The Effect of Inspections, Rotations and Client Preferences on Staffing Decisions

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Abstract

With increased regulatory focus on audits and concerns about whether audit regulation is achieving its stated aims, it is timely to investigate how regulator inspection of audit files and partner rotations may be affecting staffing decisions. This is an important issue, which affects all audits, as the calibre of staff allocated across engagements impacts the quality of audit work delivered. This paper reports the results of an experiment where auditor participants allocate staff across two audits, where regulation anticipated (none, inspection, rotation) and a client request for the best staff (absent, present) are manipulated between-subjects. We find that auditors allocate lower calibre staff when neither an inspection nor rotation is anticipated than when either is anticipated. When an inspection is anticipated, auditors allocate staff with more knowledge and compliance skills. When a rotation is anticipated, auditors allocate staff with more people skills. A client

request for the best staff only has an effect when a partner is due to be rotated, where auditors allocate staff with more people skills in response to the client request. Our findings provide greater understanding of staffing decisions, which may affect audit quality if concerns around audit inspections and partner rotations are perceived by auditors as more important than the underlying risk or complexity of an engagement when allocating staff.

Keywords: Audit Inspections; Partner Rotation; Staff Allocation; Audit Quality.

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1. Introduction

Regulation has significantly changed the way that audits are conducted. Audits are subject to greater scrutiny than in the past. In an experimental setting, we examine how regulator inspection of audit files (inspections) and partner rotation affect staffing decisions. Inspections (PCAOB 2012; ASIC 2014) are having an effect on various measures of audit quality (Gramling, Krishnan, and Zhang 2011; Lamoreaux 2013) because inspectors have access to auditors' files and can hold those auditors accountable for their work (Peecher, Solomon, and Trotman 2013; Johnson, Keune, and Winchel 2014). As a result, audit firms are making modifications to the way audits are conducted (Deloitte 2014; EY 2013; KPMG 2014; PwC 2013). Further, the requirement to rotate audit partners to enhance independence is creating challenges for audit firms as it has the potential to disrupt the conduct of an audit and detrimentally impact knowledge of a client (Daugherty, Dickins, Hatfield, and Higgs 2012). In response, audit firms have implemented formal transition processes (KPMG 2014; EY 2013; Deloitte 2014) to minimize impediments to the smooth running of audit engagements.

Prior research has examined the link between audit regulations, such as inspections and partner rotation, and auditor behavior (Carey and Simnett 2006; Gramling et al. 2011; Shefchik 2014; Winn 2014; Bowlin et al. 2015). To expand our understanding of how regulation may influence the audit process, we use an experiment to measure the effect of an anticipated inspection of a client's audit file by a regulator or an anticipated partner rotation on the allocation of staff to engagements. We chose staff allocation for this study as it is an audit quality input that affects every audit (IAASB 2014; PCAOB 2015). Further, the allocation of staff to engagements should generally be based on the riskiness and complexity of the engagement (Asare, Cohen, and Trompeter 2005; Blokdijs, Driehuisen, Simunic, and Stein 2006). If regulation causes auditors to consider other—potentially irrelevant—factors when allocating staff, audit quality may be affected.

The effect of audit regulation on staff allocation was made salient when raised by panellists at the American Accounting Association Annual Meeting in 2013. A member of that panel, PCAOB Board Member Jeanette Franzel noted:

“I would be concerned if a partner is making decisions about staffing levels and hours based on that partner's assessment of whether or not that audit would be inspected. I would hope that the same levels of quality and expertise would be applied to an audit regardless. That actually makes me question what is happening on the audits that partners think will not be inspected. That makes me worry.” (CAQ 2013, 1:14:55).

Interviews with Australian regulators ahead of conducting this research support this view. While it was acknowledged by regulator interviewees that auditors may be able to predict that certain clients are more likely to be selected for inspection due to certain characteristics (for example, if they are listed or due to their risk profile), the findings of the inspection process are to be applied on all audits and so there should be no differences in auditor behavior across audits. One of the espoused goals of regulation is to raise the quality level of all audits so regulations that have a differential effect on some engagements may undermine the overall intended impact of regulation (Carcello, Hollingsworth, and Mastrolia 2011; Aobdia 2015).

Inspections and partner rotations can increase the accountability of auditors in their decision making process and the audit literature has established that when auditors anticipate that their work will be assessed it impacts their behavior at various stages of the audit (Johnson and

Kaplan 1991; Kennedy 1993; Rich, Solomon, and Trotman 1997; Tan and Trotman 2003). When allocating staff, auditors are likely to form expectations about which engagements are more likely to be impacted by inspections or partner rotations. These expectations could then influence how auditors plan individual engagements. If this occurs, there is a risk that auditors may allocate lower calibre staff to clients where an inspection or partner rotation is not anticipated, possibly undermining the quality of those engagements.

Inspections and partner rotations are expected to impact staff allocation in different ways (Westermann, Cohen, and Trompeter 2014). When an inspection is anticipated, the likelihood of being held accountable for the quality of the audit working papers increases and there is an incentive to allocate staff with appropriate skills to enhance the probability that the regulator will issue a clean report on the audit file (Johnson et al. 2014). In this instance, an auditor's priority may be to allocate more staff with good technical knowledge and a record for being compliant with firm policies and procedures. When an audit is up for partner rotation, the client is more likely to become the focus because the audit firm needs to maintain a good relationship with the client during the transition from one partner to the next (Fargher, Lee, and Mande 2008; Daugherty et al. 2012). In this instance, the priority may be to allocate more staff with good people skills to reduce concerns about the conduct of the audit in the eyes of the client. Interviews with audit partners ahead of conducting this research support the view that knowledge, compliance and people skills are important auditor traits which are assessed after most audits.

Staffing decisions can also be impacted by client concerns (Asare et al. 2005; Blokdijk et al. 2006). Some clients are more sensitive to the structure of the audit team than others, and may express a preference for the type of personnel assigned to the engagement. While the audit firm may wish to assign their best people to engagements based primarily on risk and complexity, a preference stated by the client for certain types of personnel, or even specific individuals, is likely to focus the auditors' attention on their accountability to their client and influence staffing decisions. A client's wishes may take on increased importance when a partner is expected to be rotated, since partner rotation can trigger a search for a new audit firm (Fiolleau, Hoang, Jamal, and Sunder 2013; Deloitte 2014; EY 2013; KPMG 2014; PwC 2013).

For this study, we manipulate anticipated regulatory actions (none, inspection, rotation) and a client's request for the best staff (absent, present) between-subjects. One hundred and six Big 4 and mid-tier audit partners, managers and seniors were asked to assign audit staff to one of two

pending engagements. The participants were provided background information about the two clients and details about the staff available for the engagements. Staff details included their level within the firm (ranging from senior manager to junior staff) and internal ratings of their knowledge, people and compliance skills averaged for their last three audits. Participants assigned all staff to one of the two pending engagements.¹

Our results reveal that auditors allocate lower level staff and staff with lower skill ratings when neither an inspection nor a rotation is anticipated than when either is anticipated. Further, auditors allocate staff with more knowledge and compliance skills when an inspection is anticipated and staff with more people skills to a client when a partner rotation is anticipated. A client request for the best staff only has an impact when there is an upcoming partner rotation, increasing the people skills of staff allocated to the engagement. When asked to explain the rationale for their allocation decisions, the most common explanation, given by close to 60 percent of participants, was the need to balance staff and their skills between and within the two clients. Despite this expressed imperative, our findings demonstrate that auditors were nevertheless influenced by the experimental manipulations.

