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Auditor evaluation of others' credibility: A review of experimental studies on determinants and consequences[☆]



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ABSTRACT

I synthesize the extant experimental literature examining auditor evaluation of others' credibility published in six top accounting journals over the last three-and-a-half decades. I adapt the original definition of credibility by [Hovland, Janis, and Kelley \(1953\)](#): the extent of perceiving someone as competent and trustworthy. Audit guidance requires auditors to consider credibility of management, internal auditors, and staff, yet the research literature on auditor evaluation of others' credibility is fragmented and scarce, limiting our understanding of determinants and consequences of auditor evaluations. I develop a framework for analysis of research on auditor evaluation of others' credibility and review extant literature by types of examined effects (determinants of credibility vs. consequences of credibility) and by examined credibility components (competence, trustworthiness, or both). Throughout the literature review I suggest areas for future research.

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1. Introduction and background

Auditor evaluation of credibility of others is fundamental to auditing. Auditing guidance specifically requires auditors to assess competence of personnel who perform controls and of personnel who monitor performance of internal controls (PCAOB, 2007, AS5, par 46–47). Audit standards also require auditors to assess competence and objectivity of internal auditors (PCAOB, 2003, AU 322, par 9–12). In making these assessments the standards direct auditors to consider, along with other relevant sources, “information obtained from previous experience with the internal audit function, from discussions with management personnel, and from a recent external quality review, if performed, of the internal audit function’s activities” (PCAOB, 2003, AU 322, par 11). Audit guidance also requires auditors to consider manager competence and trustworthiness through auditor consideration of internal controls. Auditors are required to opine on internal controls of their public clients (Sarbanes-Oxley Act) and COSO’s 2013 Integrated Framework on Internal Controls emphasized manager competence and trustworthiness as key components of an effective control environment (COSO, 2013).

I adapt the original definition of credibility by Hovland, Janis, and Kelley (1953): the extent of perceiving someone as competent and trustworthy. COSO specifies that “competence is the qualification to carry out assigned responsibilities. It requires relevant skills and expertise, which are gained largely from professional experience, training, and certifications. It is expressed in the attitude, knowledge and behavior of individuals as they carry out their responsibilities” (COSO, 2013). The Framework emphasizes management’s competence as one of the key components of an effective system of internal controls. The Framework also emphasizes the importance of management’s trustworthiness as a vital component of an effective system. The first principle of the Framework is that the organization should demonstrate a commitment to integrity and ethical values (COSO, 2013). For the purposes of this review, I use the definitions of competence and trustworthiness that are suggested by the Framework.

Understanding the determinants and consequences of others’ credibility on auditors’ judgment is vital to the auditing profession, particularly for settings where judgment latitude is inherently great, such as in evaluation of internal control effectiveness. To-date there has been no review of the extant research on auditors’ evaluation of others credibility. This research area would greatly benefit from a research framework that would categorize the extant research and identify areas that need further examination. The goal of this review is to develop such a framework, to analyze what we know from extant research within this framework, and to identify promising areas for future research. Fig. 1 outlines the proposed framework for analysis of the research on determinants and consequences of auditors’ perceptions of others’ credibility. The framework subdivides the literature by types of examined effects (determinants of credibility vs. consequences of credibility) and by examined credibility components (competence, trustworthiness, or both). In addition, each segment is further subdivided into evaluatee types: manager or other auditor.

My review of the literature shows that much less work has been done on determinants (12 studies covered in this review) compared to consequences of credibility components (30 studies covered in this review, with 2 studies double-counted in the numbers of studies on determinants and on consequences). The literature on determinants of credibility perceptions suggests that auditor evaluations of credibility are affected by multiple factors individually and in interaction with each other, including task difficulty, familiarity with the evaluatee, hierarchical relationship with the evaluatee, the evaluatee’s attempt to prevent the problem, the auditor’s prior communication to warn management about the problem, internal auditor compensation, and perception of organizational growth. The literature on consequences of credibility perception suggests that credibility perception affects multiple judgments, including perception of information reliability, evaluation of internal control system, likelihood of suggesting an audit adjustment, evaluation of reasonableness of management’s forecasts, audit effort planning, perceived ability of other auditors to detect misstatements, and reliance on internal auditors and internal control system. In addition, at least one study reports an interaction of credibility with other factors. This analysis highlights the importance of research on credibility perceptions and suggests multiple areas for research.

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