor-client conflicts?	43US commercial bank senior loan officers	Clients are more likely to obtain their preferred accounting if their financial situation is sound and the conflict issue is not regulated by precise standards.
Farmer et al. (1987)	Do litigation risk and client retention risk have an effect on auditorsô acceptance of client-proposed accounting?	75 US auditors	Clients are more likely to obtain their preferred accounting if litigation risk is low or the risk of losing the client is high.
Lindsay (1989)	When do auditors resist client pressure in auditor-client conflicts?	49 Australian security analysts and 69 bankers	Clients are more likely to obtain their preferred accounting if the accounting issue is not precisely regulated, the audit firm is small, the audit firm is providing non-audit services to the client or the market for audit services is highly competitive.
Lindsay (1990)	When do auditors resist client pressure in auditor-client conflicts?	55 Canadian bankers	Clients are more likely to obtain their preferred accounting if the accounting issue is not precisely regulated, the audit firm is small, the audit firm is providing non-audit services to the client or the market for audit services is highly competitive.

Author	Research questions	Experiment participants	Main findings
Gul (1991)	When do auditors resist client pressure in auditor-client conflicts?	49 New Zealand bankers	Clients are more likely to obtain their preferred accounting if the ratio audit fee/auditorôs total audit fee is large, the auditor provides management advisory services to the client, the audit firm is small or the competition in the audit market is high.
Trompeter (1994)	Do audit partnersô compensation schemes or precision of GAAP have an effect on whether partners require downward income adjustments in auditor-client conflicts?	54 US audit partners	The more compensation schemes are tied to client retention, or the less specific GAAP, the less likely is the partner to require downward income adjustments.
Goodwin and Trotman (1995)	Do litigation risk and the risk of losing a client have a combined effect on auditorsô accounting judgments?	59 New Zealand Big 6 audit partners and managers	There is a strong interaction effect between the factors.
Windsor and Ashkanasy (1995)	What are the effects of client management bargaining power, auditor moral reasoning development and belief in a just world on auditor judgments	61 US auditors	The factors are found to interact.
Tsui and Gul (1996)	Do auditorsô locus of control (belief in a just world) and ethical reasoning have an effect on auditorsô ability to resist client pressure in auditor-client conflicts?	80 Hong Kong auditors	Ethical reasoning has a strong moderating effect on the effect of locus of control.
Hackenbrack and Nelson (1996)	Does engagement risk have an effect on auditorsô acceptance of client-preferred accounting?	90 US supervising senior auditors from one Big 6 firm	When engagement risk is high, the auditor requires more conservative reporting than if engagement risk is moderate.

Author	Research questions	Experiment participants	Main findings
Salterio (1996)	Do different characteristics of precedents and clientôs preferred accounting policy have an effect on auditorôs financial accounting policy judgments?	65 audit managers and partners form one of the Big 6 audit firms	Precedent content and perceived precedent similarity with current case have an effect on auditor judgments.
Salterio and Koonce (1997)	How do auditors respond to precedents when authoritative guidance does not exist?	123 managers and partners from a Canadian Big 6 audit firm	If auditors know the clientôs preference and precedents give mixed guidance, the auditor is more likely to accept the clientôs proposed accounting than if the precedents all give the same guidance.
Shafer et al. (1999)	Do formal sanctions have a deterring effect on auditorsô acceptance of client-preferred accounting?	323 US AICPA members	Auditors perceive that litigation risk and peer-review risk are effective means for inducing wanted behavior.
Dopuch et al. (2001)	Does mandated auditor rotation have an effect on auditorôs willingness to accept client preferred accounting?	114 subjects playing auditors and client management	Mandated auditor rotation makes it less likely that auditors will accept client preferred accounting.
Chang and Hwang (2003)	Do client business risk and client retention risk have a combined effect on auditorsô acceptance of client-preferred accounting?	55 US audit seniors and managers	There is an interaction effect between the two factors.
Kadous et al. (2003)	Does qualitative assessment have a deterring effect on auditorsô acceptance of client-preferred accounting when auditors have directional goal commitment?	227 US auditors	Performing quality assessments amplify the effect of the directional goal.

Author	**Research questions**	**Experiment participants**	**Main findings**
Jenkins and Haynes (2003)	Do timing of communication and client credibility have an effect on the persuasiveness of client preferences?	40 auditors from one non-Big 5 firm and 24 big 5 auditors	If auditors receive the client preference before they evaluate audit evidence, judgments may be biased towards the clientôs preference.
Ng and Tan (2003)	Do authoritative guidance availability and audit committee effectiveness have a combined effect on auditor-judgment in auditor-client conflicts?	101 US audit managers from one Big 6 firm	Authoritative guidance has a larger effect if the audit committee is not effective than if it is effective.
Iyer and Rama (2004)	When do clients expect to be able to persuade their auditor about reporting choices?	124 US CPAs employed as CEOs, CFOs, controllers or treasurers	Clients that have a short relationship with their auditor or believe their business is important to the auditor believe they are more likely to persuade their auditors than do other clients.
Bamber and Iyer (2007)	Does auditor familiarity with a client have an effect on his acceptance of client-preferred accounting?	252 US Big 5 auditors	Auditors that identify with their clients are more likely to accept the clientôs preferred accounting. More experienced auditors are less likely to accept the clientôs position.
Lin and Fraser (2008)	Does culture have an effect on auditorsô ability to resist client pressure in auditor-client conflicts?	93 Chinese and UK auditors	UK auditors are less likely to be affected by regulation of the accounting issue, auditor tenure, provision of MAS, and audit market competition than Chinese auditors.
Chang and Hwang (2010)	Do client business risk, client retention risk and litigation risk have a combined effect on auditorsô acceptance of client-preferred accounting?	59 US and 61 Hong Kong Big-4 auditors	The variables interact.

Author	Research questions	Experiment participants	Main findings
Ng and Shankar (2010)	What are the effects of technical department advice, quality assessment standards, and client justifications on auditorsô propensity to accept client-preferred accounting methods?	129 auditors from two Singaporean Big 4 audit firms	The presence of a quality assessment standard has an effect on the auditorôs propensity to accept client-preferred accounting methods but only if the auditor has received advice from a technical expert recommending the most appropriate method and the clientôs justification is strong.

(2) Experiment participants: auditors

Several experimental studies focus on different risks and rewards that may have an effect on the auditorôs decision process such as retention risk (Farmer et al. 1987; Goodwin and Trotman 1995; Chang and Hwang 2003; Chang and Hwang 2010), litigation risk (Farmer et al. 1987; Goodwin and Trotman 1995; Shafer et al. 1999; Chang and Hwang 2010), client business risk (Chang and Hwang 2003; Chang and Hwang 2010), engagement risk (Hackenbrack and Nelson 1996) and partner compensation schemes (Trompeter 1994). These studies will be presented first in my presentation of auditor-client conflict studies that use auditors as participants in the experiments.

Farmer et al. (1987) examine whether auditors incorporate non-accounting factors into their decision model when judging the appropriateness of a client proposed accounting treatment. The results indicate that the likelihood that an auditor will accept a clientôs proposed accounting treatment is highest if the perceived **risk of client loss** is high and the **risk of litigation** is low. Partners and managers seem to agree less with the clientsô position than do audit staff (i.e. **auditor experience** seems to have an effect).

Trompeter (1994) studies whether **partner compensation schemes** and **precision of GAAP** have an effect on audit partner judgments in auditor-client conflicts over accounting issues. The study concludes that auditors are more likely to require downward income adjustments if the relevant accounting standards are specific than if they are vague. The study also finds that partners who have compensation schemes that are closely tied to **client retention** are more reluctant to require downward income adjustments than partners with compensation schemes that are less tied to client retention.

Goodwin and Trotman (1995) extend the study of Farmer et al. (1987) by using a different context and a design that allows for the testing of interactions, and they investigate the effect of two conflicting risks; the **litigation risk** stemming from the client breaching a covenant and the **risk of the auditor losing the client** on auditorsô judgments related to revaluation of property. Findings suggest that there is a strong interaction effect between the two factors: when there is both a low risk of losing the client and a high risk of breaching the covenant, the auditor is less likely to accept the clientôs valuation judgment than otherwise.

Hackenbrack & Nelson (1996) examine the relationship between **engagement risk** and auditorsô evaluation of clientsô accounting choices. Finding that more conservative reporting is required if engagement risk is high, Hackenbrack and Nelson suggest that auditorsô conflicting incentives lead them to compromise their independence by accepting aggressive accounting in situations with less than high engagement risk.

Shafer et al. (1999) express concerns that auditors are willing to accept aggressive accounting if the threat of sanctions is low and the amounts involved are relatively immaterial. In their study they investigate whether **formal sanctions** (litigation risk, peer-review-risk and risk of professional disciplinary action) have a deterrent effect on auditorsô acceptance of a clientôs proposed accounting. Shafer et al. find that auditors perceive that litigation risk and peer-review risk are effective means for inducing desired auditor behavior while risk of professional discipline is not perceived as an effective method.

Chang and Hwang (2003) study the effects of the **clientôs business risk** and **client retention risk** on auditorsô acceptance of clientsô aggressive reporting practice in an experimental study with 55 audit seniors and managers. The study replicates the findings in Farmer et al. (1987) and in Hackenbrack and Nelson (1996). Additionally the study finds statistical support for an interaction effect between the two factors so that if business risks are high, auditors do not accept the aggressive reporting but if business risks are only moderate, auditors are more likely to accept the suggested aggressive reporting when retention incentives are high than when they are low. Chang and Hwang (2010) expand the 2003-study by including differing **litigation environments** (Hong-Kong vs. US) and find that all three variables interact: US auditors behave in accordance with the findings in the 2003-study whereas Hong-Kong auditors (a less litigious environment) behave differently: no interaction effect is observed between business risk and retention risk.

As pointed out in the introduction to this section and as follows from the aforementioned studies, auditors seem to accept client-preferred accounting more often if factors such as litigation risk is low and risk of client loss is high. One of the regulatory responses that has been suggested is different types of auditor rotation. Dopuch et al. (2001) study the effect of **mandatory auditor rotation** and find that auditors are less likely to accept client preferred accounting under a regime of mandatory auditor rotation.

When making decisions related to difficult accounting issues, auditors will often seek help; for instance, they may ask for the opinion of an accounting expert. In large audit firms, the central office may give this sort of guidance in the form of precedents, i.e. information about how similar issues have been solved previously either by the audit firm itself or by other audit firms (Salterio 1996). Salterio (1996) investigates the effect of the content, similarity to the current case and source (in-house vs. external) of **accounting precedents**, as well as the clientøs preferred accounting position on audit partnersô and managersô financial accounting policy judgments. Findings from the experiment show that the similarity to the current case and content has an effect on the auditorøs judgment. The clientøs preferred position and source is found to have an effect on what precedents are presented. These factors do not, however, have a direct effect on auditorsô judgments. Findings from an accompanying archival study suggest that there may be an indirect effect of the clientøs preferred position and the precedent source on auditor judgment via the effect of precedent content and case similarity.

Salterio and Koonce (1997) study how audit managers and partners act in accounting disputes when there is no authoritative guidance: however, **precedents** are available. Findings indicate that if all precedents support the auditorøs opinion, he will not heed the client-suggested solution. If precedents are mixed in their solutions and the auditor knows what the client prefers, the auditor is more likely to accept the clientôs solution.

Ng and Tan (2003) study the combined effect of the **availability of authoritative guidance** as well as **audit committee effectiveness** on auditorsô judgment related to an audit adjustment that affects the clientôs ability to meet earnings forecasts. Their results show that these factors both have a positive effect (both the presence of authoritative guidance and the presence of an effective audit committee lead to a higher likelihood that the amount that will be booked will make the client miss the earnings forecast). Additionally, the effect of authoritative guidance is larger when the audit committee is ineffective than when the audit committee is effective. This suggests that the two factors are substitute mechanisms for making audits more effective.

One of the means to improve the quality of accounting reporting implemented by accounting regulation is that auditors be required to discuss the clientôs chosen accounting methods with the clientôs audit committee. Kadous, Kennedy and Peecher (2003) conduct an experiment in which they study the effect of **quality assessment of accounting methods** and **directional goal commitment** on auditors´ acceptance of client-preferred accounting methods. They find that making a quality assessment ñamplifies the effect of directional goal commitment on auditors´ acceptance rates and their assessment of the quality of the client-preferred methodò (Kadous, Kennedy and Peecher, 2003, p.761). In other words, this finding indicates that making a quality assessment will have the desired effect on accounting reporting only if auditors already have incentives to reject the client preferred accounting method. If by contrast, auditors have incentives to accept the client-preferred accounting method, making a quality assessment will amplify the effect of these incentives on auditor judgments.

Ng and Shankar (2010) build on Kadous et al. (2003) and study the extent to which the factorsð **advice from the technical department**, the **presence of a quality assessment standard** and the **clientôs justification of the use of an accounting method**ð have an effect on the likelihood that an auditor will accept client-preferred accounting methods. Findings indicate that the three factors interact so that if the auditor receives advice from a technical expert that recommends a particular accounting method and the clientôs justification is strong (in the strong condition the clientôs arguments are based on a specific analysis of the transaction, in the weak condition the justification is more general), the presence of a quality assessment standard lower the likelihood that the auditor allows the client-preferred accounting method.

Jenkins and Haynes (2003) study the effect of the **timing of persuasion attempts** and **client credibility** on the clientôs perceived ability to persuade the auditor to accept his preferred accounting in an experiment involving the disclosure of a contingent liability and the collectability of a customer account. Findings from the disclosure case suggest that the auditorôs judgment may be affected (biased towards the clientôs preference) if the preference is revealed before the audit evidence is collected but not if the evidence is collected at the end of the evidence evaluation process. No such bias is found for the collectability case. No effect is found for the hypothesized interaction effect between client credibility and the clientôs timing of preference communication.

Several studies investigate the effect of the auditorôs personal characteristics on the likelihood that the auditor will accept the clientôs preferred accounting solution. Windsor and Ashkanasy (1995) find that when auditors are pressured by clientôs bargaining power the likelihood that they accept the clientôs preferred accounting is affected by the **auditorôs development of moral reasoning** and his belief in a just world (**locus of control**). Tsui and Gul (1996) find an interaction effect between these two variables; ethical reasoning moderates the effect of locus of control on auditorsô ability to resist client management pressure.

Bamber and Iyer (2007) measure **auditorôs identification with their client** and hypothesize that client identification makes it more likely that an auditor acquiesces to the clientôs preferred accounting. Data is collected through a questionnaire that includes questions to measure client identification and a short case to elicit the auditorôs propensity to be persuaded by the client. Support is found for the hypothesis. Bamber and Iyer also test a number of other variables that may have an effect on auditorsô acceptance of client preferred accounting and find that more **experienced** auditors and auditors who score high on **professional identification** are less likely to be persuaded. **Auditor tenure** is found to have a marginally significant effect. The variable client size is not found significant.

In addition, the impact of possible **cultural differences** in auditor-client conflicts has been studied: Lin and Fraser (2008) compare the auditorsô ability to resist client pressure in an audit conflict situation between Chinese and UK auditors. The results suggest that UK auditors are less likely to be affected by the extent to which the issue is **precisely regulated**, **auditor tenure**, the **provision of MAS**, or **competition in the audit market** than their Chinese counterparts. Chinese auditors perceive that MAS and audit market competition are significant variables whereas UK auditors perceive that precision of accounting regulation and auditor tenure are significant variables.

2.4.6.3. Auditorǒs decision to waive proposed audit adjustments

Research that investigates auditorsô decision to book or waive proposed adjustments can shed light on which variables have an impact in auditor-client negotiations over accounting issues, even though these studies do not only investigate accounting issues that are negotiated for the following reasons: first, these studies do not distinguish between proposed adjustments that are negotiated and proposed adjustments that are not (clients do not necessarily disagree with the auditor on the correct accounting of proposed adjustments). Secondly, many proposed adjustments can be relatively small and consequently be waived due to immateriality reasons and not due to the client being successful in persuading the auditor. Issues that auditors negotiate with their clients are, by contrast, typically material and take more time and several people to solve. An overview of the waive-adjust-studies is given in Table 2. An overview of the independent variables that are found significant is given in Table 4.

Prior research on auditorsô decisions to book or waive proposed adjustments show that the size (absolute and relative) and the type (objective vs. subjective) of the proposed adjustment, are factors that explain why these adjustments are corrected or not (Houghton and Fogarty 1991; Icerman and Hillison 1991; Wright and Wright 1997 and Braun 2001).

Table 2 - Auditorôs decision to book or waive proposed adjustments

Author	**Research question**	**Research method**	**Main findings**
Icerman and Hillison (1991)	Which factors have an effect on auditorsô decision to book or waive proposed adjustments?	Archival	More proposed adjustments are booked the larger the ratio PA-size/net revenue and the more structured the audit firm is.
Houghton and Fogarty (1991)	What characterize waived adjustments?	Archival	Waived adjustments are smaller than booked adjustments.
Wright and Wright (1997)	Which factors have an effect on auditorsô decision to book or waive proposed adjustments?	Archival	The auditorôs decision to waive proposed adjustments is affected by the size of the PA, its directional effect on income, the nature of the adjustment and the size of the client.
Braun (2001)	Why do auditors waive proposed adjustments?	Experiment	Proposed adjustments are corrected more often if adjustments are objective and income increasing and clientôs financial health is bad.
Nelson et al (2005)	Does choice of qualitative materiality approach (cumulative vs. current-period) have an effect on auditorôs decision to book/waive proposed adjustments?	Experiment	The auditor is more likely to book the PA if he uses the approach that makes the PA look more material.
Ng (2007)	How likely is it that an auditor will book an audit difference that has an effect on the clientôs ability to meet different earnings thresholds?	Experiment	The auditor is most likely to book differences which have an effect on the clientôs ability to report positive earnings. The auditor is less likely to book differences which have an effect on meeting recent earnings and is even less likely to book differences which have an effect on the clientôs possibility to meet analystôs expectations. Auditors are less likely to book subjective differences than more objective differences.

Author	Research question	Research method	Main findings
Ng and Tan (2007)	Does increasing the salience of qualitative factors have an impact on auditorsôdecision to book or waive proposed adjustments?	Experiment	Increased salience increase the likelihood of auditors booking PAs but only for auditors with low materiality thresholds. If clients express concern over the booking, the benefit of salience disappears.
Joe et al. (2011)	Which client and misstatement characteristics have an effect on auditorsô decision to book or waive proposed adjustments?	Archival	Auditors are more likely to waive proposed adjustments if tenure is long or the adjustment was also proposed last year.

Houghton and Fogarty (1991) study a sample of 3060 proposed adjustments and find that the waived misstatements in this sample are significantly smaller than the misstatements that are booked, i.e. the **absolute size of proposed adjustments** has an effect.

Icerman and Hillison (1991) study 1424 proposed adjustments from 49 manufacturing companies in the period 1979-1981 and find that the more proposed adjustments are booked the larger the **ratio proposed adjustment size to net revenue**. Clients that are audited by a **structured audit firm** (a firm that uses a more structured audit approach) also book more proposed adjustments than clients that are audited by more unstructured firms (firms that use a less structured audit approach).

Wright and Wright (1997) examine a sample of 368 misstatements from 186 audit engagements and find that the more proposed adjustments are corrected the larger **the ratio proposed adjustment to planning materiality**. Proposed adjustments that are objective (regulated by **unambiguous GAAP**) are corrected more often than proposed adjustments that are subjective (open for judgment/more ambiguous GAAP) in nature. Adjustments that will **increase income** if implemented are corrected more often than adjustments that have an income decreasing potential. More proposed adjustments are also corrected if the **client is small** as opposed to large (suggesting that incentives related to client retention have an impact on auditorsô decisions to waive or adjust proposed adjustments). Industry affiliation is found to be insignificant (financial institutions vs. other industries).

Braun (2001) builds on the findings in Wright and Wright (1997) and conducts an experimental study (155 managers and partners participate) to investigate the effect of risk and reward factors on auditorsô adjustment decisions. The findings indicate that reward factors (fee size) do not have an effect on their decision whereas factors related to auditorsô risk are found to impact significantly auditorsô adjustment decisions (**objective adjustments** are corrected more often than subjective adjustments, adjustments are corrected more often if the **clientsô financial health** is bad, and adjustments that **increase income** are corrected more often than adjustments that decrease income).

Two recent experimental studies investigate the effect of different types of **decision aids/ regulation** on auditorǿs adjustment decisions. Nelson et al (2005) provide experimental participants with either a current-period format (the format compares misstatements added in the current period to net income) or a cumulative format (the format compares cumulative misstatements to net income) as a decision aid when judging whether a client should be required to book a proposed adjustment. Findings indicate that the format of the decision aid has an effect (the auditors are more likely to book the proposed adjustment under the format that makes it look more material), and the researchers suggest that auditors be required to consider both formats when making book/waive decisions. Ng (2007) investigates which **earnings thresholds** seem to be most important in affecting auditors to book audit differences and find that auditors are most likely to book audit differences which have a effect on the clientǿs ability to report positive earnings. Ng suggests that differences in importance for different thresholds may be caused by the auditorsô awareness of the thresholds and find that **availability of materiality guidance** will have an effect on auditorsô booking of audit differences. Ng and Tan (2007) investigate whether the **salience of qualitative factors** has an effect on auditorsô book and waive decisions and whether the effect of salience is moderated by cognitive factors (the **auditorǿs mental model** of the appropriate materiality threshold) and incentive factors (**client concern about not booking the proposed adjustment**). Findings suggest that salience has an effect but only for auditors with low materiality thresholds and if client concern is not communicated.

Joe et al. (2011) study 458 proposed adjustments from 163 audit engagements in a Big 4 firm conducted in 2002. Proposed audit adjustments are more likely to be waived if **auditor tenure** is long (but auditors are not more likely to waive **income increasing adjustments**) or if the **adjustment was also proposed the previous year**. The strength of the clientôs internal control is not found to have an effect on the decision to book or waive proposed adjustments.

<u>2.4.6.4. Auditor-client negotiation studies</u>

A major problem in auditing research is the fact that one seldom knows the ñcorrectò answer to an accounting question at least before some time has passed. A tendency in the aforementioned research is an underlying assumption that conservative accounting is ñbetterò than less conservative accounting. At least from a theoretical point-of-view, this is not necessarily the case. It should also be emphasized that management occasionally has incentives to reduce the reported income instead of increasing it. By studying auditor-client disagreements over accounting issues using a negotiation framework, the researcher tries to enter the black box of how audits are conducted in order to provide knowledge about how auditors and clients behave when they negotiate, how their behavior is affected by different context variables and the effect of their behavior on the negotiated outcome.

The negotiation studies presented in section 2.4.6.4 differ from studies presented in section 2.4.6.2 and in section 2.4.6.3 in that they explicitly study the negotiation process and not only the outcome of this process. In this section I will first discuss the negotiation studies in which the data-collection is based on interviews and then present studies that use the experimental method.[17]

Interview-based studies

Gibbins et al. (2001) use prior literature and interview data to identify 29 contextual features that are thought to have an effect in auditor-client negotiations over accounting issues.[18] See Table 4 for an overview of these context-variables. The respondents rate these features

[17] To my knowledge, no auditor-client negotiation studies use other research methods to collect data.
[18] See section 2.4.2 for an introduction to this study.

according to their importance on a 5-point scale from ñnoneò to ñessentialò. Apart from two of the contextual factors in the model: tax considerations and client size relative to audit firm size, all factors are considered essential in at least one of the reported examples. Respondents rate accounting and disclosure standards and audit firmôs negotiation expertise to be the most important contextual features. Gibbins et al. (2001) also investigate the associations between the process elements and the contextual features and conclude that ñthe existence of so many associations indicates that the reported negotiation processes varied with context and supports the contextualized frameworkò. (Gibbins et al. 2001, p. 555)

In Gibbins et al. (2007), the respondents rate accounting and disclosure standards, relationship with audit partner, organizationôs accounting expertise, audit firmôs accounting expertise and competence of audit partner to be the most important contextual factors. Some changes are made in labeling the variables compared to Gibbins et al. (2001) and some additional variables are included so that the total number of variables in the two Gibbinsô papers is 39. Table 4 gives an overview of these variables.

Beattie et al. (2004) conduct matched interviews with the finance directors and audit partners of six major UK listed companies that recently have experienced accounting disagreements and use these interviews to suggest a different model of auditor-client negotiations than the Gibbins et al.ôs (2001) model.[19]

The model of Beattie at al. (2004) differs from Gibbins et al.ôs (2001) model in several ways; first, because it only studies the association between a number of context variables and the outcome of a negotiation. The importance of the type of issue and the negotiation process are not considered. Second, the model places more importance on variables related to conflict and power.

Gibbins et al. (2001) distinguish between three groups of contextual factors: (1) the role of external conditions and constraints, (2) the interpersonal auditorïclient context, and (3) the capabilities of the parties (including accounting expertise). Beattie et al. (2004) differs from Gibbins et al. by distinguishing between six different context variables: (1) level of integrity of audit engagement partner, (2) company type and situation, (3) effectiveness of corporate

[19] Beattie et al. (2004) also construct a typology of different audit partner types (the crusader, the safe pair of hands, the accommodator and the truster).

governance, (4) clarity of accounting rules on issue, (5) level of audit firm support and quality control, and (6) quality of primary relationship.

Beattie et al. (2004, p. 2) point out that ñcompaniesô aggressiveness in financial reporting is an important contemporary topicò and suggest that contextual factors such as the company type (aggressive vs. conservative) and situation have an effect on the nature of the outcome of a negotiation. Gibbins et al. (2001 and 2007) find that contrary to generic negotiation theory, absolute and relative size of the organizations (variables often used as proxies for power) does not have an impact on accounting negotiations, and they suggest that this finding illustrates the uniqueness of accounting negotiations.[20]

Gibbins et al. (2001, p. 559) find that even though external accounting standards are seen ñby partners as pervasively important, they are not associated particularly with any element of the negotiation processò. Gibbins et al. (2007, p. 389) find that ñthe CFOs tended to view the financial-reporting and negotiation objective as having to comply with form (following the rules) rather than having to represent economic substanceò and conclude that accounting standards as well as accounting expertise is crucial to the negotiation and its outcome. Beattie et al. (2004, p.2) theorize that ñthe clarity of the accounting rules relating to the interaction issueò is an important contextual variable associated with the outcome of auditor-client negotiations.

Beattie et al. (2004) further suggest that high partner integrity and the effectiveness of corporate governance arrangements in the company are important contextual variables associated with the outcome of auditor-client negotiations. Gibbins et al. (2001), by contrast, neither finds that personal characteristics related to the partner nor that the clientôs audit committee has an important impact on negotiations over accounting issues; Gibbins et al. (2007), however, find that partner competence is an important context variable.

Based on the presentation above, we see that the two models do not provide a common understanding of which context variables are the most important in auditor-client negotiations, and the research does not tell us anything on the importance of context as opposed to the importance of the other elements of the proposed model (issues negotiated or

[20] The presence of standards as well as the professionalism of auditors is thought to account for this difference.

the negotiation process) when it comes to explaining the outcomes of auditor-client negotiations over accounting issues.

The major limitations of the projects of Gibbins et al. are two: the examples described are based on retrospective recall and the interviewees are allowed to describe their own negotiation examples with a possible resultant self-selection bias. (The fact that in the audit partner sample only 4 per cent of the described negotiations end up with the initial solution proposed by the client whereas 34 percent of the CFOôs examples end up with the initial solution suggested by the client may illustrate these possible biases). As Beattie et al. (2004) conduct their interviews on a sample of pairs of finance directors and audit engagement partners, limitations from self-selection bias and retrospective recall are much smaller (but the sample size in this study is relatively small). Neither Gibbins et al. (2001 and 2007) nor Beattie et al. (2004) conduct empirical tests of their suggested frameworks.

The studies by Gibbins et al. (2001, 2005 and 2007) and Beattie et al. (2004) do not investigate ñwhy features took on the importance or lack of it that they didò (Gibbins et al. 2001, p. 559). According to Gibbins et al. (2001, p. 559): ñfurther elaboration of the contextual features we suggested would be useful, taking into account that some appear generally important and some do not, but also that all appear to have a role in some negotiationsò. One of the main reasons for conducting research in accounting negotiations rather than building on generic negotiation research is that findings will depend on context. To gain more knowledge related to the importance of both process-related and contextual variables is a worthy goal for this promising area in future negotiation research. Gibbins et al. (2001, p. 559) suggest a number of negotiation aspects that are particularly promising for further research. ñThese include: the pervasive role of accounting; disclosure and other external standards, the level of auditor expertise (both absolute and in comparison to the client), interpersonal relationships within the audit firm and with the client, who identifies the issue and what negotiation edge is thereby provided, and separating negotiationôs personal and career importance to the auditorò.

McCracken et al. (2008) interview both the CFO and the auditor, (one at a time) in eight different companies and ask them to tell about an auditor-client negotiation they have recently experienced to learn more about auditor-client relationships and roles in auditor-client negotiations. The study concentrates specifically on how parties in a negotiation do not focus only on the issue that they negotiate but also on how to keep and develop their relationship.

The audit partner is found to be the one who has the responsibility ñto manage the relationship so that it would be considered ógoodô by both partiesò (McCracken et al. 2008, p. 380). The relationship between the negotiation parties is found to be either proactive (the CFO consults the auditor as soon as he identifies a potential issue) or reactive (the CFO does not inform the auditor about a potential issue until year-end or even later). If the auditor wants to change a reactive relationship to become more proactive, he is typically replaced (by the audit firm) by an auditor who is willing to be the auditor in a reactive relationship. The study also reveals several ñmethodsò used by the client to get what he wants in the relationship such as threatening to end the relationship, insisting on a second opinion from the audit firmôs national office or claiming that GAAP does not reflect the economic realities of a transaction.

A number of empirical auditor-client negotiation studies have been conducted after 2001, and in the following section I provide an overview of the most important of these experimental studies which have been conducted with a focus on findings related to the impact of auditor behavior and contextual variables.

Experimental negotiation studies

Before and during a negotiation process, the auditor must decide on issues such as negotiation strategies and tactics to use, whether there is a need to consult an accounting expert (or other experts), which team members to use, and what information is needed. We know little about how auditors behave when they negotiate with their clients, but recently a small number of studies using an experimental design have investigated the effects of a selection of contextual variables on the auditorôs choice of negotiation strategy and on the subsequent negotiation outcome.

Table 3 gives an overview of the studies in this area with emphasis on research questions, research methods and main findings. An overview of the independent variables that are studied and found to be significant is given in Table 4.

Goodwin (2002) conducts an inventory valuation experiment to investigate the effect of **client size** and **corporate governance mechanism** on auditorsô use of the conflict management styles integrating, dominating (contending), obliging (conceding), compromising and avoiding. Using univariate-analysis, she finds that the size of a client is a significant factor in explaining when auditors use the integrating negotiation style and a marginally significant factor in explaining when auditors use the dominating style (contending). Auditors are more likely to use these styles when the client is small. The auditors are more likely to use the obliging style when the clientøs corporate governance is strong (only marginally significant). Partners are found less likely than managers to use the compromising, obliging and avoiding styles. No other significant relationships between the independent variables and the negotiation styles are found.

Trotman et al. (2005) draw on the generic negotiation literature and its finding that understanding the counterpartøs position is critical for successful negotiation performance. Trotman et al. investigate whether three **intervention methods** (role-playing, passive and practice intervention) have an effect on negotiation effectiveness in an experimental study. In the first method, a role-playing intervention, the participants engage in a mock negotiation in which they play the role as the CFO before they engage in the final negotiation playing the role as the auditor. In the second method, the passive intervention method, the participants are asked to document the clientøs interests and opinions before engaging in a negotiation. In the third method, the practice intervention method, the participants engage in two negotiations, both in the role as the auditor. According to the study, the role-playing intervention method led to the most effective negotiation outcome (measured as the largest proposed inventory write-down).

