

Attributes and Drivers of Audit Quality: The Perceptions of Quality Inspectors in the UK

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ABSTRACT

This study examines the UK's Audit Quality Review's quality inspectors' perceptions of attributes and drivers of audit quality. A survey questionnaire was distributed to quality inspectors with high 'performance of the audit process' and low 'client service quality' as relevant attributes for audit quality. A range of internal factors – behavioural, technical and relational – is perceived to affect audit engagements and potentially cause variation in audit quality between audits. Further, competition in the audit market and audit regulation are perceived as key contextual factors in the auditing environment affecting audit quality. Half of the quality inspectors perceived the level of audit quality in practice varies in different audit engagements. The majority highlighted the lack of challenge by the external auditors and adequacy of evidence and documentation as two key recurring issues in the inspection process. This study extends the scope of prior research by gathering perceptions of quality inspectors on a broader spectrum of attributes and drivers on audit quality that have not been previously studied in this line of research. The findings have implications for regulators and audit practitioners in monitoring and promoting audit quality in practice.

Keywords: audit quality; quality inspectors; perceptions of audit quality; audit regulation; audit inspection

INTRODUCTION

Highly publicised cases of corporate collapses and audit failures (such as Enron-Arthur Andersen and Parmalat-Deloitte and Touche and Grant Thornton) have spurred debate on the need to understand attributes and drivers of audit quality. For example, in 2004, the Institute of Chartered Accountants in England and Wales (ICAEW) initiated the Audit Quality Forum that provides a platform to discuss major factors underpinning audit quality in practice (<https://www.icaew.com/en/technical/audit-and-assurance/audit-quality-forum-aqf>). Also, the UK regulator the Financial Reporting Council (FRC) released a discussion paper: *The Audit Quality Framework* that discusses audit quality concepts and major drivers affecting audit quality (FRC 2008). More recently, the International Auditing and Assurance Standards Board (IAASB) has published an audit quality framework: *A Framework for Audit Quality: Key Elements that Create an Environment for Audit Quality* discussing various interacting elements affecting audit quality in practice (IAASB 2014). Likewise, academic research has examined various concepts and determinants affecting audit quality and mainly examined it from the perspective of the preparers and users of the financial statements, auditors and audit committee members (see Watkins, Hillison & Morecroft 2004; Francis 2011; Knechel, Krishnan, Pevzner, Shefchik & Velury 2013; Simnett, Carson & Vanstraelen 2016; for reviews of literature).

This study identifies key attributes and drivers of audit quality from the perspective of inspectors who are the members of the Audit Quality Review (AQR) in the UK.

They had a significant role in monitoring quality of audit services and recognised as a key constituent group in the auditing system. The views of the inspectors about audit quality are potentially important for two reasons. First, the ways in which inspectors conceptualise audit quality and factors affecting it are relevant for understanding the operation of inspection as part of the regulatory process. This study provides evidence regarding business, accounting and auditing environment and internal factors that may drive audit quality in practice. Second, their views may provide an indication of how good or bad audit practice is, as the inspectors have the opportunity to assess audit records that are not available to any other group apart from auditors themselves.

This paper aims to provide evidence on key attributes and drivers of audit quality perceived by quality inspectors. Further, it examines quality inspectors' views on the level of audit quality and issues arising in the audit inspection. This research seeks to address the following questions:

- RQ1: What are the most important attributes of audit quality perceived by quality inspectors?
- RQ2: Which internal and contextual factors drive audit quality in practice?
- RQ3: What is the level of audit quality in practice?
- RQ4: What are the issues that emerge in the inspection process?

This paper contributes to audit quality research in several ways. First, prior research has examined the perceptions of audit partners, preparers and users of

financial statements on audit quality attributes (see, for example, Schroeder, Solomon & Vickrey 1986; Pham, Amaria, Bui & Tran 2014; Brown, Gissel & Neely 2016). This paper adds evidence drawn from audit inspectors as a group that has not previously been examined but operates close to regulatory policy on audit quality (FRC, 2008). Evidence from the views of inspectors may add to understanding the attributes and drivers of audit quality from the perspective of those responsible for monitoring the audit services. Their views should also be considered because understanding each other's view and how one's actions may impact on others' perceptions of audit quality is critical to efforts to enhance audit quality (IAASB 2011). Second, prior behavioural research has tended to focus on the effect of the audit team, and audit firm attributes on audit quality (Carcello, Hermanson & McGrath 1992; Kilgore, Harrison & Radich 2014). This study extends the scope of the investigation by examining broader aspects attributed to audit quality including the internal and contextual factors. Third, it contributes to the growing literature on independent audit inspection that is mainly confined to the US setting. Prior research has examined audit quality and audit inspection by examining the correlation between audit oversight reports and indicators of audit quality (Gunny, Krishnan & Zhang 2007; Cohen, Dey & Lys 2008; Carcello Hollingsworth & Mastrolia 2011) or obtaining perceptions of audit clients and external auditors on audit inspection and its effect on audit quality (Lennox & Pittman 2010; Daugherty & Tervo 2010). This study extends the scope of the literature by gathering the quality inspectors' perceptions regarding attributes and drivers affecting the delivery of high audit quality services in practice.

The remainder of this paper is structured as follows. Section 2 provides a review of the literature. Section 3 outlines methodology of the study. The results are presented in section 4 while section 5 provides concluding remarks.