This study makes important contributions to audit literature and practice. First, the study responds to regulator comments regarding staffing decisions and auditor inspections. We find that while auditors are mindful of the need to allocate staff efficiently across clients based on risk and complexity, they are influenced by an anticipated inspection, with the consequent allocation of staff with lower knowledge and compliance skills to clients not anticipated to be inspected. Second, we also assess differences in auditor behavior when anticipating either an inspection or a rotation. This provides insights into how each impacts auditor behavior in different ways. Third, we provide evidence that client expressed preferences related to staffing decisions become salient when a partner rotation is imminent.

The remainder of the paper is organized as follows. In the next section we provide an overview of staff allocation and regulation literature and develop our hypotheses. This is followed by a discussion of the research design. The results are then presented ahead of our concluding comments.

¹ The forced choice of assigning all available staff to an engagement reflects the commercial incentives of an audit firm to avoid having unassigned staff. However, individual partners may not feel the same way in practice since they may not view unassigned staff as their “problem”. We acknowledge this as a potential limitation in the concluding section.

2. Background and Development of Hypotheses

2.1 Audit Staff Allocations

The make-up and skill set of the engagement team is a critical input to the audit which can affect the quality of the audit delivered (IAASB 2014; PCAOB 2015). As outlined in this section, a number of studies have considered the way that audit staff are allocated to clients. Staffing can be influenced by the need to provide stability in the audit team from year to year, to facilitate the development of client-specific knowledge, to foster the development of audit team cohesion and compatibility, and develop rapport and goodwill with client personnel (Blocher 1979; Balachandran and Zoltners 1981). These factors must be balanced against the benefits of giving staff exposure to different types of clients and providing opportunities to learn and advance in the firm. Audit staff allocation can be complex as the needs of the client need to be balanced against the availability of appropriate staff (Dodin, Elimam, and Rolland 1998). Staffing assignments are generally based on matching the skill set of available auditors (Chan and Dodin 1986) with client needs, audit team dynamics, client deadlines and time budgets (Balachandran and Zoltners 1981; Balachandran and Steuer 1982).

Audit staff allocation is also impacted by client characteristics such as size, industry, complexity, risk, whether it is a first time or recurring audit, client integrity and client internal controls (Balachandran and Zoltners 1981; Hackenbrack and Knechel 1997; Johnstone and Bedard 2001; Asare et al. 2005; Blokdijs et al. 2006). Staff allocation across different stages of the audit (planning, testing etc.) is impacted by client size, industry, complexity and risk (Hackenbrack and Knechel 1997). Clients with lower integrity are allocated more experienced auditors (Asare et al. 2005) and higher risk clients are allocated auditors with appropriate expertise (Johnstone and Bedard 2001). When audit effort is allocated in response to client characteristics, rather than procedurally, audit quality is enhanced (Blokdijs et al. 2006). Although extant research has identified several factors that influence audit staff allocations, most of these studies were conducted in periods before the audit profession became subject to extensive external regulation. We expect that different aspects of regulation may be important factors that currently impact audit staff allocation.

2.2 Regulation and Accountability

In general, the purpose of regulation is to improve the quality of audit decision making and to provide mechanisms by which auditors can be held accountable for poor audit outcomes.

Accountability is the expectation, either implicit or explicit, of being called upon to justify one's beliefs, feelings or actions with the related risk of negative consequences if found wanting (Tetlock 1992; Kennedy 1993; Lerner and Tetlock 1999). Prior research has considered how individuals react when being held accountable in a range of settings. Tetlock (1985) argues that when held accountable, individuals react by taking action that is believed to be acceptable by shifting their attitude, by acting defensively, or by increasing their cognitive effort. Individuals may shift their attitude when they are aware of the preferences of the person they are accountable to, a behavior observed when audit working papers are stylized by a preparer in line with the known preferences of the reviewer (Rich et al .1997; Tan and Trotman 2003).

Individuals may act defensively when justifying and rationalizing their judgments ex post (Emby and Gibbins 1988; Rich et al. 1997). Individuals may increase cognitive effort, search for an acceptable stance, and demonstrate more cautious behavior when unaware of the preferences of the principal (Gibbins and Newton 1994; Asare, Trompeter, and Wright 2000; Turner 2001; Bagley 2010). Accountability has been linked with improved consistency and consensus (Johnson and Kaplan 1991), a reduction in recency effects (Kennedy 1993), increased documentation of justifications (Koonce, Anderson, and Marchant 1995) and increased testing of errors (Asare et al. 2000). Similarly, Lord (1992) found that senior auditors are less likely to issue an unqualified opinion when accountable for their decision than when guaranteed anonymity. In this paper, we argue that regulation is an important source of accountability in auditing.

Predecisional accountability occurs when an individual anticipates that they may be held accountable for their current decisions and put effort into identifying the most defensible decision or choice (Tetlock 1985; Messier and Quilliam 1992). Predecisional accountability influences how decisions are made at every stage of the audit (Peecher and Kleinmuntz 1991) and auditors employ a range of tactics in response (Messier and Quilliam 1992). In the current context, auditors are expected to be affected by predecisional accountability when allocating staff based on whether a regulation is anticipated to impact their client and whether a client has requested the best available staff.

Prior research has shown that people respond differently depending on the source of accountability (Tetlock 1983). People are strategic, moderating their behaviour based upon their beliefs of who will be assessing their actions. Tetlock (1983) found that people expressed liberal attitudes when being assessed by a liberal and conservative views when being assessed by a

conservative. Accountability has been found to drive a desire to make decisions that are believed to be favourably thought of and avoid any criticism by others (Simonson and Nye 1992). In auditing, the advent of regulator inspections and partner rotation mean that audit files are more likely to be scrutinized by parties external to the team that conducted the audit. As a result, auditors may feel that they are more likely to be held accountable for the content of their audit files and may be penalized if problems are uncovered (ASIC 2013; Peecher et al. 2013; Dowling et al. 2015; Johnson et al. 2014).

In the case of inspections, there is clear accountability to an independent regulator for technical compliance with standards and regulations. When a partner is to be rotated, increased accountability may arise from having a new partner in charge but the focus of that accountability could shift to smoothly managing the transition from one partner to the next so as to not disrupt the auditor-client relationship (Daugherty et al. 2012). As a result, both inspections and partner rotations can encourage the allocation of staff with an appropriate skill set and experience level to minimize problems associated with the focus of the accountability, i.e., technical and compliance problems in the case of inspections and client-relationship problems in the case of a partner rotation. As staff resources are limited, we expect that clients that are not anticipated to be impacted by either an inspection or a rotation in the near term may be allocated lower calibre staff than when either is anticipated, leading to our first hypothesis:

H1a: Auditors allocate lower **level staff** and staff with lower **skills** ratings when **neither** an inspection nor a rotation is anticipated than when either is anticipated.