Bame-Aldred and Kida (2007) compare auditor and client negotiation behavior when they are faced with the same negotiation context. Findings indicate that auditors and clients behave quite differently in negotiations; clients are more flexible and understand their negotiation partner better than auditors do. Clients also use negotiation strategies that are not used by the auditors. The findings may reflect that auditors on the whole are less open to negotiations than their client counterparts.

Table 3 - Auditor-client negotiation studies

Author	Research question	Experiment participants	Main findings
Goodwin (2002)	Do client size and client corporate governance mechanisms have an effect on auditorơs choice of negotiation style?	72 Australian and New Zealand audit managers and partners	The size of the client as well as corporate governance mechanisms has an effect on the choice of negotiation style.
Trotman et al. (2005)	What are the effectiveness of the methods pragmatic intervention, role-playing intervention and practice intervention on negotiation outcomes?	45 Australian managers and partners	Role-playing intervention leads to the largest write-downs.
Bame-Aldred and Kida (2007)	What are the differences between clientsô and auditorsô pre-negotiation decisions and negotiation tactics?	71 auditors and financial managers.	Clients are more flexible, understand auditorơs goals and limits more accurately and are more likely to use bid-high, concede later and trade-off tactics than auditors.
Sanchez et al. (2007)	Does auditorsô use of a reciprocity-based strategy have an effect on the negotiation outcome in an auditor-client negotiation?	124 controllers and CEOs in experiment 1 and 36 audit managers and partners in experiment 2.	Clients are more willing to post significant income decreasing adjustments when auditors use a reciprocity-based strategy. Client satisfaction and retention is greater when this strategy is used.
Hatfield et al. (2008)	Do client managementơs negotiation style and client retention risk have an effect on auditorơs use of a reciprocity-based strategy and the negotiation outcome?	60 audit partners and managers in experiment 1 and 44 audit partners and managers in experiment 2.	If client management has a competitive style and/or retention risk is high, the auditorơs likelihood of using a reciprocity-based strategy is higher than otherwise and the financial statement becomes more conservative.
Brown and Johnstone (2009)	Do auditor experience and engagement risk have an effect on negotiation process and outcome?	65 US audit managers and partners	Auditors with lower negotiation experience use a more concessionary negotiation strategy and accept more aggressive accounting than more experienced auditors when they audit a high risk client.

Author	Research question	Experiment participants	Main findings
Trotman et al. (2009)	What are the effects of auditor rank on pre-negotiation judgments?	23 US audit partners and managers and 20 Australian audit partners and managers	Partners suggest higher initial write-downs, higher minimum write-downs and higher expected write-downs than managers. Partners also believe that clients are willing to accept higher write-downs than managers.
Wang and Tuttle (2009)	How does mandatory auditor rotation impact auditor-client negotiations?	54 graduate business students	Mandatory auditor rotations lead to less cooperative strategies and outcome more in line with the auditorǿs preferences.
Gibbins et al. (2010)	Do flexibility of client initial counting position and nature of the auditor-client relationship have an effect on auditorǿs strategy selection?	140 Canadian audit partners	If the client is perceived as inflexible, the partner is more likely to use the contending tactics and less likely to use the compromising and conceding tactics. A cordial relationship or a flexible client leads to lower reductions in net income compared to less cordial relationships or inflexible clients.
Hatfield et al. (2010)	Do magnitude of audit difference and prior client concession have an effect in auditor-client negotiations?	40 partners, 60 managers and 2 seniors	The independent variables have an effect on auditorǿs initial negotiation positions and the negotiated outcome.
Tan and Trotman (2010)	What are the effects of the timing of auditorsǿ concessions on the size of the write-downs that financial officers accept in auditor-client negotiations?	80 Australian CPAs and chartered accountants	Concessions that are given gradually or late in the negotiation process give larger write-downs than concessions that are made early in the process.
McCracken et al. (2011)	Do audit managers intend to use the same negotiation tactics as audit partners?	73 partners and 105 audit managers	Audit managers seem to use more of the concessionary and compromising tactics. Partners seem to use more of the contending tactics.

Author	Research question	Experiment participants	Main findings
Fu et al. (2011)	Do auditor negotiation experience and client negotiation style have a combined effect on auditorsô perceived negotiation outcome?	99 Chinese audit managers and partners from one of the Big 4 firms.	Client negotiation style only has an effect on perceived negotiation outcome when auditors have low experience.
Perreault and Kida (2011)	What is the effectiveness of different persuasion tactics?	147 practicing managers and professionals attending management training programs	Informing clients about how other companies deal with an issue may be as effective as other tactics in obtaining client concessions. Clients are also found to prefer that auditors use a cooperative communication style.
Brown-Liburd and Wright (2011)	Do past client relationship and strength of the audit committee have an effect in auditor-client negotiations?	63 Big 4 managers and partners	Past client relationship and strength of the audit committee are found to interact: the most contending negotiation strategy is used when past relationship is contending and audit committee is strong.
Brown-Liburd et al. (2012)	Do earnings forecasts and professional skepticism have an effect on the outcome in auditor-client negotiations?	38 Big 4 managers and partners	Auditors who exhibit heightened professional skepticism are more likely than auditors who do not exhibit heightened professional skepticism to acquiesce to client preferences. Earnings forecasts are not found to have a main effect on accounting outcomes but an interaction effect is found.

A negotiation tactic suggested in generic negotiation theory is the bid highï concede later strategy. Findings from audit research show that auditors view this strategy as unprofessional (Ng and Tan 2003). Sanchez et al. (2007) suggest that auditors can use a variant of the bid highï concede later strategy by using a **reciprocity based strategy** to achieve the mutual goal of high quality reporting combined with an adequate relationship with the client. Using this tactic, auditors show the client all adjustments they propose, even those that are clearly inconsequential, and the auditors have the intention of waiving some of the smaller (and inconsequential) misstatements to induce a good negotiation climate. Findings from the study suggest that the clients who are shown all discovered misstatements, as opposed to only the misstatements that the auditor requires them to correct, are more willing to post income-decreasing adjustments. The experiment also shows that auditors perceive that the use of this strategy is positive for client satisfaction and retention.

Hatfield et al. (2008) build on the findings in Sanchez et al. (2007) and investigate the effect of the **client management’s negotiation style** and the **client’s retention risk** on auditor’s use of a reciprocity-based negotiation tactics (trade-off of issues) in a study using an experimental design. Findings indicate that if the client management has a competitive style and/or the retention risk is high, the auditor’s likelihood of using the reciprocity-based negotiation strategy is higher than if the client management has a non-competitive style and/or the retention risk is low. Findings also suggest that the use of reciprocity-based tactics can lead to more conservative accounting.

Brown and Johnstone (2009) set up a computerized experiment using the Internet in which 60 audit managers and partners negotiate a complex revenue recognition issue to investigate the effect of **negotiation experience** (task-specific measure) and **engagement risk** on choice of negotiation tactics and negotiation outcome. They find that auditors with more audit experience use a more contending strategy than auditors with less audit experience and that auditors with little negotiation experience use a more concessionary negotiation strategy in negotiations with high negotiation risk compared to the strategy used by auditors with little negotiation experience in negotiations with low engagement risk as well as compared to the strategy used by experienced auditors (irrespective of the client’s engagement risk). Brown and Johnstone also find that more experienced auditors make more conservative final bids and that these auditors feel more confident that the chosen solution is acceptable under GAAP.

Trotman et al. (2009) examine the effect of **auditor negotiation experience** on their pre-negotiation judgments. An experiment is conducted with 43 participants who are asked to evaluate a difficult inventory write-down case. The findings show that the participating partners ask for a higher initial proposed write-down, require a higher minimum write-down and expect a higher write-down than do the participating managers.

Wang and Tuttle (2009) study the impact of mandatory **auditor rotation** on auditor-client negotiations and find that mandatory rotation leads to less frequent use of cooperative strategies and to accounting outcomes more in line with the auditorøs preferences.

Gibbins et al. (2010) experimentally investigate the effect of the **nature of the auditor-client relationship** and the **auditorøs initial assessment of client management flexibility** in its accounting positions on the auditorøs choice of negotiation strategy and on the auditorøs goal commitment to income reduction. Their findings indicate that if clients are inflexible (compared to a flexible), the more likely is the auditorøs use of the contending negotiation strategy and the less likely is their use of the concessionary and compromising strategy. If the auditor-client relationship is friendly (compared to unfriendly), the study finds an increased likelihood that auditors intend to use a more concessionary negotiation strategy (only marginally significant) but no effect is found on the auditorøs intention to contend. The study also finds that the more inflexible the client and/or the less friendly the relationship, the more committed is the auditor to assure a substantial reduction in client income.

Hatfield et al. (2010) argue that the **size of the audit difference** and **existence of prior client concessions** may have an effect in auditor-client negotiations, and they investigate the effect of these factors in an experiment where there is a disagreement about either an objective audit issue concerning a professional service invoice or a subjective audit issue (an inventory valuation case). Findings indicate that auditors have significantly lower negotiation goals and limits and that initial negotiation position is lower if the audit difference is large than if it is small. If the client has conceded on an adjustment prior to this negotiation, the auditorøs initial negotiation position is also lower than if the client has not conceded. Auditors also obtain an outcome that is closer to the client proposed solution if the size of the audit adjustment is large and/or there has been a prior client concession.

According to Tan and Trotman (2010) clients who negotiate a subjective accounting issue are likely to expect some concessions. Prior auditing research suggests several tactics, such as the ñbid-high-concede-laterò tactic (Bame-Aldred and Kida 2007) and the ñreciprocity-basedò tactic as described in Sanchez et al. (2007), which can be used to encourage the client to record the proposed adjustments. Tan and Trotman (2010) suggest that auditors can also use the timing of their concessions to obtain their preferred accounting outcome. According to the findings in Tan and Trotman (2010), the **timing of auditorøs concessions** have an effect on the judgments that are made by the clients in auditor-client negotiations; gradual or late concessions are seen to lead to higher final offers (larger write-downs) than early concessions. Gradual or late concessions also seem to give higher client satisfaction with the auditorôs final offer and the negotiation outcome. The likelihood that the client will keep the auditor is higher than if the auditor makes early concessions. The clientôs satisfaction with the negotiation process, however, is unaffected by the timing of the auditorôs concessions.

Motivated by previous negotiation studies using surrogates for partners and the fact that audit managers often try to solve audit conflict issues before the partner is involved, McCracken et al. (2011) examine the consequences of using different types of surrogates for partners in experimental audit negotiation studies. Their most important finding is that audit managers seem to be more likely to use both compromising and concessionary tactics than audit partners. Audit managers are less likely than partners to use contending tactics.

Fu et al. (2011) study the combined effect of **auditor negotiation experience** and **client negotiation style** on auditorsô perceived negotiation outcome. First, they find that when clients have a contentious negotiation style, auditors with high experience report higher perceived write-downs than auditors with less negotiation experience. Second, they find that client negotiation style only has an effect on auditors with little negotiation experience (low experience auditors report higher perceived write-downs when the client has a collaborative negotiation style than when the client has a contentious negotiation style).

Perreault and Kida (2011) investigate the **effectiveness of four different persuasive tactics**: threatening to qualify the audit opinion, warning about the possibility of quality control, providing the opinion of a technical expert and the use of precedents (describing how other companies have resolved similar issues). Whether the communication style has an effect on negotiations is also investigated. Findings indicate that describing how other companies have solved similar issues is at least as effective to induce client concessions as the use of threats and that a cooperative communication style leads to more concessions from the client and larger client satisfaction than does a more contentious style.

Brown-Liburd and Wright (2011) study the interaction effect of past **auditor-client relationship** and **strength of the audit committee** on auditorsô pre-negotiation judgments

(judgments regarding preferred writedown, first-offer and reservation price) and on the willingness to concede (concessions and final offer) in a negotiation. Findings indicate a strong interaction effect: first-offers are highest and concessions smallest when the audit committee is strong and the past auditor-client relationship is contending.

Brown-Liburd et al. (2012) conduct a negotiation experiment to investigate whether negotiation accounting outcomes are affected by the **client managementôs ability to meet earnings forecasts** and **the auditorôs professional skepticism** (measured as the participantsô salience of client risk factors). The experiment participants conduct a negotiation with a hypothetical client. The findings suggest that the auditors in the experiment are not influenced by earnings forecasts. Auditors who exhibit heightened professional skepticism make more conservative accounting decisions (participants chose from booking two proposed adjustments, waiving one of the adjustments or waiving both the proposed adjustments) than participants who do not exhibit heightened professional skepticism. In addition, the study identifies an interaction effect between the two variables.

2.4.7. Summary

In this section I summarize the presentation of prior research by presenting Table 4 which focuses on the independent variables that are identified and/or found significant in this research. I also summarize other important findings.

The literature review in chapter 2 has presented three different research streams in the area of auditor-client conflict research: (1) auditorsô acceptances of client-proposed accounting in situations of auditor-client conflicts, (2) auditorsô decisions to waive proposed audit adjustments and (3) auditor-client negotiation studies.

The research streams identify and test a number of contextual and process variables that seem to have an impact in auditor-client negotiations, and the review provides an overview of prior research that is useful when developing hypotheses in the area of auditor-client negotiations. Table 4 summarizes the findings on the impact of different variables: the first part of Table 4 (Interview-based studies) gives an overview of the independent variables that are identified in prior interview-based research, and the second part of Table 4 (Experimental and archival studies) present the variables that are studied and found significant.

If we look at the auditor-client negotiations studies (last page of Table 4), we see that many of the variables that are suggested by Gibbins et al. (2001 and 2007) to have an impact in auditor-client negotiations are not empirically tested, some are tested once and the variables negotiation style/strategy and auditor experience are tested several times. The presentation of the studies in the literature review shows that findings related to experience are mixed.

Table 4 is summarized in a comprehensive model in Figure 3 which includes both the factors that are tested in prior experimental/archival research and factors that are suggested to have an impact based on interview-based-research. This model gives an overview of contextual variables that it may be necessary to control for when studying auditor-client negotiations.

The review further shows that all prior auditor-client negotiation studies have been conducted with the experimental method (see Table 3). We have also seen that even though a relatively large number of studies investigate the effects of contextual variables in the process and on the outcome of auditor-client conflicts, none of the studies focus on the relative importance of different contextual variables.

Table 4 - An overview of independent variables identified and/or found significant in prior empirical research

Interview-based studies

	Variables identified			
Study	Input	Client	Auditor / audit firm	Environment
Gibbins et al. (2001 and 2007)		Client's inherent risk Business reputation of client management Dominant client CEO Client's audit committee chair Client's board chair Client's internal auditors Other client personality characteristics Size of the client relative to audit firm Client's audit committee Client's accounting expertise Client's financial reporting reputation Client's negotiation expertise Client size	Auditor's power to qualify Ethical considerations Past relationship with client Client service considerations Client retention Audit firm's accounting expertise Audit firm's negotiation expertise Interpersonal relationships in audit firm Audit firm's central consultation unit Size of the audit firm Cost of negotiation and data gathering Competence of audit partners Audit firm's tax services Time pressure	Owner and investor considerations Accounting and disclosure standards Industry practices Securities and exchange regulations Auditing standards Reporting or filing deadline Creditor or lender consideration Legal considerations Tax considerations Dominant shareholder or owner Financial analysts
Beattie et al. (2004)		Company type and situation Client's audit committee	Level of audit firm support and quality control Level of integrity of audit engagement partner Quality of primary relationship	

Experimental and archival studies

	Variables found significant			
Study	Input	Client	Auditor / audit firm	Environment
Audit-conflict studies:				
Knapp (1985)	Technical accounting standards	Financial condition		
Farmer (1987)			Risk of client loss Auditor experience	Litigation risk
Lindsay (1989) and (1990)	Regulation of accounting issue		Audit firm size Provision of non-audit services	Competition in audit market
Gul (1991)			Audit fee Provision of MAS Audit firm size	Competition in audit market
Trompeter (1994)	Precision of GAAP		Partner compensation scheme	
Goodwin and Trotman (1995)			Risk of client loss	Litigation risk
Windsor and Ashkanasay (1994) and Tsui and Gul (1995)			Auditor's locus of control Auditor's ethical reasoning	
Hackenbrack and Nelson (1996)		Engagement risk		
Salterio (1996) and Salterio and Koonce (1997)			Accounting precedence (decision aid)	
Shafer et al. (1999)				Formal sanctions
Dopuch et al. (2001)				Mandatory auditor rotation
Kadous et al. (2003)			Auditor's directional goal commitment Quality assessment of accounting methods	
Ng and Tan (2003)	Authoritative accounting guidance	Audit committee		
Jenkins and Haynes (2003)		Timing of persuasion Client credibility		

Experimental and archival studies (cont.)

	Variables found significant			
Study	Input	Client	Auditor / audit firm	Environment
Chang and Wang (2003)		Business risk	Retention risk	
Iyer and Rama (2004)		Client's perception of his importance for the auditor	Tenure	
Bamber and Iyer (2007)			Auditor identification with client Auditor identification with profession Experience Tenure	
Lin and Fraser (2008)	Precision of accounting regulation		Tenure Provision of MAS	Competition in audit market Cultural differences
Chang and Hwang (2010)		Business risk	Retention risk	Litigious environment
Ng and Shankar (2010)	Presence of quality assessment std.	Client justification	Advice from tech. department	
Waive / adjust-studies:				
Icerman and Hillison (1991) *	Issue size		Audit firm structure	
Houghton and Fogarty (1991) *	Issue size			
Wright and Wright (1997) *	Objective vs. subjective Issue size Income increasing	Client size		
Braun (2001)	Objective vs. subjective Income increasing	Financial Health		
Nelson et al (2005)			Decision aid	
Ng (2007)	Objective vs. subjective		Decision aid Earnings thresholds	
Ng and Tan (2007)		Client concern about not booking	Auditor's mental model Salience of qualitative factors	
Joe et al. (2011) *			Tenure Adjustment proposed previously	

*) Archival study

Experimental and archival studies (cont.)

	Variables found significant			
	Input	Client	Auditor / audit firm	Environment
Auditor-client negotiation studies:				
Goodwin (2002)		Size Corporate governance mechanism		
Trotman et al. (2005)			Intervention methods	
Sanchez et al. (2007)			Reciprocity-based tactic	
Hatfield et al. (2008)		Management's negotiation style	Retention risk	
Brown and Johnstone (2009)		Engagement risk	Auditor-experience	
Trotman et al. (2009)			Auditor experience	
Wang and Tuttle (2009)				Mandatory auditor rotation
Gibbins et al. (2010)		Management flexibility		Auditor-client relationship
Hatfield et al. (2010)	Size of audit differences	Prior client concessions		
Tan and Trotman (2010)			Timing of auditor's concessions	
McCracken et al. (2011)			Auditor experience	
Fu et al. (2011)		Client negotiation style	Auditor experience	
Perrault and Kida (2011)			Contending tactics	
Brown-Liburd and Wright (2011)		Audit committee		Past auditor-client relationship
Brown-Liburd et al. (2012)			Auditor's professional skepticism	Earnings forecasts

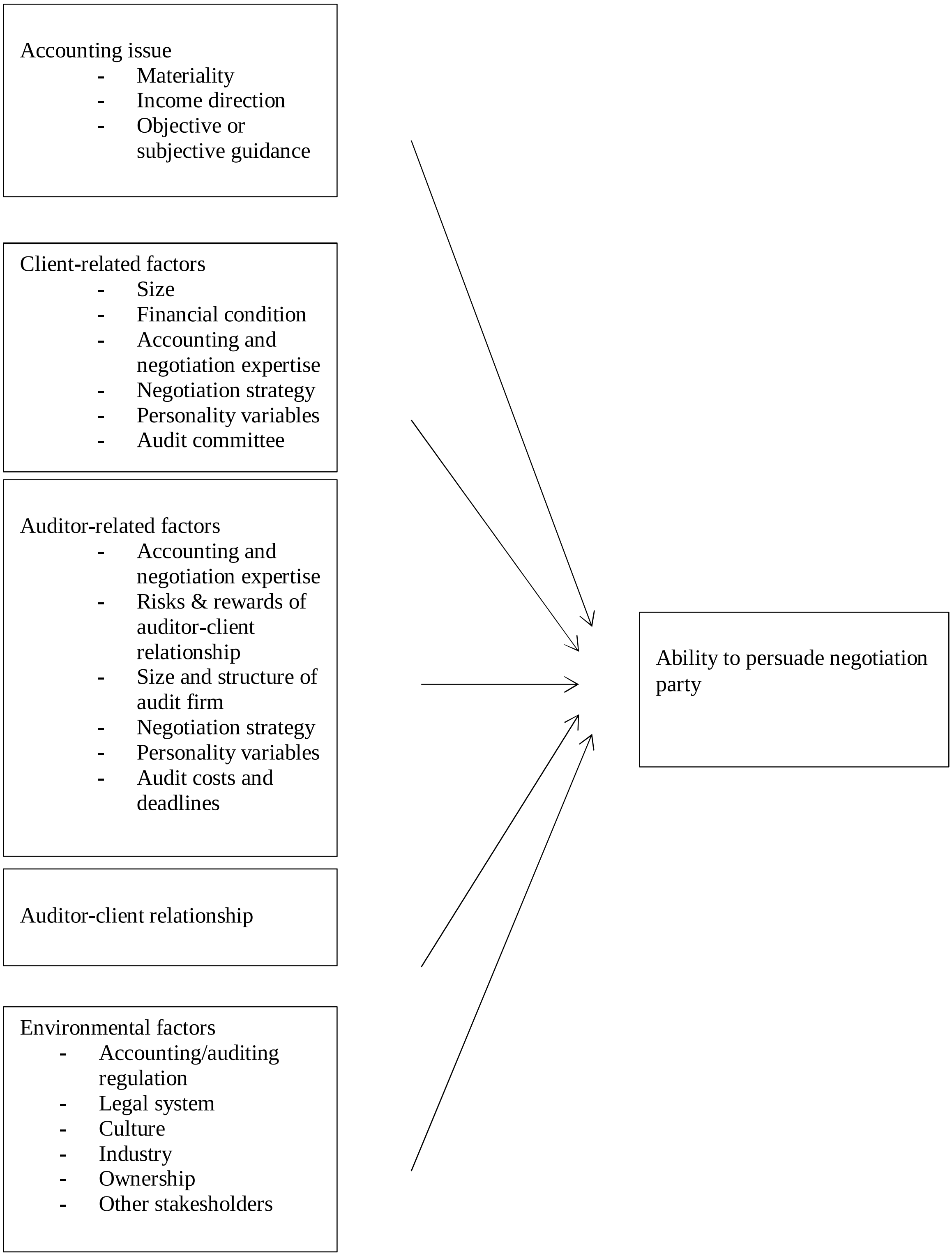


Figure 3 - An auditor-client negotiation model: an overview of independent variables identified and/or found significant in prior empirical research

3.0. Research model and development of hypotheses

3.1. Introduction

According to Libby, ñWhether accountants are concerned with their own or otherôs decisions, the focus of their concern is on the improvement of decisions.ò (Libby 1981, p. 3) A necessary first step to improve decision-making is to obtain more knowledge about how decisions are made. The purpose of this thesis is to provide knowledge about auditor-client negotiations by investigating the relationship between different contextual variables and the strategies used and accounting outcomes obtained in such negotiations with a particular focus on the relative importance of different contextual variables.

In this chapter I first present my research model in section 3.2. I then develop hypotheses about the relationships between the variables in the model in section 3.3. In section 3.4, I discuss the use of the research model when trying to predict accounting outcomes in auditor-client negotiations over accounting issues.

3.2. Research model

As mentioned previously, Gibbins et al. (2001) identify 29 variables that have a potential impact on auditor-client negotiation processes and outcomes, but they find that relatively few contextual variables seem to have an impact in all such negotiations (Gibbins et al. 2001; Gibbins et al. 2005; Gibbins et al. 2007). According to Gibbins et al. (2007), the most important features seem to be the role of accounting standards, the level of expertise on both sides of the negotiation and the relationship between the two parties. As one of the main aims with this study is to examine the relative importance of different contextual variables in auditor-client negotiations, it follows that my study will focus on the variables that are identified by Gibbins et al. (2007) as the most important variables. (As stated previously, Gibbins et al. (2001, 2005, and 2007) do test statistically neither the impact nor the importance of the variables that their studies identify.

More specifically I will study the impact of the precision of accounting regulation, the quality of the auditor-client relationship, the clientôs accounting expertise, and the partnerôs experience in auditor-client negotiations. It follows from my literature review in chapter 2 that these variables have either not yet been studied or have been studied but in a small number of previous experimental studies, and I will in the next section develop hypotheses about their relationship with auditorsô choice of negotiation strategy. (See section 2.4 for a thorough review of prior research. The second part of Table 4 gives an overview of the contextual variables that are studied and found significant in prior studies.)

When auditors and clients negotiate, it should be noted that auditors will normally have incentives to support a more conservative solution than the one the client prefers, otherwise there would be no conflict[21], (Bame-Aldred and Kida 2007). (Nevertheless, this is not equivalent to saying that the most conservative solutions are necessarily the best solutions: the auditor has a professional obligation to give his opinion on whether a financial statement is in accordance with the accounting standards, not, for instance, to ensure as large write-downs as possible). Often this will mean that he uses the contending strategy to persuade the client to accept his solution,[22] and this strategy is likely to be very important in the auditing context.

At the same time, auditor-client negotiations take place in an ongoing relationship, and it is the client who makes the decision about which auditor he wants. Consequently the auditor is likely to care not only about the accounting outcome when he negotiates accounting issues but also the effect of the negotiation process and outcome on the auditor-client relationship. If the auditor accepts a compromise or even accepts in its entirety the solution the client has suggested, the auditor uses the conceding strategy.

To summarize we see that the dual-concern-model (see section 2.4.4) is of particular interest in accounting as it captures the two important dimensions care for self (desire to make sure the accounting outcome is at least acceptable/defendable) and concern for others (desire to secure relationship).

[21] Occasionally, auditors and clients disagree because clients want more conservative outcomes than the auditor. In particular, smaller clients may have incentives to reduce income to pay smaller taxes, but larger clients may also want to reduce income to build reserves (an example is the phenomenon ñbig-bath-accountingò).
[22] It should be noted that the solution that the auditor suggests will not always be the solution that is the closest to the «correct» solution, because the client may have a better understanding of the issue than the auditor has.

Most prior audit research examines the effect of different contextual variables on the different negotiation strategies in isolation. Use of the conceding (concern for other) negotiation strategy is, however, likely to weaken the effect of the contending strategy. In addition, a strategy in which the use of the contending strategy is high and the conceding is low is likely to be experienced as ñmore contendingò than a strategy in which the use of both the contending and the conceding strategy is rated as high. As the dual-concern model is particularly interesting in accounting, I will in this thesis study the relationship between the contextual variables listed above and the combined use of these two strategies.[23]

A model of my research is presented in Figure 4 below. This model differs from the model in Figure 3 in that whereas Figure 3 should be understood as a summary of all independent variables that are identified and/or found significant in prior research, Figure 4 includes only the variables that are suggested by Gibbins et al. (2007) to be the most important contextual variables in auditor-client negotiations. Whereas Figure 4 includes the variables that I study in my thesis, Figure 3 gives an overview of other variables that it may be necessary to include as control variables in my study.

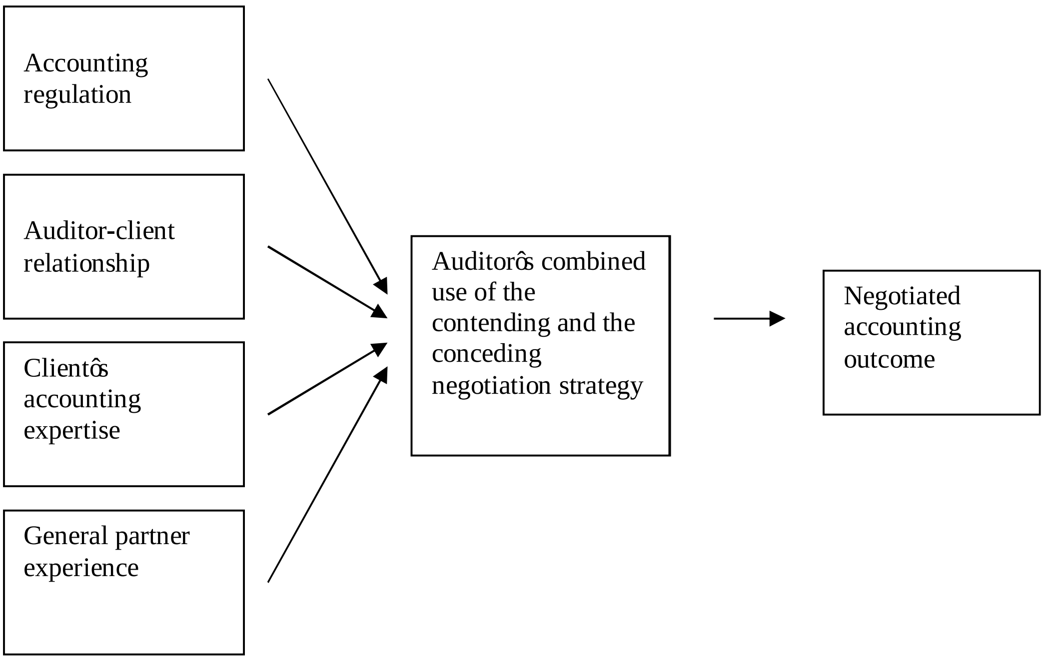


Figure 4 - Factors that affect the negotiated outcome

[23] As I am interested in auditorsô behavior in auditor-client conflicts as a situational construct and as I will not study ñhow a person commonly deals with conflictò, I will use the terms strategies and tactics when I describe and report my own research project.

The hypotheses that are tested in my study are indicated by the five arrows in the figure. In the following section 3.3, I develop hypotheses to predict how the precision of accounting regulation, the quality of the auditor-client relationship, clientsô accounting expertise and audit partnerôs general experience is likely to relate to the auditorsô combined use of the contending and the conceding negotiation strategies. In section 3.3.4, I develop a hypothesis to predict how the auditorôs combined use of the contending and the conceding strategy is likely to relate to the accounting outcome of the negotiation.

I will then build on the model in Figure 4 to investigate the relevance and importance of the precision of accounting regulation, the quality of the auditor-client relationship, clientsô accounting expertise, audit partnerôs general level of experience and auditorsô combined use of the contending and the conceding negotiation strategies when trying to predict accounting outcomes in auditor-client conflicts over accounting issues. Use of the model in Figure 4 will be discussed in more depth in section 3.4.

3.3. Development of hypotheses

Several audit studies have found that auditors change their negotiation strategies and tactics depending upon different contextual factors (e.g. Goodwin 2002; Hatfield et al. 2008; Gibbins et al. 2010). Prior audit research, as discussed in chapter 2, also suggests that the accounting outcomes of auditor-client negotiations over accounting issues depend upon the negotiation strategies and tactics that the negotiation parties decide to use in the negotiation (e.g. Gibbins et al. 2001). In auditor-client negotiations over accounting issues, the auditor can use a number of different negotiation strategies and tactics, see section 2.4.4 for an elaborate presentation of these strategies and tactics.[24]

In an auditor-client negotiation over accounting issues, the auditor is likely to use the strategy that he thinks is most likely to lead to his preferred outcome. It should be noted that this outcome is not necessarily the outcome where the auditor ñwinsò the negotiation; the auditor may prefer to accept the clientôs solution even though he initially thinks that the client is

[24] Some researchers call the use of negotiation strategies and tactics ñauditorôs negotiation styleò, see section 2.4.4.

wrong. An underlying assumption in this study is that when disagreements occur, the auditor will sometimes choose a strategy that involves looking for evidence that is supportive of the clientôs opinion (i.e. is it possible to find evidence so that the clientôs solution can be accepted). At other times, the auditor chooses to focus on showing that the client is wrong, i.e. the clientôs solution is not acceptable, and the auditor looks for evidence that rejects the clientôs solution and supports the auditorôs solution.[25]

Auditor-client negotiations take place in an ongoing relationship and negotiations may occur each year with some of the clients. It is therefore likely that the auditor is also concerned with how he best creates and retains a positive relationship with his client. As the contending strategy involves different types of persuasive behavior, possibly even threats, this strategy may have a negative impact on the auditor-client relationship, and an underlying assumption when developing hypotheses is that the auditor will not want to use more of the contending tactics than is absolutely necessary.[26] At the same time, it is an inherent part of an audit that the auditor should be independent of the client and that he conducts his audit work in accordance with his professional obligations. Consequently, it is likely that the auditor will use some contending tactics. Auditors can also use various combinations of the contending and the conceding strategy, and it is likely that the effect of a given strategy will be greater the less frequently this strategy is coupled with the other strategy.