LITERATURE REVIEW

THEORETICAL FRAMEWORK OF AUDIT QUALITY

There is a lack of consensus on a unified definition and measurement of audit quality (FRC 2008; IAASB 2014). It may be due to different roles and expectations of the audit market participants (e.g., auditors and audit committee) (Sutton 1993) and the inability of the users of audit services to directly observe the production of the audit services (Power 1997). Consistent with the agency and contracting theory, differentiation and assessment in audit quality are affected by measures and/or factors that are observable to interest groups in the audit market (Craswell 2000).

Consequently, various approaches have been used to measure audit quality involving a combination of inputs measures (size of audit firms, audit tenure and non-audit services) linked to the audit outcomes (financial reporting quality-earnings management and accurate audit opinion) (Gul, Sun & Judy 2003; Ruiz-Barbadillo, Gomez-Aguilar & Fuentes-Barbera 2004), process measures that are related

to auditor performance (Sutton 1993; Knechel et al. 2013), and behavioural studies that capture perceptions of users and preparers of financial statements on audit quality attributes (Carcello et al. 1992; Kilgore et al. 2014). The behavioural studies assess audit quality by examining attributes perceived to be associated with audit quality (Kilgore, Radich & Harrison 2011)

A large volume of the academic research employs the definition proposed by DeAngelo (1981) in investigating audit quality, in which the concept of audit quality is related to the ability of the auditor to detect material misstatements (competence) and to report it (independence) during the course of the audit. Much of the research has focused on notions of competence and independence of auditors as a framework of analysis in examining audit quality (Duff 2009; Knechel et al. 2013). Some scholars have argued that the framework of analysis might not be sufficient to represent audit quality because it does not represent the complete spectrum of audit quality attributes (Warming-Rasmussen & Jensen 1998; Duff 2004). Equally, Francis (2004) stated that audit quality could be conceptualised as a theoretical continuum ranging from very low to very high audit that can be affected by various factors. He further stated that audit quality should be studied comprehensively by considering the people (individual auditor or audit team), audit procedures, external environment (such as audit market) and institutions related to auditing (such as the audit inspection), thus recognising broader factors affecting audit quality (Francis 2011).

Likewise, the ICAEW (2002) identifies five factors that could drive audit quality in practice: leadership, people, working practices, monitoring quality practices, and client relationships. Correspondingly, the FRC (2008) issued its Audit Quality Framework and identified multiple elements that could drive audit quality: the culture within an audit firm; the skills and personal qualities of audit partners and staff; the effectiveness of the audit process; the reliability and usefulness of audit reporting; and factors outside the control of auditors (such as interactions with audit clients and audit committees). Subsequently, the IAASB (2014) published a comprehensive framework recognising five interacting elements affecting audit quality: inputs (auditors' values, knowledge, skills and experience), process (firm's audit process, audit methodology and quality control procedures), outputs (auditor's reports to various groups), interactions (supporting roles of other key stakeholders) and contextual factors (business practices, audit regulation and financial reporting framework).

Overall, prior research and publications relevant to audit quality indicate audit quality is affected by people and internal and contextual factors that are briefly considered in the next section.

PEOPLE AND INTERNAL FACTORS AFFECTING AUDIT QUALITY

Audit quality is perceived to be affected by the people and processes involved in the production of the audit services (FRC 2008; Francis 2011). Thus, audit quality is connected

to a range of auditors' attributes including personal credibility of the auditors, auditors' scepticism, knowledge of the industry, independence, expertise, level of partner or manager attention, communication between the team and management, auditors' conformance to the auditing standards, technical skills and experience (Carcello et al. 1992; Duff 2009; Kilgore et al. 2011; Qi, Li & Tian 2015). It is suggested that these attributes are needed for the auditors to be able to identify material misstatements and form an accurate opinion on the financial statements. Prior research also suggests a broad range of internal factors affecting the production of audit and its quality. For example, proper audit planning, audit software, audit methodology, risk assessment, and quality control procedures are important attributes supporting audit quality (Schroeder et al. 1986; Sutton 1993; Eining, Donald & James 1997; Agoglia, Hatfield & Brazel 2009). In addition, internal factors within the audit firm such as training, peer review and supervision are important attributes for supporting audit quality (Meier & Fuglister 1992; Francis 2011). Various internal factors will influence the action plan, the identification of areas to be examined, the extent of the risk assessment procedures, the extent of tests of controls and substantive procedures in the audit and, subsequently, the ability of the auditors to detect material misstatements (Cohen & Hanno 2000; Richard 2006; Knechel et al. 2013).

CONTEXTUAL FACTORS AFFECTING AUDIT QUALITY

Research has examined the effect of various contextual factors on audit performance that includes audit clients and inspections regimes (Simnett et al. 2016). Studies have reported that preparers of financial statements and the auditors perceive audit quality as being a related aspect of a client's service quality including responsiveness and empathy of auditors to the client needs (Carcello et al. 1992; Behn, Carcello, Hermanson & Hermanson 1997; Sucher, Moizer & Zarova 1998; Duff 2009). Beattie, Fearnley and Hines (2011) showed audit partners rated highly factors related to an aspect of business relationships or between auditor and audit client as affecting audit quality. Nonetheless, some studies have shown a negative effect of 'client service' on audit quality by way of impairing the auditors' independence (Carmichael 2014; Coram & Robinson 2017; Meckfessel & Sellers 2017).

