

Auditor Expertise, Jurors' Social Identities and Evaluations of Auditor Negligence

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This paper employs Social Identity Theory to investigate the impact of auditor expertise and jurors' identification with auditors on jurors' perceptions of auditor negligence. Consistent with expectations, jurors who identified more strongly with auditors (strong identifiers) levied more lenient negligence judgments to auditors than weak identifiers. These findings suggest that lay jurors demonstrate the ability to empathize with auditors. However, the significant interaction between jurors' social identities and the firm's level of expertise suggests that the effects of jurors' identities on negligence verdicts may be constrained by firm characteristics.

INTRODUCTION

Social Identity Theory (SIT) proposes that individuals have a positive image of themselves, which may result in a more favourable judgment of others who they consider similar. Attempts to understand juror biases using SIT have not been undertaken until recently, when Reffett et al. (2012) anecdotally suggested that lay jurors' biases may be explained by SIT. The present study differs from Reffett et al. (2012), as this study's objective is to empirically examine whether the strength of jurors' identification with auditors impacts their perceptions of auditor negligence by operationalizing SIT.

This study is motivated by the scarcity with which juror bias is examined in auditing research. Outside of Kadous' (2001) use of the "affect-as-information" theory and Reffett et al.'s (2012) anecdotal attribution of juror behaviour to SIT, research that operationalizes psychology theories is needed to explain juror behaviour. Reffett et al. (2012) suspect that lay jurors are more likely to express empathy towards auditors, since their study assumes that lay jurors' lack of auditing experience makes them unfit to empathize with auditors. However, it is unknown whether lay jurors are unable to identify with auditors solely because they do not have audit experience. Hence, it is an empirical question as to whether the strength of jurors' identification allows them to empathize with auditors, thereby creating more "accurate and favourable outcomes" for auditors in negligence cases. This paper attempts to accomplish this task.

Mock jurors were recruited from undergraduate students at a public university in the United States as a proxy for jurors.¹ To understand whether the strength of jurors' identification with auditors influences their assessments of auditor negligence, a 2 x 2 between-subjects experiment was adapted from Thornton and Shaub (2014). The case consists of an auditor who was involved in a negligence lawsuit following the audit of a client to whom aggressive tax services (ATS) was provided. Two independent variables were manipulated. Juror identification was manipulated between strong and weak identifiers. These levels were

collected from participants via Mael and Ashforth's Organizational Identification Scale and analysed to stratify the sample. One other independent variable, industry expertise, was manipulated based on the firm capturing thirty-percent of the market share, a threshold that was used in prior research (McGuire et al., 2012; Neal and Riley, 2004). This variable was included to account for the impact of expertise, which has been found to reduce the likelihood that an auditor would succumb to client pressure when a close-client relationship exists (Bamber and Iyer, 2007).

Consistent with expectations, the results of this study indicate that the strength of jurors' identification with auditors significantly (as a main effect variable) impacts their perceptions of auditor independence, objectivity, and auditor negligence. These findings suggest that lay jurors demonstrate the ability to empathize with auditors, as evidenced by strong identifiers' assignment of lower negligence verdicts to auditors than weak identifiers. This study also proposed a hypothesis that examined jurors' identification with auditors and expertise as main effects variables as well as the interaction between these variables. The significant interaction term indicates that while juror identification is a major factor in the assignment of liability, their negligence verdicts also depend on other important factors such as an auditors' expertise. Collectively, these results suggest that the strength of jurors' identification with auditors impacts their negligence verdicts, but the effect may be constrained by certain auditor characteristics.

The findings from this study have implications for research and practice. From a research perspective, this study is the first to employ the Social Identity Theory to examine the role juror bias in auditor negligence cases. This contribution advances the work of Reffett et al. (2012), who interpret lay evaluators' judgments in light of SIT, but do not operationalize the theory in their analysis. The current study overcomes this limitation by adapting Mael and Ashforth's Organizational Identification Scale to measure the strength of jurors' identification with auditors, and including this measurement as an independent variable. This leads to the recognition of a subset of jurors whose judgments may be unknowingly have a predetermined bias that may be identified during the juror selection process. Through this identification process, juror panels may be likely to reflect panels of peers who are able to express empathy with respect to their evaluations of auditor negligence.

From a legal standpoint, Brandon and Mueller (2006) propose that jurors' perceptions – not reality – may ultimately determine an auditor's fate in court. Bauer (2015) suggests that heightening the salience of an attribute may increase a desired result (i.e. heightening professional salience increases professional scepticism). The findings that the strength of juror identification impacts negligence verdicts may be instrumental to attorneys in their decision as to whether to take a case to trial or to settle out of court.