In the following sections I develop directional hypotheses that predict how the precision of accounting regulation, the quality of auditor-client relationship, clientsô accounting competence and auditorsô negotiation and accounting competence are likely to relate to auditorsôuse of the contending and the conceding negotiation strategy.

3.3.1. Precision of accounting regulation

Prior research in auditing (Wright and Wright 1997; Braun 2001) finds that the precision of accounting regulation has an effect on which adjustments are corrected; proposed adjustments

[25] In other words, when auditors negotiate (and audit) their working hypothesis will sometimes be supportive of the clientôs initial position and sometimes supportive of the auditorôs initial position. This distinction is parallel to the distinction between falsification and verification, the primer suggested by Popper to be the criterion of science (Popper, 1959).

[26] Compared to many other negotiations, the auditor does not have to hesitate on the use of the contending tactic to avoid a non-agreement situation as he in such situations of non-agreement can issue a qualified audit opinion.

of a subjective nature (i.e. estimates) are waived more often than objective proposed adjustments (i.e. posting and footing of transactions). Prior research also shows that auditors are more influenced by client preferences (e.g. require smaller downward income adjustments) if an accounting issue is not regulated by precise accounting standards (Trompeter 1994) and that auditors justify their choice of accepting aggressive accounting by their interpretation of vague accounting standards (Hackenbrack and Nelson 1996). These findings suggest that the auditor uses a more contending negotiation strategy when accounting regulation is precise than when accounting regulation is less precise.

Auditors are faced with a constant struggle to keep both a functional and positive relationship with their clients and to fulfill their professional obligations. It is therefore likely that they are more reluctant to accept client-proposed accounting solutions in situations where there is relatively high consensus (precise regulation) about what constitutes the correct solution because this situation is riskier to the auditor than if accounting regulation allows for a larger degree of decision subjectivity. For instance, Braun (2001) argues that liability exposure is lower for highly subjective issues than for less subjective accounting issues.

Prior research (Neale and Bazerman 1985) shows that people seem to respond to risks in negotiations by using a more contending strategy when risks are high than when risks are low. By contrast, Brown and Johnstone (2009) find in an experiment involving a low versus a high engagement risk setting that this accounts only for decisions of the less experienced auditors.

More precise accounting standards not only heighten the *risks* (i.e. liability risk) the auditor faces as the quality of his decisions are easier to judge in retrospect but also provides the auditor with bargaining ammunition and power to refuse to give a clean audit opinion if the accounting rules are not followed (Ng and Tan 2003). In previous research using the experimental method, powerful negotiators are shown to use more threats and punishments than less powerful negotiators (Michener et al. 1975); therefore, auditors who negotiate precisely regulated accounting issues can be expected to use a negotiation strategy that includes more persuasive arguments and more threats.

As it is likely that precise accounting regulation makes it more risky for the auditor to concede at the same time as precise regulation makes the auditor more powerful and consequently more likely to use a more contending strategy, the arguments lead to my first hypothesis (in alternative form):

H_1: When negotiating difficult accounting issues, the more precisely regulated the negotiated accounting issue, the more likely it is for the auditor to use an overall negotiation strategy that is more contending than the overall negotiation strategy used by auditors when the negotiated accounting issue is less precisely regulated.

3.3.2. The quality of the auditor-client relationship

Recent accounting scandals have led to an increased focus on the concept of auditor independence, and regulators have imposed new regulations on accounting firm rotation and banned certain auditor consulting activities (Bamber and Iyer 2007). Underlying these regulations is the perception that not only financial ties but also personal relationships are detrimental to the quality of financial audits. Paradoxically, it will often be easier to perform an audit when the auditor is familiar with the client. The conflict between a necessary familiarity and related threats to auditor independence has even led critics to argue that it is not possible for auditors to perform objective audits (Bamber and Iyer 2007).

One of the ways to characterize relationships is by the dimension, ñpositive ï negativeò. Positive relationships typically include trust, and the parties involved are concerned not only for their own but also the other partyôs negotiation outcome. Negative relationships, by contrast, are characterized by distrust and negative attitudes (Pruitt and Carnevale 1993). Generic negotiation research typically has studied relationships by comparing the behavior of friends, lovers or married couples with the behavior of people who interact but are more or less strangers to one another. Not surprisingly, people engaged in positive relationships concede more often and use less contentious tactics than people who are not engaged in such relationships. By contrast, people engaged in negative relationships want to secure the best possible outcome for themselves and are likely to use more contending tactics than people in less negative relationships (see Pruitt and Carnevale 1993, p. 136, for an overview of studies on positive and negative relationships).

The relationship between auditors and clients is different from many of the relationships previously studied in negotiations. Auditors are required to conduct their audits using professional skepticism and have a professional reputation to consider. Yet as auditors conduct their audits in ongoing relationships and have incentives to conduct their audits to retain their clients, it is not unlikely that how the auditors assess their relationship with a client is related to the type of negotiation strategy/tactics that the auditor chooses in auditor-client negotiations.

Prior research in auditor-client conflict (see Table 4) has primarily focused on the consequences of financial ties (factors related to risks and rewards) between the auditor and the client and that the effect of cognitive-based /socially-based ties has just barely been considered. Some exceptions are found. Bamber and Iyer (2007) use social identity theory and find that auditors who identify with a client are more likely to accept the client-preferred accounting position than auditors who identify less with their clients.

There is only study in the area of auditor-client conflict over accounting issues that directly examine the effect of the auditor-client relationship; Gibbins et al. (2010) who study the effect of auditor-client relationship on auditorôs choice of negotiation strategies and negotiation outcomes. The study shows a significant relationship ($p<0.053$) between the quality of the relationship (positive and cordial versus negative and contentious) and audit partnersô use of the concessionary negotiation strategy. By contrast, Gibbins et al. (2010) find no relationship between the quality of the relationship and audit partnersô use of the contending negotiation strategy. Findings from generic research (see above) do, however, suggest that such a relationship is likely to exist.

As auditors may be expected to dislike the use of contending tactics because they are likely to think that such tactics may harm the relationship, auditors who have a good relationship with their clients are likely to use less of these tactics and a more conceding strategy than auditors who have a bad relationship with their client.

Given prior findings from generic research on the effect of positive versus negative relationships, the findings from Gibbins et al. (2010) on the effect of relationship quality on auditorôs use of the contending negotiation strategy, and auditorô general incentives to keep a positive relationship with their clients, auditors may be expected to let the quality of their auditor-client relationship affect their combined use of the contending and the conceding negotiation strategy. This leads to the following hypothesis (in alternative form):

H$_2$: When negotiating difficult accounting issues, the more positive the auditor perceives the auditor-client relationship, the more likely it is for the auditor to use an overall negotiation strategy that is less contending than the overall negotiation strategy used by auditors who perceive the auditor-client relationship to be more negative.

3.3.3. The negotiation partiesô experience and expertise

3.3.3.1. The audit partnerôs experience

According to Brown and Wright (2008), generic negotiation research finds that ñnegotiation experience improves negotiation performance and outcomesò (Brown and Wright 2008, p. 97). For instance, in a study by Thompson (1990), knowledge and experience generated in previous negotiations are found to improve the negotiatorsô negotiation skills.

Audit theory distinguishes between experience and expertise and defines audit expertise loosely as superior judgment performance caused by the factors knowledge and ability (Bonner and Walker 1994). According to Bonner and Walker (1994), knowledge consists of *declarative* (knowledge of facts and definitions) and *procedural* knowledge (knowledge of the rules or steps that are necessary for the completion of a task).

According to a model by Libby (1995), see Figure 5, *instruction* and *experience* induce knowledge. Instruction is thought to be acquired formally and informally in school and through firmsô continuing education courses (Bonner and Walker 1994). Experience is thought to produce knowledge as different tasks (judgments) are performed and feedback is received on these judgments (Bonner and Walker 1994). Learning theories suggest that at least some practice followed by further defined feedback is necessary for the acquisition of procedural knowledge. Experience *per se* will consequently not cause superior judgment performance, and auditors can be experts in different audit tasks.

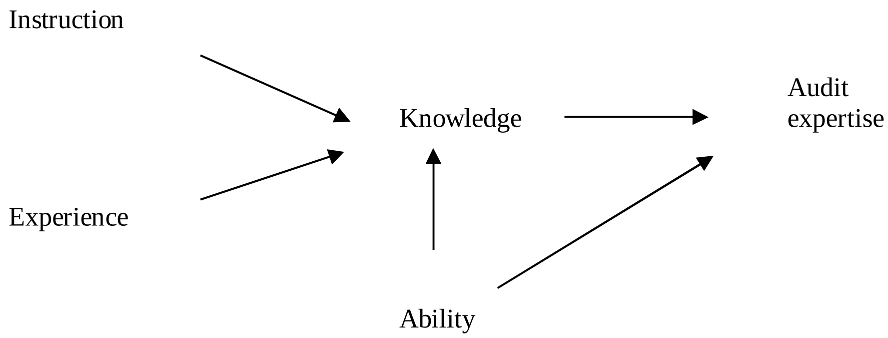


Figure 5 - Libbyôs (1995) model of the Acquisition of Audit Expertise

In many audit tasks, auditors will have acquired the necessary procedural knowledge as audit seniors. In other tasks, experience as managers or partners is needed to acquire procedural knowledge, as seniors do not perform these tasks. Little seems to be known about what types of procedural knowledge are needed for superior negotiation performance in auditing.

Kaplan et al. (2008) suggest that auditors gain persuasion knowledge[27] (an example of procedural knowledge that can be of use in negotiations) as they gain audit experience, and find that more experienced auditors are less likely to rely on management information when this information is congruent with management self-interest than auditors with less experience.

Prior research in auditor-client negotiations over accounting issues find that experienced auditors (partners) ask for and are able to enforce larger write-downs in auditor-client negotiations than less experienced auditors (managers) (Trotman et al. 2009). This difference may be caused by negotiation expertise but, for instance, it may also be caused by differences in status/authority.

Auditor-client negotiations are tasks that are normally dealt with at the partner level; consequently, it should be expected that much negotiation knowledge is learned after the partnership is received. Contrary to this expectation, Bame-Aldred and Kida (2007) and Brown and Johnstone (2009) find that general experience measures (years of experience and

[27] Kaplan et al. (2008, p. 68) define auditorôs persuasion knowledge as ñan auditorôs beliefs about how, when, and why managers try to influence auditors, and consequently, help auditors respond to these persuasion attemptsò.

rank) are not closely related to auditorsô negotiation behavior. Brown and Johnstone (2009) also test a task-specific measure of experience and find that managers and partners who have experienced many (11 or more) auditor-client negotiations during the last three years use a less concessionary negotiation strategy, obtain more conservative accounting and are more confident that the obtained accounting is allowed under GAAP than participants who have experienced fewer such client-auditor interactions in recent years. In contrast to the findings referred above, McCracken et al. (2011) find that partners plan to use more contending tactics than audit managers but this finding depends upon the accounting context. Partners also plan to use a less concessionary strategy than managers and this finding is not context-dependent.

More experienced audit partners are likely to behave differently than their less experienced partner colleagues for many reasons; they are likely to have more relevant procedural knowledge and better negotiation skills (negotiation expertise). In addition, it is likely that their negotiation experience makes them more self-confident and more likely to try to obtain the solution they initially found correct even if this is likely to lead to more contending behavior.

By contrast, younger partners may be more aggressive in order to ñmake their markò (always contending behavior) whereas more senior partners are wiser and know what battles to fight (contending behavior only when necessary). Younger partners may also want to ñplay toughò in their first negotiations with clients to build a reputation as a tough negotiator.

Based on prior research findings as well as the above-presented arguments, we see that it is difficult to construct a directional hypothesis about the relationship between partner experience and use of negotiation strategies and tactics. This leads to the following non-directional hypothesis (in alternative form):

H$_3$: When negotiating difficult accounting issues, more experienced audit partners differ from less experienced audit partners in their combined use of the contending and conceding negotiation strategies.

3.3.3.2. The clientôs technical accounting knowledge

Findings from Gibbins et al. (2001) and (2007) indicate that auditors and clients disagree with one another about the importance of the clientôs accounting expertise in auditor-client negotiations. Whereas auditors do not think that the clientôs accounting expertise is an important variable in an auditor-client negotiation, CFOs think that only accounting regulation is a more important variable.

Performing different accounting tasks requires various types of knowledge (Bonner and Lewis 1990). In similar fashion: to find good accounting solutions when an accounting issue is disputed will also require different types of knowledge. For example, the necessary knowledge may include general domain knowledge (i.e. basic knowledge about GAAP), as well as, subspecialty knowledge (i.e. knowledge related to a specific client or industry including client and industry specific knowledge about GAAP as well as knowledge about the clientôs economic situation). Auditors and clients may possess these different types of accounting knowledge in varying degrees depending upon their instruction, experience and abilities (see 3.3.3.1 for a presentation of Libbyôs (1995) model).

Gibbins et al. (2001) claim that negotiation is a ñcalculated, strategic activity informed by the partyôs knowledge, perceptions, preferences and beliefs (...) and that the private information of the parties is unequalò. Auditors will often, but not always, possess more general domain knowledge and subspecialty domain knowledge related to GAAP than their clients (client employees may, for instance, have the same formal education as their auditors and have previous working experience as auditors). Auditors often have the possibility to consult a central consultation unit which has extensive knowledge of accounting methods and standards, making it possible for the auditor to compare the practices of different clients. This knowledge is first of all related to how to interpret and understand accounting standards and how to solve accounting issues not directly regulated (I label this knowledge ñtechnical accounting knowledgeò). According to Gibbins et al. (2001 and 2007), audit partners believe that they have an expertise advantage over their clients related to technical accounting knowledge; 85% of the respondents agree that they have a better understanding of GAAP than their clients (Gibbins et al. 2001) and the clients seem to agree that auditors know GAAP better than they do (Gibbins et al. 2007).

By contrast, client management is likely to know more than the auditor when it comes to subspecialty knowledge about their own economic situation, the industry to which the client belongs, the economic situation of their suppliers and customers and other types of knowledge necessary to predict future economic conditions (business knowledge). Despite these types of management knowledge, 72% of the audit partners in the Gibbins et al. (2001) study disagree that clients understand their own situation better than do audit partners.

Assuming that auditors in the same audit firm have approximately the same amount of accounting expertise[28], auditorsô relative accounting expertise will differ depending upon the accounting expertise of the client, i.e. the less technical accounting knowledge possessed by a client, the more the auditor is an expert in accounting. In-depth information about a subject (e.g. technical accounting knowledge) may induce expert power. Consequently, the less technical accounting knowledge possessed by the client, the greater the expert power possessed by the auditor. Findings from generic negotiation research suggest that powerful negotiators make more threats, i.e. use more contending tactics (Pruitt and Carnevale 1993). Auditors who work with audit clients with little technical accounting knowledge are consequently likely to use an overall negotiation strategy that is more contending than auditors with clients who have more technical accounting knowledge.

Clients who have high technical accounting knowledge are to a greater extent than other clients able to come up with acceptable accounting solutions, and they are also able to discuss and defend their solutions with viable technical arguments. Consequently, it is likely that tactics other than contending tactics are more useful when negotiating with such clients even when the aim is to persuade the other party.

Given prior findings from generic negotiation research that reports that powerful negotiators use more contending tactics (threats) and the argument that auditors are likely to find other strategies more useful than the contending strategy when clients have high technical accounting knowledge, clientôs technical accounting knowledge is likely to be related to

[28] Even though auditors will differ in experience, personal abilities and accounting knowledge, the assumption is not as unrealistic as it may seem, as audit firms have incentives to secure that they deliver audits with the desired level of quality. For instance, auditors in the same firm have access to consult accounting experts employed in the firmôs accounting department when solving difficult accounting issues, and administrative mechanisms are in place to secure audit quality.

auditorsô combined use of the contending and the conceding negotiation strategy. Based on these arguments, I suggest the following hypothesis (in alternative form):

H_4: When negotiating difficult accounting issues, auditors who audit clients with higher levels of technical accounting knowledge are more likely to use an overall negotiation strategy that is less contending than the overall negotiation strategy used by auditors who audit clients with lower levels of technical accounting knowledge.

3.3.4. Auditorsô combined use of the contending and the conceding negotiation strategy

As pointed out previously, auditors are likely to choose the negotiation strategies that they think will contribute to the preferred outcome. It should be noted that the accounting outcome is not the only important outcome resulting from a negotiation; other outcomes can also be important for the negotiation parties such as how easily the resolution was found and what impact the negotiation has on the relationship between the auditor and the client. In this thesis, no other negotiation outcomes than the accounting outcome are investigated.

Prior research indicates that auditors who use more contending tactics obtain more conservative accounting outcomes than auditors who use more compromising or concessionary tactics (e.g. Brown and Johnstone 2009). As auditors normally have incentives to support more conservative solutions than what the clients do (Bame-Aldred and Kida 2007), it is likely that when auditors use much of the contending strategy and little or nothing of the conceding strategy, the accounting outcome will either be the one the auditor requires or the parties will not come to an agreement resulting in a modified audit opinion. When auditors use little of the contending strategy and much of the conceding strategy, the accounting outcome is likely to be either a compromise or the solution suggested by the client.

Based on the arguments above, I hypothesize that (in alternative form):

H_5: The more auditors use an overall contending negotiation strategy, the more likely is a solution that equals the solution initially preferred by the auditor.

3.4. A model that predicts accounting outcomes in auditor-client negotiations over accounting issues

In this section I discuss how the model in Figure 4 can be used to predict the accounting outcomes that result from auditor-client negotiations. The model will be tested in section 5.7.

Prior research has shown that a large number of independent variables seem to have an impact on the accounting outcome in situations of auditor-client conflict over accounting issues, (see section 2.4.6.2), but because none of the studies are based on data from real conflicts, we know little about which of these variables have a large vs. a small effect and the test of the model will be exploratory in its approach and aim to find which variables are the most important ones. As pointed out previously, the left-hand-side variables that are included in Figure 4 are the variables that the respondents in the Gibbins et al. 2001 and 2007 studies indicate are the most important context variables in auditor-client negotiations over accounting issues.

Based on the expected relationship between auditorsô use of negotiation strategy and the accounting outcome (see section 3.3.4), this variable is included in the model. This variable will capture some of the effect of the independent variables previously studied in this thesis: accounting regulation, auditor-client relationship, audit partnerôs general experience and client accounting expertise.

Based on prior findings (see section 2.4.6.2), precision of the accounting regulation of the accounting issue is expected to be a very important variable when making such predictions, and it is likely that there will also be a direct effect of this variable and not only the effect that is captured by the negotiation strategy variable. In addition, it is likely that when the parties have been negotiating for some time and the auditor has to make a final *decision* about what accounting solution he is willing to accept, whether the negotiated issue is a precisely regulated issue will play an important role in the auditorôs decision model. Consequently, the precision of accounting regulation is included as a second independent variable.

As Gibbins et al. (2001 and 2007) find that the other independent variables that are tested in hypotheses 2, 3 and 4 are the most important variables in auditor-client negotiations over accounting issues, these variables will also be included in the model even though the effect of these variables is likely to be at least partly captured by the negotiation strategy variable.

4.0. METHODOLOGY

4.1. Introduction

The objective in this chapter is to present and discuss a research design that is appropriate when the goal is to test the hypotheses that are developed in chapter 3, to explore whether my research model (see Figure 4) can be used to predict accounting outcomes in auditor-client negotiations, and to investigate the relative importance of these contextual variables. In section 4.2 I present my choice of using a cross-sectional design and discuss the implication of this choice for the understanding of the hypotheses in chapter 3. In section 4.3 I provide detailed information about the research method on the issues of data collection, research instrument, and sample size. In section 4.4 I discuss the operationalization and measurement of the independent and dependent variables in my research model (see Figure 4), as well as the control variables that are included in the study. In section 4.5 I present the studyøs limitations.

4.2. Research design

Despite the fact that the theoretical research model, as specified in Figure 4, is a causal model, I have chosen to investigate the research questions in a non-experimental (cross-sectional) study. The reasons behind the choice are several. Pruitt et al. (1993, p. 11), emphasize that laboratory research (experimental) in the study of negotiation practices has two main shortcomings: First, ñit does not reveal the relative importance of different variables as they influence negotiationò and second, ñthere are often difficulties in generalizing results from laboratory settings to natural settingsò. Pruitt et al. (1993, p. 11) then suggest parallel research in laboratory and natural settings in which ñthe natural research establishes the relevance of these mechanisms to real-life negotiationò.

My choice of research design is related to these major shortcomings: First, prior experimental studies in auditor-client negotiations focus on only one or two such contextual variables at a time and are consequently not able to say anything about the relative importance of the variables that have an impact in auditor-client negotiations. As one of the aims with my study is to study this relative importance, a non-experimental design is preferable.

Second, we know from prior research in auditor-client conflicts that auditors are affected by client pressure when making accounting choices (see section 2.4.6.2). But as all prior deductive audit negotiation studies are conducted in the laboratory, the real client pressure is not present in these studies. With a non-experimental (cross-sectional) design I have the opportunity to study negotiations in a setting where the client pressure is present and focus on ñhow auditors believe that they behavedò in a recently experienced negotiation over difficult accounting issues instead of studying ñhow auditors believe they will behaveò when they participate in auditor-client negotiations over accounting issues.

Finally, we see that prior studies of auditor-client negotiations mainly investigate a small number of types of negotiations (see section 2.4.3 for an overview). Compared to an experimental study, a cross-sectional study has the potential to result in a sample that includes many different types of auditor-client negotiation and can as a consequence shed light on which types of accounting issues are negotiated. As a cross-sectional study is likely to include types of negotiations that have not yet been investigated, it can also contribute to the generalizability of prior findings.

Compared to an experimental or quasi-experimental design (see for instance Pedhazur and Schmelkin 1991 or Shadish, Cook and Campbell 2002), a non-experimental design includes neither manipulation of the independent variables nor randomization. As the design makes it difficult to control for the effects of confounding variables, it follows that a non-experimental design makes it difficult to make causal claims.

I therefore emphasize that the hypotheses in chapter 3 should be understood as relational hypotheses. Whereas relational hypotheses often use constructions such as ñx is associated with yò, see for instance Joe et al. 2011, the ñmore likelyò construction that I have chosen is used in prior cross-sectional research in auditing (see for instance Wright and Wright 1997) but also in experimental studies (see Braun 2001). In my thesis, the ñmore likelyò hypothesis has an advantage over an ñassociated withò hypothesis in that it does not only hypothesize a relation between two variables so that for instance ñhigh x is associated with low yò but hypothesize that "the higher scores of x, the higher scores of y" without the latter construction saying or intending to say anything about x causing y.

4.3. Research method

4.3.1. Data collection and respondents

To investigate the proposed research questions, data from auditor-client negotiations are needed. As no secondary data exist on the variables I need to measure, and I have chosen not to use an experimental design, data can be collected either by the use of structured interviews or a structured questionnaire. A relatively large sample will be necessary to test the hypotheses; therefore I have chosen to use a structured questionnaire.

Prior research in auditor-client negotiations normally includes both audit managers and partners as experimental participants.[29] Findings in previous research on whether managers can be used instead of partners in this type of research are mixed (Brown and Johnstone 2009 and McCracken et al. 2011). As one of the aims of my study is to investigate a potential behavioral difference between auditors with little and those with much partner experience, I include only audit partners in my study.

To obtain a broad sample of data from auditor-client negotiations, all engagement partners in one of the Big 4 audit firms were given a detailed questionnaire to collect information about one or several auditor-client negotiations conducted during the previous year's audits. Two reasons lie behind the decision to study a sample from only one audit firm: access to data from one firm is easier to obtain and collecting data from only one firm may make it easier to obtain "richer" data with better quality and a sufficiently large sample. Differences in auditor negotiation behavior based on audit firm affiliation are thought not to exist, but as audit firm cultures may differ and may have an impact on negotiation behavior, including data from only one firm controls for possible differences.[30]

[29] Gibbins et al. (2010) is the only prior study that only includes partners, see Table 3. Two studies (Brown and Johnstone 2009 and McCracken et al. 2011) compare the behavior of managers and partners.

[30] Knowledge about differences among the big audit firms is sparse; but degree of variables such as industry specialization and business risk methodology adoption may differ from one Big 4 firm to another, and these variables are found to have an impact on audit quality (Bruynseels et al. 2011). Research in audit quality

In June 2009, each partner in the participating audit firm received three questionnaires[31] and was asked to identify the three largest clients with the largest audit fees with whom they had disagreed about an accounting procedure (disagreements about amounts and principles but not disclosure) during the 2008-audit.[32] If they did not experience such disagreements with as many as three clients in 2008, the auditors were asked to fill in the questionnaires based on the disagreements they experienced. If no disagreement was experienced in 2008, the auditors were asked to fill in the questionnaire based on disagreements in 2007, if possible. (See Appendix 2 for a copy of the questions that were included in the questionnaire for use in this study). Each partner then received a slightly less voluminous questionnaire in May 2010 during a second round of data collection where some of the questions that were not intended for this thesis were omitted and were asked to fill in the questionnaire for one or two of their clients.

To obtain a good response rate in both rounds of data collection, the head of assurance in the participating firm enclosed a cover letter with the questionnaires in which he emphasized the importance of responding for the participating firm. The audit firm also sent out two reminders to partners who did not respond.

Out of 130 contacted partners, 42 partners responded in one or both rounds of data collection.[33] One of these 42 partners responded with an empty questionnaire. 41 partners responded with one to five questionnaires. Two of the questionnaires could not be used in the final analysis (see section 4.3.3), leaving a total of 39 partners responding with 79 cases.[34]

normally assumes homogenous audit quality among ñBig nò audit firms. Quality differences are found when comparing big audit firms to small audit firms (e.g. Blokdijk et al. 2006).

31 To limit recall problems, data collection in May and June was found preferable. Additionally, auditors are normally not as busy during these months as in other times of the year.

32 This way of constructing the sample potentially introduces a self-selection bias in the sample as the participants may choose to omit reporting about disagreements they feel they did not handle properly. This bias is not expected to be problematic for the testing of the hypotheses in the study.

33 Two of the partners are not formally partners but are permitted to sign audit opinions. The questionnaires from these auditors are included in the sample.

34

Number of questionnaires per responding partner	
Questionnaire returned empty	1
Non-usable response	2
1 case	19
2 cases	7
3 cases	9
4 cases	1
5 cases	3
	42

Nineteen of the partners responded with one questionnaire. Twenty of the partners responded with more than one questionnaire, three of these responded with one questionnaire in the first collection round and one in the second round.

4.3.2. Research instrument

The questionnaire builds on research instruments developed in Gibbins et al. (2001 and 2007) and Gibbins et al. (2010). In order to test the proposed research questions, several methodological requirements must be fulfilled. First, I need variation in the independent and dependent variables. To investigate whether the questionnaire could be expected to provide this needed variation, pilot testing of the instrument was undertaken. At the same time, I also want to restrict variation in other possible explanatory variables or facilitate the possibility to control for the effect of these variables. A number of questions were included in the questionnaire to measure these possible confounding factors. Restricting the effect of possible confounding factors is also done by including only partners and only auditors from one firm.

The questionnaire was initially pre-tested on one partner in the participating audit firm. The partner filled in the first version of the questionnaire and was then interviewed about his experiences with the questionnaire. A second version of the questionnaire was then tested on four other respondents: one partner and one director in the participating audit firm, one partner in another big-four audit firm and one CPA not currently working as an auditor. Feedback was given on clarity as well as on the meaning/understanding of the questions in the questionnaire. Based on this pilot-testing the final version of the questionnaire was completed.

The questionnaire consists of six parts; the participants first answer questions about the disagreement they experienced. In the second part they respond to their agreement with different assertions about their negotiation behavior. The respondents then answer questions about outcomes of the negotiations and give information about the client, the audit and themselves.

Partners contacted in 2009	125
Partners without audit clients	5
Additional partners contacts in 2010	10
	130

To ensure correct and truthful responses, several precautions were taken. The participating partners had the possibility to answer anonymously (instructions were given to put each questionnaire in a sealed envelope when finished). The questionnaire was written in English and translated into Norwegian, developed in collaboration with the audit firm and guidance was included where necessary.[35]

4.3.3. Sample

The data collection resulted in a sample of 81 negotiations. In one of the cases, the description of the disagreement reveals that the case is not a negotiation-case but an uncertainty-case. One of the partners forgot to answer the questions related to the statements on use of negotiation strategy. This left a usable sample of 79 negotiations. Information on demographics and sample characteristics is given in section 5.2.

[35] Even though the respondents are fluent in English, they were more likely to respond more quickly and precisely if they replied in Norwegian (based on feed-back from the audit firm in the first round of pilot-testing). Consequently, all respondents received the questionnaire in Norwegian (including the final pilot testing).

4.4. Operational definitions and measurement

In this section I discuss the operationalization and the measurement of the concepts that are necessary to test the hypotheses and the model that are developed in chapter 3. In section 4.4.1 I present and discuss how I operationalize the negotiation concept itself and present the relevant level of analysis for the analyses in chapter 5. To be able to test the hypotheses and use my research model, I need to operationalize the theoretical construct that an overall strategy is more or less contending. This issue is presented in section 4.4.2. Operationalization and measurement of the dependent and the independent variables is then presented respectively in section 4.4.3 and 4.4.4. In section 4.4.5 I use the knowledge obtained in the literature review in chapter 2 to discuss which control variables must be included in the model that is used to test the hypotheses and in the model that will be used to predict accounting outcomes in auditor-client negotiations.

4.4.1. Auditor-client negotiations over accounting issues

Prior research (e.g. Beattie et al. 2000 and Gibbins et al. 2001) that investigate auditor-client disagreements over accounting issues build on different negotiation definitions. Gibbins et al. (2001) use the definition of Murnighan and Bazerman (1990) in which negotiations are broadly defined as ñany context in which two or more parties with differing preferences jointly make decisions that affect the welfare of both (all) partiesò (Murnighan and Bazerman, 1990, p. 642). Beattie et al. (2000) build on Gulliver (1979) who defines negotiations as ñprocesses of interaction between disputing parties whereby, without compulsion by a third-party adjudicator, they endeavor to come to an interdependent, joint decision concerning the terms of agreement on the issues between themò.

In order to study negotiations, it must be understood how to distinguish between negotiations and discussions. Gibbins et al. (2001) clarify this distinction by presenting an operational definition that only includes as negotiations *disagreements* between clients and auditors.

Gibbins et al. (2001, p. 543) operationalize the definition of negotiation, providing the following example in their questionnaire: ñL.H. from public accounting firm W&W, is on the way to a meeting with audit client RT Inc., to discuss an accounting issue that has arisen. The meeting is being held because the auditor and the client have different views about how to handle the issue in RT´s financial statements and disclosures. L. H. has considered the process to be a negotiation, including the upcoming meeting.ò After reading this example, the participating auditors are required to choose their own negotiation example and use it when answering the questions.

