

# Mandatory Audit Firm Rotation: A Student Perspective

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## Declaration

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## **Dedications and acknowledgements**

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## **Abstract**

The purpose of the research project was to obtain an understanding of student's perception of Mandatory Audit Firm Rotation (MAFR). The perception is determined based on the impact students consider MAFR to have on auditor independence, audit quality and other aspects of the auditing profession and practice are considered. A theoretical framework for the auditing profession and practice as well as MAFR is outlined, considering the role conflict theory, the audit expectation gap, economic theories of regulation and the living law of auditing. Literature currently available on audit firm rotation shows a mixture of both a positive and negative impact resulting from the implementation of MAFR on independence, quality and other aspects. The study follows a post-positivist research paradigm which informs the quantitative approach in addressing the objectives of the project. The population for the study is defined as auditing students at the universities of Zululand and KwaZulu-Natal (determined to be 1 619). Those in attendance at a pre-determined auditing lecture time slot or session were handed out the questionnaire for completion. A total of 413 questionnaires were collected, coded and captured for analysis. The data was then analysed using descriptive and inferential statistics to determine the perception of students on MAFR. Other comments on MAFR, solicited from participants were summarised as part of the data analysis. The study concludes that the majority of students believe that the implementation of MAFR would primarily yield positive outcomes on independence, quality and other aspects and are thus can be considered to be in favour of the implementation of MAFR.

## **Key words**

Mandatory Audit Firm Rotation, MAFR, independence, audit quality, auditor rotation.

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## LIST OF ABBREVIATIONS USED

BASA	Banking Association of South Africa
BCom (Acc)	Bachelor of Commerce (Accounting)
BCom (AccScie)	Bachelor of Commerce (Accounting Science)
Big Four	KPMG, EY, Deloitte and PWC
CA	Chartered Accountant
CAQ	Centre for Audit Quality (United States)
CPC	Code of Professional Conduct
CTA	Certificate in the Theory of Accounting
EC	European Commission
EU	European Union
G20	An international forum for the governments and central bank governors of 19 countries and the European Union
IAASB	International Auditing and Assurance Standards Board
IFAC	International Federation for Accountants
IGAE	Spanish General Comptroller of State Administration
IRBA	Independent Regulatory Board for Auditors
ISA	International Standards on Auditing
MAFR	Mandatory Audit Firm Rotation
MBA	Master of Business Administration
PCAOB	Public Company Accounting Oversight Board
PGDA	Postgraduate Diploma in Accounting
PIE	Public Interest Entity
SA	South Africa
SAICA	South African Institute of Chartered Accountants
RA	Registered Auditor
UKZN	University of KwaZulu-Natal
UNIZULU	University of Zululand

# **CHAPTER 1: INTRODUCTION**

## **1.1. Introduction**

This chapter contains an introduction to the research project that will be undertaken and provides background information to the study. The chapter discusses the aim of the project which is to examine the perception of university auditing students about the Mandatory Audit Firm Rotation (MAFR) rule, objectives and research questions for the project. The project will seek to determine whether or not according to students, the intended implementation of the MAFR rule in South Africa will result in benefits for the auditing profession and the country. Current students are an important consideration and are also stakeholders in discussions on the introduction of the MAFR rule as they will be amongst the first audit teams to be affected by the implementation of the rule.

## **1.2. Background to the study**

It would appear as though the jury is still out on whether MAFR should be implemented or not. This, as no clear consensus, has been reached on the ongoing world debate on the benefits and disadvantages of the implementation of this audit reform. The appropriateness of the implementation of the MAFR rule remains under dispute as proponents and opponents of the rule outline the benefits and negative impact the rule brings. Notwithstanding the current discourse, the Independent Regulatory Board for Auditors (IRBA) of South African issued a notice in accordance with the Auditing Profession Act, 26 of 2005 the rule on MAFR which will come into effect on 1 April 2023 for South African auditors. According to the rule, an audit firm auditing a Public Interest Entity (PIE) shall not accept re-appointment as auditor after having served for ten consecutive years IRBA (2017). The South African Institute of Chartered Accountants (SAICA) and the accounting profession (represented mainly by audit firms) are against the implementation of this rule in its current form [SAICA MAFR Indaba (2016) & SAICA (2017)], citing amongst other issues that the current research on whether or not there are benefits to the implementation of MAFR is mixed.