There are multiple sources of accountability for auditors to consider in addition to regulators when undertaking an audit (Gibbins and Newton 1994; Westermann et al. 2014; Winn 2014; Libby, Rennekamp, and Seybert 2015). Different situations will generally elicit different responses from auditors (Tetlock 1983). While most of the accountability literature considers how individuals or auditors react to one source of accountability, some research has looked at how auditor behaviour can be affected by conflicting accountability, i.e., where different sources of accountability place different demands on auditors. Bolten and Crockett (1979) note that auditors have two masters, financial report users and their client, which creates a challenge for auditors when needing to maintain a good working relationship with their client while maintaining their independence when reporting to users. Jensen (2000) found that when an auditor is accountable to

two parties—in this case the parent company of the audited division being sold and the purchaser of that division—they take more time on a task and are more likely to consult with another auditor than when accountable to one party. Auditors need to balance accountability to their clients and the need to avoid damage to their reputation, regulatory enforcement and litigation (Hackenbrack and Nelson 1996).

It is likely that client requests will influence the staffing of an engagement. Such a request needs to be balanced by the auditor against their strategy for coping with regulation that might apply to a specific engagement. A specific client request might augment the influence of regulation in an engagement or could work counter to the regulation. For example, a client who wants the “best” technical staff would augment the staffing incentives when an engagement is likely to be subject to inspection. On the other hand, a client request for staff with the “best” communication skills might work against assigning auditors with a high level of technical skills to an engagement likely to be subject to inspection. Thus, the interaction between regulation and client requests will depend on the context and is discussed in more detail in the next section. However, the one setting where the impact of a client request could be clear-cut is when an engagement is not likely to be subject to regulatory attention, leading to our next hypothesis:

H1b: A client request that the best staff be assigned to their engagement is expected to affect the gap in staff **levels** and **skills** ratings when **neither** an inspection nor a rotation is anticipated and when **either** is anticipated.

2.3 Sources of Accountability

In the internal audit literature (Abbott, Parker, and Peters 2010; Hoos, Kochetova-Kozloski, and d’Arcy 2015; Hoos, Messier, and Smith 2014) it is noted that internal auditors are accountable to two masters: to the audit committee and management. When an audit committee is relatively more active in their oversight of the internal audit function, more effort is put into monitoring internal controls (Abbott et al. 2010). The head of internal audit can influence how internal auditors respond to the different priorities of their two masters by focusing more on controls effectiveness, in line with audit committee concerns, or cost reduction, in line with management concerns (Hoos et al. 2014). In the context of the current research, an anticipated inspection suggests accountability to an inspector and an anticipated partner rotation suggests accountability

to a different partner (or the firm more generally) in circumstances where maintaining good terms with a client at a time of transition is paramount.

Inspections and partner rotations are both forms of regulatory accountability, which likely have different effects on staffing decisions, as each source of accountability place different demands on auditors. This expectation is consistent with prior literature where auditors are found to behave differently when faced with different types of accountability, including inspections (Westermann et al. 2014; Winn 2014). Because different regulations raise different issues in an audit, the skills that may be most needed for an engagement that is likely to be inspected could vary from those that are most appropriate when a partner rotation is anticipated. Further, these differences could be influenced by client concerns expressed about the quality of staff allocated to their engagement.

The client has long been recognized as a party that induces auditor accountability (Bolten and Crocket 1979; Winn 2014; Libby et al. 2015). The increasing focus on commercialism in audit firms increased the importance of managing the client relationship (Robson, Humphrey, Khalifa, and Jones 2007). The ability to attract and retain clients distinguishes more successful auditors, and is seen as a key factor for auditors being made partner (Carter and Spence 2014). The importance placed on client retention means auditors have incentives to respond to clients who vocalize preferences concerning the structure of the audit team assigned to their engagement. In the case of inspections, an engagement that is found to have deficiencies could negatively impact the auditor-client relationship. However, the audit firm may feel that the best way to manage that inspection risk is by reducing the likelihood that an inspector finds deficiencies in an engagement and the issue of an inspection is not likely to be salient to a client until after the completion of the inspection. In the case of a partner rotation, the need to successfully manage the client-auditor relationship is magnified since forced partner rotation can trigger a client to consider changing audit firms (Fiolleau et al. 2013; Deloitte 2014; EY 2013; KPMG 2014; PwC 2013).

2.3.1 The Effect of an Anticipated Inspection on the Need for Knowledge and Compliance Skills

Inspections are conducted by a regulator with a view to assessing compliance with audit regulations and enhancing audit quality (PCAOB 2004; ASIC 2014). Inspectors report on the adequacy of the audit firm's quality control processes as well as whether audits are conducted in line with auditing standards and regulations (PCAOB 2012; ASIC 2014). In Australia the audit inspection program conducted by the Australian Securities & Investments Commission (ASIC)

commenced after the passing of the Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004 (CLERP 9) and is targeted at all firms conducting audits, with an emphasis on firms auditing listed companies and public interest entities. The focus of ASIC inspections is on audit quality, as well as compliance with the Corporations Act, auditing standards, and professional and ethical standards (ASIC 2014). The inspection process conducted by an independent regulator holds auditors accountable for the content of their audit file and answerable for documented conclusions (Lennox and Pittman 2010; Shefchik 2014; ASIC 2014; Aobdia 2015).

Audit firms take the regulator inspection process seriously and endeavor to make improvements in anticipation of future inspections (Deloitte 2014; EY 2013; KPMG 2014; PwC 2013; Aobdia 2015). There is evidence that the inspection process has improved audit quality for firms found to have deficiencies (Gramling et al. 2011) and for all audits, whether client files have been inspected or not (Carcello, Hollingsworth, and Mastroia 2011; Aobdia 2015). However, there is mixed evidence regarding the association between the concurrent identification of deficiencies in audit files and audit quality, with this link only being established for triennially inspected firms but not annually inspected firms (Gunny and Zhang 2013).²

While there is uncertainty surrounding which client's files will be selected for inspection by the regulator, partners believe that they can predict the clients that are most likely to be selected (Houston and Stefaniak 2013).³ Lamoreaux (2013) considers the ex-ante impact of inspections and finds that the anticipation of an inspection is sufficient to impact auditor behavior. Specifically, auditors are more likely to issue a going concern opinion when they anticipate an inspection than when they do not anticipate an inspection. This finding suggests that predecisional accountability regarding an inspection by a regulator is sufficient to impact auditor behavior. In an experimental setting, inspections by regulators impact accountability such that audit effort is increased (Shefchik 2014) or decreases in audit effort are less likely (Winn 2014).

Audit firms concerned about the significant negative ramifications of receiving a negative report from the regulator can try to reduce this inspection risk by assigning better personnel to engagements that they believe are more likely to be selected for inspection. In this scenario, better

² The impact of inspections on audit firm market share is unclear with some research finding no client reaction to negative reports (Lennox and Pittman 2010) while others find that clients switch from firms with poor reports to firms with good reports (Abbott, Gunny, and Zhang 2013; Nagy 2014).

³ This belief was shared by partners at the participating firms, who aided in the design of the research instrument.

personnel means allocating auditors with more technical knowledge (i.e., about standards and regulation) and compliance skills (i.e., working within firm policies and procedures) as these qualities should aid in the attainment of a clean report from the regulator and help the firm avoid regulatory penalties (ASIC 2013; Peecher et al. 2013; Johnson et al. 2014). Knowledge and compliance skills are expected to be relatively more important in the case of an anticipated inspection than on other engagements, leading to our next hypothesis:

H2a: Auditors allocate **staff with more knowledge and compliance skills** to a client when an inspection is anticipated than to a client due for partner rotation.

This expectation is demonstrated in Panel A of Figure 1 where the solid “Inspection” line is above the dashed “Rotation” line.