In the introduction to their research instrument, Beattie et al. (2000) operationalize the concepts discussion and negotiation with the following paragraphs (page 181): ñThe process which each year culminates in the production of financial statements which are contained in a company´s annual report is described as a ñprocess of negotiationò between the auditor and the company. Discussion on various issues takes place and may lead to negotiation. This is a continuing process which includes issues identified and discussed prior to the commencement of the final audit and is not restricted to the year-end audit. We define ñdiscussionò and ñnegotiationò as follows: Discussion: matters are raised by one side or the other (or both) and are considered in speech or writing. Negotiation: in the process of reconciling conflicting views advanced in discussion, by concessions on one or both sides.ò

Gibbins et al. (2007) study auditor-client negotiations as experienced by CFOs without using the word ñnegotiationò because CFOs may view this term pejoratively. Instead they ask for ñcases where difficult accounting measurement, valuation and/or disclosure issues arise. ñDifficultò here means that there was an *initial difference of opinion* between you and your staff and your external auditors about the appropriate accounting and/or disclosure.ò

As interviews with Norwegian auditors suggested that they also view the term ñnegotiationò pejoratively, I did not use the word ñnegotiationò in my questionnaire but asked for ñinitial *disagreements* about difficult accounting issuesò.

To ensure that the respondents give information about negotiations that have taken place, the following paragraph was included in the introduction to the questionnaire:

> This research project is related to audits in which difficult accounting measurement or valuation issues with a potentially material impact to the financial statements arose. ñDifficultò means that there was an initial difference of opinion between you and your client about the appropriate accounting. Most studies in this area are made on experimental data and studies on real data will

> therefore contribute to our understanding of the judgments auditors really make.

When analyzing the data collected in chapter 5, the unit of analysis of these data will be one accounting issue that is negotiated and not for instance the client level. As a consequence it is important that all answers in the questionnaire can be used at the accounting issue level. We know that auditors may negotiate several accounting issues with a client at a time. To make sure that all answer in the questionnaire pertains to the same issue, the following paragraph was included in the questionnaire: ñIf you experienced more than one difficult accounting issue with any of the identified clients, please answer the questionnaire with the issue that potentially could have the largest monetary impact for the financial statements in mind.ò

4.4.2. Strategies and tactics

4.4.2.1 Introduction

Measurement in previous studies on negotiatorôs use of strategies and tactics

Kipnis and Schmidt (1980) suggest seven influence tactics: reason, coalition, ingratiation, bargaining, assertiveness, higher authority and sanctions that can be used in a negotiation. Beattie et al. (2004) use these categories in their study and find that each of these tactics is used to a varying degree in different auditor-client negotiations by auditors and clients. The following operationalizations are listed in the Beattie et al. (2004) article: state positions firmly at the outset (assertiveness), threaten to involve additional parties (sanctions), threaten to qualify the auditorôs report (sanctions), use evidence to support argument (reason), use reasoned argument (reason), take blame (ingratiation), willingness to bargain and a give and take strategy (bargaining), get support from third party (coalesce), seek confirmation and authority for position (higher authority) and apply conditions to acceptance (conditions). We see that all the above-mentioned tactics except for the ingratiation and bargaining tactics fit into the Pruitt and Carnevaleôs (1993) definition of a contending tactic.

Rahim (1993) develops an instrument to measure negotiatorsô conflict management style. This instrument has been validated and used extensively. Conflict management style is defined as the general approach or mindset individuals use to resolve disputes (Rahim 1992 and 2000).

Goodwin (2002) builds on Rahim (1993) and measures auditorsô conflict management style with an instrument consisting of 28 statements to measure the five styles in Rahim (1993): avoiding, obliging, compromising, integrating and dominating (see section 2.4.4 for a presentation of these styles). Auditorsô agreement with the statements is measured on a seven-point scale from 1 (strongly disagree) to 7 (strongly agree).

Gibbins et al. (2010) develop a research-instrument based on Rahim (1993) to measure auditorœs use of different negotiation strategies and tactics. The instrument consists of 25 statements, each representing different tactics and strategies. The instrument is intended to measure the use of contending, conceding, compromising, problem solving and expanding the agenda negotiation strategies. The auditorsô likelihood of using the tactics and strategies listed in the instrument is measured on an eight-point scale from 0 (very unlikely) to 7 (very likely). To validate the instrument, 183 accounting students participated in an experiment and a confirmatory factor analysis was run to ensure that the items loaded as intended.

<u>Measurement and operational definitions in this study:</u>

In order to test the relationships as specified in the research model, I need to measure whether an overall negotiation strategy is more or less contending. As I want to measure the overall strategy and the use of the conceding strategy is likely to weaken the effect of the contending strategy, the measurement must include the use of both the contending and the conceding negotiation strategies. This combined measure will mean the following: if two auditors respond that they use the same ñamountò of the contending strategy (e.g. get the same score on a measurement scale), the one who responds by using the least amount of the conceding strategy in sum uses a strategy that is more contending than the strategy used by the other auditor.

Consequently I first need to measure auditorsô use of the contending negotiation strategy and the conceding negotiation strategy, so I use the instrument that was used by Gibbins et al. (2010) with some changes to measure the use of these strategies. Minor changes in wording are made as Gibbins et al. (2010) study the behavior the auditors think they will have in a possible negotiation whereas I study the behavior the auditors think they had in a negotiation that had already taken place. I also made some changes to item 3 so that it better represents one of the facets of the concept the item seeks to measure (in our version of this item the auditor threatens the client). The statements measure the participantsô subjective understanding of what they did.[36]

The respondents are asked to rate their agreement with 20 statements (10 of which relates to the use of the contending and the conceding negotiation strategy) on an eight-point scale from 0 (no agreement with statement) to 7 (very high agreement with statement). The statements measure the auditorôs use of the contending, the conceding, the problem solving and the compromising strategy and are presented in a random order, (the same order is used in all the questionnaires), see Appendix 1 for the complete questionnaire. The latter two strategies are not studied in my thesis, but the statements trying to measure their use are included make it easier for the respondents to use the measurement scale and to help the respondents think about their use of the contending and the conceding strategy in relation to their own use of other possible strategies. The scale is slightly modified from the Gibbins et al. (2010) who use an eight-point scale from 0 (very unlikely to use) to 7 (very likely to use). The change reflects the fact that the auditors in my study have completed the negotiation, and it gives a possible response (0) if the tactic was not used during the negotiation.

Alternatively, the use of the two strategies could have been measured with two single variables rather than using composite measures. A composite measurement has several advantages because the inclusion of several facets of the underlying concepts gives a more well-rounded perspective and allows the use of an average / typical response (Hair et al. 1998, p. 10). It also provides more knowledge on what the auditors actually do when negotiating, and it is likely to encourage more truthful responses as the researcherôs intentions with the questions are not as easy to discern by means of a several-statement approach compared to a single-question approach. (Auditors may be reluctant to admit using compromising and

[36] Subjective measures relate to how a phenomenon is perceived by a subject (here the respondent) and it thus relates to his/hers reality construction influencing beliefs and actions.

concessionary behavior.) It should be noted that using an un-weighted additive scale implies that all statements are equally important (i.e. answering ñvery highò on two statements have the same effect on the measuring of the underlying concept) and that moderate use of two statements has the same effect on the measure as high use of one of the statements and no use of the other statement.

See Table 5 for a listing of the 10 statements that are included in the questionnaire to measure the conceding and the contending strategy. To ensure that the respondents read the statements carefully even though they may look similar and that respondents do not get bored when giving their ratings, the following paragraph was included in the questionnaire: ñThe study has a particular focus on what auditors do when they experience such difficult accounting issues. To successfully be able to analyze this, a number of questions are included in part B which at first sight may seem very similar. This is a consequence of the research design used in the project, and as a consequence it is important that you read all questions and statements carefully.ò

Table 5 - Statements used to measure the contending and the conceding negotiation strategy

CONTEND

s3: To obtain a resolution in my favor, I told the client that I would use my ability to qualify the financial statements if he did not change his accounting.

s4: I argued with the client to show them the merits of my position.

s6: I used my influence as auditor to get my position accepted by the client.

s9: I used my expertise in accounting to influence the resolution in my favor.

s17: I was firm in pursuing my position.

CONCEDE

s1: I tried to satisfy the expectations of the client.

s7: I attempted to accommodate the wishes of the client.

s12: I tried to satisfy the needs of the client.

s13: I made concessions from my position to the client.

s18: I gave in to the wishes of the client.

Item 3, 4, 6 and 9 are statements about different types of contending behavior (different tactics) that the auditor may use when he negotiates with clients and the list includes different types of persuasive behavior that the auditor may use. Item 3, 4 and 9 describe the use of threatening behavior, the use of arguments and expertise. Item 6 and 17 are more general statements describing contending behavior.[37]

Item 1, 7, 12, 13 and 18 are statements about different aspects of conceding behavior.

Descriptive statistics strategy statements

Descriptive statistics for the 10 statements used to measure the auditorôs use of the contending and the conceding negotiation strategy are presented in Table 6 below.

Table 6 - Descriptive statistics for the statements describing conceding and contending behavior

CONCEDING	**s1**	**s7**	**s12**	**s13**	**s18**
N	79	79	78	78	78
Mean	3.37	2.43	3.46	1.73	1.23
Std. Error of Mean	.212	.198	.224	.178	.165
Std. Deviation	1.882	1.759	1.978	1.568	1.459
Skewness	-.208	.387	-.256	.689	1.699
Std. Error of Skewness	.271	.271	.272	.272	.272
Kurtosis	-.987	-.659	-1.020	-.550	2.951
Std. Error of Kurtosis	.535	.535	.538	.538	.538
Minimum	0	0	0	0	0
Maximum	6	6	7	5	7

[37] To make sure that there is an even clearer distinction between how the process and the outcome is measured, future research should consider including a ñto try toò in all the statements. Statement 3 would then read: ñTo try to obtain a resolution in my favor, I told the client that I would use my ability to qualify the financial statements if he did not change his accountingò.

CONTENDING	s3	s4	s6	s9	s17
N	79	79	79	79	79
Mean	2.82	4.76	4.51	5.29	4.72
Std. Error of Mean	.307	.228	.250	.192	.254
Std. Deviation	2.726	2.027	2.218	1.711	2.259
Skewness	.351	-1.312	-.913	-1.587	-1.144
Std. Error of Skewness	.271	.271	.271	.271	.271
Kurtosis	-1.505	.910	-.292	2.263	.190
Std. Error of Kurtosis	.535	.535	.535	.535	.535
Minimum	0	0	0	0	0
Maximum	7	7	7	7	7

We see from the Table 6 above that one of the contending tactics is used less often than the others (statement 3 which measures the use of a ñthreat to qualify the opinionò), which may signal that this is a behavior which is only used when necessary. This explanation is supported by the finding that this behavior is not used at all in 33.3% of the negotiations (see Appendix 2 for frequency tables for all statements).

We also see that statement 9 represents the behavior that is used the most (s9 measures auditorsô use of their accounting expertise). The frequency tables shows us that 81% of the auditors agreed with this statement from a ñmoderate to highò, ñhighò or ñvery highò degree.

4.4.2.2. Exploratory factor analysis

As the instrument has not been used extensively in accounting settings and as it has to my knowledge not been used in a Norwegian setting, I use factor analysis to validate the strategy-measures. Following Hair et al. (1998, p. 98), factor analysis is applicable if the sample size is larger than 50 (preferably the sample size should be larger than 100) and the number of observations per variable to be analyzed is larger than 5 (preferably larger). According to Field (2009), the variables included should be approximately normally distributed but this assumption is mainly important if the factor analysis is conducted to generalize findings beyond the sample collected.

Dimensionality of constructs

Two factor analyses are first run on the items that intend to measure each different negotiation strategy (79 questionnaires included) to investigate the dimensionality of the two scales.

Contending scale items

The 5 items of the contending scale are subjected to principal components analysis (PCA). As the correlation matrix reveals that most of the coefficients are 0.3 and above, the KMO-value is 0.652 and Bartlettős Test of Sphericity is statistically significant, the data are suitable for factor analysis.

The factor analysis suggests a one-factor solution (based on eigenvalues larger than 1) with an explanation of 53.4% of the total variance. One factor is further supported by the underlying theory.

The factor loadings and the communalities are given in Table 7 below.

Table 7 - Component analysis for PCA of contending scale items

Item	Component 1	Communalities
s6 (Use influence as auditor)	.899	.808
s9 (Use expertise as in accounting)	.741	.549
s4 (Argue with client)	.710	.504
s17 (Stay firm)	.652	.425
s3 (Threaten to qualify)	.618	.381

Conceding scale items

The 5 items of the conceding scale are then subjected to principal components analysis (PCA). As the correlation matrix reveals that many of the coefficients are 0.3 and above, the KMO-value is 0.695 and Bartlett's Test of Sphericity is statistically significant, the data are suitable for factor analysis.

The factor analysis suggests a two- factor solution (based on eigenvalues larger than 1) with the factors explaining 49.9% and 24.7% of the variance respectively. The two-factor solution explains 74.6% of the total variance. The scree-plot, see Figure 6, indicates a possible break after the second factor.

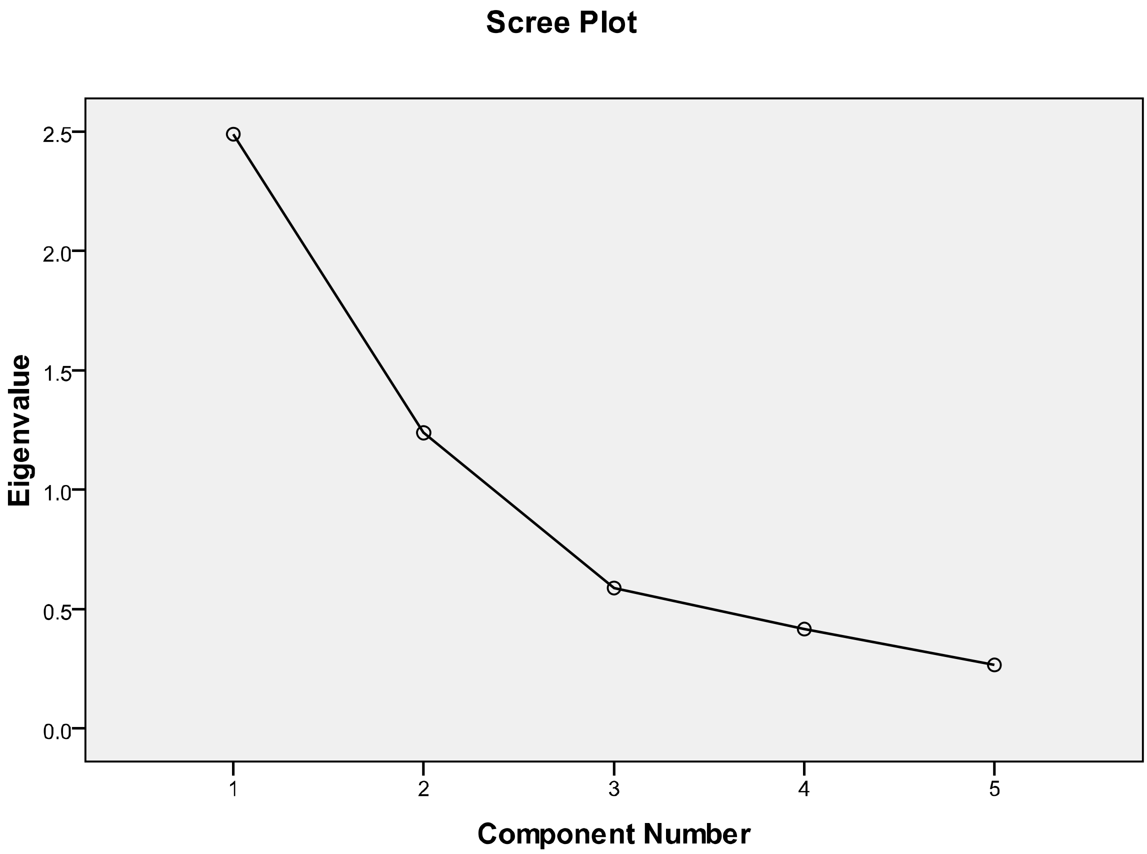


Figure 6 - Scree plot conceding strategy items

To better interpret the two components, oblimin rotation was performed. The results of the rotation show that the items load strongly on the two components (see Table 8 below).

Table 8 - Structure Matrix for PCA with Oblimin Rotation of Two Factor Solution of Conceding Strategy Items

Item	Structure coefficients		Communalities
	Component 1	Component 2	
s1 (Satisfy client expectations)	.893	.156	.802
s12 (Satisfy client needs)	.887	.235	.787
s7 (Accommodate client wishes)	.819	.242	.672
s18 (Gave in for wishes)	.098	.870	.769
s13 (Made concessions)	.349	.821	.699

A closer study of the items reveals that they are of two types; the first type consists of items that focus on trying to ñpleaseò the client if possible (item 1, 7 and 12) and these items are likely to be understood as ñpositiveò by the auditor. The second type (item 13 and 18) consists of items that verbally focus on the compromising part of conceding behavior. These items are likely to be understood less positively by the auditors due to the independence requirements inherent in auditing. As items 1, 7 and 12 measure the extent to which the auditor tried to satisfy the clientôs needs, expectations and wishes, there seems to be a good correspondence between what these items measure and the ñconcern for otherò dimension in the Thomasô model (1976), and items 13 and 18 are removed from the scale.[38] It should be noted that in principle, these changes will impede the comparability of findings with previous research findings using these scale items. In practice this is a relatively small problem as only Gibbins et al. (2010) use these items to measure auditorsô choice of negotiation strategy.

[38] Question 13 and 18 seem to be susceptible to a response bias, i.e. the respondents have responded using the answer that they think is òcorrectò instead of answering how they really behaved in the negotiation. We see in Appendix 2 that few of the respondents ñadmitò to have behaved as indicated in statements 13 and 18 and the Spearmanôs rank order correlation coefficient between statements 13 and 18 and the accounting outcome of the negotiation solution is very low (r=0.057 and r=-0.003, respectively).

It is arguable that leaving out items 13 and 18 moves the measurement from measuring what the auditor did to measuring the auditorôs intention (to what extent did the auditor want to win the negotiation) or goal commitment (the latter term is used in Kadous et al. (2003) as a measure of motivation and is measured with 5 statements on a five-point Likert scale). But as pointed out previously (see section 2.4.4), the two dimensions of the Thomasô (1976) model also reflect the motivational orientation of the negotiator. Consequently we see this issue more as a question of terminology than of substance, and we will continue to use the term strategy in this thesis.

Factor analysis (8 items)

To make sure the remaining 8 items that measure the contending and the conceding scale items load as intended on the two factors so that these two scales can be used, the 8 items were subjected to PCA. As the correlation matrix reveals many coefficients of 0.3 and above, the KMO-value is 0.668 and Bartlett's Test of Sphericity is statistically significant, the data are suitable for factor analysis.

The factor analysis suggests a two- factor solution (based on eigenvalues larger than 1) with the factors explaining 34.0% and 30.6% of the variance respectively. The two-factor solution explains 64.5% of the total variance. Inspection of the scree-plot, see Figure 7, indicates a clear break after the second factor. Two factors are further supported by the underlying theory.

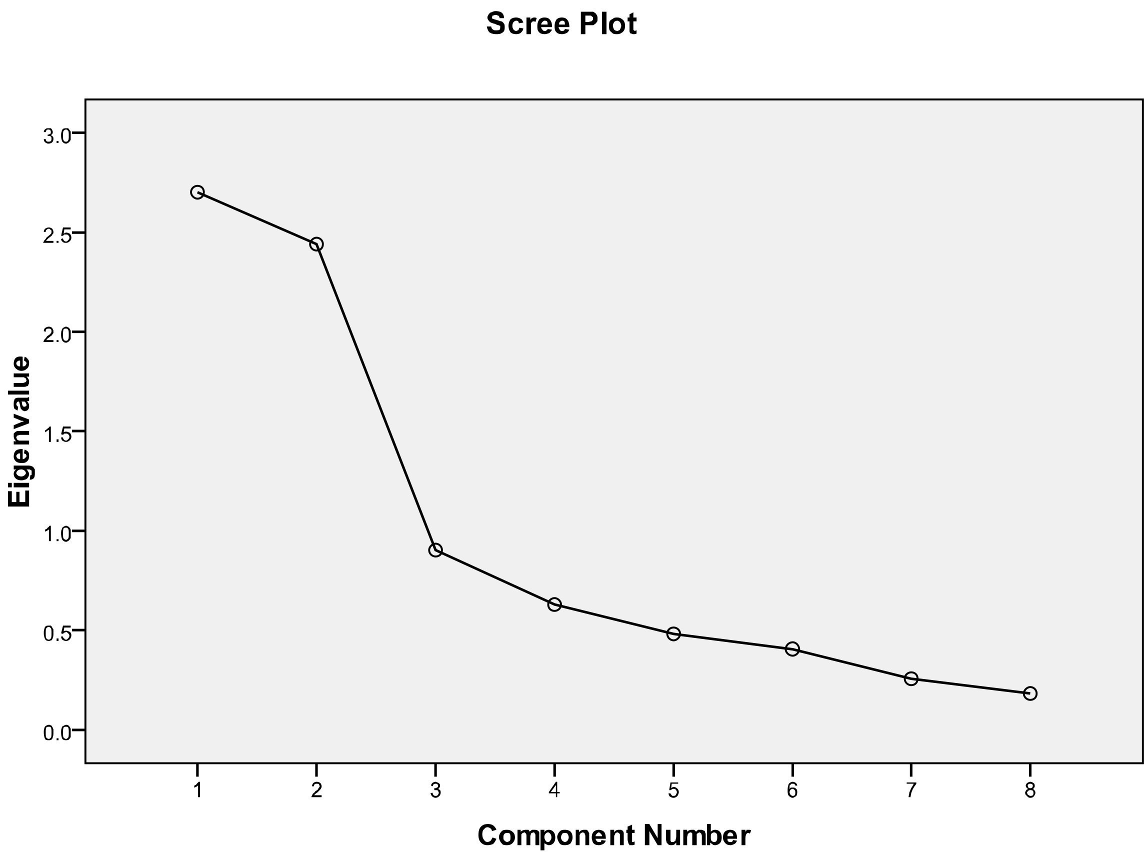


Figure 7 - Scree plot contending and conceding items

To better interpret the two components, oblimin rotation was performed. The results of the rotation show that the items load strongly on the two components. One of the items (s4) loads on more than one factor with a larger loading than 0.3 on both factors, see Table 9 below. As this item loads the most on the factor it is supposed to load on and as it reflects an important facet of the contending scale, this item is kept in calculating the contending scale.

Table 9 - Pattern and Structure Matrix for PCA with Oblimin Rotation of Two Factor Solution of Negotiation Strategy Items

Item	Structure coefficients		Communalities
	Component 1	Component 2	
s6 (Use influence as auditor)	**.891**	.102	.815
s9 (Use expertise as in accounting)	**.744**	-.106	.558
s4 (Argue with client)	**.689**	.400	.665
s17 (Stay firm)	**.667**	-.272	.502
s3 (Threaten to qualify)	**.639**	-.161	.425
s12 (Satisfy client needs)	.023	**.875**	.769
s1 (Satisfy client expectations)	-.129	**.869**	.762
s7 (Accommodate client wishes)	-.126	**.811**	.665

Note. Major loadings for each item are given in bold

The interpretation of the two components is consistent with the theoretical foundations as the contending items load strongly on component 1 and the conceding items load strongly on component 2. The results further support the use of two separate scales as suggested by previous research.

Scale reliability:

The contending scale has good internal consistency with a Cronbachôs alpha of 0.764. Removal of any of the items will not improve the scale. It follows from the factor analysis above that item 4 also loads on the conceding scale, but as Cronbachôs alpha for the contending scale is slightly higher with this item included, item 4 will not be removed from the scale.

The conceding scale also has good internal consistency with a Cronbachôs alpha of 0.833. It will improve slightly to 0.843 with exclusion of item 7. As two items have already been removed from the conceding scale, item 7 will be kept when calculating the conceding scale.
To summarize: we have the following items that will be used when calculating the two scales:

Factor 1 (contend) = item no. 3, 4, 6, 9 and 17
Factor 2 (concede) = item no. 1, 7 and 12

4.4.2.3. Use of the two scales to test the hypotheses

To construct the measure ñmore contendingò, I first measure each respondentôs score on the contending scale (I add the score on each of the five "contending" statements and divide by five) and then on the conceding scale (I add the score on the three conceding statements and divide by three). I then subtract the score on the conceding scale from the contending scale. The resulting scale gives each of the respondents a score from -7 to +7.

The plot below, (see Figure 8), illustrates the scores of the respondents on the contending scale on the x-axes and the scores of the respondents on the conceding scale on the y-axes so that each circle in the diagram represents the scores of one respondent (one negotiated accounting issue). We see that some respondents are high on both axes, some are high on one of the axes and low on the other and a few are low on both axes.

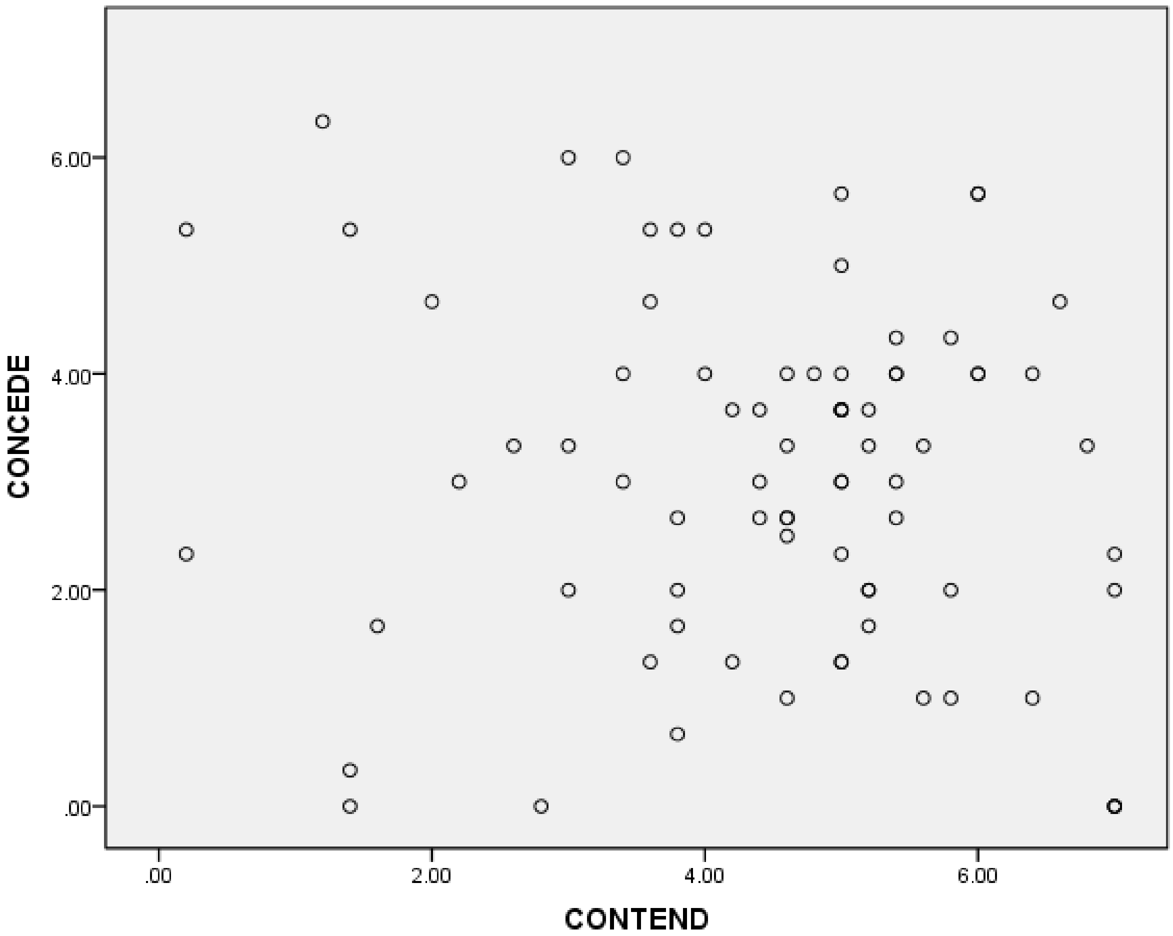


Figure 8 - The respondents combined use of the contending and conceding negotiation strategies

The plot supports the idea that the strategies are used in combination. We see from Figure 8 that the majority of the respondents score relatively high on the contending scale so that the use of the conceding strategy seems to be what really differs among the respondents. Nevertheless there are also respondents who are relatively low on the contending scale.

The respondents who are relatively low on both measures may differ considerably from the respondents who are relatively high on both measures, but the difference may also only reflect that these respondents use the scale differently than other respondents. Additionally, because what I am studying is whether the respondents believe they use more of the contending strategy than the conceding strategy and vice versa, the low-low cases are in themselves as interesting as the high-high cases as long as they reflect how auditors conduct auditor-client negotiations over accounting issues.

To investigate whether there are reasons to exclude these low-low cases from the study, I carefully read through all the cases that have a score of three or lower on both strategies to look for anomalies.[39] The cases can be divided into two groups; the first group consists of respondents who answer that they use little of the two strategies and much of other strategies. The second group uses few of all tactics and strategies. Apart from the low score on both axes, no other particularities were identified; consequently no cases are excluded from the following analysis. To make sure no problems are caused by this, the analyses will also be made with the low-low cases excluded as a sensitivity test.

The ñmore contending strategyò measure will be used to analyze a sample of 79 negotiations.

4.4.3. Outcome of auditor-client negotiations over accounting issues

The accounting outcome of the negotiation was measured approximately as in Gibbins et al. (2001) and the respondent was asked to ñIndicate the resolution of the issueò as:

- agreement on the clientôs initial position
- agreement on the auditorôs initial position
- somewhere between the suggested solutions
- a new solution

I gave the following example in my questionnaire so that the respondents should see the difference between a compromise and a new solution: ñA compromise and a new solution differ in that the latter is not a ñmeeting-on-a-halfway-solutionò. An example of a new solution is a disagreement where the auditor is of the opinion that an amount should be booked as a cost while the client thinks that no booking should be made. After a thorough

[39] The investigation revealed that one of the respondents (case no. 17) had forgotten to respond to one of the statements and as a consequence the scale was then computed as too low. To construct the score on the conceding scale for this respondent, the total score was divided by two instead of three. One of the respondents (case no. 201) answered 7 on one of the contending tactics (I was firm in pursuing my position) and not relevant on all the other contending tactics. He also responded ñnot relevantò on all the conceding statements. This type of response indicates that the respondent may have misunderstood the statements; it may be that his behavior *was* little contending (as the score on the scale indicates), or it may be that he has used other types of contending behavior that are not included in the questionnaire or that he did not need to use more than one tactic. In the latter case his average score does not represent his true behavior. Other answers in the questionnaire indicate that his behavior was very contending. As an average score will not reflect what this respondent really did, the average score is replaced with the score on the only tactic he used.

study of the relevant accounting rules, the auditor and the client agree that the amount should be accounted for directly against retained earnings.ò

A new solution is likely to have the properties of an integrative solution (higher collective utility for the negotiation parties) but as pointed out in chapter 2, it should be noted that integrative solutions are not always desirable in accounting. It should also be noted that there are some challenges related to the distinction between new solutions and compromises as it is likely that the distinction is more related to the type of issue that is negotiated than the negotiation itself (i.e. sometimes a new solution is possible but more often no possible new solution exists). From a theoretical point-of-view it is also a question whether the distinction is of any use: is there an interesting distinction between compromises and new solutions when what we strive to obtain is accounting that as good as possible reflects the underlying economic situation of a company and not a solution with higher collective utility for the negotiation parties? From the sake of comparability with prior studies, I use the same measurement categories as the ones used in Gibbins et al. 2001 and 2007.