The next section reviews the literature and develops the hypotheses examined in the study. The third section describes the study's research method. The fourth section provides the results, followed by the conclusion and opportunities for future research in the fifth section.

THEORY AND HYPOTHESES

Auditor independence is an essential element of audit quality and a requirement for registered public accounting firms (PCAOB, 2004). The SEC asserts that both independence "in fact" and "in appearance" are equally important (SEC, 2001). The SEC declares auditor independence to be impaired if the provision of nonaudit services "(a) creates a mutual or conflicting interest between the accountant and the audit client, (b) places the accountant in the position of auditing his or her own work, (c) results in the accountant acting as management or an employee of the audit client, or (d) places the accountant in a position of being an advocate for the audit client" (SEC, 2001). Several survey-based research studies find independence to be impaired when auditors provide audit and nonaudit services to an audit client (Briloff, 1966; Lavin, 1976; Firth, 1981; Shockley, 1981; Pany and Reckers, 1988).² Some experimental research supports these findings (Lowe and Pany, 1996; Mishra et al., 2005), while others do not (McKinley et al., 1985; Pany and Reckers, 1987).

Brandon and Mueller (2006, p. 3) highlight the importance of juror-based research, as they state that jurors' perceptions of auditor independence are likely to determine an auditor's fate in court. The present

study extends their line of research to investigate whether one psychological aspect – jurors’ identification with auditors –impairs their perceptions of auditor independence when auditors are prohibited from providing ATS to their audit clients.

Aggressive Tax Services

The AICPA indicates that tax professionals of accounting firms who provide tax services to their audit clients “become advocates [for their clients] that develop favourable tax positions that fall within the boundaries of the tax law (AICPA, 2000).” Accounting regulators suggest that the provision of ATS “place the auditor in a position inconsistent with the necessary objectivity” (SEC, 2001). Accordingly, the SEC (2006) and the PCAOB (2005) declare registered public accounting firms to be non-independent if they engage in the marketing, planning, or expressing of an opinion on aggressive tax positions for their audit clients.³

Research suggests that the proscription of these services was a reaction to accounting scandals at the turn of the century rather than the result of empirical evidence that ATS impair independence (Thornton and Shaub, 2014; Sloan, 2005). Thornton and Schaub (2014) report that jurors deem auditor independence to be impaired by the joint provision of audit and ATS. The goal of the present study is not to investigate whether ATS services impair perceptions of auditor independence, but to investigate whether perceptions of independence may be skewed by jurors’ social identities. The Social Identity Theory is employed to accomplish this task.

Social Identity Hypothesis

The Social Identity Theory is a cognitive-based theory that is concerned with when and why individuals identify with and/or adopt the shared attitudes and behaviours of certain groups (Tajfel and Turner, 1985). An individual’s social identity represents their sense of who they are based on their group membership(s). The four components in the development of a social identity are: (1) categorization, (2) identification, (3) comparison, and (4) psychological distinctiveness. This study is concerned with the elements of categorization (which addresses how individuals categorize themselves) and comparison (which addresses an individual’s favourable bias towards one group over another). The process of developing a social identity begins with an individual defining oneself, and then aligning themselves with groups where people in the group are perceived by the individual to be similar to that individual. While it is possible for individuals experiencing a social identity crisis to possess multiple distinct identities, the most prevalent identity usually manifests itself.

Much research has explored the use of SIT to understand service organizations, employees and auditors. Social identity problems are prevalent in service organizations and knowledge-intensive organizations (Alvesson, 2000). Social psychology and organizational behavioural research find that social identity problems may significantly affect employees’ attitudes and behaviours (Hogg and Terry, 2000; Ellemers et al., 2002; Riketta, 2005). Psychology literature suggests that auditors who feel a strong social identity with their client are more likely to internalize the client’s accounting and business norms, which may affect how the auditor makes accounting decisions (Lembke and Wilson, 1998).