The literature on two masters discussed above suggests that balancing client wishes with allocating appropriately skilled staff to clients anticipated to be inspected can add complexity to an already difficult task. When a client requests that the “best” staff be assigned to their engagement, an auditor will consider this request within the context of what they think is most important for that client. As previously discussed, an auditor’s reaction to the client request will depend on the context and what the client actually means when they ask for the “best” staff. While a regulatory inspection may not be directly salient to the client, at least on an ex ante basis, given the auditor’s potential concern for that inspection they are more likely to want to avoid a negative outcome in the presence of a client’s request for the best people. That is, a negative outcome could be interpreted by a client as a signal that they did not receive the “best” people. This focus is likely to cause the auditor to allocate staff with good knowledge and compliance skills when an inspection is anticipated. In the current context, when a client requests the best staff available, the auditor is likely to be more sensitive to the issue of passing the inspection than they would be without such a request although, it would be high in both cases, leading to our next hypothesis that builds on Hypothesis 2a:

H2b: The gap in **knowledge and compliance skills** of staff allocated (where an inspection versus a rotation is anticipated) will be greater when a client requests that the best staff be assigned to their engagement than when a client does not make such a request.

This expectation is demonstrated in Panel A of Figure 1 by the increasing gap between “Inspection” and “Rotation” lines (moving from client request absent to present).

[Insert Figure 1 here]

2.3.2 The Effect of an Anticipated Partner Rotation on the Need for People Skills

Partner rotation has been mandated in several jurisdictions to enhance independence and audit quality (Stewart, Kent, and Routledge 2016).⁴ Partner rotation has been shown to be associated with lower unexpected accruals (Hamilton et al. 2005; Fargher et al. 2008) and an increased propensity to issue modified audit opinions (Firth, Rui, and Wu 2012). Carey and Simnett (2006) report a negative association between partner tenure and the propensity to issue going concern modified opinions to distressed companies.

Audit partners acknowledge that rotation enhances independence but it may also impact overall audit quality in the early years as client specific knowledge is lost (Daugherty et al. 2012). Chi and Huang (2005) report that audit quality improves with tenure as partners get to know their clients, but after five years audit quality diminishes. Stewart et al. (2016) report that audit fees increase in the year of a partner rotation. In an experimental setting, auditors new to a client propose larger audit adjustments than continuing auditors (Hatfield, Jackson, and Vandervelde 2011) and they decrease audit effort and increase partner time spent on documentation at the expense of other quality enhancing activities ahead of a partner rotation (Winn 2014). Another experiment finds that mandatory rotation impedes audit quality when an auditor takes on a skeptical frame (Bowlin et al. 2015).

A partner rotation provides a fresh perspective on audit issues, reduces the potential social bonding that comes from familiarity between client and audit personnel, reduces the threat that a partner acts in their own self-interest, and enhances independence (Deloitte 2014; EY 2013). However, managing the process of partner rotation and resulting transitions in the audit team is challenging for both auditors and their clients (Daugherty et al. 2012). In response, firms have implemented formal processes to minimize any disruption (Fargher et al. 2008; KPMG 2014; EY 2013; Deloitte 2014) as clients do not always react favourably to a change in audit partners. Given the potential disruption on the client-auditor relationship, it is important that the audit team possess

⁴ In Australia, a partner cannot play a significant role in the audit of a listed company for more than five out of seven successive financial years.

the people skills necessary to help the client through the transition. Based on this, our next hypothesis is:

H3a: Auditors allocate **staff with more people skills** to a client when a partner rotation is anticipated than to a client when an inspection is anticipated.

This expectation is demonstrated in Panel B of Figure 1 where the dashed “Rotation” line is above the solid “Inspection” line.

Partner rotations were introduced to enhance auditor independence and enhance audit quality. Following a rotation, an audit partner is less likely to acquiesce to client wishes regarding accounting choices (Laurion, Lawrence and Ryans 2017). However, client wishes around the conduct of the audit may become more salient when a partner rotation is anticipated, a time when auditors are specifically concerned with managing the transition process (Daugherty et al. 2012; Deloitte 2014; EY 2013). In this case, the auditor may focus on the challenges of managing the transition so that people skills become the most salient to the audit process. Thus, a client’s request for the best staff available may increase the gap in people skills between engagements when a partner rotation is anticipated and engagements expected to be subject to inspection. Building on our expectation expressed in Hypothesis 3a, this leads to our final hypothesis:

H3b: The gap in **people skills** of staff allocated (where a rotation versus an inspection is anticipated) will be greater when a client requests that the best staff be assigned to their engagement than when a client does not make such a request.

This expectation is demonstrated in Panel B of Figure 1 by the increasing gap between “Rotation” and “Inspection” lines (moving from client request absent to present).

3. Research Design

3.1. Participants

One hundred and six auditors, with experience allocating staff to audits, from Big 4 and mid-tier firms took part in this study.⁵ Participants comprised eight partners, 90 managers and

⁵ Participants came from all Big 4 firms and three mid-tier firms. ANOVAs with tier and then firm as covariates were run separately for each of the dependent variables. Tier ($p > 0.2$) and firm ($p > 0.5$) differences are not significant.

eight seniors with an average 10.6 years audit experience (ranging from 4.5 to 34 years).⁶ Senior partners invited colleagues with appropriate skills and experience to participate. Participants were assured anonymity and were given a \$50 gift card, provided by the researchers, by an administrative assistant within their firm. The experiment was conducted online and participants were randomly allocated across treatments when logging on.

3.2 Experimental Task

The experimental task was developed in close collaboration with partners from the participating firms. The task included information about two audit clients (Morling and Kelward) and details regarding audit staff available for allocation across those two clients. Participants were told that both clients are large listed companies, have been a client for a number of years, and there have not been any significant changes to the leadership team of either client. They were told that a recent change in regulation affects Morling's disclosure requirements, there had been a change in Morling's accounting policy around inventory valuation, areas of focus for this year's audit are inventory and intangibles, that Morling had goods in transit at the end of the last financial year that were subsequently found to be damaged in route, and that Morling were underinsured. They were told that a recent change in government policy affects Kelward's warranty provision estimation, there had been a change in Kelward's accounting policy around fixed asset valuation, areas of focus for this year's audit are motor vehicles and depreciation, and that one of Kelward's debtors went into liquidation after the end of the last financial year due to an unforeseen event and was unable to pay the amount outstanding.

Information about audit staff available for allocation and the system used to rate them was held constant across treatments (see Figure 2). Participants were told that audit staff at their firm are rated on their technical knowledge (demonstrated knowledge of standards and regulations), people skills (demonstrated ability to interact with the client and the audit team), and compliance (demonstrated compliance with firm policies and procedures).⁷ They were told that each auditor is assessed on each of these dimensions on a scale from one (performance needs improvement) to five (performance is exceptional). Participants were given a list of staff to be allocated to the clients. The list included staff identifiers in the form of their initials, level (senior manager, manager, assistant manager, senior or junior staff), and their ratings (1-5), averaged across their

⁶ ANOVAs with level (partner, manager, senior) and then years of audit experience as covariates were run for each of the dependent variables. Level ($p > 0.4$) and years of experience ($p > 0.5$) are not significant.

⁷ A significant aspect of compliance is workpaper documentation.

last three audits, for each of the three skill dimensions (knowledge, people, compliance).⁸

Participants were asked to assign all staff across the two audits using the background information provided.⁹ These allocations are used to test our hypotheses.