As all the above-mentioned alternatives except for ñagreement on the auditorôs initial positionò entail that the auditor has changed his position, the binary variable that will be used when analyzing the sample is ñchange in auditorôs position versus no change in auditorôs positionò.[40] This variable is labeled SOLUTION in later analyses.

4.4.4. Independent variables

Accounting regulation is measured in relation to the specific accounting issue negotiated on a 5-point scale from ñvery low precisionò to ñvery high precisionò. Consequently I measure the respondentsô perception of the relevant accounting rules, i.e. their *subjective understanding* of the regulation.

The *clientôs accounting expertise* is measured on a 5-point scale from ñvery high technical accounting knowledgeò to ñvery low technical accounting knowledgeò. This measure is also subjective in that I measure the auditorôs judgment of the clientôs accounting competence.

[40] From time to time, the auditor and the client do not manage to come to an agreement and the consequence will be a modified audit opinion. As non-agreement cases may differ from agreement cases, separate analyses will be run on the agreement cases as sensitivity analyses.

The *auditor-client relationship* is measured on a 5-point scale from ñmuch better than other clientsò to ñmuch worse than other clientsò. By using a relative measurement to measure the quality of the auditor-client relationship, I hope to obtain a satisfactory variance in this measure. Like the two measures above, this measure is also subjective.

Partnerôs experience is measured two ways:

- years since inception of partnership
- numbers of negotiations experienced per year (measured with four categories[41])

As the first measure is more general than the second it has higher construct validity as the second measure only measures a specific part of an auditorsô partner experience. The second measure is included as Bame-Aldred and Kida (2007) and Brown and Johnstone (2009) find that general experience measures do not seem to have an impact in auditorsô decision-making in auditor-client negotiations.

As discussed in section 3.3.3.1, the two measures are not expected to be linearly related to the dependent variable since it is likely that a certain number of years of experience or a certain number of negotiations experienced yearly will be enough to obtain, for instance, the necessary negotiation expertise. The measures are therefore transformed into dichotomous measures with the use of independent samples t-tests.

An independent-samples t-test was conducted to compare the combined use of the contending and the conceding negotiation strategy for partners who have short or long partner experience. A median split shows that partners who have been partners for four years or more use a more contending negotiation strategy (mean=1.88, std. dev.=2.01, n=45) than partners who have been partners for less than four years (mean=0.70, std. dev.=2.94, n=30); $t=2.068$; $p<0.05$. Partners who have been partners for three years or more use a more contending negotiation strategy (mean=1.98, std. dev.=1.04, n=54) than partners who have been partners for less than three years (mean=-0.04, std. dev.=3.09, n=21); $t=2.787$, $p<0.05$. The last split is used to construct the binary variable AUDITOREXP; all partners who have one or two years of

[41] In the follow-up round in 2010, no categories were imposed on the respondents.

partner experience are placed in one group and the other partners are placed in a second group.[42]

An independent samples t-test was also conducted to compare the combined use of the contending and the conceding negotiation strategy for partners who experience few versus many difficult accounting issues per year. A median split shows that partners who experience three or more difficult accounting issues a year have a higher negotiation score (mean=1.76, std.dev.=1.81, n=39) than partners who experience less than three difficult accounting issues a year (mean=1.07, std.dev.=2.86, n=40) but the difference is statistically insignificant. The negotiation score was also compared for partners who experience more than two difficult accounting issues a year, and they have a higher negotiation score (mean=1.78, std.dev.=2.19, n=61) than partners who experience two difficult accounting issues or less a year; (mean=0.15, std.dev.=2.74, n=18); $t=2.613$, $p<0.05$. The last split is used to construct the binary variable EXPDIFFCASES; all partners who experience more than two difficult accounting issues per year are placed in one group and the rest of the partners are placed in another group.

4.4.5. Control variables[43]

As follows from the presentation in 2.4.6.4 (summarized in Table 4 and Figure 3), many variables are found to have an effect on the choice of negotiation strategy or the negotiated accounting outcome or both in previous auditor-client conflict. To control for the effect of these possible confounding factors when testing the research model as specified in Figure 4, I include the following variables in the models that are used in the forthcoming analyses:

- *client size* ï measured as a categorical variable (7 categories)
- *tenure* ï measured as the number of years the client has been audited by the audit firm
- *audit risk* ï measured on a 5 point scale from very low to very high

[42] Two auditors in the study are not formally partners, but as they have been working as auditors for many years they are included in the AUDITOREXP-variable together with partners with long experience. This inclusion has no significant effect on findings.
[43] See Figure 3 for an overview of variables for which it may be necessary to control.

To make sure that a number of relatively large clients are included in the study, the respondents are asked to

> Identify to yourself the three of your clients (for whom you are the engagement leader) which generate the largest audit fee and with whom you experienced one or more such difficult issues, as defined above, during the 2008-audit (exclude governmental clients and clients belonging to the banking and insurance industry). If you did not experience such difficult accounting issues with any of your clients in 2008 (or you experienced it with less than three clients), you may include audits from previous years among the clients about which you fill in the questionnaires.

Prior research in the auditorŝs decision to book or waive misstatements indicates that auditor behavior is affected by the *absolute as well as the relative size* of the conflict issue (Robinson and Fertuck 1985; Icerman and Hillison 1991; Houghton and Fogarty 1991; Wright and Wright 1997). As underlined previously, see section 2.4.6.3, many proposed adjustments can be relatively small and consequently be waived due to immateriality reasons and not due to the client being successful in persuading the auditor. To exclude such smaller disagreements from the sample, I asked only for disagreements that could potentially have a material impact on the financial statements and included a question in the questionnaire about the materiality of the issue. In two of the cases, the respondents answered that the issue was immaterial but because other answers in the questionnaires indicate that the issues that are discussed in these cases could have a large monetary impact on the financial statements and they potentially were material when the negotiation took place, these negotiations are included in the final sample of 79 negotiations. If the respondent experienced more than one difficult accounting issue with the client, they were asked to respond on the issue that potentially could have the largest monetary impact for the financial statements.

Industry is not found to have a significant impact on the auditorŝs decision to waive or adjust proposed adjustments in Wright and Wright (1997). Industry is partly controlled for in this study as participants are asked not to include banking, insurance or governmental clients (these industries are heavily regulated).

Several variables are included as control variables in the supplementary analyses in section 5.8.5. *Ownership* has not been included in prior negotiation research and the potential effect of this variable is likely to be captured by the size variable. In this study the variable is included with a measure that distinguishes between public clients, non-public clients with a public mother and non-public clients.

The effect of the *clientôs financial condition* on the auditorôs choice of negotiation strategy is likely to be captured by the audit risk variable, but the variable is also included in this study with a measure of whether or not the client experienced financial difficulties.

Audit fee (absolute) or *audit fee relative to the other clients of the partner* is also an important independent variable in audit research. The absolute audit fee is mainly a function of client size and risk and necessary controls for the impact of this variable are included in the supplementary analyses section.

As the study is conducted in a low-litigious environment, it is not necessary to control for the potential effect of *formal sanctions* or *litigation risk*.

Auditor competence (in particular caused by technical accounting knowledge) may also be an important variable but as the auditors in this study all work in the same audit firm, the design gives some control for this potential effect. The participating audit company has a system with two types of partnerships. As a supplementary analysis, type of partnership will be used as a proxy for auditor competence and included in the study.

4.5. Limitations

The study is designed to be as appropriate as possible for the study of the research topics presented in chapter 3. Nevertheless, some of the choices related to the design give rise to the studyôs limitations as presented below.

The entire population of auditor-client negotiations from the relevant audit years is an unknown population and because no information about this population is compiled in the audit firm, it is also impossible to ñconstructò. Consequently we cannot be assured that the sample is representative of the entire population of auditor-client negotiations over difficult accounting issues. Sample statistics (see section 5.2) show that the negotiation sample consists of many different types of negotiations with clients from many different industries, with different size and ownership structure.

As often in accounting/auditing research, it is not possible with my design to evaluate the quality of the chosen accounting solution. Instead, I study the extent to which the auditor accepted another accounting solution than the one he initially preferred.

Finally, as all data is collected after the negotiation took place, the auditorõs ex-post judgments may be affected by inaccurate recollections of the events and facts. To the extent that such inaccurate recollections occur, this is most likely when auditors answer questions about sensitive issues. In this study, information about the accounting outcome may constitute a sensitive issue if the auditor has been persuaded to concede more than he thinks is ñcorrectò. In such cases, the auditor has two ñchoicesò: he can either choose not to report anything about this case or he may report ña solution identical to the one he initially considered correctò instead of reporting that the solution was a compromise. If the auditor chooses the latter way, this is likely to work against finding significant relationships between the variables in the study and the accounting outcomes of the negotiations.

5.0. RESEARCH FINDINGS

5.1. Introduction

In this chapter, I will present general characteristics of the sample in section 5.2. I will then report descriptive statistics for the variables used in the regression analyses in section 5.3. Section 5.4 reports the findings from the hypotheses testing. In section 5.5, I present the analysis of the importance of the independent contextual variables followed by findings on the relationship between the auditorsô combined use of the contending and the conceding negotiation strategy and the accounting outcome of auditor-client negotiations in section 5.6. In section 5.7, I include findings on factors that are related to the accounting outcomes of auditor-client negotiations, and in section 5.8, I present the sensitivity analyses undertaken.

5.2. Sample characteristics

As we see in Table 10 below, the sample consists of many different types of negotiations. We see that the sample includes negotiations about how to account for investments, goodwill, intangibles, stock and work in progress, and a number of other types of negotiations.

Table 10 - Type of issues in sample

Investments	15
Goodwill and immaterial assets	14
Stock and work in progress	11
Debtors	9
Fixed assets	7
Accounting of taxation issues	5
Group matters	3
Leasing	3
Contingencies	3
Going concern	3
Related party transactions	2
Disclosure/subsequent events	1
Liabilities	2
Compliance with Company Act	1
	79

We see below that the sample consists of clients from different industry categories (see Table 11); with different types of ownership structure (see Table 12).

Table 11 - Industry classification

Utilities	3
Shipping	4
Oil and gas	4
Manufacturing	17
Merchandising	17
Telecom, media and technology	8
Construction	4
Investments / finance	6
Real estate and business activities	8
Others[44]	8
	79

[44] The category ñothersò consists of clients in fishing, service (2), transport, logistics and not specified (3).

Table 12 - Ownership

Public	8
Non public company with public parent	8
Non public	61
Not specified	2
	79

Many of the clients in the sample are relatively large[45], 36 out of 76 companies have annual revenue larger than NOK 500 million[46] (see Table 13).

Table 13 - Company annual revenue[47]

Less than 10 million NOK	10
Between 10 and 50 million NOK	13
Between 50 and 100 million NOK	10
Between 100 and 500 million NOK	7
Between 500 and 1000 million NOK	11
Between 1000 and 3000 million NOK	15
Larger than 3000 million NOK	10
Not specified	3
	79

The sample consists of 65 clients (83%) that received an unmodified audit opinion, 4 clients that received an unmodified audit opinion with an emphasis of matter paragraph and 10 clients (13%) that did not receive an unmodified audit opinion. Of these 10 clients, only 6 received the modified audit opinion as a consequence of the negotiation described in the questionnaire. One of these clients received an adverse opinion.

The conflicts described in the sample took place in the years 2007, 2008 and 2009. Due to the financial crisis many of the companies had a problem with their profitability: the respondents

[45] As the 500th largest Norwegian company in 2008 had an annual revenue of NOK 643 million (Dagens Næringsliv, June 3rd, 2009), at least 36 of the companies in the sample are on the Norwegian ñTop-500-Listò. 1USD=5.69NOK and 1EURO=7.42NOK, DnB, September 15, 2012.

[46] Three of the respondents had forgotten to give information about annual revenue. These cases are not included in the analyses when company size is included as one of the variables.

[47] These categories are used to measure company size in the following analyses.

indicate that 65% of the clients in the sample experienced a profitability problem in the period when the audit was conducted.

On a question related to the extent to which the clients used aggressive accounting; 41.8% of the respondents checked ñvery low or lowò, 46.8% checked ñneither high nor lowò and 11.4% checked ñhighò.

Female auditors are represented with a total of five cases in the sample while male auditors have responded with 74 cases.

The auditors who participate in the study have worked as auditors from 5 to 36 years with an average working experience of 17.16 years (std. dev. 7.29). They have been partners from 1 to 30 years with an average partner experience of 7.07 years (std. dev. 7.22).[48] Twenty-one of the cases in this study come from partners who have only one or two years of partner experience. The auditors in the study experience on average 3.56 difficult accounting issues (std. dev. 2.49) per year. Eighteen of the cases in the study come from partners who experience two or fewer difficult accounting issues per year. Calculation of the Spearmanôs rank order correlation coefficient shows that there is a positive and significant correlation between the partner experience and the number of difficult accounting issues experienced yearly so that more experienced partners report that they experience more difficult accounting issues per year than do less experienced partners ($r=0.279$; $p<0.05$).

5.3. Descriptive statistics: dependent and independent variables

In this section I present descriptive statistics for the dependent and independent variables (see Table 14 and 16). Respondents in the survey were also asked to give verbal information about the accounting solutions that were obtained in the negotiations. A summary of this verbal information is given in this section. In the end of the section, I present a correlation matrix of the dependent and independent variables (see Table 17).

---

[48] Two of the respondents in the study are not formally partners but are allowed to sign audit opinions. They have worked as auditors in 18 and 25 years respectively and participate with a total of four cases. These auditors are not included in the descriptive statistics that are based on partnership.

Table 14 - Descriptive statistics for the dependent and independent variables in the main analyses

Variables	N	Min	Max	Mean	Std. dev.	Skewness		Kurtosis	
						Stat.	Std. error	Stat.	Std. error
ACCREGULATION	79	1	5	3.23	1.00	-.398	.271	-.439	.535
CLIENTACCEXP	79	1	5	2.92	0.78	.135	.271	-.442	.535
AR	79	1	5	3.35	0.75	-.507	.271	.296	.535
CLIENTSIZE	76	1	7	4.07	2.04	-.072	.276	-1.385	.545
RELATIONSHIP	79	1	4	3.22	0.71	-.998	.271	1.850	.535
TENURE	79	1	30	7.38	6.30	1.894	.271	3.701	.535
AUDITOREXP	79	0	1	0.73	0.45	-1.081	.271	-.854	.535
EXPDIFFCASES	79	0	1	0.77	0.42	-1.323	.271	-.257	.535
CONTEND	79	0.20	7.00	4.49	1.57	-.736	.271	.392	.535
CONCEDE	79	0.00	6.33	3.08	1.62	-.098	.271	-.630	.535
DIFFSTRAT	79	-5.13	7.00	1.41	2.40	-.269	.271	.918	.535

Notes:

ACCREGULATION	= precision of relevant accounting regulation; scale from 1 to 5
CLIENTACCEXP	= clientôs technical accounting knowledge; scale from 1 to 5
AR	= audit risk; scale from 1 to 5
CLIENTSIZE	= clientsô income; 7 ordinal categories
RELATIONSHIP	= auditor-client relationship; scale from 1 to 5
TENURE	= number of years the client has been audited by the incumbent auditor
AUDITOREXP	= 0 if the partner has two years of partner experience or less, 1 otherwise
EXPDIFFCASES	= 0 if the partner normally experiences 2 or fewer difficult accounting issues, 1 otherwise
CONTEND	= score on use of contending negotiation strategy; scale from 0 to 7
CONCEDE	= score on use of conceding negotiation strategy; scale from 0 to 7
DIFFSTRAT	= score to measure ñmore use of contending negotiation strategyò; scale from -7 to +7

A paired-samples t-test shows that auditors report more use of contending tactics than of the conceding strategy, $t=5.199$; $p<0.0005$ (two-tailed).[49] This is in line with findings in prior research (Gibbins et al. 2010). The auditors in my study seem to use less of the contending tactics and more of the conceding strategy than the respondents in Gibbins et al. (2010).[50] The finding is not surprising as Gibbins et al. study what auditors plan to do whereas I study what the auditors did: It is likely that auditors in many negotiations will end up conceding more than they planned prior to the start of the negotiation.

We see from the Table 15 below that my findings on the resolution of the issues differ from prior findings on the number of times a compromise is the obtained solution.

Table 15 - The resolution of the issue ï compared to findings in Gibbins et al. 2001 and 2007

	Current study	Gibbins et al. 2001	Gibbins et al. 2007
Agreement on the clientôs original position	14%	4%	34%
Agreement on the auditorôs original position	46%	32%	19%
Somewhere between the suggested solutions	20%	41%	26%
A new solution	13%	16%	17%
No agreement	8%	1%	1%
Question not answered/other outcome	0%	5%	3%
	100%	100%	100%

Table 16 below shows the frequency table for the accounting solution as a binary variable (SOLUTION).

[49] See Table 6 and Appendix 2 for statistics of the statements that make up the negotiation strategy scales.

[50] Gibbins et al. (2010) report a mean of 1.82 (recalculated to be comparable) for the use of the conceding strategy and a mean of 4.86 for the use of the contending tactics. It should be noted that both studies use an 8-point scale from 0-7 but that the scale in Gibbins et al. (2010) varies from ñVery unlikely to useò to ñVery likely to useò. The scale in my study varies from ñNo agreement with statementò (i.e. no use of tactic) to ñVery high agreement with statementò (i.e. very much use of tactic).

Table 16 - Accounting solution as binary variable

SOLUTION	
The auditor has kept his initial position	42[51]
Other solution	37
	79

After checking the solution that resulted from the negotiation, the respondents were asked to give more information verbally about the solutions. These verbal descriptions give us more information about auditor-client negotiations.

When auditors describe solutions that end up as they initially suggested, they often use words and phrases such as ñcorrectò, ñcompletely written downò, or ñin accordance with *my* (the auditorôs) understanding of the accounting rulesò.

Some examples from the sample are stated in the following ways: ñThe reserve was increased according to what we (the auditor) found *correct.ò* ñGoodwill was written down *according to the expectations* of the auditor.ò ñThe issue was accounted for *according to GAAP*.ò ñThe deferred tax asset was *completely written down.ò* ñThe *entire contingency* was accounted for.ò ñRemoval costs were accounted for.ò ñThe client realized that his opinion on the accounting issue was wrong.ò ñI (the auditor) collected information from the audit firmôs central consultation unit and communicated this information to the client.ò ñThe solution was obvious but the client initially disagreed.ò ñThe entire amount was accounted for.ò ñThe shares were written down.ò ñAfter a while the client realized he was wrong.ò ñThe auditorôs *understanding of the accounting rules* (IFRS 5) was used as the basis for the accounting.ò ñThe errors were corrected.ò ñThe client did eventually agree.ò ñThe amount was written down completely in accordance with the auditorôs request.ò

One of the descriptions differs from the others: ñThe CFO calculated the necessary write-down. The amount written down was ñin the corridorò that I found a *reasonable estimate.*ò It follows from below that the description of this solution resembles the description of a compromise. One possible interpretation of this case can be that the auditor initially did not

[51] It follows from Table 15 that the auditor and the client have agreed on the auditorôs original position in thirty-six of the cases. In six cases no agreement was reached and the auditor issued a modified opinion.

have a clear idea about what size of write-down he would accept, but he meant that the client suggested solution was not correct. If the auditor does not initially have a clear opinion about which solutions he is likely to accept, it is possible that he eventually accepts a reasonable solution and in retrospect is of the opinion that he ended up with the solution he initially preferred.

Compromises are typically described in the following way: ñGoodwill was written down but with a larger amount that our (the auditor) *best estimate*.ò ñParameters were changed so that they were *acceptable.***ò** ñA *reasonable* solution was obtained.ò ñThe deferred tax asset is a very *uncertain estimate*. The final solution was that the asset was not increased from last year. The last yearôs asset was found *sufficiently justifiable*.ò ñThe solution was backed by the accounting rules.ò

Descriptions of negotiations where the clientôs solution is accepted typically include the words information and documentation: ñThe client came up with *sufficient information* for us (the auditor) to conclude that their (the clientôs) suggested solution was *ok.***ò** ñThe client did a thorough job *documenting* their view and we could accept it.ò ñWe (and the client) found the IFRS solution illogical and used the audit methodology to argue that the negotiated issue was *immaterial.***ò** ñThe client presented sufficient information that we could audit.ò ñThe client solution was acceptable as supplementary information were in support of the clientôs solution.ò ñWith new information, we (the auditor) could agree with the clientôs solution.ò ñWe could defend the clientôs solution.ò

The examples above successfully describe how audits (and auditor-client negotiations) differ; on the one hand, the auditor may choose to impose his view of an accounting issue on the client and he obtains solutions that he finds correct; on the other hand, he may choose to support and defend the clientôs solution and obtain solutions that he finds reasonable and justifiable. Consequently, the auditor sometimes allows the client to decide more of the accounting than at other times. This is not necessarily wrong because the client may be the one of the two negotiation parties who has suggested the correct solution. But if this is the entire explanation, one would expect that the accounting is not associated with variables such as auditorï client relationship and auditor experience. I will investigate this issue further in section 5.7.

We see above that in ten cases in my sample, the obtained solution is characterized by the auditor as a new solution. Further study of these cases reveals the following: in four of the cases, the auditor and the client disagree about input parameters/definitions in a valuation model and they reach an agreement about new parameters to use; in three of the cases, the parties disagree about the necessity of booking an amount in the income statement; in two of the cases, the parties agreed to book the amount directly against equity, and in one of the cases, the solution was to use different solutions for the company accounts (Norwegian entity) and for the group accounts (international group accounts). In the last three cases, the disagreement is about the necessity and/or size of writing-down assets and the probability of an event, and the parties agree on a solution that differs from the ones initially suggested.

It is not explicitly expressed by the respondents in any of the ten cases that the ñnew solutionò is *better* from an accounting point of view than the solution the auditor initially suggested, and due to the design of this study, it is not possible to evaluate whether these new solutions are ñbetterò than alternative solutions. In one of the cases, the respondent explicitly expresses that the ñnew solutionò was *acceptable*, a statement that may indicate that this new solution is not better than the solutions initially suggested.

Strength and direction of a linear relationship can be measured with the Pearson product-moment coefficient or the Spearman rho (Pallant, 2007). As the Pearson product-moment coefficient should be used with interval level variables only (one of the two variables can be a dichotomous variable) and some of the correlations that I need to calculate are between two dichotomous variables (of which one is ranked), I use the Spearman rank order correlation coefficient in my thesis as this correlational measure can also be used with ranked variables.

A correlation matrix of the dependent and independent variables is presented in Table 17. A comparison of the Spearmanôs rank order correlation of the two measures shows that the AUDITOREXP-variable covaries more (r=0.301, p<0.01) with the dependent variables than EXPDIFFCASES (r=0.246, p<0.05), see Table 17. I therefore use the first measure, AUDITOREXP, in the following analyses.

We see that the measure of the overall negotiation strategy (DIFFSTRAT) correlates positively with the precision of the accounting regulation of the negotiated accounting issue (p<0.001) and the audit partnerôs general level of experience (p< 0.01) and correlate negatively with the auditor-client relationship ($p<0.01$) and the client firmôs technical accounting knowledge ($p< 0.01$). We also see that the accounting outcome of the negotiation (solution) correlates positively with the precision of the accounting regulation ($p<0.001$), the partnerôs level of experience ($p<0.05$) and the overall negotiation strategy ($p<0.001$). The accounting outcome correlates negatively with the auditor-client relationship ($p<0.05$).

Table 17 - Correlation matrix ï Spearmanôs rho

Variable	*CLIENTACCEXP*	*AR*	*CLIENTSIZE*	*RELATIONSHIP*	*TENURE*	*AUDITOREXP*	*EXPDIFFCASES*	*CONTEND*	*CONCEDE*	*DIFFSTRAT*	*SOLUTION*
ACCREGULATION	-0.022	-0.035	-0.171	-0.035	-0.048	-0.061	0.142	*0.442	-0.181	*0.406	*0.450
CLIENTACCEXP		0.031	0.193	**0.341	-0.198	-0.203	-0.097	-0.223	**0.318	**-0.301	-0.069
AR			0.175	-0.075	-0.017	-0.102	-0.105	0.112	0.210	-0.055	0.168
CLIENTSIZE				0.139	0.116	-0.178	-0.064	-0.066	0.089	-0.088	-0.145
RELATIONSHIP					0.091	-0.169	0.072	***-0.252	**0.368	**-0.383	***-0.227
TENURE						**0.259	-0.007	0.109	-0.111	0.162	0.132
AUDITOREXP							0.140	0.159	**-0.338	**0.301	***0.239
EXPDIFFCASES								***0.280	-0.145	***0.246	***0.277
CONTEND									-0.083	*0.662	*0.422
CONCEDE										*-0.743	-0.172
DIFFSTRAT											*0.410

(The table is continued on the next page)

* Significant at the 0.001 level (two-tailed)
** Significant at the 0.01 level (two-tailed)
*** Significant at the 0.05 level (two-tailed)

Notes:

ACCREGULATION	= precision of relevant accounting regulation; scale from 1 to 5
CLIENTACCEXP	= clientôs technical accounting knowledge; scale from 1 to 5
AR	= audit risk; scale from 1 to 5
CLIENTSIZE	= clientsô income; 7 ordinal categories
RELATIONSHIP	= auditor-client relationship; scale from 1 to 5
TENURE	= number of years the client has been audited by the incumbent auditor
AUDITOREXP	= 0 if the partner has two years of partner experience or less, 1 otherwise
EXPDIFFCASES	= 0 if the partner normally experience 2 or fewer difficult accounting issues, 1 otherwise
CONTEND	= score on use of contending negotiation strategy; scale from 0 to 7
CONCEDE	= score on use of conceding negotiation strategy; scale from 0 to 7
DIFFSTRAT	= score to measure ñmore use of contending negotiation strategyò; scale from -7 to +7
SOLUTION	= 1 if the solution is equal to the solution the auditor initially considered correct, 0 otherwise

5.4. Test of hypotheses 1-4

In this section I use multiple regression analyses to test the first four hypotheses. As I measure whether the auditorôs negotiation strategy is more or less contending by using a combined measure of the contending and the conceding negotiation, I will then use ANOVA-analyses to investigate which of the strategies has a unique contribution to the findings.

<u>Multiple regression analysis</u>

The first four hypotheses consider the relationship between one metric dependent variable ñauditorôs overall negotiation strategyò and several independent variables ñprecision of accounting regulationò, ñclientôs accounting expertiseò, ñquality of auditor-client relationshipò, and ñaudit partnerôs experienceò. As ñmultiple regression analysis is a statistical technique that can be used to analyse the relationship between a single dependent (criterion) variable and several independent (predictor) variablesò (Hair et al. 1998, p. 148), it is an appropriate method for my analysis.

It should be noted that multiple regression analysis requires the independent and the dependent variable to be metric (independent variables can be transformed with dummy-coding if necessary). In my study, the measures of three of the independent variables, the ñprecision of accounting regulationò, the ñclientôs accounting expertiseò and the ñquality of the auditor-client relationshipò, are non-metric and the measurement scales are ordinal (categorical variables). The ñaudit partnerôs experienceò is measured in two ways, one with a metric measurement scale and one with a non-metric measurement scale. Even though the independent variables in my study are not metric, I follow the common practice in which non-metric ordinal variables are allowed as independent variables in multiple regression analysis.

Preliminary analyses were performed to make sure there are no violations of the assumptions of normality, linearity, multicollinearity and homoscedasticity.[52]

The following regression model is used to test the hypotheses:

> Model 1A: Overall negotiation strategy (DIFFSTRAT) = β_0 + β_1 accounting regulation (ACCREGULATION) + β_2 clientôs accounting expertise (CLIENTACCEXP) + β_3 auditor-client relationship (RELATIONSHIP) + β_4 audit partnerôs experience (AUDITOREXP) + β_5 audit risk (AR) + β_6 client size (CLIENTSIZE) + β_7 tenure (TENURE) + e

The variables in the model are measured as described in section 4.4. Table 18 below presents the OLS-results for model 1A. Findings related to the four hypotheses will be discussed in the following pages.

---

[52] Inspection of the correlation matrix indicates no problem with multicollinearity neither do the Tolerance or VIF values.

Inspection of the normal probability plot (P-P) of residuals indicates normally distributed errors and that the assumptions of linearity and homoscedasticity have been met.

Inspection of the boxplots suggests several univariate outliers. The 5% trimmed means are, however, not very different from the total sample means and all suggested outliers are kept in the following analysis. Mahalanobis distances do not identify any potential outliers neither do the casewise diagnostics. The scatterplot shows that no cases have standardized residuals of more than 3 or less than -3.

Table 18 - Main analysis: OLS-regression results

Model 1A
(n=76)

Dependent variable: DIFFSTRAT

Independent variable	Pred. Sign	Std. Coefficients	t-statistic	
ACCREGULATION	+	0.482	5.749	*
CLIENTACCEXP	-	-0.214	-2.285	***
RELATIONSHIP	-	-0.322	-3.561	*
AUDITOREXP	?	0.252	2.798	**
AR		-0.121	-1.399	
CLIENTSIZE		0.110	1.240	
TENURE		0.113	1.251	
Adjusted R^2		0.490		

* Significant at the 0.001 level (one-tailed)
** Significant at the 0.01 level (two-tailed)
*** Significant at the 0.05 level (one-tailed)

Notes:

ACCREGULATION	= precision of relevant accounting regulation; scale from 1 to 5
CLIENTACCEXP	= clientôs technical accounting knowledge; scale from 1 to 5
AR	= audit risk; scale from 1 to 5
CLIENTSIZE	= clientsô income; 7 ordinal categories
RELATIONSHIP	= auditor-client relationship; scale from 1 to 5
TENURE	= number of years the client has been audited by the incumbent auditor
AUDITOREXP	= 0 if the partner has two years of partner experience or less, 1 otherwise
DIFFSTRAT	= score to measure ñmore use of contending negotiation strategyò; scale from -7 to +7

We see from Table 18 that ACCREGULATION, CLIENTACCEXP, RELATIONSHIP and AUDITOREXP are all significant variables. ACCREGULATION and RELATIONSHIP are significant at the 0.001 level (one-tailed), AUDITOREXP is significant at the 0.01 level (one-tailed) and CLIENTACCEXP is significant at the 0.05 level (one-tailed).

Hypothesis 1 ï Type of accounting issue

Hypothesis 1 predicts that auditors are likely to use an overall negotiation strategy that is more contending if the negotiated accounting issue is more precisely regulated than the overall negotiation strategy used if the accounting issue is less precisely regulated. We see from Table 18 that there is a significant positive relation ($p<0.001$) between auditorsô negotiation strategies and the degree of precision of the negotiated accounting issue: the more precision there is in the regulation of a particular accounting issue confronted by auditors, the more contending is their overall negotiation strategy. The result provides support for hypothesis 1.

To better understand the findings, a one-way between groups ANOVA was conducted to compare the scores on the use of the contending strategy with the precision of accounting regulation. ñAnalysis of variance (ANOVA) is a collection of statistical methods and models that deal with differences in the means of a variable across groups of variables.ò (Iversen and Norpoth 1987, p. 7) and is an appropriate statistical method when ñthe groups of observations are created by a categorical independent variableò (Iversen and Norpoth 1987, p. 8) and we want to determine whether these groups differ in their mean scores of the dependent variable.

The cases in my study are placed in five groups according to what the respondents answer on a question on the precision of accounting regulation of the issue at stake, and what I want to determine is whether the groups have mean scores on the negotiation strategy variable that is significantly different from one another and whether we can identify a linear trend in these differences.

Table 19, Panel A, reports group means and ANOVA results. Table 19, Panel B reports the results of the linear contrast used to test the relationship between the precision of accounting regulation and the auditorôs use of the contending negotiation strategy.