The mixed research results (Ewelt-Knauer *et al.* 2013, Junaidi *et al.* 2016 & Stern 2015) have caused different jurisdictions to take opposing positions on the legislation of auditor rotation, with some opting not to implement it at all. The United States House of Representatives voted in support of a bill prohibiting the proposal of MAFR for the US in 2013 (Tysiac 2013; Edwards 2014). This vote followed a concept paper of the Public Company Accounting Oversight Board (PCAOB) on independence together with the rotation of audit firms PCAOB (2011), soliciting the views and comments from stakeholders. The responses and comments were generally opposed to audit firm rotation (Williams & Wilder 2017). The European Union (EU), on the other hand, adopted the implementation of MAFR rules emanating from their green paper “*Audit Policy: Lessons from the Crisis*” in 2014 European Commission (2014) for implementation from in 2016.

Currently in South Africa, the rotation of auditors is provided for in company legislation and the IRBA Code of Professional Conduct for auditors (IRBA CPC), specifically for the individual (person) designated auditor (compared to the audit firm as per the new MAFR rule). According to the Companies Act 71 of 2008 (Section 92), “the same individual may not serve as the auditor or designated auditor of a company for more than five consecutive financial years” (RSA Companies Act, 2009). The IRBA CPC on the other hand, recognises that familiarity and self-interest threats to independence are formed by utilising the same higher-ranking employees on an audit client over a lengthy period which could be a cause of significant threats to the independence of the auditor, depending on a number of factors. Continuing auditor-client relationships can lead to auditor complacency and undue trust of the client which threaten their independence (Church *et al.*, 2015). With regard to an audit of a PIE, the code requires an individual not to be the partner in charge for longer than seven years (or else as stated by law or regulation, which in this case is the five years required by the Companies Act (IRBA, 2009a).

The debate over the implementation of MAFR has been ongoing for over five decades around the world (Kwon, Lim and Simnett, 2014). Although IRBA has confirmed the implementation of MAFR for South Africa, similar to observations in the rest of the world, there are bound to be diverse views on whether it is the best solution to meet the objectives put forward by IRBA or not. University auditing students that are

currently studying towards qualification with an IRBA accredited professional body, namely SAICA will, after completing all the requirements, become registered auditors and will be amongst the first auditors to put the new rule into practice. Students can give us, based on varying factors, a unique perspective on the work of auditors, as they see it.

The university auditing student population is comprised of students at various levels of study at universities across the country. Students at these universities are gradually working through formal competency-based academic education (an academic programme) in preparation to write the SAICA Initial Test of Competence (ITC) after successful completion. The academic programmes follow the competency framework provided by the institute SAICA (2016). Students after qualification as chartered accountants with SAICA – CA (SA) and completing the Audit Development Programme (ADP) of the IRBA, are eligible for registration as auditors (Registered Auditor - RA). Thus, students form an essential constituency as the future of the auditing profession. This study will seek to determine the perception of university auditing students about the MAFR rule, given the intended implementation in South Africa from 1 April 2023 for public interest entities as prescribed by the IRBA.

### **1.3. Problem statement**

The IRBA has decided on a date for the implementation of MAFR despite the objections put forward by SAICA (together with the accounting profession and some stakeholders in general (SAICA 2017; SAICA MAFR Indaba 2016). One of the objections was that the results of the research on the effects of MAFR are mixed, not necessarily favouring its implementation (Ewelt-Knauer *et al.* 2013, Junaidi *et al.* 2016 & Stern 2015). The IRBA is of the view that MAFR will improve the independence of auditors which it believes is somewhat compromised by the long audit tenures. The IRBA had also considered the effect(s) that MAFR could have on audit quality, the transformation of the profession and deconcentrating the audit market IRBA (2017). This study examines the perceptions of future auditors (currently university students) about the implementation of MAFR.

#### **1.4. The aim of the study**

The aim of the study is to understand the perception of university auditing students on the MAFR rule that has been issued and prescribed by IRBA for public interest entities, determining whether or not they agree that the auditing profession will reap benefits (such as the enhancement of auditor independence as well as audit quality) from its implementation and whether it will meet the objectives outlined.

#### **1.5. Objectives of the study**

To examine whether according to university students:

- The introduction and implementation of MAFR will enable the IRBA to meet the objective of enhancing auditor independence and whether the quality of audits would be improved.
- Any other benefits will be reaped from the introduction of MAFR, particularly those considered by the IRBA, other regulators and scholars.
- Potential negative unintentional consequences could result from the looming implementation of MAFR.

#### **1.6. Research questions**

Do auditing university students believe that:

- The introduction and implementation of MAFR will enable IRBA to meet its primary objective of improving auditor independence?
- The introduction and implementation of MAFR will enable IRBA to realise the complimentary objective and effect of increasing audit quality?
- There will be any other advantages from the introduction and implementation of MAFR in South Africa?
- There will be any negative consequences resulting from the introduction and implementation of MAFR in South Africa?