[Insert Figure 2 here]

After allocating staff across the clients, participants were asked to explain the rationale for their allocation decisions. Their explanations are described in the supplementary analysis section of the paper. Participants were then asked to rank the importance of the skills (knowledge, people and compliance) from one to three for each client. These rankings, also described in the supplementary analysis section of the paper, are used to confirm the criteria used by participants when allocating staff across the clients in an unconstrained setting. Lastly participants answered manipulation check and demographic questions.

3.3 Design

We use a 3x2 between-subjects design to test our hypotheses (see Table 1). Regulation Anticipated was manipulated at three levels: none, inspection, partner rotation. Client Request for the best staff was manipulated at two levels: absent or present. When testing Hypothesis 1, the Inspection and Rotation cells are collapsed.

[Insert Table 1 here]

The experiment was administered via computer. Participants logged on using a link provided by the researchers by a contact at each firm. When logging on to participate, auditors were randomly allocated two clients across two cells providing 212 data points.¹⁰ The background information about the two clients was counter-balanced within each cell.

For the ‘Regulation Anticipated: None’ treatment, client background information included no details about either an inspection or a rotation. For the ‘Regulation Anticipated: Inspection’ treatment the background information included: ‘Due to (client name)’s risk profile, it is believed that ASIC are likely to inspect this year’s audit file’. For the ‘Regulation Anticipated: Rotation’ treatment the background information included: ‘The (client name) audit is up for partner rotation

⁸ Staff ratings across the three dimensions were not significantly correlated (knowledge and compliance skills $p = 0.625$; knowledge and people skills $p = 0.083$; people and compliance skills $p = 0.100$).

⁹ Participants were asked to assign all personnel in order to reduce the concern for costs that might influence the assignment of staff. That is, if staff could be left idle, some participants might make their assignments based on anticipated—but unknown—costs rather than experience and skill levels. This is consistent with firm level incentives but abstracts from partner level incentives that can vary across individuals (Knechel et al. 2013).

¹⁰ The numbers are not evenly distributed across the six cells primarily because some auditors logged on, were allocated a version of the research instrument and then dropped out before commencing the task.

next year'. For the 'Client Request: Absent' treatment, the following details were included in the background information: 'A meeting has been held with the chair of (client name)'s audit committee to review the upcoming audit. At that meeting the timing of the audit was discussed'. For the 'Client Request: Present' treatment, the following details were included in the background information: 'A meeting has been held with the chair of (client name)'s audit committee to review the upcoming audit. At that meeting the timing of the audit was discussed and the quality of the staff allocated to the audit was noted. The chair of the audit committee requested that the best staff be assigned to their audit'. The wording used in these manipulations was recommended by partners from the participating firms.

4. RESULTS

4.1 Manipulation Checks

After completing the staff allocation task, participants answered four manipulation check questions. Two questions (one for each client) relate to the regulation treatment and two questions (one for each client) relate to the client request treatment. For the regulation treatment, participants were asked to indicate which of three statements is true. Two statements mirrored the wording in the background information regarding an inspection or a rotation and the third option was neither. For the client request treatment, participants were asked to indicate which of two statements is true. The two statements matched the wording in the background information regarding details of the meeting with the clients' audit committees. Twenty participants answered a manipulation check question incorrectly. They were scattered across treatments. The majority answered that an inspection was likely when there was no mention of an inspection (10) or a client requested the best staff when there was no mention of such a request (5). The results presented are for all 106 participants who answered all four manipulation check questions correctly. There is no difference in the statistical conclusions if the twenty participants who failed manipulation check questions are included in the testing of the hypotheses.

4.2 Tests of Hypotheses

4.2.1 Results Hypothesis 1

Hypothesis 1 predicts that auditors allocate lower level staff and staff with lower skills ratings when neither an inspection nor a rotation is anticipated than when either is anticipated (H1a) and that a client request for the best staff affects this relationship (H1b). Staff Levels were calculated by first assigning a number to each staff member and then summing that number for

each client. The senior managers were each assigned a five, managers were each assigned a four, assistant managers were assigned a three, seniors were assigned a two and junior staff were assigned a one. The Skills Ratings variable was calculated by summing the knowledge, people and compliance skills ratings of staff allocated to each client.

The descriptive statistics in Panel B of Table 2 show that regulation has an effect on the staff levels and skills ratings of staff allocated to clients. Staff Levels are lower when neither regulation is anticipated (17.63) than when either regulation is anticipated (18.19). Skills Ratings are lower when neither regulation is anticipated (79.08) than when either regulation is anticipated (82.77). The main effect for Regulation (see the ANOVA in Panel A of Table 2) is significant for Staff Levels ($F=9.780$, $p=0.002$) and for Skills Ratings ($F=10.674$, $p=0.001$). These results support Hypothesis 1a. The insignificant main effects for Client Request and for the interactions between Regulation and Client Request, indicate that the client request for the best staff did not affect the Staff Levels and Skills Ratings of staff allocated. The pattern of results for Skills Ratings indicate that auditors allocate staff with lower skills ratings when neither an inspection nor a rotation is anticipated than when either is anticipated regardless of whether Client Request is absent ($t=2.50$, $p=0.01$) or present ($t=2.13$, $p=0.03$).¹¹ The pattern of results for Staff Levels is different with auditors allocating lower level staff when neither an inspection nor a rotation is anticipated than when either is anticipated only when a Client Request is present ($t=3.17$, $p=0.00$) but not when it is absent ($t=1.21$, $p=0.23$). This provides some support for Hypothesis 1b.

[Insert Table 2 here]

4.2.2 Results for Hypothesis 2

Hypothesis 2a predicts that auditors allocate staff with more knowledge and compliance skills to a client when an inspection is anticipated than to a client due for partner rotation. The ANOVAs in Panel A of Table 3 show that the Type of Regulation main effect is significant for both Knowledge ($F=9.888$, $p=0.002$) and Compliance ($F=51.536$, $p=0.000$) skills providing support for Hypothesis 2a. The descriptive statistics in Panel B of Table 3 show that overall, knowledge skills are higher when an inspection is anticipated (28.72) than when a partner rotation is anticipated (27.19) and compliance skills are higher when an inspection is anticipated (29.57)

¹¹ The pattern of results for skills ratings when testing H1a and H1b holds for each type of skill – knowledge, compliance and people skills. The lack of a result for client requests could be due to the participants interpreting “client request” to mean different things in the context of “no regulation” as discussed in the theory section of the paper.

than when a partner rotation is anticipated (24.92). This result is demonstrated graphically in Figure 3 where the “Inspection” line (solid) is above the “Rotation” line (dashed) for knowledge (Panel A) and compliance (Panel B) skills.