There is a statistically significant difference in auditorôs use of the contending negotiation strategy for the five different groups ($F(4,74)=4.752$; $p<0.01$). The linear contrast shows a significant positive linear trend ($F(1,74)=16.41$; $p<0.001$): the more precisely regulated the accounting issue, the more contending tactics the respondents report that they use.

A one-way between groups ANOVA was also conducted to compare the scores on the use of the conceding strategy with the precision of accounting regulation (see Table 19). There is a marginally significant difference in auditorôs use of the conceding negotiation strategy for the five different groups ($F(4,74)=2.152$; $p=0.083$). The linear contrast shows a marginally significant linear negative trend (F(1,74)=3.629; p=0.061): the more precisely regulated the accounting issue, the less conceding strategy the respondents report that they use.

Table 19 - ANOVA results for the relationship between the precision of the regulation of the negotiated accounting issue and the use of the contending and the conceding negotiation strategy.

Panel A: ANOVA results

Dependent variable	Group ACCREG = 1, n=4	Group ACCREG = 2, n=15	Group ACCREG = 3, n=24	Group ACCREG = 4, n=31	Group ACCREG = 5, n=5	F-stat.	p-value (two-tailed)
Contend							
Mean	3.50	3.25	4.60	4.97	5.52	4.752	0.002
Std. dev.	2.07	1.57	1.25	1.49	1.00		
Concede							
Mean	3.00	3.64	3.15	3.06	1.27	2.152	0.083
Std. dev.	0.98	1.87	1.31	1.69	1.23		

Panel B: Planned comparison: linear trend

	F-stat.	p-value (two-tailed)
Contend	16.410	0.000
Concede	3.629	0.061

To summarize, I find that auditors who audit precisely regulated issues with their clients use more contending tactics and they are less willing to concede than auditors who audit less precisely regulated issues.

Hypothesis 2 ï Auditorï client relationship

Hypothesis 2 predicts that the more positive the auditor perceives the auditor-client relationship, the more likely it is for the auditor to use an overall negotiation strategy that is less contending than the overall negotiation strategy used by auditors who perceive the auditor-client relationship to be more negative. We see from Table 18 that there is a significant negative relationship ($p<0.01$) between auditorsô overall negotiation strategies and the auditorsô perceptions of their relationship with the client: the more favorably auditors perceive their relationship with the client; the less contending is the overall negotiation strategy that the auditors use. The result provides support for hypothesis 2.

To better understand the difference, two one-way between groups ANOVA analyses with planned comparisons were performed to compare the use of contending tactics as well as the use of the conceding strategy in the four auditor-client relationship groups.[53] Table 20 reports the results of the analyses.

There is a marginally significant difference in the auditorsô use of the contending negotiation strategies for the four groups ($F(3,75)=2.331$; $p=0.081$). The linear contrast shows a statistically significant underlying negative linear trend ($F(1,75)=4.55$; $p<0.05$) in the groupôs mean score of use of contending tactics. A contrast test between group 3 and 4[54] shows a statistically significant difference in mean scores $t=-2.342$; $p<0.05$: the more positive the auditor-client relationship, the less contending tactics are used by the auditors.

There is a statistically significant difference in auditorsô use of the conceding negotiation strategies for the four groups ($F(3,75)=3.778$; $p<0.05$). The linear contrast reveals a statistically significant underlying positive linear trend, $F(1,75)=10.581$; $p<0.01$, and a statistically significant difference in mean scores between group 3 and 4, $t=2.465$; $p<0.05$, [55] when we study the groupsô use of the conceding strategy: the more positive the relationship between the auditor and the client, the more the conceding strategy is used by the auditor.

[53] None of the respondents indicated that they had a relationship with their client that was ñvery much betterò than the relationship they have with their other clients.
[54] I restrict the contrast test to this comparison as almost all the respondents (72 out of 79) belong to one of these two groups.
[55] I restrict the also this contrast test to a comparison between group 3 and 4 as almost all the respondents (72 out of 79) belong to one of the two groups.

Table 20 - ANOVA results for the relationship between the quality of the auditor-client relationship and the use of the contending and the conceding negotiation strategy

Panel A: ANOVA results

Dependent variable	Group RELATION-SHIP = 1, n=3	Group RELATION-SHIP = 2, n=4	Group RELATION-SHIP = 3, n=45	Group RELATION-SHIP= 4, n=27	F-statistics	p-value (two-tailed)
Contend						
Mean	4.60	5.40	4.76	3.89	2.331	0.081
Std.dev.	2.75	1.12	1.33	1.76		
Concede						
Mean	1.89	1.75	2.86	3.78	3.778	0.014
Std.dev.	0.19	1.20	1.31	1.75		

Panel B: Planned comparisons: linear trend

	F-stat.	p-value (two-tailed)
Contend	4.550	0.036
Concede	10.581	0.002

Panel C: Contrast test between groups: Group 3 versus group 4

	t-statistics	p-value
Contend	2.342	0.022
Concede	-2.465	0.016

Consequently, I find that partners who have a good relationship with their clients both use less contending tactics and are more willing to concede than partners who have a less positive relationship with their client.

Hypothesis 3 ï Audit partner experience

Hypothesis 3 predicts that more experienced audit partners differ from less experienced audit partners in their combined use of the contending and conceding negotiation strategies. We see from Table 18 that audit partnerøs experience variable (AUDITOREXP) is significantly positively related ($p<0.01$) to auditorsô overall negotiation strategy (DIFFSTRAT). The result provides support for hypothesis 3.

To understand more about this difference, I investigated the difference between the two partner groups and their use of the contending and the conceding strategy using an independent samples t-test. Findings show that auditors with more than two years of partner experience (group mean score for use of the contending strategy=4.73; Std. dev=1.48) seem to use more contending tactics than partners with two years partner experience or less (group mean score for use of the contending strategy=3.99; Std. dev=1.69) but the difference is only marginally statistically significant ($t=1.870$; $p=0.066$, two-tailed).

More experienced auditors also use less of the conceding strategy (care less for the clientsô needs and wants) than partners with less experience (mean score for use of the conceding strategy= 2.74 for the most experienced group vs. 4.03 for the group with less partner experience) and the difference is statistically significant ($n=75$; $t=3.230$; $p<0.01$).

The finding indicates that experienced negotiators are more confident about their own ability to find the right solution than are less experienced auditors who care more about the extent to which the final accounting outcome is accepted by the client.

Hypothesis 4 ï Client accounting competence

Hypothesis 4 predicts that auditors who audit clients with higher levels of technical accounting knowledge are more likely to use an overall negotiation strategy that is less contending than the overall negotiation strategy used by auditors who audit clients with lower levels of technical accounting knowledge. We see from Table 18 that the clientøs accounting expertise is significantly negatively related to auditorsô overall negotiation strategy ($p<0.01$). The result provides support for hypothesis 4.

To better understand the findings, a one-way between groups ANOVA was conducted to compare the scores on the use of the contending strategy with the clientós accounting competence. There is no statistically significant difference in auditorós use of the contending negotiation strategy for the five groups ($F(4,74)=1.591$; $p=0.186$). The linear contrast shows a significant negative linear trend ($F(1,74)= 3.873$; $p=0.053$) showing that auditors use less contending tactics when the client is more competent in accounting (see Table 21).

Table 21 - ANOVA results for the relationship between the clientós accounting competence and the use of the contending and the conceding negotiation strategy

Panel A: ANOVA results

Dependent variable	Group CLIENTACCEXP= 1, n=1	Group CLIENTACCEXP = 2, n=23	Group CLIENTACCEXP = 3, n=37	Group CLIENTACCEXP = 4, n=17	Group CLIENTACCEXP = 5, n=1	F-stat.	p-value (two-tailed)
<u>Contend</u>							
Mean	3.40	4.91	4.61	3.75	4.00	1.591	0.186
Std.dev.		1.53	1.34	1.96			
<u>Concede</u>							
Mean	3.00	2.49	3.07	3.78	5.33	2.163	0.081
Std.dev.		1.49	1.62	1.58			

Panel B: Planned comparisons: linear trend

	F-stat.	p-value (two-tailed)
Contend	3.873	0.053
Concede	7.716	0.007

A one-way between groups ANOVA was also conducted to compare the scores on the use of the conceding strategy with the precision of accounting regulation. There is a marginally significant difference in the auditorós use of the conceding negotiation strategy for the five groups (F(4,74)=2.163; p=0.081). The linear contrast shows a significant linear positive trend (F(1,74)= 7.716; p<0.01) indicating that auditors are more concerned with the clientôs opinion about an accounting issue when the clientôs accounting competence is higher.

In sum, I find that when the client is more competent in accounting, auditors use fewer contending tactics and more conceding negotiation strategies than when the client is less competent in accounting.

5.5. Importance of independent variables

In this section I examine the importance of the different independent variables in auditor-client negotiations. As the independent variables in model 1A are measured in different units: ñprecision of accounting regulationò, ñquality of auditor-client relationshipò and ñclientôs technical accounting knowledgeò are measured on a five-point scale and òaudit partnerôs experienceò is a dummy variable, standardized regression coefficients must be used to assess the relative importance of the variables.

Table 18 includes these standardized coefficients and we see that ñprecision of accounting regulationò is the most important variable followed by the ñauditor-client relationshipò, the ñaudit partnerôs experienceò, and the ñclientôs accounting expertiseò.

The findings are in line with the findings in Gibbins et al. (2001). The respondents (CFOs) in Gibbins et al. (2007) also respond that accounting regulation is the most important variable but they rate the clientôs accounting expertise as the second most important variable.

5.6. Relationship between auditorsô use of the negotiation strategies and the negotiationôs accounting outcome

In this section I present findings about the relationship between auditorsô combined use of the contending and the conceding negotiation strategy and the accounting outcomes of the negotiations. Hypothesis 5 predicts that the more auditors use an overall contending negotiation strategy, the more likely is a solution that equals the solution initially suggested by the auditor. The hypothesis considers the relationship between one independent (metric) variable (auditorôs combined use of the contending and the conceding strategies) and one dependent non-metric, categorical variable with three categories (accounting outcome). ANOVA is an appropriate analysis method to investigate this relationship.

Calculation of the Spearmanôs rank order correlation coefficient between ñAuditorsô use of negotiation strategyò and the accounting outcome of the negotiation shows that there is a positive and significant correlation ($r=0.410$; $p=0.000$, two-tailed), see Table 17. A one-way between groups analysis of variance was then conducted to study whether the auditors had used different negotiation strategies in negotiations with accounting outcome 1 (as initially preferred by client), 2 (compromise) and 3 = as initially preferred by auditor. There is a statistically significant difference in strategy use; $F=9.599$; $p<0.001$ between the three groups of negotiations (see Table 22). The analysis also shows a positive linear trend ($F(1,76)=18.871$; $p<0.001$): in negotiations where the resulting accounting outcome is the solution initially suggested by the client, the auditor uses a strategy that is less contending than the strategy used in negotiations where the resulting accounting outcome was a compromise. In negotiations where the resulting outcome is the solution initially suggested by the auditor, the strategy used is even more contending.

Table 22 - ANOVA-results for the relationship between the combined use of the contending and the conceding negotiation strategy and the negotiated accounting outcome

Panel A: ANOVA Results

Dependent variable	Group SOLUTION = 1, n=11	Group SOLUTION =2, n=26	Group SOLUTION= 3, n=42	F-statistics	p-value
DIFFSTRAT					
Mean	-0.44	0.64	2.37	9.599	0.000
Std.dev.	2.28	2.24	2.11		

Panel B: Planned comparison ï linear trend

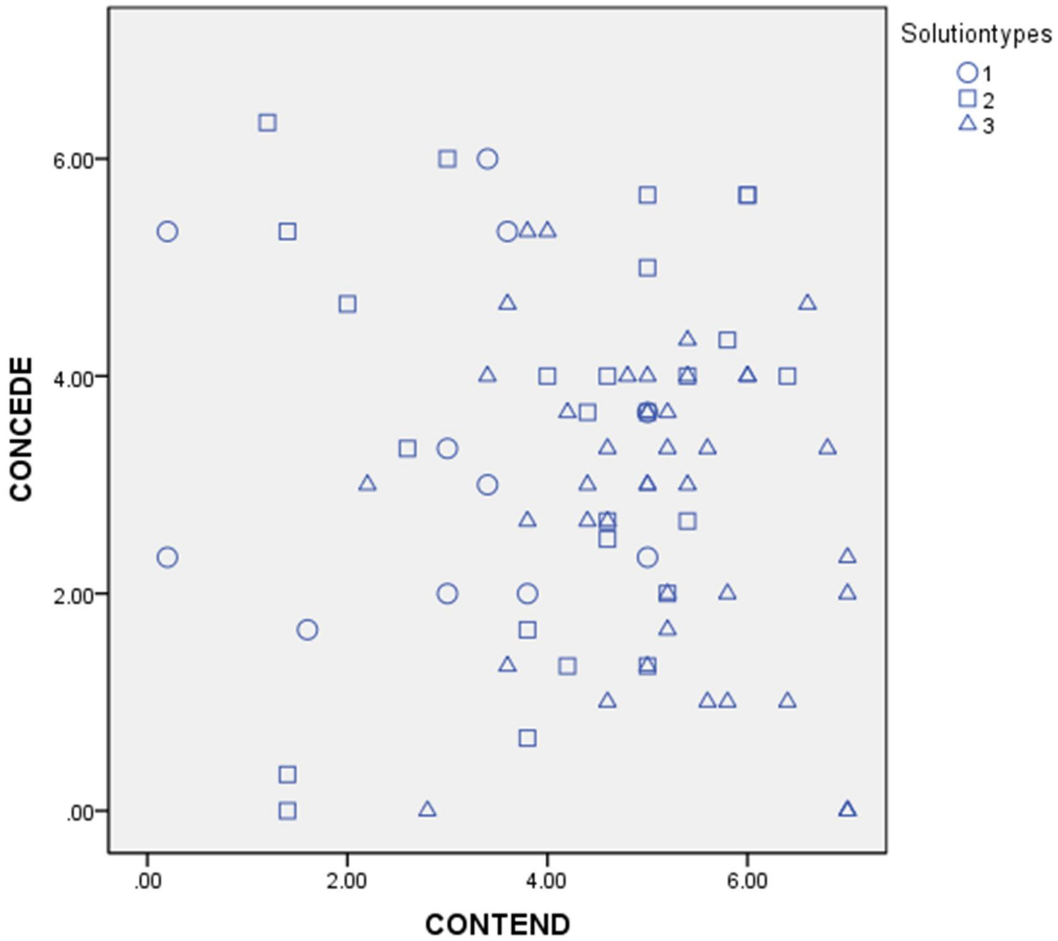
	F-statistics	p-value
Linear trend	18.871	0.000

1 = as initially preferred by client, 2 = compromise, 3 = as initially preferred by auditor

We see from Table 23 and Figure 9 below that for very negative scores on the strategy measure (scores lower that -1.73, i.e. high scores on the conceding scale and low score on the contending scale), all accounting outcomes are either as initially suggested by the client or compromises. We also see that for very high scores on the strategy measure (scores equal to or higher than 3.80, i.e. low scores on the conceding scale and high scores on the contending scale), all accounting outcomes are as initially suggested by the auditor. For scores in the interval between these two scores we see that the percentage of solutions that equal the solution initially suggested by the auditor increases as the score on the strategy variable increases.

Table 23 - Overall contending negotiation score and accounting outcome

Solution	[-7.00, -1.73]		<-1.73, 0.00]		<0.00,2.00>		[2.00, 3.80>		[3.80,7.00]	
1	4		2		4		1		0	
2	4		4		10		8		0	
3	0	0%	5	45%	15	52%	13	59%	9	100%
	8		11		29		22		9	



1 = as initially suggested by client, 2 = compromise, 3 = as initially suggested by auditor

Figure 9 - The respondents combined use of the contending and conceding negotiation strategies with the cases marked according to the negotiated accounting outcome

5.7. A model predicting negotiated accounting outcomes

In this section the aim is to specify and test a model consisting of different context and process variables that can be used to predict accounting outcomes in auditor-client negotiations. It follows from section 4.4 that the model I want to test consists of several independent variables and one binary dependent variable (accounting outcome). Consequently, I will use logistic regression analysis in the following analyses to predict accounting outcomes because logistic regression is ña specialized form of regression that is formulated to predict and explain a binary (two-group) categorical variable rather than a metric dependent variable.ò (Hair et al. 1998, p. 246) (It should be noted that SEM-analysis is not applicable due to sample size. Hair et al. (1998, p. 605) recommends for instance a sample size of at least 200.)

My research model in Figure 4 includes five independent variables that are thought to be related to negotiated accounting outcomes. We know from the findings in section 5.4 that four of these variables (accounting regulation, clientôs accounting expertise, auditor-client relationship and audit partnerôs experience) are statistically related to the fifth variable (overall negotiation strategy) and that this last variable is statistically related to accounting outcomes. As underlined in section 3.4, even though the model indicates that there is no direct relationship between the four context variables and accounting outcome, it is likely that some of the contextual variables are directly related to the accounting outcome and that others are not directly related to the outcome. As we do not know which of the context variables have a direct relationship in addition to the indirect relationship found in section 5.4 and as we have not specified any hypotheses about this, I will in this section use a two-step process to model the relationships: I first specify and test a model (model 2A) that includes all four contextual variables and the three control variables included in section 5.4 and then specify and test a model (model 2B) in which all clearly insignificant variables are removed. As we know little about expected effect sizes, backward stepwise logistic regression analysis could have been an alternative but because the number of cases per independent variable is recommended at 50:1 in stepwise regression (Hair et al. 1998, p. 166), I use ordinary logistic regression analysis. After testing model 2B, I will use this model to examine the relative importance of each of the independent variables that are found significant.

The following *logistic regression model* is used to assess the impact of the variables in the research model (see Figure 4 and section 3.4) on the likelihood that the accounting outcome of the auditor-client negotiation is the accounting outcome that the auditor initially preferred:

Model 2A: Accounting outcome* = β_0 + β_1 overall negotiation strategy + β_2 accounting regulation + β_3 clientôs accounting expertise + β_4 auditor-client relationship + β_5 audit partnerôs experience + β_6 audit risk + β_7 client size + β_8 tenure + e[56]

where Accounting outcome = 1 if Accounting outcome* >= 0 and Accounting outcome = 0 if Accounting outcome* < 0.

The variables in the model are measured as described in section 4.4. Descriptive statistics for the independent variables are presented in Table 14. A frequency table for the accounting outcome variable is presented in Table 16. For calculation of the Spearmanôs rank order correlation coefficient (see Table 17).

Preliminary analyses were performed to ensure there are no violations of the assumption of multicollinearity. The sample meets the minimum ratio of 5-to-1 suggested by Hair et al. (1998, p. 258) of observations to independent variables. The smallest group (binary solution=0) is larger than the minimum requirement of 20 (Hair et al. 1998) and is of approximately the same size as the other group (solution=1), see Table 16.

The model 2A is statistically significant, χ^2= 34.334 (df=8, n=76), p<0.001. This indicates that the model is able to distinguish between negotiations that ended with the solution that the auditor initially found correct (no conceding on the part of the auditor) and the negotiations that ended with other solutions (all these solutions entail some conceding on the part of auditor). The model as a whole explains between 36.3% (Cox and Snell R square) and 48.5% (Nagelkerke R square) of the variance in accounting outcome, and it classifies 78.9% of the cases correctly.

[56] The relationships in the models are expected to have the same directions as in the regression model in section 5.4. When it comes to the relationship between the negotiation strategy and the accounting outcome, the direction of the relationship also follows clearly from what has been discussed and found in section 5.6.

We see from Table 24 that there is a significant relationship ($p<0.05$, one-tailed) with three of the independent variables: accounting regulation, audit risk and negotiation strategy and the accounting outcome. Auditor experience is marginally significant ($p<0.10$). The precision of the accounting regulation has an odds ratio of 3.263. Consequently auditors that negotiate an accounting issue where the accounting rules have very high precision is 3.263 times more likely to report an accounting outcome that is equal to the outcome the auditor suggested before the negotiation took place than auditors that audit an accounting issue where the rules have high precision.

Table 24 - Main analysis: Logistic regression results; model 2A

Dependent variable: SOLUTION

VARIABLES IN THE EQUATION	B	S.E.	Wald	df	Sig.	Odds ratio
ACCREGULATION	1.183	.428	7.649	1	.006	3.263
CLIENTACCEXP	.626	.469	1.785	1	.181	1.870
AR	.878	.429	4.184	1	.041	2.406
CLIENTSIZE	-.174	.169	1.064	1	.302	.840
RELATIONSHIP	-.165	.509	.105	1	.745	.848
TENURE	.080	.068	1.400	1	.237	1.084
AUDITOREXP	1.240	.755	2.701	1	.100	3.457
DIFFSTRAT	.328	.190	2.980	1	.084	1.388
Constant	-9.073	3.354	7.320	1	.007	.000

Notes:

ACCREGULATION	= precision of relevant accounting regulation; scale from 1 to 5
CLIENTACCEXP	= clientôs technical accounting knowledge; scale from 1 to 5
AR	= audit risk; scale from 1 to 5
CLIENTSIZE	= clientsô income; 7 ordinal categories
RELATIONSHIP	= auditor-client relationship; scale from 1 to 5
TENURE	= number of years the client has been audited by the incumbent auditor
AUDITOREXP	= 0 if the partner has two years of partner experience or less, 1 otherwise
DIFFSTRAT	= score to measure ñmore use of contending negotiation strategyò; scale from -7 to +7

All variables that are clearly insignificant are then excluded from the model and I test model 2B:

> Model 2B: Accounting outcome* = β_0 + β_1 overall negotiation strategy + β_2 accounting regulation + β_3 audit partner's experience + β_4 audit risk + e
>
> where Accounting outcome = 1 if Accounting outcome* >= 0 and Accounting outcome = 0 if Accounting outcome* < 0.

The new model is statistically significant, χ^2= 34.296 (df=4, n=79), p<0.001. The model as a whole explains between 35.2% (Cox and Snell R square) and 47.0% (Nagelkerke R square) of the variance in accounting outcome, and it classifies 77.2% of the cases correctly.

We see from Table 25 that all the variables in Model 2B make a significant contribution. There is a significant positive relationship (p<0.05, one-tailed) between the auditors' combined use of the contending and the conceding negotiation strategy and the accounting outcome of the negotiation, thus indicating that the more contending style the auditors have, the more likely is it that the accounting outcome equals the solution the auditor suggested before the negotiation (i.e. an outcome where the auditor has not made any concessions).

There is a significant positive relationship (p<0.01, one-tailed) between the precision of accounting regulation and the accounting outcome of a negotiation, indicating that issues that are more precisely regulated are more likely to end up with the solution that the auditor initially suggested than issues that are less precisely regulated.

There is a significant positive relationship between the auditor's experience and the accounting outcome of the negotiation (p<0.05, two-tailed), indicating that more experienced auditors are more likely than auditors with less experience to end up with the solution that they initially suggested.

Finally, there is a significant positive relationship between audit risk and the accounting outcome of the negotiation (p<0.05, one-tailed) indicating that auditors are more likely to concede from their initially preferred solution if the audit risk is low than if the audit risk is high.

Table 25 - Main analysis: Logistic regression results; model 2B

Dependent variable: SOLUTION

VARIABLES IN THE EQUATION	B	S.E.	Wald	df	Sig.	Odds ratio
ACCREGULATION	1.196	.379	9.960	1	.002	3.307
AR	.788	.398	3.925	1	.048	2.199
AUDITOREXP	1.403	.706	3.946	1	.047	4.068
DIFFSTRAT	.308	.165	3.493	1	.062	1.361
Constant	-7.810	2.189	12.734	1	.000	.000

<u>The importance of the predictor variables</u>

To assess the relative importance of the variables when using logistic regression analysis, Tabachnick and Fidell (2001) suggest either comparing the odds ratios of the variables or standardizing the predictors before running the regression and then treating the obtained coefficients as standardized coefficients. As measurement scales differ considerably in model 2B, the second procedure is found the most preferable.

We see from Table 26 below that the strongest predictor of an accounting outcome equal to the outcome the auditor initially suggested is the precision of the accounting regulation. The second strongest predictor is the overall negotiation strategy, followed by the partnerǿs experience and audit risk.

Table 26 - Main analysis: Logistic regression results: model 2B, standardized variables

Dependent variable: SOLUTION

Variables in the equation	B	S.E.	Wald	Df	Sig.	Odds ratio
ACCSTD	1.195	.379	9.960	1	.002	3.303
ARSTD	.593	.299	3.925	1	.048	1.809
EXPSTD	.624	.314	3.946	1	.047	1.867
DIFFSTRATSTD	.739	.395	3.493	1	.062	2.094
Constant	.151	.286	.279	1	.597	1.163

Notes:

ACCSTD = ACCREGULATION standardized

ARSTD = AR standardized

EXPSTD = AUDITOREXP standardized

DIFFSTRATSTD = DIFFSTRAT standardized

5.8. Supplementary analyses

The aim of this supplementary analysis section is to explore the robustness of the findings in sections 5.4 to 5.7 by rerunning the analyses under conditions that are slightly different from the conditions in prior sections.

In this section I will first rerun the main analyses from section 5.4 and 5.7 with a different measure for ñoverall negotiation strategyò. These tests will examine the sensitivity of the findings to the way the overall negotiation strategy is measured. I then rerun the analyses on two different subsamples to investigate whether there are subgroups in the sample that drive the findings. I will in these analyses first exclude the cases in which the respondents have answered that they used little of both the conceding and the contending negotiation strategy and then exclude the cases in which the auditor has not issued a clean audit opinion. I will also run the analyses with some of the independent variables dichotomized and with alternative control variables to see if these differing conditions have an impact on the results of the analyses. To conclude the supplementary analyses section, I will investigate which independent variables are important if the cases with very large differences between use of the contending and the conceding negotiation strategy are excluded from the sample.

If not specified otherwise, the following multiple regression model is used in this section:

> Model 1A: Overall negotiation strategy (DIFFSTRAT) = β_0 + β_1 accounting regulation (ACCREGULATION) + β_2 clientôs accounting expertise (CLIENTACCEXP) + β_3 auditor-client relationship (RELATIONSHIP) + β_4 audit partnerôs experience (AUDITOREXP) + β_5 audit risk (AR) + β_6 client size (CLIENTSIZE) + β_7 tenure (TENURE) + e

It follows from the logistic regression analyses in section 5.7 that four variables seem to give a unique contribution to the prediction of accounting outcomes. If not specified otherwise, the following underlying model is used in this section:

> Model 2B: Accounting outcome* = β_0 + β_1 overall negotiation strategy + β_2 accounting regulation + β_3 audit partnerôs experience + β_4 audit risk + e,
>
> where Accounting outcome = 1 if Accounting outcome* >= 0 and Accounting outcome = 0 if Accounting outcome* < 0.

5.8.1. Alternative measure for the auditorôs use of overall negotiation strategy

As emphasized in section 4.4.2, both the contending and the conceding strategy are measured with composite measures. The statements used to measure the contending strategy try to reflect *different types of behavior* that the auditors may have had: use of threats, use of discussion, use of authority as an auditor and use of accounting expertise. It should be noted that the contending strategy is by definition implemented via different tactics. One of the statements is more general in its formulation, stating: ñI was firm in pursuing my positionò (statement 17). The measurement of the conceding strategy is done by the average score of three statements that capture the *same behavior* with different wordings as this strategy is by definition not implemented via different tactics.

As there are also other types of contending behavior that are not reflected in the measurement scale: Perrault and Kida (2011) study for instance the following persuasion tactics: use of precedents, use of a technical expert, warning of a possible quality control, the analyses are also made with an alternative measurement of the contending strategy in which only statement 17 is used to represent the contending strategy. The conceding strategy is measured as in prior analyses. I test the following model:

> Model 1B: Overall negotiation strategy (DIFFSTRATSIMPLE) = $ß_0$ + $ß_1$ accounting regulation (ACCREGULATION) + $ß_2$ clientôs accounting expertise (CLIENTACCEXP) + $ß_3$ auditor-client relationship (RELATIONSHIP) + $ß_4$ audit partnerôs experience (AUDITOREXP) + $ß_5$ audit risk (AR) + $ß_6$ client size (CLIENTSIZE) + $ß_7$ tenure (TENURE) + e

The variables in the model, apart from DIFFSTRATSIMPLE, are measured as described in section 4.4. Table 27 below presents the OLS - results for model 1B.

Table 27 - Supplementary findings: Alternative measure for the contending strategy

Panel A: Descriptive statistics

Variables	N	Minimum	Maximum	Mean	Standard deviation
CONTENDP17	79	0.00	7.00	4.72	2.26
CONCEDE	79	0.00	6.33	3.08	1.62
DIFFSTRATSIMPLE	79	-6.33	7.00	1.64	3.04

Notes:

CONTENDP17	= score on statement 17; scale from 0 to 7
CONCEDE	= score on use of conceding negotiation strategy; scale from 0 to 7
DIFFSTRATSIMPLE	= score to measure ñmore use of contending negotiation strategyò; scale from -7 to +7 (=CONTENDP17-CONCEDE)

Panel B: OLS-regression results

Dependent variable: DIFFSTRATSIMPLE

Model 1B
(n=76)

Independent variable	Pred. Sign	Std. Coefficient	t-statistic	
ACCREGULATION	+	0.435	4.765	*
CLIENTACCEXP	-	-0.165	-1.620	****
RELATIONSHIP	-	-0.313	-3.185	**
AUDITOREXP	?	0.212	2.159	***
AR		-0.074	-0.780	
CLIENTSIZE		0.044	0.453	
TENURE		0.145	1.476	
Adjusted R^2		0.396		

* Significant at the 0.001 level (one-tailed)

** Significant at the 0.01 level (one-tailed)

*** Significant at the 0.05 level (two-tailed)

**** Significant at the 0.10 level (one-tailed)

Panel C: Logistic regression results, model 2C

Dependent variable: SOLUTION

Variables in the equation	B	S.E.	Wald	df	Sig.	Odds ratio
ACCREGULATION	1.168	.372	9.866	1	.002	3.216
AUDITOREXP	1.410	.716	3.871	1	.049	4.094
AR	.787	.406	3.761	1	.052	2.197
DIFFSTRATSIMPLE	.329	.132	6.228	1	.013	1.390
Constant	-7.818	2.206	12.555	1	.000	.000

We see from the Table 27 above that this alternative way of measuring the contending part of the overall strategy used has only a small effect on the linear regression findings.

I then test the following logistic regression model:

Model 2C: Accounting outcome* (SOLUTION) = $\beta_0 + \beta_1$ overall negotiation strategy (DIFFSTRATSIMPLE) + β_2 accounting regulation (ACCREGULATION) + β_3 audit partner's experience (AUDITOREXP) + β_4 audit risk (AR) + e

where Accounting outcome = 1 if Accounting outcome* >= 0 and Accounting outcome = 0 if Accounting outcome* < 0.

Findings from the logistic regression analysis are reported in Table 27 above. The full model including all four predictor variables is statistically significant, χ^2 (4, n=79) =38.049, p< 0.001. The model explains between 38.2% (Cox and Snell R square) and 51.0% (Nagelkerke R square) of the variance in accounting outcome. We see from the Table 27 that all the four variables are significantly related to the accounting outcome. 81% of the cases are correctly classified by the model.

By using only statement 17 to measure the auditors' use of the contending strategy (how firm the auditor was in pursuing his own opinion) and then subtracting the use of the conceding strategy (to what extent the auditor tried to satisfy the client), I get a measure that is more a measure of "to what extent the auditor wanted to win the negotiation", i.e. the auditor's intention/goal commitment (see section 2.4.6.4) than the original measure of auditor behavior.

When it comes to predicting the accounting outcome in an auditor-client negotiation, we see that this alternative measure of the contending negotiation strategy gives a model that is slightly better than model 2B in that it classifies more cases correctly and has a higher Cox and Snell R square.