A notable feature in the contextual factors in auditing in recent years has been independent oversight and inspection to stimulate and reinforce audit quality (FRC, 2015, p.5; IAASB, 2013, p.40). For example, the Public Company Accounting Oversight Board (PCAOB) inspects the work of audit firms in the US, and since 2003 the AQR has exercised similar responsibilities within the FRC in the UK. The regulators perform inspection and supervision of auditors' compliance with auditing standards, impose penalties for misconduct, and require audit firms to demonstrate the effectiveness of their control systems and audit methodologies (DeFond & Lennox 2011). It is

expected that both the objective and outcome of inspection could affect the conduct of audits, the behaviour of auditors, audit firm culture and ultimately audit quality (FRC 2008; IAASB 2013; Carmichael 2014, p. 903).

Several studies have examined whether inspections lead to an improvement in audit quality. Studies report a decline in earnings management (Cohen et al. 2008; Carcello et al. 2011) and that auditors appear to be more conservative (Lobo & Zhou 2006) after PCAOB inspections, and high-quality auditors are associated with less critical inspection reports issued by the PCAOB (Gunny et al. 2007). Some research also suggests an increase in the likelihood of audit firms issuing going concern modified opinions after the PCAOB inspections (Gramling, Krishnan & Zhang 2011) and that lower quality auditors are more likely to exit the market (DeFond & Lennox 2011). Further, Stefaniak, Houston and Brandon (2017) showed that PCAOB enhances audit quality by increasing the audit effort of auditors.

On the contrary, assessment of the inspections reports by Huang and Chong (2016) showed the inspections' impediments in influencing audit quality. They identified recurring failures of the audit firms to collect sufficient and reliable audit evidence and perform an adequate internal quality review that negatively affects audit quality. A survey study has also reported that smaller US audit firms perceive that the PCAOB inspections have a negative impact on audit activities which do not contribute to the enhancement of audit quality (Daugherty & Tervo 2010). Overall, a review of prior research shows different participants perceived audit quality differently which suggests multidimensional concepts of audit quality. Also, audit quality can be affected by various factors within the audit setting. Nonetheless, far too little attention has been paid to the all-encompassing factors attributed to audit quality from the perceptions of the quality inspectors.

METHODOLOGY

RESEARCH INSTRUMENT

The research instrument was developed with close reference to the literature on questionnaire design (Bryman & Bell 2011). The questionnaire comprised six primary sections. The first section gathered personal background information related to the respondents. The second section gathered the perceptions of quality inspectors about the attributes of audit quality in practice, which are adapted from studies on perceptions of audit quality (see, Schroeder et al. 1986; Carcello et al. 1992; Duff 2009). The third section obtained views of the quality inspectors about the impact of the business, accounting and auditing environment on audit quality as identified by prior literature and publications on audit quality including changes in accounting standards, audit regulation and competition in the audit market (see, Beattie et al. 2011; Francis 2011; FRC 2008; IAASB 2011).

The fourth section examined quality inspectors' views on the effect of internal factors within accounting

firms which are framed using prior literature including audit methodology, internal reviews, consultation, audit system and training (see, Sutton 1993; Cohen & Hanno 2000). The final section obtained quality inspectors' view of the level of audit quality in practice and information of potential issues identified in the inspection process. The questionnaire was pilot-tested by reference to a senior member of the inspection unit and academic staff before it was administered to the respondents. Amendments were made to the questionnaire based on the comments and suggestion received so as to improve its validity. The questions incorporated a five-point Likert scale for responses.

SAMPLE, DATA COLLECTION AND ANALYSIS

The management of the FRC has given the researcher permission to distribute a questionnaire to the quality inspectors who comprise the inspection teams. The questionnaire was administered through a web survey to the entire population of quality inspectors which was identified as 20 individuals (AIU, 2010, pg. 13). The confidentiality of information given to the respondents was guaranteed in the introduction of the questionnaire together with the explanatory letter. A reminder email was sent two weeks after the administration of the questionnaire. Responses were received from 12 individuals, i.e. a 60% response rate. Although this provides good proportionate coverage of the quality inspector group, it is inevitably a relatively small absolute number because of the size of the inspection group. As a result, detailed statistical analysis or testing (such as differences within the sample) is restricted, and the study does not aim to test any hypothesis or examine specific cause and effect relationships. Descriptive statistics such as central tendency and dispersion (mean and standard deviation) are used to present the data collected from the survey questionnaire.

FINDINGS AND DISCUSSION

PROFILE OF QUALITY INSPECTORS

Table 1 presents information on the personal backgrounds of the group of quality inspectors. A small majority of the respondents (58%) were male, and their age ranges were relatively evenly distributed between 28-37 and 38-47 years old. Three respondents (25%) have master degrees, and the remainder held a first university degree (75%). All the respondents were professionally qualified with ICAEW.

Additional background information on the inspectors' roles and professional experience is contained in Table 1. The largest group described themselves as inspection team members, the rest indicating that their role was as team leader (25%) or both leader and member (25%). In terms of experience, 17%, 33% and 17% of the respondents had auditing experience between 5-10 years, 11-15 years, and 16-20 years, respectively, and 33% had more than 20 years' experience. Five of the 12 respondents (42%) had more

than 5 years' experience in audit inspection, while 33% and 25% had 3-5 years and less than 3 years' experience in inspection respectively.

Two-thirds of respondents indicated that they had spent more than 50% of their time reviewing the Big Four firms in the last year of inspection. Only one of the 12 respondents reported that they had spent more than 50% of their time reviewing audits of FTSE 100 companies, but other listed entities occupied more than 50% of the time of another five inspectors.