Despite the application of SIT in auditing literature, this theory has not been employed to investigate whether jurors’ identification with auditors impacts their verdicts in auditor independence cases. Two competing lines of reasoning may be advanced with respect to this matter. Arguably, one of the most sinister threats to a juror’s proper rendering of an unfavourable negligence verdict in an audit independence case may arise when jurors strongly identify with auditors. Ingriselli (2015, p. 1697) suggests that the core of the social identity theory is that individuals desire to have a positive image of themselves, and are willing to be more lenient when judging those they consider to be similar to them. By doing so, this promotes favourable perceptions of individuals’ social groups, which may increase individuals’ self-esteem. Following this logic, this study proposes that jurors who strongly identify with auditors may judge auditors less harshly than jurors who do not identify with auditors. The following hypothesis examines this theory:

- H1a: Strong identifiers will perceive auditors to be more independent than weak identifiers
- H1b: Strong identifiers will perceive auditors to be more objective than weak identifiers
- H1c: Strong identifiers will perceive auditors to be less negligent than weak identifiers

Industry Expertise Hypothesis

An alternative line of reasoning suggests that auditor-identifying jurors who believe that an auditor's industry expertise insulates the auditor from factually impairing their independence may fail to find expert auditors negligent when providing nonaudit services to clients. Over time, accounting firms develop their expertise by training, by auditing clients in the same industry (Ferguson et al., 2003) and by sharing knowledge and experience across clients. Wilson (2015b) posits that auditors' concerns about their reputation for quality is a financial incentive which deters them from compromising their objectivity during an audit. However, the literature is mixed as to whether a firm's reputation as an industry expert will motivate them to provide a high quality audit.

Psychology research predicts that more experienced decision makers have highly-developed knowledge structures that allow them to focus on evidence that is relevant to the situation at hand (Patel and Groen, 1986; Lesgold et al., 1988). Likewise, expert auditors have incentives to provide high quality audit services (Chin and Chi, 2009; Eichenseher and Danos, 1981). Expert auditors are also associated with higher quality disclosures (Dunn and Mayhew, 2004), exhibit a higher degree of compliance with audit standards (O'Keefe et al., 1994), and protect their reputations to reduce the occurrences of frivolous lawsuits (Datar and Alles, 1999). Research also indicates that expertise is associated with higher audit quality (Reichelt and Wang, 2010) and the reduced likelihood to succumb to client pressure (Bamber and Iyer, 2007). Given these findings, conventional wisdom suggests that in the absence of regulations prohibiting auditors' provision of these services, expert firms' audit quality and objectivity may not be impaired during the audit.

However, this prediction is not without tension. Auditing research does not find a direct relationship between expertise and financial reporting reliability (Wilson, 2015a; DeZoort et al., 2012; Sainty et al., 2002). Likewise, psychology research also indicates that less experienced auditors possess a "surface level" understanding of domain-specific knowledge (Frederick and Libby, 1986; Bedard and Biggs, 1991), which tends to result in the generation of fewer alternative hypotheses and explanations regarding evidence collected during the engagement. Hence, it is an empirical question as to whether industry expertise will convince jurors that expert firms' independence and objectivity will not be compromised by providing ATS to an audit client.

When concurrently considering expertise and jurors' level of identification with auditors, another question that arises is whether the significance of jurors' identification would be greatest among the levels of the firm's expertise, or equally significant under each condition. That is, it is unknown whether jurors' identification is a main effect or an interaction effect. The following hypothesis addresses this line of reasoning:

- H2: In cases of alleged auditor negligence, juror identification will significantly impact jurors' perceptions of the auditor's negligence when auditing and providing ATS to the client across levels of the firm's expertise.

METHODOLOGY

Participants

Undergraduate student participants were recruited from undergraduate classes at a public university in the United States as a proxy for jurors. The use of college undergraduates as a proxy for jurors is consistent with prior auditing research (Reffett et al., 2012; Wilson, 2015b; Brandon and Mueller, 2006; Kadous, 2000), which fails to find consistent differences between students and mock jurors (Zickafoose and Bornstein, 1999; Bornstein, 1999).

A total of 120 responses were collected. Of these, 87 usable responses were obtained (Table 1, Panel A). Thirty-two responses were removed due to a failed response to the manipulation check question. One

response was not recorded, as the student opted not to complete the study. On average, participants were 28.7 years of age, which indicates a high percentage of non-traditional students, and speaks to the maturity of the students participating in the study. Approximately 31.8 percent of the participants indicated that have owned stock. Regarding their political preferences, 17.2 percent indicated that they were liberal, while 57.5 percent indicated that they were conservative. Finally, nearly 70.5 percent of participants' indicated that they had taken three or fewer political science classes.