5.8.2. Sample excluding low-low cases

To ensure that the cases in which the respondents have indicated that they use little of both the contending and the conceding negotiation strategy do not drive the results, the regression analysis in 5.4 as well as the logistic regression analysis in section 5.7, are also run without the cases that score lower than 3.0 on both scales. We see from Table 28 below that exclusion of the six low-low cases does not have any practical significance for the findings.

Table 28 - Supplementary findings: Sample excluding low-low cases

Panel A: Descriptive statistics

Variables	N	Minimum	Maximum	Mean	Standard deviation
ACCREGULATION	73	1	5	3.27	0.976
CLIENTACCEXP	73	1	5	2.93	0.788
AR	73	1	5	3.37	0.755
CLIENT SIZE	70	1	7	4.11	2.089
RELATIONSHIP	73	1	4	3.23	0.677
TENURE	73	1	30	7.51	6.515
AUDITOREXP	73	0	1	0.71	0.456
DIFFSTRAT	73	-5.13	7.00	1.49	2.445

Panel B: OLS-regression results

Dependent variable : DIFFSTRAT

Model 1A (n=70)

Independent variable	Pred. Sign	Std. Coefficient	t-statistic	
ACCREGULATION	+	0.445	5.034	*
CLIENTACCEXP	-	-0.219	-2.250	***
RELATIONSHIP	-	-0.302	-3.249	**
AUDITOREXP	?	0.277	2.956	**
AR		-0.128	-1.419	
CLIENTSIZE		0.117	1.246	
TENURE		0.100	1.061	
Adjusted R^2		0.494		

* Significant at the 0.001 level (one-tailed)

** Significant at the 0.01 level (one-tailed test for predicted relationship otherwise two-tailed)

*** Significant at the 0.05 level (one-tailed)

Panel C: Logistic regression results, model 2B

Dependent variable: SOLUTION

Variables in the equation	B	S.E.	Wald	df	Sig.	Odds ratio
ACCREGULATION	1.289	.416	9.587	1	.002	3.630
AUDITOREXP	1.456	.726	4.023	1	.045	4.288
AR	.584	.409	2.045	1	.153	1.794
DIFFSTRAT	.291	.174	2.782	1	.095	1.338
Constant	-7.428	2.230	11.093	1	.001	.001

Findings from the logistic regression analysis are reported in Table 28. The full model including all four predictor variables is statistically significant, χ^2 (4, n=73) =32.115, p< 0.001. The model explains between 35.6% (Cox and Snell R square) and 47.6% (Nagelkerke R square) of the variance in accounting outcome. We see from Table 28 above that only three of the predictor variables are statistically related to accounting outcomes. 78.1% of the cases are correctly classified by the model.

5.8.3. Sample excluding modified opinion cases

In six cases in the sample, the auditor did not come to an agreement with the client about the solution of the issue that was negotiated in the case. In one additional case, the respondent indicated that he expected to lose the client after the negotiation (in this case a clean opinion was given). These cases are likely to differ from the other cases in the sample in that the disagreements in these cases may be more severe than the disagreements in other cases or the partners in these cases may be tougher than other partners. To ensure that these cases do not drive the results, the regression analysis in 5.4 and the logistic regression analysis in section 5.7 are run without these seven cases. Findings from the analyses are presented in Table 29.

Table 29 - Supplementary findings: Sample excluding modified opinion cases

Panel A: Descriptive statistics

Variables	N	Minimum	Maximum	Mean	Standard deviation
ACCREGULATION	72	1	5	3.18	0.954
CLIENTACCEXP	72	1	5	2.96	0.795
AR	72	1	5	3.36	0.718
CLIENT SIZE	69	1	7	4.16	2.055
RELATIONSHIP	72	1	4	3.28	0.633
TENURE	72	1	30	7.47	6.349
AUDITOREXP	72	0	1	0.72	0.451
DIFFSTRAT	72	-5.13	7.00	1.25	2.407

Panel B: OLS-regression results

Dependent variable: DIFFSTRAT

Model 1A
(n=69)

Independent variable	Pred. Sign	Std. Coefficient	t-statistic	
ACCREGULATION	+	0.399	4.475	*
CLIENTACCEXP	-	-0.209	-2.102	***
RELATIONSHIP	-	-0.321	-3.421	**
AUDITOREXP	?	0.251	2.615	***
AR		-0.168	-1.829	
CLIENTSIZE		0.091	0.981	
TENURE		0.146	1.525	
Adjusted R^2		0.479		

* Significant at the 0.001 level (one-tailed)

** Significant at the 0.01 level (one-tailed)

*** Significant at the 0.05 level (one-tailed test for predicted relationship otherwise two-tailed)

Panel C: Logistic regression results, model 2B

Dependent variable: SOLUTION

Variables in the equation	B	S.E.	Wald	Df	Sig.	Odds ratio
ACCREGULATION	1.066	.386	7.625	1	.006	2.903
AR	.994	.448	4.929	1	.026	2.703
AUDITOREXP	1.331	.715	3.463	1	.063	3.784
DIFFSTRAT	.295	.165	3.169	1	.075	1.343
Constant	-8.104	2.306	12.347	1	.000	.000

Comparing the findings in the linear regression analysis, see Table 29, to the findings in section 5.4, we see that excluding the cases with modified audit opinions has only a small effect on the linear regression findings.

Findings from the logistic regression analysis are also reported in Table 29. The full model including all four predictor variables is statistically significant, χ^2 (4, n=72) =28.742, $p < 0.001$. The model explains between 32.9% (Cox and Snell R square) and 43.9% (Nagelkerke R square) of the variance in accounting outcome. We see that all four variables are significantly related to the accounting outcomes with a significance level of at least p=0.10 (accounting regulation p=.006; audit risk p=.026; auditor experience p=.063; and negotiation strategy p=.075). 79.2% of the cases are correctly classified by the model.

5.8.4. Skewed independent variables dichotomized

Field (2009) suggests as a rule-of-thumb that a variable should have a z-score lower than 1.96 in small samples to be approximately normally distributed. Calculating z-scores for the variables in model 1A, we see that the tenure-variable is not normally distributed and this also accounts for the relationship-variable and the size-variable (see Table 30). Even though regression analysis does not require that the independent variables are normally distributed[57],

[57] See, for example, Tabachnick and Fidell 2001, p. 119.

the regression analysis is rerun with these three variables dichotomized as a sensitivity test as several of the independent variables in Model 1 and Model 2 are not metric (see section 4.4).

Table 30 - Independent variables: z-scores

	Z-scores skewness	Z-scores kurtosis
ACCREGULATION	-1.47	-0.82
CLIENTACCEXP	0.50	-0.83
AR	-1.87	0.55
CLIENTSIZE	-0.26	-2.54
RELATIONSHIP	-3.68	3.46
TENURE	6.99	6.92
AUDITOREXP	-3.99	1.60

I test the following model:

Model 1C: Overall negotiation strategy (DIFFSTRAT) = β_0 + β_1 accounting regulation (ACCREGULATION) + β_2 clientôs accounting expertise (CLIENTACCEXP) + β_3 auditor-client relationship (RELATIONSHIPBIN) + β_4 audit partnerôs experience (AUDITOREXP) + β_5 audit risk (AR) + β_6 client size (CLIENTSIZEBIN) + β_7 tenure (TENUREBIN) + e

Table 31 - Supplementary findings: Skewed independent variables dichotomized

Panel A: Descriptive statistics

Variables	N	Number of 0s	Number of 1s	Mean	Standard deviation
RELATIONSHIPBIN	79	52	27	0.34	0.477
TENUREBIN	79	59	20	0.25	0.438
CLIENTSIZEBIN	76	40	36	0.47	0.503

Panel B: OLS-regression results

Dependent variable: DIFFSTRAT

Model 1C
(n=76)

Independent variable	Pred. Sign	Coefficient	t-statistic	
ACCREGULATION	+	0.417	4.621	*
CLIENTACCEXP	-	-0.235	-2.411	**
RELATIONSHIPBIN	-	-0.297	-3.159	**
AUDITOREXP	?	0.275	2.858	**
AR		-0.143	-1.560	
CLIENTSIZEBIN		0.077	0.808	
TENUREBIN		0.117	1.192	
Adjusted R^2		0.467		

* Significant at the 0.001 level (one-tailed)

** Significant at the 0.01 level (one-tailed test for predicted relationship otherwise two-tailed)

Notes:

ACCREGULATION	= precision of relevant accounting regulation; scale from 1 to 5
CLIENTACCEXP	= clientôs technical accounting knowledge; scale from 1 to 5
AR	= audit risk; scale from 1 to 5
CLIENTSIZEBIN	= clientsô income; 0 for categories 1, 2, 3 and 4, 1 otherwise
RELATIONSHIPBIN	= auditor-client relationship; 0 for categories 1, 2 and 3, 1 otherwise
TENUREBIN	= number of years the client has been audited by the incumbent auditor; 0 for less than 10 years, 1 for 10 years or more
AUDITOREXP	= 0 if the partner has two years of partner experience or less, 1 otherwise

We see from Table 31 above that dichotomization of the most skewed variables only has a marginal effect on findings.

5.8.5. Supplementary control variables

To investigate whether control variables other than the ones included in the regression analysis in section 5.4 should have been included in the main model, a correlational analysis is conducted to see if the following model should be tested:

> Model 1D: Overall negotiation strategy (DIFFSTRAT) = β_0 + β_1 accounting regulation (ACCREGULATION) + β_2 clientôs accounting expertise (CLIENTACCEXP) + β_3 auditor-client relationship (RELATIONSHIP) + β_4 audit partnerôs experience (AUDITOREXP) + β_5 audit risk (AR) + β_6 client size (CLIENTSIZE) + β_7 tenure (TENURE) + β_8 fee (FEE) + β_9 client profitability (PROFITABILITY) + β_{10} auditor competence (AUDITORCOMP) + β_{11} ownership (OWNERSHIP) + e

Descriptive statistics for these additional control variables are presented in Table 32.

Table 32 - Supplementary control variables: Descriptive statistics

Variables	N	Min	Max	Mean	Standard deviation
FEE	79	1	4	1.43	0.673
PROFITABILITY	78	0	1	0.65	0.479
OWNERSHIP	77	1	3	2.69	0.654
AUDITORCOMP	79	0	1	0.23	0.422

Notes:

FEE	= client fee in percentage of the auditorô total audit fees; scale from 1 to 4
PROFITABILITY	= client profitability problem; 1 if yes, 0 if no
OWNERSHIP	= 1for public clients, 2 for clients with public mother, 3 for non-public clients
AUDITORCOMP	= 0 for partner type 1 and 1 for partner type 2

Table 33 - Supplementary control variables: Spearmanôs rank order correlation

	PROFITA-BILITY	OWNER-SHIP	AUDITOR-COMP	DIFF-STRAT	SOLUTION
FEE	.039	-.062	.078	***-.220	**-.252
PROFITABILITY		-.182	***.207	-.113	.010
OWNERSHIP			**-.284	-.005	-.141
AUDITORCOMP				-.100	.026
DIFFSTRAT					*.398

* Significant at the 0.01 level (two-tailed)

** Significant at the 0.05 level (two-tailed)

*** Significant at the 0.10 level (two-tailed)

We see from Table 33 that only the fee-variable correlates with the strategy and the solution variable and the following regression model are tested:

Model 1E: Overall negotiation strategy (DIFFSTRAT) = β_0 + β_1 accounting regulation (ACCREGULATION) + β_2 clientôs accounting expertise (CLIENTACCEXP) + β_3 auditor-client relationship (RELATIONSHIP) + β_4 audit partnerôs experience (AUDITOREXP) + β_5 audit risk (AR) + β_6 client size (CLIENTSIZE) + β_7 tenure (TENURE) + β_8 fee (FEE) + e

This new model has an adjusted R-square of 50.3%, and it follows from Table 34 below that the fee variable does not have a significant impact on the negotiation strategy variable.

Table 34 - Supplementary control variables: OLS-regression results

Dependent variable: DIFFSTRAT

Model 1E
(n=76)

Independent variable	Pred. Sign	Std. Coefficient	t-statistic	Sign
ACCREGULATION	+	0.458	5.436	*
CLIENTACCEXP	-	-0.207	-2.237	***
RELATIONSHIP	-	-0.985	-3.307	**
AUDITOREXP	?	0.192	1.998	****
AR		-0.126	-1.464	
CLIENTSIZE		0.163	1.744	
TENURE		0.152	1.646	
FEE		-0.168	-1.658	
Adjusted R^2		0.503		

* Significant at the 0.001 level (one-tailed)

** Significant at the 0.01 level (one-tailed)

*** Significant at the 0.05 level (one-tailed)

**** Significant at the 0.10 level (two-tailed) with a p=0.05

I then test whether the suggested control variables have an impact on accounting outcome.

The auditor competence variable (AUDITORCOMP) and the financial condition variable (PROFITABILITY) barely correlate with the outcome variable so to limit the number of independent variables in the model these variables are excluded from further analysis (see Table 33).

To limit the number of independent variables, the variables that were found to be clearly insignificant in section 5.7 are also excluded from the model, and I test the following model:

> Model 2D: Accounting outcome* (SOLUTION) = β_0 + β_1 overall negotiation strategy (DIFFSTRAT) + β_2 accounting regulation (ACCREGULATION) + β_3 audit partner's experience (AUDITOREXP) + β_4 audit risk (AR) + β_5 ownership (OWNERSHIP) + β_6 fee (FEE) + e
>
> where Accounting outcome = 1 if Accounting outcome* >= 0 and Accounting outcome = 0 if Accounting outcome* < 0.

Findings from the logistic regression analysis are reported below. The full model including all four predictor variables is statistically significant, χ^2 (df=6, n=77) =34.976, p < 0.001. The model explains between 36.5% (Cox and Snell R square) and 48.7% (Nagelkerke R square) of the variance in accounting outcome and classifies 75.3% of the cases correctly. We see from Table 35 that four of the variables are of significant importance to the model; the accounting regulation is the only significant variable at the 5%-level (p<0.01, one-tailed), experience (p<0.10, two-tailed), audit risk (p<0.10, two-tailed) and negotiation strategy (p<0.10, one-tailed) are not significant at the 5%-level. None of the additional control variables are statistically significant.

Table 35 - Supplementary control variables: logistic regression results, model 2D

Dependent variable: SOLUTION

Variables in the equation	B	S.E.	Wald	Df	Sig.	Odds ratio
DIFFSTRAT	.276	.173	2.550	1	.110	1.318
ACCREGULATION	1.255	.405	9.591	1	.002	3.509
AUDITOREXP	1.245	.740	2.833	1	.092	3.474
AR	.736	.418	3.093	1	.079	2.087
FEE	-.340	.499	.463	1	.496	.712
OWNERSHIP	-.733	.521	1.984	1	.159	.480
Constant	-5.209	2.615	3.969	1	.046	.005

5.8.6.ò Large difference between use of the contending and the conceding negotiation strategyò ï cases excluded

It follows from the findings in section 5.6 that if the difference between the auditorǿs use of the contending and the conceding strategy is very high and positive, the accounting solution will equal the solution that is suggested by the auditor. If the difference is high and negative, the solution will equal the solution that is suggested by the client or it will be a compromise.

In the following analyses I will investigate whether the same independent variables are important if I exclude the cases with a large difference between the use of the contending and the conceding negotiation strategy from the sample.

To do this, I test model 2B with a sample size of 62, i.e. I exclude the 8 cases in Table 23 which have a negotiation strategy score in the interval [-7.00,-1.73] and the 9 cases in the interval [3.80,7.00]. Findings from the logistic regression analysis are reported below. The full model including the four predictor variables is statistically significant, ȷ ^{2} (df=4, n=62) =17.613, $p < 0.01$. The model explains between 24.7% (Cox and Snell R square) and 33% (Nagelkerke R square) of the variance in accounting outcome and classifies 69.4% of the cases correctly. We see from the Table 36 that the negotiation strategy variable is clearly insignificant.

Table 36 - Supplementary analysis: Large difference between contending and conceding negotiation strategy use

Panel A: Logistic regression results: Model 2B

Dependent variable: SOLUTION

Variables in the equation	B	S.E.	Wald	df	Sig.	Odds ratio
ACCREGULATION	1.196	.383	9.744	1	.002	3.306
AR	.741	.404	3.360	1	.067	2.098
AUDITOREXP	1.303	.775	2.829	1	.093	3.680
DIFFSTRAT	-.087	.241	.129	1	.720	.917
Constant	-5.694	1.921	8.789	1	.003	.003

Panel B: Logistic regression results: Model 2E

Dependent variable: SOLUTION

Variables in the Equation	B	S.E.	Wald	df	Sig.	Odds ratio
ACCREGULATION	1.165	.373	9.781	1	.002	3.207
AR	.750	.405	3.431	1	.064	2.117
AUDITOREXP	1.248	.749	2.776	1	.096	3.482
Constant	-5.758	1.918	9.014	1	.003	.003

I then exclude the negotiation strategy variable and test the following model:

Model 2E: Accounting outcome* (SOLUTION) = β_0 + β_1 accounting regulation (ACCREGULATION) + β_2 audit partner's experience (AUDITOREXP) + β_3 audit risk (AR) + e

where Accounting outcome = 1 if Accounting outcome* >= 0 and Accounting outcome = 0 if Accounting outcome* < 0.

Findings from the logistic regression analysis are reported in Table 36. The full model including the three predictor variables is statistically significant, χ^2 (df=3, n=62) =17.483, $p<0.01$. The model explains between 24.6% (Cox and Snell R square) and 32.8% (Nagelkerke R square) of the variance in accounting outcome and classifies 72.6% of the cases correctly.

If the latter model is combined with the finding that very low/very high values on the negotiation strategy variable give complete information about the solution in these cases, we have a two-step model that is able to correctly classify 78.5% of the cases. This is only slightly better than the main model (one-step) in section 5.7.

To summarize: we see that the supplementary analyses seem to support the main findings from the analyses in section 5.4 and 5.7. The main findings of the thesis will be discussed further in the chapter conclusion.

6.0. DISCUSSION AND CONCLUSIONS

6.1. Introduction

This dissertation was designed to study the impact of four variables: the precision of accounting regulation, the clientôs technical accounting knowledge, the auditor-client relationship and the audit partnerôs experience in auditor-client negotiations over accounting issues. The impact of the variables is studied both in the negotiation process and in relation to the accounting outcome that results from the negotiation.

In this chapter I summarize and discuss the dissertationôs main findings and its contribution to audit negotiation theory. I then discuss the contribution of the thesis to the methodology of survey research in auditing and conclude with its implications for audit practitioners, auditing regulators and future research.

6.2. Contribution to theory

The impact of the precision of accounting regulation

The dissertationôs first hypothesis suggests that there exists a positive relationship between the precision of accounting regulation and the auditorôs combined use of the contending and the conceding negotiation strategy. The overall negotiation strategy is *more* contending the more precisely regulated the accounting issue is. We see from Table 18 that the relationship is positive ($t=5.468$; $p<0.001$) and statistically significant.

The finding is in line with prior research on the effects of audit regulation on *accounting outcomes* in auditor-client negotiations: with more precise regulation there is less to discuss and the accounting solution has a tendency to be in accordance with what the auditor suggests.

Even though accounting regulation is included in many auditor-client conflict studies, none of the auditor-client *negotiation* studies have included this presumably very important variable.

My study contributes to accounting theory by directly measuring that the precision of accounting regulation is related to how the auditor behaves: the less subjective accounting regulation, the more contending is the auditorøs overall negotiation strategy.

Because accounting regulation is measured as the respondentøs subjective understanding of the accounting regulation, the respondentøs type of partnership (the participating audit firm has a system with two levels of partnership) was included in the analysis to control for a possible competence effect. No such effect was found (see section 5.8.5).

The impact of the auditor-client relationship

The dissertationøs second hypothesis suggests that there is a negative relationship between the quality of the auditor-client relationship and the auditorøs combined use of the contending and the conceding negotiation strategy. The overall negotiation strategy is *more* contending the less positive the relationship is, and we see from Table 18 that the relationship is negative (t=-3.144; p<0.01) and statistically significant.

According to the respondents in the studies of Gibbins et al. (2001 and 2007), the quality of the auditor-client relationship is one of the most important contextual variables in auditor-client negotiations over accounting issues. In an experimental study, however, Gibbins et al. (2010) do not find that the relationship quality has a significant impact on auditorsô strategy selection. Consequently my study is the first to measure that auditor behavior in negotiations is related to the quality of the auditor-client relationship.

The impact of the audit partnerøs experience

The dissertationøs third hypothesis suggests that there is a relationship (no direction is specified) between the audit partnerøs experience and the auditorøs combined use of the contending and the conceding negotiation strategy. We see from Table 18 that the relationship is positive (t=3.455; p<0.01) and statistically significant: the overall negotiation strategy is more contending the more partner experience possessed by the auditor.

Prior findings on the impact of experience in auditor-client negotiations over accounting issues indicate that experience has an effect on auditorôs choice of negotiation strategy, and Brown and Johnstone (2009) find that task experience is a better measure than years of experience when studying the effect of negotiation experience. Prior studies include both partners and managers. My approach to the study of auditor experience is that I study whether the behavior of newly appointed partners differs from the behavior of more experienced partners. Consequently I use a binary measure for auditor experience and find that auditors who recently have received the partnership (less than three years of partner experience) seem to care more about the clientôs wishes and expectations than do auditors with more partner experience, thus indicating that a new partner needs a few years of experience to become fully accustomed to his new role.

My findings differ from the findings in Bame-Aldred and Kida (2007) and Brown and Johnstone (2009) in that I find that a general dichotomous experience measure (years since inception of partnership) is related to auditor-client negotiation behavior and that this measure correlates more with the auditorôs negotiation behavior than a task-specific measure of auditor negotiation experience when both measures are dichotomized.

The impact of the clientôs accounting competence

The dissertationôs fourth hypothesis suggests that there is a negative relationship between the clientôs technical accounting knowledge and the auditorôs combined use of the contending and the conceding negotiation strategy. The overall negotiation strategy is more contending when the client has less technical accounting knowledge. We see from Table 18 that the relationship is negative ($t=-2.460$; $p<0.01$) and statistically significant.

According to Gibbins et al. (2007), the clientôs accounting competence is one of the most important variables in auditor-client negotiations over accounting issues, but this variable has not been included in prior experimental or archival auditor-client conflict or negotiation studies; consequently my findings contribute to the accounting theory in this area.

Importance of contextual variables

The analysis in section 5.5 shows that the precision of accounting regulation is by far the most important variable followed by ñthe auditor-client relationshipò, ñthe audit partnerôs experienceò, and ñthe clientôs accounting expertiseò (see also Table 18).

A model predicting negotiation accounting outcomes

In addition to contributing to the understanding of which contextual variables are related to the auditorôs choice of negotiation strategies, the study intends to use the data collected in the questionnaire to test a model that can be used to predict accounting outcomes in auditor-client negotiations over accounting issues and provide knowledge on which variables are the most important.

Logistic regression analysis indicates that the precision of the accounting regulation of the issue ($p<0.001$), the auditorôs experience ($p<0.05$), the auditorôs use of negotiation strategy ($p=0.062$) and the clientôs audit risk ($p<0.05$) are the most important variables if one aims at predicting the accounting outcome in auditor-client negotiations over accounting issues (see Table 25). Prior research (see Table 4) suggests that a number of different variables have an impact on the accounting outcomes of negotiation and/or audit conflicts; my contribution is to identify the most important ones.

The main analyses use a measure of the auditorôs overall negotiation strategy that includes a composite measure of the contending strategy composed of five different statements that intend to measure different aspects of an auditorôs behavior. An alternative measure is tested in one of the supplementary analyses (see section 5.8.1). This alternative measure is based on the respondentsô agreement with the statement ñI was firm in pursuing my position.ò Whereas this statement is an indirect measure of auditor behavior, it is likely that when it is used in isolation it more directly measures the auditorôs goal commitment. The analysis indicates that this alternative measure of the auditorôs overall negotiation strategy is a better predictor variable than the variable that is used in the main analysis. As my study intends to focus on auditor negotiation behavior, the alternative measure is used only in the supplementary analyses section. The implication of this finding for future research is discussed in section 6.4.

6.3. Contribution to methodology

My study is the first auditor-client negotiation study that combines the use of a structured questionnaire and hypotheses testing: consequently, it contributes to auditor-client negotiation research by providing knowledge on how auditors perceive a negotiation that has occurred (i.e. including the real client pressure that exists in such negotiations) rather than providing knowledge on how auditors think they will behave in a hypothetical negotiation.

Due to its perceived objectivity, critics will question why negotiation outcome is not the preferred measure when studying auditor-client negotiations. Several reasons can be given. First, it should be noted that in a questionnaire-based study, accounting outcome is not a more objective measure than auditorsô negotiation strategy. Auditorsô initial opinion on the issue is normally not documented (and if documented, access to the documentation is likely to be difficult to obtain). Consequently, the answers to questions on accounting outcome are not more objective than answers to questions on negotiation strategy. Second, when data is collected after the negotiation is finished, auditors who conceded only a little, auditors who feel that conceding in the situation was politically incorrect or auditors who did not have a clear opinion when the negotiation began are all likely to check off that the final solution is identical to the auditorõs initial opinion as they compromised ñonly a littleò. Third and as emphasized previously, in order to improve auditorsô negotiation judgments and decisions, knowledge about how such negotiations take place is imperative.

As auditors have incentives not to report truthfully on questions related to the final negotiation outcome, future questionnaire-based research should attempt to develop new ways to measure accounting outcome in order to overcome this problem as much as possible. One possibility is to use a scale-based measurement that is more in line with the scale used in this study for measuring negotiation strategy.

6.4. Implications for practitioners, regulators and future research

My study indicates that auditorsô approaches to an audit of different issues vary according to how precisely the accounting of the issue is regulated (see section 5.4). Consequently and as emphasized by Ng and Tan (2003), accounting regulation seems to have a function as bargaining ammunition on behalf of the auditor. Auditors seem to possess more authority when accounting issues are precisely regulated. My study also shows that auditors are less frequently persuaded by the client when an issue is precisely regulated (see section 5.7).

Because accounting regulation to an increasing extent requires the use of fair value in the financial statements, accounting has in recent years increasingly become more subjective, and as a consequence, it is likely that we, all other factors equal, have envisioned a shift in power from the auditor to the client. More competent auditors can be a way *to mitigate* this weakened authority of the auditor. (In the same period, audit scandals and regulatory development are likely to have enlarged the auditorôs power base). My study indicates that negotiation experience is particularly important, and my findings suggest that it may be necessary to have mechanisms in place to safeguard the quality of negotiation decisions made by new partners.

My study also indicates that auditors may need to be more aware of how auditor-client negotiations over accounting issues are colored by the extent to which the auditor likes and trusts the client. The association between the quality of the auditor-client relationship and the auditorôs choice of negotiation strategy is not necessarily negative, for a high quality relationship typically will occur when clients take their accounting seriously; but because the quality of the auditor-client relationship does not always correlate positively with risks, auditors ought at least to be aware of how the perceived relationship quality may have an impact on their behavior.

One of the aims with this thesis has been to provide knowledge about how auditors *behave* when they are involved in auditor-client negotiations over accounting issues, using a set of statements developed by Gibbins et al. (2010) to measure auditorsô use of different negotiation strategies. Findings indicate that auditors use the different contending tactics to varying extents depending upon the negotiation context. As the statements are relatively ñvagueò in their formulation, it is, however, a question whether the statements measure auditor behavior or the auditorsô ñmotivational orientationò during the conflict, i.e. a variable that corresponds to Kadous et al.ôs (2003) variable ñdirectional goal commitmentò. As emphasized previously, this difference is not crucial for my project, and is, perhaps first of all, a question of terminology. An alternative understanding of my project could be to interpret negotiation strategy as a behavioral intention variable and accounting outcome as a measure of manifested behavior. It should also be noted that this issue of construct validity seems to be more important when using the alternative measurement of strategy suggested in section 5.8.1. Nevertheless, a suggestion for future research is to clarify the distinction between intentions/motivational orientation and behavior and focus on measuring what auditors *really do* when they negotiate.

REFERENCES

Antle, R., and B. Nalebuff. 1991. Conservatism and auditor-client negotiations. *Journal of Accounting Research* 29 (Suppl.): 31-54.

Ashton R. H. and A. H. Ashton. 1995. Perspectives on judgment and decision-making research in accounting and auditing. In Ashton R. H. and A. H. Ashton. (ed.), *Judgment and Decision-Making Research in Accounting and Auditing*: 3-25. New York, NY: Cambridge University Press.

Bamber, E. M. and V. M. Iyer. 2007. Auditorsô Identification with Their Clients and Its Effect on Auditorsô Objectivity. *Auditing: A Journal of Practice & Theory* 26 (2): 1-24.

Bame-Aldred, C. W., and T. Kida. 2007. A comparison of auditor and client negotiation decisions. *Accounting, Organizations and Society* 32 (6): 497-511.

Barron, O., J. Pratt, and J. D. Stice. 2001. Misstatement Direction, Litigation Risk, and Planned Audit Investment. *Journal of Accounting Review* 39 (3): 449-462.

Beattie, V., R. Brandt, and S. Fearnley. 2000. Behind the Audit Report: A Descriptive Study of Discussions and Negotiations Between Auditors and Directors. *International Journal of Auditing* 4: 177-202.

Beattie, B., S. Fearnley and R. Brandt. 2004. A grounded theory model of auditor-client negotiations. *International Journal of Auditing* 8: 1-19.

Blake, R. R. and J. S. Mouton. 1964. *The managerial grid.* Houston: Gulf

Blokdijk, H., F. Drieenhuizen, D. A. Simunic and M. T. Stein. 2006. An Analysis of Cross-Sectional Differences in Big and Non-Big Public Audit Firmsô Audit Programs. *Auditing: A Journal of Practice & Theory* 25 (1): 27-48.

Bonner, S. E. and B. L. Lewis. 1990. Determinants of Auditor Expertise. *Journal of Accounting Research* 28 (Suppl.):1-20.

Bonner, S. E. and P. L. Walker. 1994. The Effects of Instruction and Experience on the Acquisition of Auditing Knowledge. *The Accounting Review* (January): 157-178.

Bonner, S. E. 1999. Judgment and Decision-Making Research in Accounting. *Accounting Horizons* 13 (4): 385-398.

Braun, K. W. 2001. The Disposition of Audit-Detected Misstatements: An Examination of Risk and Reward Factors and Aggregation Effects. *Contemporary Accounting Research* 18 (1): 71-99.

Brown, H. L., and K. M. Johnstone. 2009. Resolving Disputed Financial Reporting Issues: Effects of Auditor Negotiation Experience and Engagement Risk on Negotiation Process and Outcome. *Auditing: A Journal of Practice & Theory* 28 (2): 65-92.

Brown, H. L. and A. M. Wright, 2008. Negotiation research in auditing. *Accounting Horizons* 22 (1): 91-109.

Brown-Liburd, H. L. and A. M. Wright. 2011. The effect of Past Client Relationship and Strength of the Audit Committee on Auditor Negotiations. *Auditing: A Journal of Practice & Theory* 30 (4): 51-69.

Brown-Liburd, H. L., J. Cohen and G. Trompeter. 2012. Effects of earnings forecasts and heightened professional skepticism on the outcomes of client-auditor negotiation. Working Paper. Rutgers University, Boston College and University of Central Florida.

Bruynseels, L., W.R. Knechel and M. Willekens. 2011. Auditor Differentiation, Mitigating Management Actions, and Audit-Reporting Accuracy for Distressed Firms. *Auditing: A Journal of Practice & Theory* 30 (1): 1-20.

Burgstahler, D. and I. Dichev. 1997. Earnings management to avoid earnings increases and losses. *Journal of Accounting and Economics* 24: 99-126.

Carey, P. and R. Simnett. 1996. Audit Partner Tenure and Audit Quality. *The Accounting Review* 81 (3): 653-676.