IMPORTANT ATTRIBUTES OF AUDIT QUALITY PERCEIVED BY QUALITY INSPECTORS

Quality inspectors attached more importance to the conduct or content of an audit as key attributes of audit quality (see Table 2). For this reason, the level of challenge to the management of the audit (mean 4.92) and the sufficiency of audit evidence (mean 4.92) are important attributes for the quality inspectors when assessing audit quality during the inspection process. Quality inspectors also associate high importance to attributes tied to quality control applied within the audit firm and various 'compliance' on the notion of audit quality. The inspectors view internal quality standards within the audit firm as important for audit quality: 'the work done in carrying out the audit is subject to review before the audit is completed' (mean 4.75) and 'the audit meets the quality standards applied internally by the audit firm' (mean 4.17) as linked to high audit quality. Quality inspectors see a strong link between audit quality and compliance with the ethical standards (mean 4.58), auditing standards (mean 4.42) and quality control standards (mean 4.08). Further, the quality inspectors perceived highly the relative importance of the auditor's competence and independence to audit quality (Carcello et al. 1992; Duff 2009).

A further notable feature of the results is what might be referred to as the 'client service' attributes of the audit which are scored as of relatively low importance by the inspectors. This includes attributes such as the timely completion of the audit (mean 3.58), satisfying client expectations (mean 3.00) and providing value for money (mean 2.33). Six of the lowest seven ranked items relate to such service attributes, and the lowest score of any item is the provision of additional services (mean 1.42), indicating that synergy between audit and other services is not viewed as important attributes to audit quality.

Prior research shows other key constituents of audit market such as audit clients and audit committees perceived highly a range of auditor's characteristics attributed to audit quality (Carcello et al. 1992; Kilgore et al. 2014). However, findings of this study show quality inspectors rated performance of the audit and various 'compliance' requirements as key attributes of audit quality. This is not surprising given the responsibilities of quality inspectors in assessing audit services and the ability of the quality inspectors to observe the actual delivery of audit services. Key differences are also noted between perceptions

TABLE 1. Demographic Information on Participants

	Frequency	Percent
Gender		
Male	7	58
Female	5	42
Total	12	100
Age Range		
28 – 37	4	33
38 – 47	4	33
48 – 57	3	25
Above 57	1	9
Total	12	100
Educational Level		
Bachelor degree	9	75
Master degree	3	25
Others	-	-
Total	12	100
Professional Qualification		
ICAEW	12	100
ICAS	-	-
ACCA	-	-
Other	-	-
Total	12	100
Position of Quality Inspectors		
Leader of inspection team	3	25
Member of inspection team	6	50
Both leader and member of inspection teams	3	25
Total	12	100
Auditing Experience of Quality Inspectors		
5 to 10 years	2	17
11 to 15 years	4	33
16 to 20 years	2	17
More than 20 years	4	33
None	-	-
Total	12	100
Experience in Audit Inspection		
Less than 3 years	3	25
3 to 5 years	4	33
More than 5 years	5	42
Total	12	100
Proportion of Time on Inspection of Different Types of Audit Firm		
Big four firms: More than fifty percent	8	67
Less than fifty percent	4	33
Total	12	100
Other firms: More than fifty percent	2	17
Less than fifty percent	10	83
Total	12	100
Proportion of Time on Inspection of Different Types of Audit Engagement		
FTSE 100 companies: More than fifty percent	1	8
Less than fifty percent	11	92
Total	12	100
Other listed entities: More than fifty percent	5	42
Less than fifty percent	7	58
Total	12	100
Other public interest entities: More than fifty percent	-	-
Less than fifty percent	12	100
Total	12	100

TABLE 2. Attributes of Audit Quality

Id	Attribute	Quality Inspectors (n=12)					Rank	Mean	Standard deviation
		1	2	3	4	5			
1	The auditor demonstrates an appropriate level of challenge to the management of the audit client	-	-	-	1	11	1=	4.92	0.39
2	The auditor does sufficient work to obtain sufficient evidence to support an audit opinion	-	-	-	1	11	1=	4.92	0.39
3	The work done in carrying out the audit is subject to review before the audit is completed	-	-	-	3	9	3	4.75	0.96
4	The auditor reports the correct audit opinion on the financial statements	-	-	1	2	9	4=	4.67	1.11
5	The auditor is technically competent	-	-	-	4	8	4=	4.67	1.13
6	The auditor is independent	-	-	-	4	8	4=	4.67	1.13
7	The audit is carried out in accordance with ethical standards	-	-	-	5	7	7	4.58	1.24
8	The audit work undertaken is based primarily on an assessment of the risks associated with the client's financial statements	-	-	-	6	6	8	4.50	1.28
9	The audit is carried out in accordance with auditing standards	-	-	-	7	5	9=	4.42	1.24
10	The role of the audit partner is at the centre of the audit process	-	-	-	7	5	9=	4.42	1.24
11	The audit work is determined through an appropriate planning process	-	-	2	5	5	11=	4.25	1.41
12	The auditor maintains effective communication and interaction with the audit committee	-	-	1	7	4	11=	4.25	1.11
13	The audit meets the quality standards applied internally by the audit firm	-	-	1	8	3	13=	4.17	0.92
14	The auditor maintains a high level of documentation in the completed audit files	-	-	2	6	4	13=	4.17	1.26
15	The audit is carried out in accordance with quality control standards (ISQC1)	-	1	1	6	4	15	4.08	1.32
16	The audit is valued by the audit client	-	1	3	7	1	16	3.67	1.13
17	The audit is completed in a timely manner	-	1	3	8	-	17	3.58	1.23
18	The auditor maintains a good relationship with the management of the audit client	-	3	4	5	-	18	3.17	1.65
19	The audit firm is free from negative findings in inspection reports	2	2	1	7	-	19	3.08	2.39
20	The auditor satisfies the audit client's expectations	-	6	-	6	-	20	3.00	2.56
21	The auditor provides good value for money to the audit client	2	5	4	1	-	21	2.33	1.34
22	The audit firm provides additional services in association with the audit	7	5	-	-	-	22	1.42	1.24