TABLE 1
DEMOGRAPHIC OVERVIEW

Panel A: Jurors' Demographics

| | |
|--|------|
| Age (years) | 28.7 |
| Female (percentage) | 61.4 |
| Participants Who Have Owned Stock (percentage) | 31.8 |
| Political Preference (percentage) | |
| Liberal | 17.2 |
| Conservative | 57.5 |
| Percentage Who Have Taken Three or Fewer Political Science Classes | 70.5 |
| Approximate Level of Income (percentage)* | |
| Less than \$60,000 | 75.6 |
| More than \$60,000 | 10.4 |
| No Answer Provided | 14.0 |

*Differences in 100% due to rounding

Panel B: Participant Distribution

| <u>Experimental Manipulation</u> | <u>Random Distribution</u> | <u>Usable Responses (Passed Manipulation Check)</u> |
|--|--------------------------------|---|
| Weak Auditor Identification * High Expertise | 30 | 24 |
| Weak Auditor Identification * Low Expertise | 30 | 22 |
| Strong Auditor Identification * High Expertise | 30 | 22 |
| <u>Strong Auditor Identification * Low Expertise</u> | 30 | <u>19</u> |
| Usable Responses | | 87 |

Independent Variable of Interest and Research Task

Participants were randomly assigned to one of the two experimental case studies through Qualtrics®, the online platform used to administer the study.⁴ In the following sections, “Task One” provides an overview of participants’ first task, which was undertaken to acquire how strongly participants identified with auditors. “Task Two” discusses the construction of the experiment, the manipulation check and the collection of demographic data.

Task One (Juror Social Identity)

The first task was to complete Mael and Ashforth’s Organizational Identification Scale in order to collect information regarding participants’ level of identification with auditors (Mael and Ashforth, 1992). Five questions from the scale were modified to acquire participants’ level of identification with auditors. Following each question, participants were asked to indicate their level of agreement with each question on a 5-point Likert scale anchored at 1 = Completely Disagree and 5 = Strongly Agree. During the research analysis phase, participants’ responses were averaged together. Participants whose average scores were between “4” and “5” were identified in the analysis as “Strong Identifiers”; all others were

identified as “Weak Identifiers.” As a result of this process, participants were post-experimentally assigned to the main variable of interest: juror identification.

Task Two

Following the completion of the Organizational Identification Scale, participants were prompted in Qualtrics® to proceed to the next section (the experiment). The experiment was adapted from prior research (Thornton and Shaub, 2014; Kadous, 2000). The experiment was constructed using an audit litigation case, since research finds that legal action is most likely to be taken against an auditor if the client experiences bankruptcy (Carcello and Palmrose, 1994; Palmrose, 1987). In addition, the motivation for grafting an alleged audit failure in the case was inspired by Casterella et al. (2009, p. 716), who suggest that a malpractice claim is a reasonable proxy for audit failure.

The experiment involved the plaintiff (Johnson, Ltd.) who relied on Western Rock and Gravel's financial statements to extend a loan to the client. The plaintiff (Johnson, Ltd.) alleges that Smith & Adams CPA Firm failed to uncover management fraud during their audit of the client, and Johnson suffered severe losses by relying on these audited financial statements to extend a loan to the client. The defendant (Smith & Adams CPA) argues that the financial statement audit was performed in conformity with the generally accepted auditing standards which were in place at the time of the audit. After reading the case, participants were asked to complete a post-experimental questionnaire. This questionnaire collected participants' perceptions of the firm's independence, objectivity and their assessments of negligence to the firm following the alleged audit failure.

Using Qualtrics®, participants were not allowed to access the case again after completion of the experimental questions. Following the completion of the post-experimental questions, participants were asked to complete a manipulation check on a separate screen to ensure that they understood the case. Finally, participants' demographic information was collected.

Expertise Manipulation

In addition to the tension in the literature centred on auditor expertise, this variable is manipulated in this study to reduce the salience of the study's focus on juror identity, thereby decreasing the likelihood of demand effects amongst the participants. The present study posits that industry expert firms will be perceived as being less negligent in auditor liability cases. In order to achieve this manipulation, the study adopts McGuire et al.'s (2012) methodology to operationalize industry expertise by designating industry expert firms as those whose market share exceeds 30 percent. The study manipulates industry experts as firms that “audit over 75% of the market share.” Non-industry experts are designated as auditing 25% of the market share.

Dependent Measures

Participants' perceptions of the following three dependent measures were collected in the study: auditor independence, objectivity and auditor negligence. Participants were asked to indicate their level of agreement with each dependent measure by providing both a dichotomous response (yes, no) and a five-point confidence-in-answer assessment. These responses were combined to create a 10-point agreement rating scale, anchored at 1 = Not Confident at All and 10 = Completely Confident. The combined confidence-in-answer measure is consistent with prior research, and provides a more predictive measure than a single dichotomous response (Wilson 2017, Brandon and Mueller, 2006). An overview of the dependent variables is as follows.