[Insert Table 3 here]

[Insert Figure 3 here]

Hypothesis 2b predicts that the gap in knowledge and compliance skills of staff allocated (where an inspection versus a rotation is anticipated) will be greater when a client requests that the best staff be assigned to their engagement than when a client does not make such a request. The interactions between Type of Regulation and Client Request reported in Panel A of Table 3 are not significant for Knowledge Skills ($F=0.000$, $p=0.992$) and for Compliance Skills ($F=0.212$, $p=0.646$). The descriptive statistics in Panel B of Table 3 show that the Knowledge and Compliance Skills of auditors allocated were greater when an Inspection was anticipated than when a Rotation was anticipated when a Client request was absent and present. This pattern of results indicates that Hypothesis 2b is not supported.¹²

4.2.3 Results for Hypothesis 3

Hypothesis 3a predicts that auditors allocate staff with more people skills to a client when a partner rotation is anticipated than when an inspection is anticipated. The ANOVA in Panel A of Table 4 shows a significant main effect for Type of Regulation ($F=12.565$, $p=0.001$). The descriptive statistics in Panel B of Table 4 shows that auditors allocate staff with more people skills to a client when a partner rotation is anticipated (28.31) than when an inspection is anticipated (26.48) providing support for Hypothesis 3a. This result is demonstrated graphically in Figure 4 where the “Rotation” line (dashed) is above the “Inspection” line (solid). People skills are important when a client is to be rotated reflecting the importance of managing the transition when a new partner joins the audit team.

[Insert Table 4 here]

[Insert Figure 4 here]

Hypothesis 3b predicts that the gap in people skills of staff allocated (where a rotation versus an inspection is anticipated) will be greater when a client requests that the best staff be

¹² The lack of a result for client requests could be due to the participants interpreting “client request” to mean different things in the context of “inspection regulation” as discussed in the theory section of the paper.

assigned to their engagement than when a client does not make such a request. The ANOVA in Panel A of Table 4 shows a significant interaction between Type of Regulation and Client Request ($F=3.600$, $p=0.060$). The descriptive statistics in Panel B of Table 4 shows that auditors allocate staff with more people skills to a client when a partner rotation is anticipated than when an inspection is anticipated only when the client requests the best staff ($t=3.63$, $p=0.00$) but not when they do not ($t=1.25$, $p=0.22$), which is consistent with our expectations in Hypothesis 3b.

5. Supplementary analysis

5.1 Staff Levels

Hypotheses 2 and 3 predict differences in the knowledge, compliance and people skills of staff allocated when an inspection is anticipated versus when a client is due for partner rotation. The levels of staff allocated may also vary under these circumstances. We find that the results for staff levels mirrors those for knowledge and compliance skills. Auditors allocated higher level staff to a client when an inspection was anticipated than to a client due for partner rotation ($F=5.345$, $p=0.022$).¹³ This means that auditors allocate higher level staff, which is a proxy for skills and ability, when an inspection is anticipated. Client Request ($F=0.132$, $p=0.717$) and the interaction between Type of Regulation and Client Request ($F=0.467$, $p=0.574$) are both insignificant.

5.2 Alternative Measures of Staff Levels and Skills Ratings

Staff levels and skills ratings were measured by summing the staff levels and skills ratings of staff allocated to each client. We measure staff levels and skills ratings in this way when testing our hypotheses as it reflects the total seniority and calibre of staff allocated to each client. The approach treats skills as being the same across all ranks. We consider alternative ways of measuring staff levels and skills ratings to determine whether the number of staff allocated to each client had an effect on our results. When we average staff levels and skills ratings of staff allocated to each client the results for skills ratings remain consistent with those reported in the main analysis while the results for average staff levels becomes insignificant. Another way of controlling for the number of staff allocated is starting with the same number of staff at each level. Three staff members were removed from the analysis resulting in an even number of staff at each level (two senior managers, two managers, four seniors, four junior staff) and the hypotheses were retested. The results remain consistent with those reported in the main analysis.

¹³ Staff levels is not significantly correlated with any of the skills ratings in the experimental task.

Staff levels and skills ratings are not necessarily independent as skills ratings will mean different things for staff at different levels. For example, a skill rating of four for a manager is of more value than the same skill rating for a senior. Skills ratings were re-weighted for staff level by multiplying skills ratings by a number representing the different staff levels (a five for senior managers, a four for managers, a three for the assistant manager, a two for seniors and a one for junior staff). The analysis reported in the paper was rerun after re-weighting skills ratings for staff levels and results are the same as our main analysis.

Skills ratings can also be analyzed by considering which client was allocated the ‘best’ auditors, where best is a rating of 4 or 5 for each skill. The analysis is re-run using the proportion of the ‘best’ staff available for each skill (knowledge, people and compliance) as the dependent variable. The results are consistent with the main analysis with participants allocating a greater proportion of staff with the best knowledge ($p=0.000$) and compliance ($p=0.000$) skills ratings when an inspection is anticipated and staff with the best people ($p=0.000$) skills rating when a rotation is anticipated. Client request is again significant when a rotation is anticipated with participants allocating staff with the best people ($p=0.033$) skills rating when a client requests the best staff available.

5.3 Rationale for Allocation Decision

After allocating staff across the two clients, participants were asked to explain the rationale for their allocation decisions. The most common explanation was a desire to balance staff across the clients and/or the skills within each client.¹⁴ Reasons provided include a wish to keep the number, level and skill set even across the clients. Close to 60 percent of participants listed this rationale. This is interesting as it highlights a strategy to allocate skills and expertise evenly across clients in spite of differences in regulatory conditions. Yet, when a regulation is likely to impact a client, the results reported in this paper demonstrate that the staff allocation process is affected, possibly subconsciously. Other explanations included, in decreasing order, the regulator was likely to inspect a client’s files, reference made to an accounting issue detailed in the background information for either or both clients, partner rotation, client request for best staff and the similarity between the two clients.

¹⁴ Our results are the same for those who mention a desire to balance staff across the clients and/or the skills within each client and those that do not.

About three-quarters of the participants in the inspection treatment referred to the need for staff with knowledge and compliance skills due to a likely inspection. About half of the participants in the partner rotation treatment referred to the need for staff with people skills due to an anticipated rotation. In both cases the proportion of participants in each treatment mentioning the need for staff with knowledge and compliance skills (inspection) or the need for staff with people skills (rotation) is significantly different from zero ($p=0.000$).

5.4 Ranking of Skills

As the staff allocation task required that all staff be allocated across two clients, participants were asked to make a trade-off in the skill set allocated to each client. To better understand the skill set valued most when a client is impacted by each type of regulation in an unconstrained setting, participants were asked to rank the importance of each skill (knowledge, people and compliance) for each client. This task was unconstrained as the skills are ranked independently for each client. When inspection is anticipated for a client, compliance skills are ranked significantly higher when compared to other engagements ($t=6.43$, $p=0.000$). When a partner rotation is anticipated, people skills are ranked significantly higher than when compared to other engagements ($t=5.39$, $p=0.000$). Knowledge skills are ranked about the same when an inspection is anticipated when compared to other engagements ($t=0.65$, $p=0.511$).

5.5 Audit Risk

While the aim of this paper is to consider how inspections, partner rotations and client concerns regarding the quality of audit staff impacts staff allocation, it also possible that audit risk is also likely to impact the way that staff are allocated to an audit. We did not manipulate audit risk across conditions and the information provided about the two clients in the case materials (Morling and Kelward) was purposefully kept very similar. Yet participants appear to treat one client (Morling) as riskier than the other. They allocated auditors with greater knowledge ($p=0.03$) and compliance ($p=0.02$) skills to Morling than to Kelward. To control for any unforeseen differences across the clients they were randomized across treatments. When client is included as a covariate and the hypotheses retested all of our results remain as reported. When the hypotheses are tested for each client separately our results remain as reported.