Notes to table:

Factors are shown in decreasing order

Response scale: 1. Little or no importance, 2. Unimportant, 3. Undecided, 4. Important, 5. Very important

High consensus (standard deviation ≤ 0.85 shown in bold) low consensus (standard deviation ≥ 1.25 shown in italics)

of quality inspectors and audit clients and auditors on attributes related to client service quality (Duff 2004; 2009). While both audit clients and auditors perceived an

aspect of client service quality as one of the most important attributes of audit quality, the quality inspectors rated it as one of the lowest.

INTERNAL AND CONTEXTUAL FACTORS DRIVE AUDIT
QUALITY IN PRACTICE

This section reports the respondents' views on internal and contextual factors affecting audit quality by investigating

the influence of internal factors within audit firms on the quality attained on audit performance (Table 3), the influence of contextual factors on audit quality (Table 4)

TABLE 3. Internal Factors Affecting Audit Quality

Id	Factor	Quality Inspectors (n=12)					Rank	Mean	Standard deviation
		1	2	3	4	5			
1	The degree of involvement of the audit engagement partner during audit planning influences the quality of the resulting audit process	-	-	1	5	6	1=	4.42	1.30
2	Technical and other consultations within the audit firm enhance the quality of judgements made during the completion of the audit	-	-	1	5	6	1=	4.42	1.30
3	Technical and other consultations within the firm during planning influence the quality of the resulting audit process	-	-	1	7	4	3=	4.25	1.11
4	Training within the audit firm enhances auditors' technical expertise	-	-	-	9	3	3=	4.25	0.96
5	Internal reviews within the audit firm enhance compliance with the technical requirements of auditing standards	-	-	2	6	4	5=	4.17	1.26
6	Effective communication from the auditor to client management influences the quality of the resulting audit process	-	-	-	10	2	5=	4.17	0.71
7	Interaction between the auditor and client management influences the quality of the resulting audit process	-	-	-	10	2	5=	4.17	0.71
8	Training within the audit firm enhances the delivery of an effective and efficient audit	-	-	1	8	3	5=	4.17	0.92
9	Audit software facilitates compliance with the technical requirements of auditing standards	-	-	1	10	11	9=	4.00	0.43
10	Risk based audit approaches facilitate the achievement of an effective and efficient audit	-	-	1	10	1	9=	4.00	0.43
11	Audit software promotes compliance with documentation requirements	-	1	-	10	1	11=	3.92	0.71
12	Internal reviews within the audit firm improve compliance with documentation requirements	-	-	2	9	1	11=	3.92	0.68
13	Audit software facilitates the achievement of an effective and efficient audit	-	1	1	9	1	13=	3.83	0.84
14	Internal reviews within the audit firm enhance the quality of audit judgements made during the audit	-	-	3	8	1	13=	3.83	0.92
15	Internal reviews within the audit firm ensure the delivery of an effective and efficient audit	-	1	3	6	2	15	3.75	1.23
16	Training within the audit firm improves auditors' ability to challenge the management of audit clients	-	-	5	7	-	16	3.58	1.24
17	Internal reviews within the audit firm enhance auditor's technical expertise	1	2	-	8	1	17=	3.50	1.75
18	Audit firm methodologies and manuals improve the quality of audit judgement applied during the audit	-	-	6	6	-	17=	3.50	1.28
19	Interaction between the auditor and the audit committee is influential in determining the content of audit work undertaken	-	2	4	5	1	19	3.42	1.41
20	Risk based audit approaches help the auditor to provide value for money to the client	-	2	5	5	-	20	3.25	1.41
21	Audit firm methodologies and manuals enhance the auditor's ability to challenge client management	1	1	6	4	-	21	3.08	1.32

TABLE 3(b). Internal Factors Affecting Audit Quality in Practice (continued)

Id	Factor	Quality Inspectors (n=12)					Rank	Mean	Standard deviation
		1	2	3	4	5			
22	Internal reviews within the audit firm ensure the auditor's independence from the audit client	-	4	4	4	-	22	3.00	<i>1.71</i>
23	Risk based audit approaches help the auditor to provide value added services to the audit client	-	4	5	3	-	23	2.92	<i>1.48</i>
24	Performance appraisal systems within audit firms increase compliance with the technical requirements of auditing standards	-	5	4	3	-	24=	2.83	<i>1.65</i>
25	Performance appraisal systems within audit firms improve compliance with documentation requirements	1	4	3	4	-	24=	2.83	<i>1.82</i>
26	Interaction between the auditor and the audit committee facilitates the correct audit opinion being reported	1	3	5	3	-	24=	2.83	<i>1.43</i>
27	Performance appraisal systems within the audit firm enhance the auditor's technical expertise	1	4	5	2	-	27	2.67	<i>1.34</i>
28	Performance appraisal systems within the audit firm improve the auditor's independence	1	5	4	2	-	28	2.58	<i>1.41</i>

Notes to table:

Factors are shown in decreasing order

Response scale: 1. Strongly disagree, 2. Disagree, 3. Neutral, 4. Agree 5. Strongly agree

High consensus (standard deviation ≤ 0.85 shown in **bold**) low consensus (standard deviation ≥ 1.25 shown in *italics*)

supported by views about the general approach to quality in audit engagements (Table 5).