Independence (Appearance)

Participants were presented with a question to measure their perceptions of auditor independence when the firm provided audit and ATS to their audit clients, which was adapted from prior research (Wilson, 2015a; DeZoort et al., 2012). To gather their perceptions of this measure, the participants were asked to respond to the following statement: “Smith & Adams, CPAs would have a conflict of interest

during the audit if they were to provide the client with tax advice that would legally help the client lower their income taxes.”

Objectivity

Similar to the construction of the independence question, a question which measured participants' perceptions of auditor objectivity during the audit was adapted from prior research (Wilson, 2015a; DeZoort et al., 2012). The following question was presented to participants to obtain this information: “Smith & Adams’ audit team was **not** objective when auditing Western.”

Negligence

In order for a plaintiff to recover for negligence against a defendant, a plaintiff must establish four elements by a preponderance of the evidence. These elements were presented to participants following the reading of the case study. Afterwards, the following question was adapted from Wilson (2015b) and presented to participants to gain their understanding of the firm’s negligence: “Was Smith & Adams, CPAs, negligent in the performance of the audit for Atlantis?”

RESULTS

Hypothesis One Test

Hypothesis 1 examines whether strong jurors perceive auditors independence, objectivity and negligence more favourably than weak identifiers when auditors perform audit and ATS for an audit client. The results indicate that jurors’ identification with auditors is significantly associated with jurors’ perceptions of firm independence, but in an unexpected direction ($p = 0.032$). Similarly, the relationship between juror identification and objectivity is marginally significant ($p = 0.053$), but in an unexpected direction. However, juror identification is significantly associated with jurors’ negligent verdict in the expected direction ($p = 0.000$). The finding that strong identifiers perceive auditors to be less negligent despite unexpectedly lower ratings for independence and objectivity appear to indicate that jurors are empathetic towards auditors, even in the midst of properly interpreting the current independence standards. Hypothesis 1 partially is supported (Table 2, Panel B).

Hypothesis Two Test

Independence and Objectivity

A preliminary analysis finds that jurors’ identification with auditors is statistically significant in explaining their perceptions of independence ($p = 0.036$, Table 3, Panel B) and marginally significant in explaining their perceptions of objectivity ($p = 0.065$, Table 4, Panel B).⁵ Although not statistically significant, the interaction between juror identification and firm expertise is practically significant, as it closely approaches marginal significance at $p = 0.10$ (independence, $p = 0.106$; Table 3, Panel B; objectivity, $p = 0.101$; Table 4, Panel B).

TABLE 2
THE IMPACT OF THE STRENGTH OF JURORS' IDENTIFICATION WITH AUDITORS
ON THEIR PERCEPTIONS OF AUDITOR INDEPENDENCE, OBJECTIVITY AND
NEGLIGENCE

Panel A: Descriptive Statistics

| <u>Jurors' Perceptions</u> | <u>Strength of Juror Identification with Auditors</u> | | |
|--------------------------------------|---|-------------------------------|-------------------------------|
| | <u>Weak Identifier</u> | <u>Strong Identifier</u> | <u>Total</u> |
| Auditor Independence (Appearance) | 6.8511 (3.21667) n = 47 | 5.2927 (3.48026) n = 41 | 6.1250 (3.41334) n = 88 |
| Auditor Objectivity | 7.1957 (2.50883) n = 46 | 5.9268 (3.48131) n = 41 | 6.5977 (3.05553) n = 87 |
| Juror Negligence Verdict | 7.7609 (2.45117) n = 46 | 5.3171 (3.48166) n = 41 | 6.6092 (3.20739) n = 87 |

Panel B: GLM Analysis of Variance

| <u>Variables</u> | <u>Sum of Squares</u> | <u>df</u> | <u>Mean Square</u> | <u>F</u> | <u>p-value</u> |
|--------------------------------------|-----------------------|-----------|--------------------|----------|----------------|
| Auditor Independence (Appearance) | 53.180 | 1 | 53.180 | 4.762 | **0.032 |
| | 960.445 | 86 | 11.168 | | |
| | 1013.625 | 87 | | | |
| Auditor Objectivity | 34.900 | 1 | 34.900 | 3.863 | ***0.053 |
| | 768.020 | 85 | 9.036 | | |
| | 802.920 | 86 | | | |
| Juror Negligence Verdict | 129.465 | 1 | 129.465 | 14.571 | *0.000 |
| | 755.248 | 85 | 8.885 | | |
| | 884.713 | 86 | | | |