After controlling for client (Morling or Kelward), participants allocated staff with greater knowledge ($p<0.003$) and compliance ($p<0.001$) skills when an inspection was anticipated, and staff with greater people skills ($p<0.003$) when a partner rotation was anticipated. When client risk

is held constant (high, i.e. data are tested for Morling only), participants allocated staff with greater knowledge ($p < 0.03$) and compliance ($p < 0.001$) skills when an inspection was anticipated and staff with greater people skills ($p < 0.06$) when a partner rotation was anticipated. This means that when a client is perceived to be higher risk, auditors still react to audit regulation when allocating staff, i.e., client risk does not supersede concerns surrounding audit regulation.

Discussion and conclusion

Staffing decisions ultimately influences the audit quality achieved for individual clients. Prior literature has focused on a range of factors that impact the choice of staff allocated to audits, such as the desire to provide stability to clients, the desire to provide an opportunity for staff to build up client knowledge, and the need to provide staff with a breadth of experience. Until now the external factors considered to influence this task have been limited to the characteristics of the client, such as size, risk and industry. While there has been considerable attention paid to audit regulation, including inspections and rotations, and how it impacts various proxies for audit quality, this study provides evidence of how regulation impacts a vital input into delivering audits, the quantity and quality of staff allocated to an engagement (IAASB 2014). In so doing, this study responds to concerns raised by regulators that audit regulation, and audit inspections in particular, might have an effect on staffing decisions and the consequent allocation of lower calibre staff when an inspection is not anticipated to impact a client.

While prior research has considered how one type of audit regulation impacts audit quality proxies, this study considers the different ways that two types of regulation (inspections and partner rotation) impact the quality of staff allocated. We make a range of predictions about how audit regulation will impact staff allocations. We also consider when a client request for the best staff will impact staff allocation. We chose this client attribute as it is likely to become salient when auditors need to manage the auditor-client relationship while simultaneously addressing issues of regulation. This tension could be most obvious in the lead up to a transition around a partner rotation, an event which can trigger a switch in audit firm (and it could also be salient if a specific engagement fails an audit inspection, which becomes relevant after an inspection).

We predict and find that regulation is associated with the allocation of lower calibre staff to clients when a regulation impact is not anticipated than when one is anticipated. Also, auditors allocate staff with more knowledge and compliance skills when a regulatory inspection is anticipated and staff with higher people skills when a rotation is anticipated. Client request for the

best staff impacts the level of staff allocated with auditors allocating lower level staff when neither an inspection nor a rotation is anticipated than when either is anticipated only when a client request is present but not when it is absent. Client request for the best staff also impacts people skills of staff allocated when a partner rotation is anticipated. This is an important finding as it suggests that auditors are more sensitive to client preferences ahead of a partner rotation. Future research could consider whether this extends to auditors acquiescing to client preferred accounting treatments ahead of a rotation.

When asked to explain the rationale for their allocation decision the most common reason noted was the need to balance staff across clients and the skill set of staff within each audit. In spite of this self-assessment, we find that audit regulation has a significant effect on the way that audits are staffed. Auditors appear to be most concerned about regulator inspections and allocate staff in such a way as to increase their chances of receiving a clean report from the regulator. When a partner rotation is anticipated, the focus appears to be on ensuring a smooth transition where people skills become the focus. At this time, auditors are also more likely to be responsive to client concerns making the transition to a new partner as smooth as possible for the client.

Our study has a number of limitations which affect the generalizability of our results. First, the audit regulations considered in this study limit the generalizability of our findings and provide avenues for further research involving other aspects of regulation. Second, we use a staff rating system that, while agreed upon by participating firms for the purposes of our study, does not match that used in any particular firm. This was by necessity given the involvement of multiple firms but a different staff rating system based on different criteria could provide different results concerning the effect of audit regulation on staff allocation. Third, we impose an artificial constraint on the range and skill set of available staff, and provide limited information about the staff. In reality auditors will have had personal experience working with the staff they allocate providing important additional insights that cannot easily be replicated in an experimental setting. Fourth, it is possible that a client request for the “best” staff could be interpreted differently by different participants.

In spite of these limitations, our results are important to regulators, audit firms and audit researchers. We demonstrate that inspections and mandatory partner rotations are having an effect on auditor behavior, even when other concerns are a priority (in this case, to allocate staff evenly across clients). We demonstrate to audit firms that inspections and rotations affect staff allocations

in different ways, with auditor focus changing depending on whether an inspection by a regulator is anticipated or a partner rotation is anticipated. We contribute to audit research by considering the effect on auditor decision making of two regulations simultaneously, expanding our understanding of when and how audit regulation impacts auditor behavior.

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Figure 1

Panel A: Expectations Regarding Knowledge and Compliance Skills

Panel B: Expectations Regarding People Skills

Note: Inspection refers to the anticipation that a client's file will be inspected. Rotation refers to whether a partner rotation is anticipated in the next year. Client Request refers to whether a client's audit committee has requested that the best staff be allocated to them. Knowledge Skills are the summed knowledge skills ratings (from 1 (performance needs improvement) to 5 (performance is exceptional) for each staff member allocated to a client. Compliance Skills are the summed compliance skills ratings (from 1 (performance needs improvement) to 5 (performance is exceptional) for each staff member allocated to a client. People Skills are the summed people skills ratings (from 1 (performance needs improvement) to 5 (performance is exceptional) for each staff member allocated to a client.

Figure 2

Staff allocation task

Audit staff at your firm are rated on each of three dimensions after each audit:

Technical knowledge – demonstrated knowledge of standards and regulations

People skills – demonstrated ability to interact with the client and the audit team

Compliance – demonstrated compliance with firm policies and procedures

Each auditor is assessed on a scale from 1-5 relative to their peers where:

5 = Performance is exceptional

4 = Performance exceeds expectations

3 = Performance meets expectations

2 = Performance falls short of expectations

1 = Performance needs improvement

The table below includes details of the staff available by name (initials), level and their ratings averaged across their last three audits. These ratings align with your assessment of these auditors' capabilities relative to their peers.

Using the background information provided above about Morling and Kelward to guide your decision, please assign staff listed across the two audits. All listed staff must be allocated to one client.

Initials	Position	Knowledge	People	Compliance	Morling	Kelward
C.D.	Senior manager	3	5	2		
W.K	Senior manager	5	2	4		
K.S.	Manager	5	3	2		
E.L.	Manager	3	5	3		
T.C.	Assistant Manager	3	2	5		
R.A.	Senior	3	5	2		
A.F.	Senior	5	5	4		
L.J.	Senior	2	5	3		
K.V.	Senior	3	3	5		
O.D.	Senior	3	3	3		
S.G.	Graduate	5	2	5		
J.A.	Graduate	5	3	2		
A.K.	Graduate	4	5	5		
J.S.	Graduate	2	5	3		
J.D.	Graduate	4	2	5		

Figure 3

Results: Knowledge and Compliance Skills

Panel A: Knowledge Skills

Panel B: Compliance Skills

Note: Inspection refers to the anticipation that a client's file will be inspected. Rotation refers to whether a partner rotation is anticipated in the next year. Client Request refers to whether a client's audit committee has requested that the best staff be allocated to them. Knowledge Skills are the summed knowledge skills ratings (from 1 (performance needs improvement) to 5 (performance is exceptional) for each staff member allocated to a client.

Compliance Skills are the summed compliance skills ratings (from 1 (performance needs improvement) to 5 (performance is exceptional) for each staff member allocated to a client.