Respondents were asked to indicate views concerning how a large number of behavioural, technical or relational factors that are internal to the audit firm and the audit process affect the audit quality. The role of the audit partner in audit planning is seen as having an important influence on the audit process (mean 4.42). The involvement of relevant staff within the firm through consultation was also identified as influencing the quality of audit judgements (mean 4.42) and the resulting audit process (mean 4.25). The respondents also strongly agreed that there is a positive impact from training on the technical competence of auditors (mean 4.25) and the delivery of an effective and efficient audit (mean 4.17).

Internal audit firm monitoring comprising the firm's quality review system is also perceived as being a significant influence in the conduct of an audit. The statement that 'internal reviews within the audit firm enhance compliance with the technical requirements of auditing standards' was given considerable support by the respondents (mean 4.17). The respondents also indicated that internal reviews improve compliance with the documentation standards (mean 3.92), enhance the quality of audit judgements (mean 3.83), ensure delivery of an effective and efficient audit (mean 3.75), and enhance the auditor's technical expertise (mean 3.50).

The respondents also recognised the impact of effective communication and interaction between the external auditor and the client management on the quality of the resulting audit process (both mean 4.17). Consistent with other perception studies (Schroeder et al. 1986; Chen, Shome & Su 2001), this finding highlights the

important role of the audit client in facilitating an audit. Interestingly, although the respondents perceived effective communication and interaction between auditors and the AC as key attributes of audit quality (see Table 2), the responses show less evidence regarding the actuality of the role of the AC in achieving audit quality in practice. The respondents gave relatively limited support for the statements that 'interaction between the auditor and the AC is influential in determining the content of audit work undertaken' (mean 3.42) and 'interaction between the auditor and the AC facilitates the correct audit opinion being reported' (mean 2.83). These views suggest the AC has a marginal effect on the actual conduct of the audit, and a range of issues related to reporting and communication with ACs have been consistently highlighted in the inspection reports (FRC 2015; AIU 2010).

Although one of the aims of the AQR is to see behavioural change among auditors promoted through the performance appraisal systems in the audit firm, low mean scores were given for the impact of these systems on: compliance with the technical requirements of auditing standards (mean 2.83), documentation requirements (mean 2.83), auditor's technical expertise (2.67) and auditor independence (2.58).

It is interesting to note, first, that four of the higher ranked contextual factors affecting audit quality are linked to the business of auditing or the commercial side of auditing (see Table 4). There is a consensus among the inspectors that competition in the audit market has had an impact on notions of audit quality: meeting expectations of the audit client (mean 4.00), delivering value for money (mean 4.00), the auditor-auditee relationship (mean 3.83) and providing value-added services (3.67). It is interesting

TABLE 4. Contextual Factors Affecting Audit Quality

Id	Factor	Quality Inspectors (n=12)					Rank	Mean	Standard deviation
		1	2	3	4	5			
1	Accounting standards requiring more estimation and judgements have resulted in greater need for technical expertise	-	-	3	5	4	1	4.08	<i>1.48</i>
2	Competition in the audit market has resulted in a greater focus on meeting client's expectations	-	-	3	6	3	2=	4.00	<i>1.28</i>
3	Competition in the audit market has resulted in greater emphasis being placed on delivering good value for money to the audit client	-	-	1	10	1	2=	4.00	0.43
4	The framework of audit regulation has led to greater attention to factors related to the auditor's independence from the audit client	-	1	3	4	4	4	3.92	<i>1.66</i>
5	Competition in the audit market has resulted in greater emphasis being placed on the auditor's relationship with the audit client's management	-	-	3	8	1	5	3.83	0.92
6	Competition in the audit market has resulted in greater attention being given to delivering value added services to the audit client	-	-	4	7	1	6=	3.75	1.11
7	Changes in the framework of audit regulation have led to increased emphasis on maintaining adequate audit documentation	-	2	1	7	2	6=	3.75	<i>1.42</i>
8	Factors in the auditing environment have resulted in greater reliance on consultation within the firm as part of the audit process	-	1	4	4	3	6=	3.75	<i>1.57</i>
9	The current business environment has resulted in greater reliance on risk based audit approaches	-	-	4	8	-	9	3.67	1.14
10	Changes in the framework of audit regulation have created a greater need for the auditor to demonstrate a challenge to client management	-	4	2	4	2	10	3.33	<i>2.07</i>
11	The current business environment has resulted in greater attention to audit planning	1	2	5	4	-	11	3.00	<i>1.48</i>
12	Factors in the auditing environment have resulted in extensive internal review of the audit engagements	-	6	1	5	-	12	2.92	<i>2.33</i>
13	The auditing standards are used by audit practitioners to justify doing less detailed audit work	2	3	3	3	1	13	2.83	<i>1.83</i>
14	The framework of audit regulation has led to increased focus on conducting an audit beyond the minimum requirements of auditing standards	1	4	4	3	-	14	2.75	<i>1.57</i>
15	The framework of audit regulation has resulted in less reliance on the auditor's professional judgement	3	6	2	-	1	15	2.17	<i>1.48</i>

Notes to table:

Factors are shown in decreasing order

Response scale: 1. Strongly disagree, 2. Disagree, 3. Neutral, 4. Agree 5. Strongly agree

High consensus (standard deviation ≤ 0.85 shown in **bold**) low consensus (standard deviation ≥ 1.25 shown in *italics*)

to note that the aspects of client 'service quality' are considered the least important attributes of audit quality (Table 2) while exerting significant influence on audit quality in practice.