*p < 0.01, ** < 0.05, *** < 0.10

Participants provided a dichotomous response (no / yes) along with a five-point confidence-in-answer scale, anchored at 1 = "not confident at all" and 5 = "completely confident." These responses were combined to create a 10-point scale, anchored at 1 = "completely not independent/objective/negligent." and 10 = "completely independent/objective/negligent." The questions to which they responded are as follows:

Independence: "Smith & Adams, CPAs would have a conflict of interest during the audit if they were to provide the client with tax advice that would legally help the client lower their income taxes."

Objectivity: "Smith & Adams' audit team was **not** objective when auditing Western."

Negligence: "Was Smith & Adams, CPAs, negligent in the performance of the audit for Atlantis?"

TABLE 3
THE IMPACT OF THE STRENGTH OF JURORS' IDENTIFICATION WITH AUDITORS ON
THEIR PERCEPTIONS OF AUDITOR FIRM'S INDEPENDENCE

Panel A: Descriptive Data

| <u>Strength of Auditor Identification</u> | <u>Level of Industry Expertise</u> | | <u>Total</u> |
|---|------------------------------------|-------------------------------|-------------------------------|
| | <u>High Expertise</u> | <u>Low Expertise</u> | |
| Weak Identifier | 7.5833 (3.02046) n = 24 | 6.0870 (3.30169) n = 23 | 6.8511 (3.21666) n = 47 |
| Strong Identifier | 4.9091 (3.55781) n = 22 | 5.7368 (3.42932) n = 19 | 5.2927 (3.48026) n = 41 |
| Total | 6.3043 (3.52054) n = 46 | 5.9286 (3.32318) n = 42 | 6.1250 (3.41334) n = 88 |

Panel B: Multivariate Test

Dependent Variable: Jurors' Perceptions of Firm Independence

| <u>Source</u> | <u>Sum of Squares</u> | <u>df</u> | <u>Mean Square</u> | <u>F</u> | <u>p-value</u> |
|----------------------------------|-----------------------|-----------|--------------------|----------|----------------|
| Corrected Model | 86.463 | 3 | 28.821 | 2.611 | 0.057 |
| Intercept | 3226.957 | 1 | 3226.957 | 292.359 | 0.000 |
| Juror Identification | 49.919 | 1 | 49.919 | 4.523 | **0.036 |
| Industry Expertise | 2.440 | 1 | 2.440 | .221 | 0.639 |
| Juror Identification x Expertise | 29.480 | 1 | 29.480 | 2.671 | 0.106 |
| Error | 927.162 | 84 | 11.038 | | |
| Total | 4315.000 | 88 | | | |
| Corrected Total | 1013.625 | 87 | | | |

*p < 0.01, **p < 0.05, ***p < 0.01

Participants were asked the following question to obtain their perceptions of auditor independence: "Smith & Adams, CPAs would have a conflict of interest during the audit if they were to provide the client with tax advice that would legally help the client lower their income taxes."

Participants provided a dichotomous response (no / yes) along with a five-point confidence-in-answer scale, anchored at 1 = "not confident at all" and 5 = "completely confident." These responses were combined to create a 10-point scale, anchored at 1 = "completely not independent" and 10 = "completely independent."

In isolation, the expertise variable is not significant in explaining jurors' perceptions of independence (p = 0.639, Table 3, Panel B) and objectivity (p = 0.594, Table 4, Panel B). It would be expected, however, that strong identifiers would likely perceive expert auditors to be more independent than auditors with lesser expertise. This expectation is rooted in Bamber and Iyer's (2007) findings that more experienced auditors are less likely to acquiesce to client pressure. Accordingly, consistent with the Social Identity Theory, it would be expected that strong identifiers would be more lenient towards high expert firms in order to protect their own image unless they deem the transgression to be grossly egregious. However, the direction of the expertise variable in both analyses is contrary to expectations.