Figure 4

Results: People Skills

Note: Inspection refers to the anticipation that a client's file will be inspected. Rotation refers to whether a partner rotation is anticipated in the next year. Client Request refers to whether a client's audit committee has requested that the best staff be allocated to them. People Skills are the summed people skills ratings (from 1 (performance needs improvement) to 5 (performance is exceptional) for each staff member allocated to a client.

Table 1

Research Design

	Client Request:	
	Absent	Present
Regulation Anticipated:		
None	n = 37	n = 36

Inspection	n = 38	n = 37
Rotation	n = 39	n = 25

Note: Regulation anticipated refers to whether a client is anticipated to be inspected or a partner rotation is anticipated in the next year.

Client Request refers to whether a client's audit committee has requested that the best staff be allocated to them.

n = number of participants

Table 2

ANOVA and Descriptive Statistics for H1: Staff Levels and Skills Ratings

Panel A: ANOVAs *

Source	Staff Levels					Skills Ratings				
	SS	df	MS	F	p	SS	df	MS	F	p
Regulation	15.661	1	15.661	9.780	0.002	636.725	1	636.725	10.674	0.001
Client Request	1.116	1	1.116	0.697	0.405	8.600	1	8.600	0.144	0.705
Regulation x Client Request	3.428	1	3.428	2.141	0.145	2.058	1	2.058	0.035	0.853
Error	333.077	208	1.601			12407.537	208	59.652		

Table 2 (Continued)

Panel B: Descriptive Statistics: Mean, (Standard Deviation)*, (n = Number of Participants)

* Two-tail

* Two-tail

Regulation	Staff Levels				Skills Ratings			
	Client Request:			Overall Mean	Client Request:			Overall Mean
	Absent	Present			Absent	Present		
Either	18.14	18.26	t = 1.42	18.19	83.05	82.42	t = 0.12	82.77
	(1.20)	(1.27)	p = 0.16	(1.23)	(8.12)	(7.33)	p = 0.91	(7.76)
	(n = 77)	(n = 62)			(n = 77)	(n = 62)		
Neither	17.84	17.42	t = 0.53	17.63	79.19	78.97	t = 0.48	79.08
	(1.38)	(1.27)	p = 0.59	(1.34)	(7.96)	(7.25)	p = 0.63	(7.56)
	(n = 37)	(n = 36)			(n = 37)	(n = 36)		
	t = 1.21	t = 3.17			t = 2.50	t = 2.13		
	p = 0.23	p = 0.00			p = 0.01	p = 0.03		
Overall Mean	18.04	17.95			81.80	81.15		
	(1.27)	(1.33)			(8.24)	(7.45)		

Note: Regulation refers to whether or not a client is anticipated to be inspected or a partner rotation is anticipated in the next year.

Staff Levels are the summed numbers used to represent levels (from 5 for senior managers down to 1 for junior staff) for each staff member allocated to a client.

Skills Ratings are the summed knowledge, people and compliance skills ratings (from 1 (performance needs improvement) to 5 (performance is exceptional) for each staff member allocated to a client.

n = number of participants

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Table 3

ANOVA and Descriptive Statistics for H2: Knowledge and Compliance Skills

Panel A: ANOVAs*

Source	Knowledge Skills					Compliance Skills				
	SS	df	MS	F	p	SS	df	MS	F	p
Type of Regulation	84.378	1	84.378	9.888	0.002	743.155	1	743.155	51.536	0.000
Client Request	8.724	1	8.724	1.022	0.314	23.153	1	23.153	1.606	0.207
Type of Regulation x Client Request	0.001	1	0.001	0.000	0.992	3.060	1	3.060	0.212	0.646
Error	1152.034	135	8.534			1946.701	135	14.420		

Table 3 (Continued)

Panel B: Descriptive Statistics: Mean, (Standard Deviation)*, (n = Number of Participants)

Knowledge Skills [*]	Compliance Skills [^]
* Two-tail	
* Two-tail	
[*] The mean (standard deviation) knowledge skills in the absence of either regulation is 26.54 (3.20) when client request is absent and 26.50 (2.90) when client request is present.	
[^] The mean (standard deviation) compliance skills in the absence of either regulation is 25.22 (3.75) when client request is absent and 24.22 (3.69) when client request is present.	

Type of Regulation	Client Request:			Overall Mean	Client Request:			Overall Mean
	Absent	Present			Absent	Present		
Inspection	28.97	28.46	t = 0.76	28.72	30.13	29.00	t = 1.29	29.57
	(2.71)	(3.11)	p = 0.45	(2.91)	(3.66)	(3.15)	p = 0.20	(3.45)
	(n = 38)	(n = 37)			(n = 38)	(n = 37)		
Rotation	27.38	26.88	t = 0.67	27.19	25.13	24.60	t = 0.54	24.92
	(2.94)	(2.92)	p = 0.50	(2.92)	(4.61)	(3.44)	p = 0.59	(4.17)
	(n = 39)	(n = 25)			(n = 39)	(n = 25)		
Overall Mean	t = 2.39	t = 2.09			t = 5.78	t = 4.48		
	p = 0.02	p = 0.04			p = 0.00	p = 0.00		
	28.17	27.82			27.60	27.23		
	(2.92)	(3.11)			(4.85)	(3.91)		

Note: Inspection refers to the anticipation that a client's file will be inspected. Rotation refers to whether a partner rotation is anticipated in the next year.

Client Request refers to whether a client's audit committee has requested that the best staff be allocated to them.

Knowledge Skills are the summed knowledge skills ratings (from 1 (performance needs improvement) to 5 (performance is exceptional) for each staff member allocated to a client.

Compliance Skills are the summed compliance skills ratings (from 1 (performance needs improvement) to 5 (performance is exceptional) for each staff member allocated to a client.

n = number of participants

TABLE 4

ANOVA and Descriptive Statistics for H3: People Skills

Panel A: ANOVA *

Source	SS	df	MS	F	p
Type of Regulation	133.979	1	133.979	12.565	0.001
Client Request	5.058	1	5.058	0.474	0.492
Type of Regulation x Client Request	38.384	1	38.384	3.600	0.060
Error	1439.471	135	10.663		

Panel B: Descriptive Statistics: Mean, (Standard Deviation)*, (n = Number of Participants)^x

Type of Regulation	Client Request:			Overall Mean
	Absent	Present		
Inspection	26.82	26.14	t = 0.90	26.48
	(2.95)	(3.37)	p = 0.37	(3.16)
	(Cell 3)	(Cell 4)		
	(n = 38)	(n = 37)		
Rotation	27.74	29.20	t = 1.74	28.31
	(3.03)	(3.87)	p = 0.08	(3.43)
	(Cell 5)	(Cell 6)		
	(n = 39)	(n = 25)		
	t = 1.25	t = 3.63		
	p = 0.22	p = 0.00		
Overall Mean	27.29	27.37		
	(3.00)	(3.86)		

* Two-tail

^x The mean (standard deviation) people skills in the absence of either regulation is 27.43 (3.21) when client request is absent and 28.25 (2.99) when client request is present.

Note: Inspection refers to the anticipation that a client's file will be inspected. Rotation refers to whether a partner rotation is anticipated in the next year. Client Request refers to whether a client's audit committee has requested that the best staff be allocated to them. People Skills are the summed people skills ratings (from 1 (performance needs improvement) to 5 (performance is exceptional) for each staff member allocated to a client.

n = number of participants.

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