Chang, C. J. and N. - C. R. Hwang. 2003. The Impact of Retention Incentives and Client Business Risks on Auditorsô Decisions Involving Aggressive Reporting Practices. *Auditing: A Journal of Practice & Theory* 22 (2): 207-218.

Chang, C. J. and N. - C. R. Hwang. 2010. Litigation environment and auditorsô decisions to accept clientsô aggressive reporting. *Journal of Accounting & Public Policy* 29 (3): 385-398.

Dagens Næringsliv, June 3rd, 2009. DN 500 største.

DeAngelo, L. 1981. Auditor independence, ñlow-ballingò, and disclosure regulation. *Journal of Accounting and Economics* 3 (August): 113-127

Dopuch, N., R. R. King and R. Schwartz. 2001. An Experimental Investigation of Retention and Rotation Requirements. *Journal of Accounting Review* 39 (1): 93-117.

Farmer, T., L. Rittenberg and G. M. Trompeter. 1987. An Investigation of the Impact of Economic and Organizational Factors on Auditor Independence. *Auditing: A Journal of Practice & Theory* 7(1): 1-14.

Field, A. 2009. *Discovering statistics using SPSS*. 3rd ed. Los Angeles: Sage.

Friedman, R. A., S. T. Tidd, S. C. Currall, and J. C. Tsai. 2000. What goes around comes around: The impact of personal conflict style on work conflict and stress. *The International Journal of Conflict Management*. 11(1): 32-55.

Fu, H., H.-T. Tan and J. Zhang. 2011. Effect of Auditor Negotiation Experience and Client Negotiation Style on Auditorsô Judgments in an Auditor-Client Negotiation Context. *Auditing: A Journal of Practice & Theory* 30(3): 225-237.

Gendron, Y., J. Bedard and M. Gosselin. 2004. Getting Inside the Black Box: A Field Study of Practices in ñEffectiveò Audit Committees. *Auditing: A Journal of Practice & Theory* 23 (1): 153-171.

Gibbins, M., S. Salterio, and A. Webb. 2001. Evidence about auditor-client management negotiation concerning clientôs financial reporting. *Journal of Accounting Research* 39 (3): 535-563.

Gibbins, M. S, S. McCracken, and S. E. Salterio. 2005. Negotiations over accounting issues: The congruency of audit partner and chief financial officer. *Auditing: A Journal of Practice & Theory* 24 (Supplement): 171-193.

Gibbins, M. S, S. McCracken, and S. E. Salterio. 2007. The chief financial officerôs perspective on negotiations with auditor on financial reporting issues. *Contemporary Accounting Research* 24 (Summer): 387-422.

Gibbins, M. S, S. McCracken, and S. E. Salterio. 2010. The auditorôs strategy selection for negotiation with management: Flexibility of initial accounting position and nature of the relationship. *Accounting, Organizations and Society* 35 (6): 579-595.

Goodwin, J. and K. T. Trotman. 1995. Audit Judgments of Revalued Non-current Assets: The Effect of Conflicting Risks. Accounting and Business Research 25 (99): 177-185.

Goodwin, J. 2002. Auditorôs conflict management styles: An exploratory study. *Abacus* 38 (3): 378-405.

Graziano, W. G., L. A. Jensen-Campbell, and E. C. Hair. 1996. Perceiving Interpersonal Conflict and Reacting to It: The Case for Agreeableness. *Journal of Personality and Social Psychology* 70(4): 820-835.

Gul, F. 1991. Size of Audit Fees and Perceptions of Auditorsô Ability to Resist Management Pressure in Audit Conflict Situations. *Abacus* 27 (2): 162-170.

Gulliver, P. H. 1979. *Disputes and Negotiation: A Cross-Cultural Perspective*. New York: Academic Press.

Hackenbrack, K., and M. W. Nelson. 1996. Auditorôs incentives and their application of financial accounting standards. *The Accounting Review* 71 (1): 43-59.

Hatfield, R. C., C. P. Agoglia and M. H. Sanchez. 2008. Client Characteristics and the Negotiation Tactics of Auditors: Implications for Financial Reporting. *Journal of Accounting Review* 46 (5): 1183-1207.

Hatfield, R. C., R. W. Houston, C. M. Stefaniak and S. Usrey. 2010. The Effect of Magnitude of Audit Difference and Prior Client Concessions on Negotiations of Proposed Adjustments. *The Accounting Review* 85 (5): 1647-1668.

Hair, J. F. Jr., R. E. Anderson, R. L. Tatham and W. C. Black. 1998. *Multivariate Data Analysis*. 5th ed. Upper Saddle River, N. J.: Prentice-Hall.

Houghton, C. and J. Fogarty. 1991. Inherent risk. *Auditing: A Journal of Practice & Theory* 10 (Spring): 1-21.

Icerman, R. C. and W. A. Hillison. 1991.Disposition of Audit-Detected Errors: Some Evidence on Evaluative Materiality. *Auditing: A Journal of Practice & Theory* 10(1): 22-34.

Iversen, G. R. and H. Norpoth. 1987. *Analysis of Variance*. Second edition. Newbury Park: Sage Publications.

Iyer, V., and D. Rama. 2004. Clientôs expectations on audit judgments: A note. *Behavioral Research in Accounting* 16: 63-74.

Jenkins, J. G. and C. M. Haynes. 2003. The Persuasiveness of Client Preferences: An Investigation of the Impact of Preference Timing and Client Credibility. *Auditing: A Journal of Practice & Theory* 22(1): 143-154.

Joe, J., A. Wright and S. Wright. 2011. The Impact of Client Misstatement Characteristics on the Disposition of Proposed Audit Adjustments. *Auditing: A Journal of Practice & Theory* 30(2): 103-124.

Kadous, K., J. Kennedy, and M. Peecher. 2003. Auditorsô judgments of the acceptability of client-preferred accounting methods. *The Accounting Review* 78 (July): 759-778.

Kaplan, S. E., E. F. OôDonnell, and B. M. Arel. 2008. The Influence of Auditor Experience on the Persuasiveness of Information Provided by Management. *Auditing: A Journal of Practice & Theory* 27(1): 67-83.

Kipnis, D. and S. M. Schmidt. 1980. Intraorganizational Influence Tactics: Explorations in Getting Oneôs Way. *Journal of Applied Psychology* 65(4): 440-452.

Knapp, M. C. 1985. Audit conflict: An empirical study of the perceived ability of auditors to resist management pressure. *The Accounting Review* 60 (2): 202-211.

Libby, R. 1981. *Accounting and human information processing: Theory and applications*. Englewood Cliffs, NJ: Prentice-Hall.

Libby, R. 1995.The role of knowledge and memory in audit judgment. In Ashton R. H. and A. H. Ashton. (ed.), *Judgment and Decision-Making Research in Accounting and Auditing*: 3-25. New York, NY: Cambridge University Press.

Lin, K. Z. and I. A. M. Fraser. 2008. Auditorsô Ability to Resist Client Pressure and Culture: Perceptions in China and the United Kingdom. *Journal of International Financial Management and Accounting* 19 (2): 161-183.

Lindsay, D. 1989. Financial Statement Usersô Perceptions of Factors Affecting the Ability of Auditor to Resist Client Pressure in a Conflict Situation. *Accounting and Finance*. November: 1-18.

Lindsay, D. 1990. An Investigation of the impact of Contextual Factors on Canadian Bankersô Perceptions of Auditorsô Ability to Resist Management Pressure. Advances in International Accounting 3: 71-85.

McCracken, S., S. E. Salterio and M. Gibbins. 2008. Auditor-client management relationships and roles in negotiating financial reporting. *The Accounting Review* 71 (1): 43-59.

McCracken, S., S. E. Salterio and R. N. Schmidt. 2011. Do Managers Intend to Use the Same Negotiation Strategies as Partners? *Behavioral Research in Accounting* 23 (1): 131-160.

Michener, H. A., J. J. Vaske, S. L. Schleiffer, J. G. Plazewski and L. J Chapman. 1975. Factors affecting concession rate and threat usage in bilateral conflict. *Sociometry* 38: 62-80.

Murnighan, J. K. and M. H. Bazerman. 1990. A Perspective on Negotiation Research in Accounting and Auditing. *The Accounting Review* 65 (3): 642-657.

Neale, M. A. and M. H. Bazerman. 1985. The effects of framing and negotiator overconfidence on bargaining behaviors and outcomes. *Academy of Management Journal* 28: 34-49.

Nelson, M. W., S. D. Smith, and Z.-V. Palmrose. 2005. The Effect of Quantitative Materiality Approach on Auditorsô Adjustment Decisions. *The Accounting Review* 80 (3): 897-920.

Ng, T. B. P., and H.-T. Tan. 2003. Effects of Authoritative Guidance Availability and Audit Committee Effectiveness on Auditorôs Judgments in an Auditor-Client Negotiation Context. *The Accounting Review* 78 (July): 801-818.

Ng, T. B.-P. 2007. Auditorsô Decisions on Audit Differences that Affect Significant Earnings Thresholds. *Auditing: A Journal of Practice & Theory* 26(1): 71-89.

Ng, T. B.-P., and H.-T. Tan. 2007. Effects of Qualitative Factor Salience, Expressed Concern, and Qualitative Materiality Thresholds on Auditorsô Audit Adjustment Decisions. *Contemporary Accounting Research* 24 (4): 1171-1192.

Pallant, J. 2007. *SPSS Survival Manual.* Berkshire: McGraw-Hill Open University Press.

Pedhazur, E. J. and L. Pedhazur Schmelkin. 1991. *Measurement, Design and Analysis: An Integrated Approach.* New Jersey: Lawrence Erlbaum Associates Inc.

Perreault, S. and T. Kida. 2011. The relative effectiveness of persuasion tactics in auditor-client negotiations. *Accounting, Organizations and Society* 36 (8): 534-547.

Popper, K. 1959. *The logic of Scientific Discovery.* London: Hutchinson.

Pruitt, D. G., and P. J. D. Carnevale. 1993. *Negotiation in Social Conflict.* Pacific Grove, CA: Brooks/Cole. Evn Open University Press.

Rahim, M. A. 1983. A measure of styles of handling interpersonal conflict. *Academy of Management Journal* 26(2): 368-376.

Rahim, M. A. and N. R. Magner. 1995. Confirmatory Factor Analysis of Handling Interpersonal Conflict: First-Order Factor Model and Its Invariance Across Groups. *Journal of Applied Psychology* 80(1): 122-132.

Raiffa, H. 1982. *The Art and Science of Negotiation.* Cambridge, MA: Harvard University Press.

Robinson, C. and L. Fertuck. 1985. *Materiality: An Empirical Study of Actual Auditor Decisions.* Research Monograph Number 12. Vancouver, British Columbia: The Canadian Certified General Accountantsô Research Foundation.

Salterio, S. 1996. The Effects of Precedence and Client Position on Auditorsô Financial Accounting Policy Judgment. *Accounting, Organizations and Society* 21 (5): 467-486.

Salterio, S., and L. Koonce. 1997. The Persuasiveness of Audit Evidence: The Case of Accounting Policy Decisions. *Accounting, Organizations and Society* 22 (6): 573-587.

Sanchez, M., and C. P. Agoglia, and R. C. Hatfield. 2007. The role of auditor strategy in auditor-client negotiations over proposed financial statement adjustments. *The Accounting Review* 82 (1): 241-263.

Savage, G. T., J. D. Blair, and R. L. Sorenson. 1989. Consider Both Relationships and Substance When Negotiating Strategically. *The Academy of Management Executive* 3 (1): 37-48.

Shadish, W. R., Cook, T. D. and D. T. Campbell. 2002. *Experimental and Quasi-Experimental Designs for Generalized Causal Inference*. Boston: Houghton Mifflin Company.

Shafer, W. E., R. E. Morris, and A. A. Ketchand. 1999. The Effects of Formal Sanctions on Auditor Independence. *Auditing: A Journal of Practice & Theory* 18 (Suppl.): 85-101.

Tabachnick, B. G. and L. S. Fidell. 2001. *Using Multivariate Statistics. 4th ed.* Boston: Allyn & Bacon.

Tan, H.-T. and K. T. Trotman. 2010. Effects of the Timing of Auditorsô Income-Reducing Adjustment Concessiopns on Financial Officersô Negotiation Judgments. *Contemporary Accounting Research* 27 (4): 1207-1239.

Thomas, K. W. 1976. Conflict and conflict management. In M. Dunnette (ed.), *Handbook of industrial and organizational psychology*: 889-935. Chicago: Rand McNally.

Thompson, L. 1990. An examination of naive and experienced negotiators. *Journal of Personality and Social Psychology* 59 (July): 82-90.

Thompson, L. and D. Hrebec. 1996. Lose-lose Agreements in Interdependent Decision Making. *Psychological Bulletin.* 120 (3): 396-409.

Trompeter, G. 1994. The Effect of Partner Compensation Schemes and Generally Accepted Accounting Principles on Audit Partner Judgment. *Auditing: A Journal of Practice & Theory* 13 (2): 56-68.

Trotman, K., A. Wright, and S. Wright. 2005. Auditor negotiations: An examination of the efficacy of intervention methods. *The Accounting Review* 80 (1): 349-367.

Trotman, K., A. Wright, and S. Wright. 2009. An Examination of the Effects of Auditor Rank on Pre-Negotiation Judgments. *Auditing: A Journal of Practice & Theory* 28 (1): 191-203.

Tsui, J. and F. Gul. 1996. Auditorsô behavior in an audit conflict situation: a research note on the role of locus of control and ethical reasoning. *Accounting, Organizations and Society* 21 (1): 41-51.

Wang, K. J. and B. M. Tuttle. 2009. The impact of auditor rotation on auditor-client negotiation. *Accounting, Organizations and Society* 34 (2): 222-243.

Windsor, C. A. and N. M. Ashkanasy. 1995. The Effect of Client Management Bargaining Power, Moral Reasoning Development, and Belief in a Just World on Auditor Independence. *Accounting, Organizations and* Society 20 (7/8): 701-720.

Wright, A. and S. Wright. 1997. An examination of factors affecting the decision to waive audit adjustments. *Journal of Accounting, Auditing & Finance* 12 (1): 15-36.

Appendix 1 - Questionnaire

AUDITORS AND THEIR RESPONSE TO DIFFICULT ACCOUNTING ISSUES[58]

This research project is related to audits in which *difficult* accounting measurement or valuation issues with a *potentially material impact* to the financial statements arose. ñDifficultò means that there was *an initial difference of opinion* between you and your client about the appropriate accounting. Most studies in this area are made on experimental data and studies on real data will therefore contribute to our understanding of the judgments auditors really make.

The study has a particular focus on what auditors do when they experience such difficult accounting issues. To successfully be able to analyze this, a number of questions are included in part B which at first sight may seem very similar. This is a consequence of the research design used in the project, and as a consequence it is important that you read all questions and statements carefully.

Enclosed to this introductory letter you will find 3 questionnaires and I ask you to complete these for three different clients. Completion of these three questionnaires will take in total between 45 and 60 minutes. It is not necessary for all the questionnaires to be filled in at the same occasion; you may well answer them one at a time if that is more convenient for you. It is important that you do not discuss the questionnaire with any of your colleagues, if you have any questions, please do not hesitate to contact the researcher. When you have answered one of the questionnaires, please put it in an envelope and seal it. When all questionnaires are filled in, they should be delivered in a large sealed envelope to: nn.

In this study you are asked to identify to yourself the three of your clients (for whom you are the engagement leader) which generate the largest audit fee *and* with whom you experienced one or more such difficult issues, as defined above, during the 2008-audit (exclude governmental clients and clients belonging to the banking and insurance industry).

[58] This appendix is a translation of the questionnaire that was used when collection data in 2010. The layout in the translation differs slightly from the layout in the original questionnaire due to differing lengths of words etc.

If you did not experience such difficult accounting issues with any of your clients in 2008 (or you experienced it with less than three clients), you may include audits from previous years among the clients about which you fill in the questionnaires.

If you experienced more than one difficult accounting issue with any of the identified clients, please answer the questionnaire with the issue that potentially could have the largest monetary impact for the financial statements in mind.

Your response will be very valuable as the utility of the study requires a high response rate. Thank you in advance for your contribution! If you want a summary of the findings of the study please send an e-mail the researcher: (ellen.kulset@nhh.no).

Regards,
Ellen M. Kulset
Research scholar, NHH

The following part was included in the letter from the Head of the audit firm accompanying the questionnaire:

ñThe questionnaire is developed in cooperation with the central consultation unit of <audit firm>. The study is anonymous and all responses will be kept strictly confidential. The questionnaire is developed solely for the purpose of this study and the responses will be destroyed when the study is completed. All responses will be publicized only in an aggregated formatò.

PART A. INFORMATION ABOUT THE ACCOUNTING ISSUE

1. For your own reference, please write a title that will identify the issue to you but will not identify you or your client to us

   ____
   ____

2. Please give a verbal description of the issue you and your client disagreed about such as ñWe disagreed about the size of the allowance for bad debtsò or ñI could not accept the recognition of income related to a large contract without more informationò etc. Please be as specific as possible in your description (include important journal entries).

   ____
   ____
   ____
   ____

3. Why did the issue arise?

   ____
   ____
   ____
   ____

4. In what accounting year was the issue discussed? ___________________________

5. What accounting implications did the issue have? Please check all boxes that apply.

Income measurement	☐	Footnote disclosure	☐
Cost measurement	☐	Tax implications	☐
Balance sheet valuation	☐	Business event / transaction implication	☐
Income / balance sheet classification	☐	Contractual implications	☐

6. How material was the issue to the clientôs financial reporting? Please check all boxes that apply.
   Material by itself: (a) in the current year ☐ (b) in future years ☐

   Material in another way ☐ please specify
   ____

   Not material ☐ (if so, why was it an issue?
   ____

7. The issue could potentially:

   Decrease income / increase costs ☐ Increase income /decrease costs ☐ Have no effect on income or costs ☐

PART B. PROCESS

8. To what extent do the following statements give a proper description of what you did during the resolution process? Please answer all items and check one box for each.

   Notice that there is a distinction between a compromise and a new solution: a new solution is not a ñsplit-the differenceò-solution. An example of a new solution is a disagreement in which the auditor believes that an amount must be accounted for whereas the client is of the opinion that the amount should not be accounted. After careful studying of the accounting rules, the auditor and the client agree that the amount can be accounted for directly towards the equity.

   Also note that not all of the statements below are relevant for all types of disagreements. If a statement is not relevant for the issue you describe in this questionnaire, (it is for instance unusual to be able to come up with a new solution if you and your client disagree about the size of the provision for bad debts) you are asked to cross in the box ñNo agreementò.

Degree of agreement with statement (Indicate on an 8-point scale[59] from ñNo agreementò to ñVery high agreementò)

1. I tried to satisfy the expectations of the client. / Jeg forsøkte å møte kundens forventninger.
2. I used ñgive and takeò so that a compromise could be made. / Jeg brukte ñgi og taò-strategi for å muliggjøre et kompromiss.
3. I used my ability to qualify the clientôs financial statements to obtain a resolution in my favor. /For å oppnå en løsning i min favør, ga jeg kunden beskjed om at han ikke ville få ren beretning dersom han ikke endret sin regnskapsføring.
4. I argued with the client to show them the merits of my position. / Jeg diskuterte med kunden for å vise dem fordelene ved min løsning.
5. I tried to find some middle ground to resolve this issue with the client. / Jeg forsøkte å finne en løsning som var akseptabel for både kunden og meg.
6. I used my influence to get my position accepted by the client /Jeg brukte min innflytelse som revisor for å få mitt forslag akseptert av kunden.
7. I attempted to accommodate the wishes of the client. / Jeg forsøkte å tilpasse løsningen slik at den var i samsvar med kundens ønsker.
8. I collaborated with the client to come up with a new solution acceptable to all of us. / Jeg samarbeidet med kunden for å komme opp med en ny løsning som var akseptabel for oss begge.
9. I used my expertise in accounting to influence the resolution in my favor. / Jeg brukte min regnskapskompetanse for å påvirke kunden i min favør.

[59] The scale was included in the Norwegian questionnaire with 8 boxes in which the auditor could tick with the alternatives: ñnoò ï ñvery lowò ï ñlowò ï ñlow to moderateò ï ñmoderateò ï ñmoderate to highò ï ñhighò and ñvery highò agreement with statement

10. I tried to work with the client to find new solutions to this issue that satisfied both of our expectations. /Jeg diskuterte med kunden for å finne en ny løsning som var i samsvar med begges forventninger.

11. I tried to investigate the issue further with the client to find a new solution accetable to both of us. / Jeg forsøkte å finne ut mer om regnskapsspørsmålet slik at vi kunne finne en ny løsning som var akseptabel for både kunden og meg.

12. I tried to satisfy the needs of the client. / Jeg forsøkte å tilfredsstille kundens behov.

13. I made concessions from my position to the client. / Jeg endret min løsning slik at den ble mer lik den løsningen kunden hadde foreslått.

14. I tried to bring all my concerns about this issue into the open with the client so that the issue could be resolved in the best possible way. / Jeg forsøkte å ha en åpen dialog med kunden om alle forhold av betydning for regnskapsspørsmålet slik at vi kunne finne en best mulig løsning.

15. I proposed some middle ground on this issue at some point during the process of resolving the disagreement with the client. / I løpet av prosessen foreslo jeg en kompromissløsning for å få finne en løsning på uenigheten knyttet til regnskapsspørsmålet.

16. I negotiated with the client so that a compromise could be made. / Jeg forhandlet med kunden for å komme frem til et kompromiss.

17. I was firm in pursuing my position. / Jeg holdt fast ved min egen løsning.

18. I gave in to the wishes of the client. / Jeg ga etter for kundens ønsker.

19. I tried to integrate my ideas about how to resolve this issue with the client to come up with a new solution jointly / Jeg forsøkte å kombinere våre ideer om hvordan spørsmålet kunne løses slik at kunden og jeg sammen kunne prøve å finne en ny løsning.

20. I played down the differences with the client to reach a compromise. / Jeg forsøkte å bagatellisere uenigheten med kunden for å oppnå en kompromissløsning.

PART C. AGREEMENT

9. What was the final treatment of the issue in the financial statements? Please check the one of the 6 boxes that most closely applies:

   a. Treated as the client originally desired because the client demonstrated it was in compliance with GAAP ☐

   b. Treated as the client originally desired because there was no convincing evidence the clientôs position was incorrect ☐

   c. Treated as the client originally desired for some other reason, please explain ☐
   ____
   ____

   d. Treated as the auditor originally desired ☐

   e. A compromise was found somewhere between the original positions ☐

   f. A new solution was generated in the process ☐

10. Give a supplementary verbal description of the final solution that you checked for in question 9.
    ____
    ____
    ____
    ____

11. To what extent give the accounting rules give a clear answer to what the solution had to be?

    Very low ☐ Low ☐ Neither high nor low ☐ High ☐ Very high ☐

12. What happened after the resolution? Please check one box for each item.
    a. The client received a clean audit opinion Yes ☐ No ☐
       If no, was this caused by accounting issue described in this questionnaire Yes ☐ No ☐
    b. The issue was to be considered again in subsequent years Yes ☐ No ☐
    c. You or your audit firm are likely to audit the client next year Yes ☐ No ☐
    d. The board was informed about the resolution Yes ☐ No ☐
    e. Other important post-resolution events Yes ☐ No ☐
       please describe
       ____
       ____
       ____

To solve an accounting issue, it is necessary to possess different types of knowledge. Important types of knowledge are for instance

- business knowledge (i.e. knowledge about the clientôs industry, the client itself, the clientôs suppliers etc. ñet selskaps drift, inkl kunnskap om kunder, leverandører, industri etcò
- technical accounting knowledge (i.e. knowledge about how to understand and interpret accounting standards etc.)

13. To what extent was it necessary to have technical accounting knowledge to solve the issue?

    Extremely important ☐ Very important ☐ Important ☐
    Not so important ☐ Not important at all ☐

14. To what extent did the client have this technical accounting knowledge?
    Very high ☐ High ☐ Not high nor low ☐ Low ☐ Very low ☐

15. To what extent was it necessary to have business knowledge to solve the issue?
    Not important at all ☐ Not so important ☐ Important ☐
    Very important ☐ Extremely important ☐

16. To what extent did the client have this business knowledge?
    Very low ☐ Low ☐ Not high nor low ☐ High ☐ Very high ☐

PART D. CLIENT SPECIFIC DEMOGRAPHIC ITEMS.

17. How do you rate the audit risk of the client as compared to the rest of your client base?

    Very high ☐ High☐ Neither high nor low ☐ Low ☐ Very low ☐

18. How large is the audit fee on this client compared to the total audit fee generated by your clients?

    More than 50% ☐ Between 30 and 50 % ☐ Between 10 and 30 % ☐ Less than 10 % ☐

19. Please classify the client by checking all the boxes that applies:

    Public company ☐ Non-traded subsidiary of public company ☐
    Private company ☐

20. Industry: please check one box

Telecom, media and high-tech	☐
Utilities	☐
Shipping	☐
Oil and gas	☐
Manufacturing	☐
Merchandising	☐
Other	☐, please specify

21. Please estimate the clientôs size (will not be used to identify client):

Annual revenue:	Less than 10 million NOK	☐
	Between 10 million and 50 million NOK	☐
	Between 50 million and 100 million NOK	☐
	Between 100 and 500 million NOK	☐
	Between 500 million NOK and 1000 million NOK	☐
	Between1000 million NOK and 3000 million NOK	☐
	More than 3000 million NOK	☐
Total assets:	Less than 50 million	☐
	Between 50 and 100 million	☐
	Between 100 and 500 million	☐
	More than 500 million	☐

22. Did the industry experience problems with profitability in 2008? Yes ☐ No ☐

23. Did you need to consider managements plans to mitigate
GC-problems during the 2008-audit Yes☐ No☐

24. How large was the clientôs reported profit as % of income last year

Negative ☐ Approx. 0 ☐ Positive but smaller than 5% ☐ Between 5 and 10% ☐
Larger than 10 % ☐

25. To what degree did client management use an aggressive reporting strategy?

Very high ☐ High ☐ Neither high nor low ☐ Low ☐ Very low ☐

26. Indicate the degree to which you agree with the following statements

a. The clientôs top management has a strong sense of justice

Disagree strongly ☐ Disagree ☐ Neither disagree nor agree ☐
Agree ☐ Agree strongly☐

b. I never have to wonder whether the clientôs top management will stick to its word

Disagree strongly ☐ Disagree ☐ Neither disagree nor agree ☐
Agree ☐ Agree strongly ☐

c. The clientôs top management tries hard to be fair in dealings with others

Disagree strongly ☐ Disagree ☐ Neither disagree nor agree ☐
Agree ☐ Agree strongly ☐

d. The clientôs top managementôs actions and behaviors are not very consistent

Disagree strongly ☐ Disagree ☐ Neither disagree nor agree ☐
Agree ☐ Agree strongly ☐

e. I like the clientôs top managementôs values

Disagree strongly ☐ Disagree ☐ Neither disagree nor agree ☐
Agree ☐ Agree strongly ☐

f. Sound principles seem to guide the clientôs top managementôs behavior

Disagree strongly ☐ Disagree ☐ Neither disagree nor agree ☐
Agree ☐ Agree strongly ☐

PART E. INFORMATION ABOUT THE AUDIT OF THIS CLIENT

27. How do you rate your relationship with the client compared to your relationship with your other clients?

A lot better ☐ Better ☐ Neither better nor worse ☐ Worse ☐ A lot worse ☐

28. How long have you been the audit partner on this engagement? ______years

29. How long has the company been a client with <audit firm>

PART F. INFORMATION ABOUT THE AUDITOR

30. With how many of your clients do you normally experience ñdifficultò issues, as defined in the introduction, during an accounting year? ____________________ clients

31. How long have you been partner in the < audit firm >? _____________

32. How many years of audit experience do you have? ________________

33. How many clients do you have? ________________________

34. How many of your clients have an audit fee above NOK 500.000?

____

35. Are you an international partner in the <audit firm>? Yes ☐ No ☐

CONCLUDING REMARKS

If you have any concluding remarks, please give these below.

Appendix 2 - Descriptive statistics: frequency tables for negotiation statements used in the thesis

s1

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	0	7	8.9	8.9	8.9
	1	8	10.1	10.1	19.0
	2	12	15.2	15.2	34.2
	3	11	13.9	13.9	48.1
	4	18	22.8	22.8	70.9
	5	9	11.4	11.4	82.3
	6	14	17.7	17.7	100.0
	Total	79	100.0	100.0	

s3

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	0	27	34.2	34.2	34.2
	1	9	11.4	11.4	45.6
	2	7	8.9	8.9	54.4
	3	2	2.5	2.5	57.0
	4	8	10.1	10.1	67.1
	5	6	7.6	7.6	74.7
	6	8	10.1	10.1	84.8
	7	12	15.2	15.2	100.0
	Total	79	100.0	100.0	

s4

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	0	8	10.1	10.1	10.1
	1	2	2.5	2.5	12.7
	2	1	1.3	1.3	13.9
	3	1	1.3	1.3	15.2
	4	12	15.2	15.2	30.4
	5	20	25.3	25.3	55.7
	6	24	30.4	30.4	86.1
	7	11	13.9	13.9	100.0
	Total	79	100.0	100.0	

s6

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	0	9	11.4	11.4	11.4
	1	3	3.8	3.8	15.2
	2	4	5.1	5.1	20.3
	3	3	3.8	3.8	24.1
	4	10	12.7	12.7	36.7
	5	17	21.5	21.5	58.2
	6	20	25.3	25.3	83.5
	7	13	16.5	16.5	100.0
	Total	79	100.0	100.0	

s7

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	0	13	16.5	16.5	16.5
	1	12	15.2	15.2	31.6
	2	21	26.6	26.6	58.2
	3	9	11.4	11.4	69.6
	4	15	19.0	19.0	88.6
	5	3	3.8	3.8	92.4
	6	6	7.6	7.6	100.0
	Total	79	100.0	100.0	

s9

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	0	2	2.5	2.5	2.5
	1	4	5.1	5.1	7.6
	2	2	2.5	2.5	10.1
	4	7	8.9	8.9	19.0
	5	19	24.1	24.1	43.0
	6	28	35.4	35.4	78.5
	7	17	21.5	21.5	100.0
	Total	79	100.0	100.0	

s12

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	0	7	8.9	9.0	9.0
	1	11	13.9	14.1	23.1
	2	7	8.9	9.0	32.1
	3	7	8.9	9.0	41.0
	4	24	30.4	30.8	71.8
	5	5	6.3	6.4	78.2
	6	16	20.3	20.5	98.7
	7	1	1.3	1.3	100.0
	Total	78	98.7	100.0	
Missing	System	1	1.3		
Total		79	100.0		

s13

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	0	21	26.6	26.9	26.9
	1	19	24.1	24.4	51.3
	2	18	22.8	23.1	74.4
	3	6	7.6	7.7	82.1
	4	8	10.1	10.3	92.3
	5	6	7.6	7.7	100.0
	Total	78	98.7	100.0	
Missing	System	1	1.3		
Total		79	100.0		

s17

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	0	11	13.9	13.9	13.9
	1	1	1.3	1.3	15.2
	2	1	1.3	1.3	16.5
	3	1	1.3	1.3	17.7
	4	13	16.5	16.5	34.2
	5	13	16.5	16.5	50.6
	6	23	29.1	29.1	79.7
	7	16	20.3	20.3	100.0
	Total	79	100.0	100.0	

s18

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	0	27	34.2	34.6	34.6
	1	32	40.5	41.0	75.6
	2	7	8.9	9.0	84.6
	3	3	3.8	3.8	88.5
	4	6	7.6	7.7	96.2
	5	2	2.5	2.6	98.7
	7	1	1.3	1.3	100.0
	Total	78	98.7	100.0	
Missing	System	1	1.3		
Total		79	100.0		