TABLE 4
THE IMPACT OF THE STRENGTH OF JURORS' IDENTIFICATION WITH AUDITORS ON
THEIR PERCEPTIONS OF AUDITOR OBJECTIVITY

Panel A: Descriptive Data

| <u>Strength of Auditor Identification</u> | <u>Level of Industry Expertise</u> | | |
|---|------------------------------------|-------------------------------|-------------------------------|
| | <u>High Expertise</u> | <u>Low Expertise</u> | <u>Total</u> |
| Weak Identifier | 7.5417 (2.26465) n = 24 | 6.8182 (2.75398) n = 22 | 7.1957 (2.50883) n = 46 |
| Strong Identifier | 5.2727 (3.34068) n = 22 | 6.6842 (3.57542) n = 19 | 5.9268 (3.48131) n = 41 |
| Total | 6.4565 (3.02366) n = 46 | 6.7561 (3.12074) n = 41 | 6.5977 (3.05553) n = 87 |

Panel B: Multivariate Test

Dependent Variable: Jurors' Perceptions of Auditor Objectivity

| <u>Source</u> | <u>Sum of Squares</u> | <u>df</u> | <u>Mean Square</u> | <u>F</u> | <u>p-value</u> |
|----------------------------------|-----------------------|-----------|--------------------|----------|----------------|
| Corrected Model | 61.220 | 3 | 20.407 | 2.284 | 0.085 |
| Intercept | 3739.448 | 1 | 3739.448 | 418.463 | 0.000 |
| Juror Identification | 31.176 | 1 | 31.176 | 3.489 | ***0.065 |
| Treatment | 2.556 | 1 | 2.556 | .286 | 0.594 |
| Juror Identification x Expertise | 24.611 | 1 | 24.611 | 2.754 | 0.101 |
| Error | 741.700 | 83 | 8.936 | | |
| Total | 4590.000 | 87 | | | |
| Corrected Total | 802.920 | 86 | | | |

*p < 0.01, **p < 0.05, ***p < 0.10

Participants were asked the following question to obtain their perceptions of auditor objectivity: "Smith & Adams' audit team was **not** objective when auditing Western."

Participants provided a dichotomous response (no / yes) along with a five-point confidence-in-answer scale, anchored at 1 = "not confident at all" and 5 = "completely confident." These responses were combined to create a 10-point scale, anchored at 1 = "completely not objective" and 10 = "completely objective."

Negligence

Hypothesis 2 examines whether juror identification will significantly impact jurors' perceptions of auditor negligence when auditing and providing ATS to the client across varying levels of industry expertise.⁶ The results are similar to those in the independence and objectivity analysis. The fundamental difference, however, is that the interaction term is significant in explaining perceptions of auditor negligence (p = 0.001, Table 5, Panel B). An untabulated general linear model regression analysis finds that the parameter estimate of the interaction term is negative, which suggest that lower negligence verdicts may occur amongst strong identifiers, but that is dependent on the auditor's level of expertise.⁷ From an academic perspective, the significant interaction term supports research which suggests that strong group identities

may result in more positive views of the group (Ingriselli, 2015; Haslam and Ellemers, 2005). Hypothesis 2 is supported.

DISCUSSION, LIMITATIONS, FUTURE RESEARCH

Concerns have been presented which question lay jurors' management of auditor negligence cases, with some auditors feeling more comfortable settling these cases prior to trial, at times to their disadvantage (Cook et al., 1992). Prior to this study, no empirical evidence existed which examined whether strength of jurors' identification with auditors influences their negligence verdicts in auditor litigation cases. The present study draws on SIT to investigate this phenomenon to investigate auditors' independence, objectivity and negligence when an accounting firm audits and provides ATS to their clients. This theory was also employed to examine whether the difference in auditor negligence verdicts due to jurors' identification with auditors depends on the firm's expertise, since Bamber and Iyer (2007) suggests that an auditor's expertise reduces the likelihood that the auditor will acquiesce to client demands.

The central finding of this study is that the strength of jurors' social identities alone influences their perceptions of auditor negligence. When an additional variable (industry expertise) is considered, it is the interaction between these two variables that was significant in explaining their auditor negligence verdicts. On one hand, the practical significance of these results is that auditors, who in the past have doubted whether lay jurors would empathize with auditors (Reffett et al., 2012), now have reason to believe that this is not a universal occurrence. On the other hand, these results may prompt the legal environment to provide additional screening procedures to ensure that a fair mix of jurors are employed to provide an unbiased estimate of juror negligence in auditor litigation cases.