This position is supported by the general view of quality inspectors that the approach to the audit quality is also driven by commercial values of the audit firms (Table 5). Four quality inspectors chose to indicate that commercial values influence audit approach, reflecting the effect of competition, fee pressure and slow growth

in the audit environment (Behn et al. 1997; Duff 2004) as against what might be seen as the more public interest oriented role of the audit.

Aspects of the regulation of accounting and auditing were also rated as having a high impact on audit quality by the inspectors (see Table 4). The most highly ranked factor influencing quality is the complexity of accounting standards and the technical expertise required of auditors as a result (mean 4.08). The analysis also shows strong recognition concerning the impact of audit regulation on

auditor independence (mean 3.92), audit documentation (mean 3.75) and consultation within the audit process (mean 3.75). These results concerning views on regulatory impact are also consistent with the fact that the largest group of inspectors regarded compliance as the primary driver of audit approach in practice (see Table 5).

This shows evidence of a positive behavioural impact by the AQR in driving the audit quality. Nonetheless, concerns have also been raised over the high level of recurring issues found in inspections (AIU, 2011). This issue is reflected in the lower level of support the respondents offer for the suggestion that audit regulation has led to an emphasis on going beyond the minimum requirements of standards (mean 2.75) or that contextual factors have led to extensive internal review (mean 2.92). The behavioural changes may be attributed to a reaction to the threat of inspection rather than the actuality in practice.

The respondents do not indicate that they see evidence of a negative impact from regulation on the development and approach of firms and auditors to audit quality. For example, the respondents tended to disagree (rating below 3) with the statements that: ‘the auditing standards are used by audit practitioners to justify doing less detailed audit

work’ (mean 2.83) and ‘the framework of audit regulation has resulted in less reliance on the auditor’s professional judgement’ (mean 2.17).

THE LEVEL OF AUDIT QUALITY IN PRACTICE

The majority (83%) of the inspector respondents agreed with the statement that in general, the level of quality of audits in the UK is high, indicating a relatively optimistic view regarding audit quality in practice (see Table 6). Most (67%) also agreed with the view that the quality of the audits has increased in the last decade, (25% expressed a neutral view on this issue and only one individual disagreed). Similarly, only 17% indicated a view that the quality of the audits in the UK has decreased in the last decade, 58% disagreed and 25% were undecided.

Perhaps of more significance is the fact that half of the respondents perceive that there is an inconsistency between audits in the quality of auditing achieved. The majority of the respondents agreed (either agree or strongly agree) that there is considerable variation between audits in terms of the level audit quality attained in practice. This suggests a significant variation in

TABLE 5. General Influences on the Conduct of Audits in Practice

Item	Rank of order	Number (n=12)	Percentage
The approach to the conduct of audits in practice reflects the compliance obligations placed on the public accounting firm	1	5	42%
The approach to the conduct of audits in practice reflects the commercial values of the public accounting firm	2	4	33%
The approach to the conduct of audits in practice reflects the professional values of the public accounting firm	3	3	25%

TABLE 6. General Views about Audit Quality

Id	Issue	Quality Inspectors (n=12)					Mean	Standard deviation
		1	2	3	4	5		
1	In general, the quality of auditing in the UK is high	-	1	1	10	-	3.75	0.947
2	The quality of auditing in the UK has increased during the last decade	-	1	3	8	-	3.28	1.231
3	The quality of auditing in the UK has decreased during the last decade	-	7	3	2	-	2.58	1.545
4	There is a high level of consistency between audits in the quality of auditing achieved in practice	2	4	5	1	-	2.42	1.408
5	There is considerable variation between audits in the quality of auditing achieved in practice	-	1	2	7	2	3.83	1.085
6	In general market participants perceive the standard of audit quality to be adequate	-	4	2	6	-	3.17	2.065
7	General concerns about audit quality in recent years are based on a proper understanding of the conduct of audits in practice	3	7	1	1	-	2.00	1.128

Notes to table:

Response scale: 1. Strongly disagree, 2. Disagree, 3. Neutral or no view, 4. Agree, 5. Strongly agree

High consensus (standard deviation ≤ 0.85 shown in **bold**) low consensus (standard deviation ≥ 1.25 shown in *italics*)

audit quality in different audit engagements and audit firms inspected by the AQR. The inconsistencies and variation could be due to the factors commented on in the previous section as sources of variation in quality between engagements, such as audit partners' involvement in planning, technical and other consultations within the firm, training, and internal firm quality reviews. Different audit firms will have different resources in terms of people, policies and procedures, internal processes and systems that may influence the production of the audit and its quality. The variation may also be due to the inconsistency between the policies and procedures that are established by the firm and their application in the actual conduct of auditors (AIU 2010, p. 3).

Only half of the respondents believe that the participants in the audit market perceive the standard of audit quality to be sufficient. If correct, such perceptions about auditing may legitimise the role of an independent oversight body to restore trust and confidence among the beneficiaries of audit services concerning audit quality. However, the majority of the respondents also believe that the concerns about audit quality in recent years are not based on a proper understanding of the conduct of audits in practice. One of the potential reasons for such a situation could be a lack of users' understanding of the audit function and the difficulty of making audit quality visible in any explicit way to those outside the engagement. This issue possibly indicates a lack of understanding about how audit quality is achieved in practice thereby highlighting the unclear connection between the auditors' performance of work tasks in practice and wider understanding of the notion of audit quality.