While these findings are instrumental in filling the void in the academic literature, must be interpreted by accounting practitioners within the limitations of the study. One, collection of jurors' social identities in this study was orchestrated using Mael and Ashforth's Organizational Identification Scale. The development of other measures to understand jurors' social identities, such as adopting Bauer's (2015) instrument to ascertain the strength of jurors' social identities, will add to the understanding of how this influences their negligence verdicts. Two, SIT theory is only one theory which seeks to predict jurors' responses. Outside of a handful of studies that specifically investigate juror bias (Reffett et al., 2015; Peecher and Piercey, 2008; Lowe and Reckers, 2006; Kadous, 2001), research on this matter is scant. Future research may investigate how other psychology and social science theories may be employed to provide a more comprehensive understanding of juror biases in auditor negligence cases.

TABLE 5
THE IMPACT OF THE STRENGTH OF JURORS' IDENTIFICATION WITH AUDITORS
ON THEIR PERCEPTIONS OF AUDITOR NEGLIGENCE

Panel A: Descriptive Data

| <u>Strength of Auditor Identification</u> | <u>Level of Industry Expertise</u> | | <u>Total</u> |
|---|------------------------------------|----------------------|--------------|
| | <u>High Expertise</u> | <u>Low Expertise</u> | |
| | 8.8333 | 6.5909 | 7.7609 |
| Weak Identifier | (0.91683) | (3.03408) | (2.45117) |
| | n = 24 | n = 22 | n = 46 |
| | 4.3636 | 6.4211 | 5.3171 |
| Strong Identifier | (3.2300) | (3.51688) | 3.48166 |
| | n = 22 | n = 19 | n = 41 |
| | 6.6957 | 6.5122 | 6.6092 |
| Total | (3.2240) | (3.22585) | (3.20739) |
| | n = 46 | n = 41 | n = 87 |

Panel B: Multivariate Test

Dependent Variable: Jurors' Perceptions of Auditor Negligence

| <u>Source</u> | <u>Sum of Squares</u> | <u>df</u> | <u>Mean Square</u> | <u>F</u> | <u>p-value</u> |
|----------------------------------|-----------------------|-----------|--------------------|----------|----------------|
| Corrected Model | 230.339 | 3 | 76.780 | 9.739 | 0.000 |
| Intercept | 3708.860 | 1 | 3708.860 | 470.427 | 0.000 |
| Juror Identification | 116.224 | 1 | 116.224 | 14.742 | *0.000 |
| Treatment | .185 | 1 | .185 | .023 | 0.879 |
| Juror Identification x Expertise | 99.827 | 1 | 99.827 | 12.662 | *0.001 |
| Error | 654.374 | 83 | 7.884 | | |
| Total | 4685.000 | 87 | | | |
| Corrected Total | 884.713 | 86 | | | |

*p < 0.01

Participants were asked the following question to obtain their perceptions of auditor negligence:
 "Was Smith & Adams, CPAs, negligent in the performance of the audit for Atlantis?"

Participants provided a dichotomous response (no / yes) along with a five-point confidence-in-answer scale, anchored at 1 = "not confident at all" and 5 = "completely confident." These responses were combined to create a 10-point scale, anchored at 1 = "completely not negligent" and 10 = "completely negligent."

ENDNOTES

1. Reffett et al. (2012) and Kadous (2000) defended the use of undergraduate students as a proxy for jurors.
2. Non-experimental research surrounding the passage of the Sarbanes-Oxley Act (SOX) suggests that the joint provision of audit and nonaudit services impairs independence (Lowe et al., 1999; Raghunandan, 2003; Krishnan et al., 2005; Francis and Ke, 2006).
3. The PCAOB defines an aggressive tax position as one that is undertaken for the purpose of tax avoidance unless the position is "more likely than not" to be allowed under the current tax laws (SEC 2006).
4. In order to maintain compliance with the Institutional Review Board, participants were provided with an informed consent form that (1) communicated to them the general nature of the research prior to beginning

- the experiment, (2) to guaranteed anonymity to the participants and (3) informed participants of their rights to opt out of the study.
5. These results were primarily driven by strong identifiers' perceptions of expert firms.
 6. To test for demand effects, ANOVA was performed to investigate whether interaction occurred where an effect was not predicted. Tests were examined to find whether the effect of weak versus strong identifiers on negligence perceptions were significant in one level of expertise but not the other. The analysis reveals that a significant difference exists between weak versus strong identifiers in the industry expertise condition ($p = 0.000$) but not in the non-expert condition ($p = 0.869$). This statistical analysis satisfies the study's goal of creating an independent variable in which demand effects do not exist (or were minimal, at best).
 7. The parameter estimates for the treatment, juror identification and interaction variables are 2.057, 4.470, and negative 4.300, respectively.

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