THE ISSUES THAT EMERGED IN THE INSPECTION PROCESS

Table 7 shows that the majority of the respondents stated that issues regarding the sufficiency of audit work arise frequently or always in inspections. Another significant area of potential disagreement between inspectors and auditors concerns compliance with auditing standards. Fifty percent of the respondents encounter compliance issues frequently or always occur in reviews.

There is strong agreement among the respondents that the lack of challenge posed by the external auditors to their audit client is a recurring issue. Ten out of 12 respondents stated that this issue frequently or always arises during the inspection process. The sufficiency of audit work is also one of the most common sources of the problem with all the respondents indicating that this frequently or always occurs as an issue during inspections.

Despite evidence of a number of areas where inspections regularly lead to potential doubts about aspects of audit quality, a large majority of the respondents indicated that issues concerning the audit opinion never arises or only rarely. This suggests that the principal questions that the inspection process identifies concern aspects of the process by which the audit is conducted and recorded rather than the appropriateness of the final outcome in the form of the audit opinion issued.

CONCLUSION

The quality inspectors are responsible for monitoring and ensuring the quality of the auditing services in the UK and are, therefore, well-positioned to provide information on the level of audit quality and possible factors that influence

TABLE 7. Issues Arising in the Process of Inspection

Id	Issue	Quality Inspectors (n=12)					Mean	Standard deviation
		1	2	3	4	5		
1	How often in the process of inspection do issues arise concerning the adequacy of audit documentation?	-	-	-	6	6	4.50	<i>1.28</i>
2	How often in the process of inspection do issues arise concerning compliance with auditing standards?	-	1	2	6	3	3.92	<i>1.27</i>
3	How often in the process of inspection do issues arise concerning the adequacy of the auditor's 'challenge' to management?	-	1	1	9	1	3.83	0.84
4	How often in the process of inspection do issues arise concerning the sufficiency of audit work?	-	1	2	8	1	3.75	0.99
5	How often in the process of inspection are issues that arise resolved by discussion with the audit team?	-	2	2	7	1	3.58	<i>1.41</i>
6	How often in the process of inspection do issues arise concerning compliance with ethical standards?	-	1	4	7	-	3.50	<i>1.30</i>
7	How often in the process of inspection do issues arise concerning compliance with international accounting standards (IAS)?	-	2	4	5	1	3.42	<i>1.41</i>
8	How often in the process of inspection do issues arise concerning the appropriateness of the audit opinion?	3	7	2	-	-	1.92	1.07

Notes to table:

Response scale: 1. Never, 2. Occasionally, 3. Seldom, 4. Frequently, 5. Always

High consensus (standard deviation ≤ 0.85 shown in bold) low consensus (standard deviation ≥ 1.25 shown in italics)

the operationalisation and attainment of audit quality in practice. It can be concluded that the quality inspectors perceived 'the performance of the audit processes as a key attribute of audit quality. They also appear to consider 'compliance' and 'technical' attributes of the audit of much greater importance than 'client service' attributes as relevant attributes for audit quality. A range of internal factors – behavioural, technical and relational – influence the performance of actual audit engagements and potentially cause variation in audit quality between audits. The evidence from this study suggests that audit firms may devote greater attention to these factors to ensure they deliver adequate quality as evaluated by the AQR on behalf of the financial reporting community.

Further, there is an agreement among the quality inspectors that contextual factors in the audit market – audit regulatory and the business aspects of auditing could drive the development and approach of firms and auditors with respect to audit quality. The impact of economic factors and the competition in the audit market in practice appears to be particularly strong. An implication of this is commercial concerns superseding professional values that negatively affect audit quality. Hence, recognising the dominance of commercial over professional values can result in more appropriate policy and regulatory practices to ameliorate the apparent quality risks (Meckfessel & Sellers 2017). This is an important issue for future research, namely determining the influence of a firm's business model and culture on audit quality.

This study provides evidence of possible areas of disagreement between the regulator and auditors over what constitutes adequate audit quality in the performance of individual audit engagements, and of the potential issues that affect the achievement of high audit quality in practice, at least from the perspective of the quality inspectors. The issues that create problems are the quality of the 'challenge' to management, evidence and documentation. Differences in underlying views about the concept of audit quality are likely to be manifest in issues and potential disagreements between the regulator and auditors about what constitutes adequate quality in auditors' work performance. Addressing such underlying differences is important from the perspective of both the audit profession and the regulator. Current initiatives to enhance audit quality may simply reinforce rather than resolve the issues about expectations and the roles of external auditors that have long been debated. The degree to which audit inspections and public oversight will affect audit practice and quality over time remains an important area for continuing research as the inspection process is still evolving.

This study has some limitations. First, due to the limitation of the survey method, it only relies on reports of opinions by respondents rather than actual delivery of audit services. Second, due to a small number of respondents, the discussion of the findings has to be impressionistic. Hence, interpretation of the evidence is subjected to some caution. Third, opinions of the inspectors' perceptions are

influenced by their roles and function as a regulator in the audit market. When there is a majority agreement from the 12 responses, it is indicative of a widely-held opinion, but when there are variations, there are limits to the strength of conclusions that can be drawn. Nonetheless, within these limits, this study is interesting and relevant because it provides evidence of audit quality inspection; a part of the overall audit system that is not easy to penetrate and which has not been extensively covered in prior research.

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