## **1.7. Assumptions of the study**

This study assumes that the auditing students surveyed at the various levels of study:

- Have a reasonable and adequate understanding of the auditing profession in order to respond to questions about the Mandatory Audit Firm Rotation (MAFR) rule.
- Answer the questions honestly and candidly. That they have a genuine interest in partaking in the study and do not have any other motives, such as receiving a better mark in the course as they are university students or impressing the lecturers as a result of participating.

## **1.8. The significance of the study**

The study provides insights into the views of future auditors on the MAFR rule that is set to be implemented in 2023. These perceptions can assist regulators and decision-makers to reflect on the matter of MAFR in South Africa and provide information that can be considered in future developments. While many different stakeholders can contribute on the matter, university students add unique value. The student population is primarily comprised of younger millennials (primarily 18 to 21 years of age for this study) who according to the theory of generations as developed by Howe and Strauss, are different to the baby boomers and generation X (Howe and Strauss, 1993 & Pew Research Center 2010). Millennials are considered amongst other things, to be self-assured, self-expressive and open to new things and ways (Pew Research Center (2010) and this study can place them in a position to help shape or influence the future of the auditing profession. Furthermore, some of these students will be amongst the first audit teams to be affected by the rule when implemented.

## **1.9. Outline of the dissertation**

**Chapter 1:** The chapter discusses a background to MAFR, introduces the research project, and expands on the problem statement, aim and objectives of the research.

**Chapter 2:** A discussion of the literature reviewed for the study. The literature is mixed in that it does not show clearly whether or not MAFR should be implemented. According to literature, it is not clear whether the implementation yields benefits (such

as improved auditor independence and quality) as often proclaimed by regulators or if there are negative consequences to its implementation (such as a decrease in audit quality).

**Chapter 3:** An explanation of the methodology that will be followed and the techniques for data analysis is provided. The study utilises quantitative methods to collect data from university students. Detailed statistical analysis methods are used to analyse the collected data. Measures put in place to ensure validity and reliability for the study are described.

**Chapter 4:** Findings are presented based on the analysis of data obtained from participants. The chapter evaluates the extent to which students support or refute findings of other research.

**Chapter 5:** This chapter summarises the key findings, what they have shown, and the way forward. A conclusion on the study is also provided.

## **1.10. Chapter summary**

An introduction and background to the study were discussed in this chapter, together with the problem statement, research questions, aims and objectives of the study. The study seeks to examine the perceptions of future auditors regarding the impending MAFR. Current auditing students will not only be amongst audit teams that will be affected by the implementation of MAFR in 2023, but they will also be seeing it through its existence, any evolution or demise. Their current perceptions on the rule can, therefore, assist regulators, practitioners and other accounting stakeholders alike by providing insights from a different stakeholder regarding the rule.

The chapter also outlined the significance that the study will have, the study's underlying assumptions, and presented an outline of this dissertation.

The next chapter discusses the literature reviewed. It first provides a theoretical framework within which the auditing profession functions and where the resulting MAFR rule stems. There is a necessary focus on independence and quality which are considered to be the main reasons behind the introduction of MAFR, however, other aspects and the perceptions of different stakeholders and scholars are discussed.

## **CHAPTER TWO: LITERATURE REVIEW**

### **2.1 Introduction**

Chapter 1 introduced the study, highlighting its purpose and research objectives. In order to achieve these objectives, and respond to the research questions discussed in the first chapter, a discussion of the state of audit firm rotation in the context of the general auditing profession and practice, is discussed. This chapter discusses the theoretical framework of this MAFR study, which relates to the rotation of audit firms. An alternate name for the chapter could have been *“To MAFR or not to MAFR: Different strokes for different folks”*. The chapter provides an outline of the incongruent literature on the implementation, impact and perceptions of MAFR, and the identified reasons and details. There is a necessary focus on the independence of auditors as well as the quality of audits performed by auditors which are amongst the main reasons cited by those arguing for the implementation of MAFR. The chapter also provides a discussion on other considerations and the perception of different stakeholders on MAFR.

### **2.2 The theoretical framework**

The auditing profession and practice has a long history of developing and evolving in over four hundred years of its recognised existence (Teck-Heang and Ali, 2008). In recent times, the profession finds itself in a critical juncture, not only relating to technological advancements that need to be adapted to, but also criticism of the profession going as far as questioning the legitimacy of the profession, with insinuations that the profession no longer wholly serves the interests of the public (The Guardian, 2015; FRC, 2018; IRBA, 2018; Humphrey et al., 2011). Auditing in its very nature is vulnerable to unconscious bias, and as a result, the profession is inherently conflicted. While advancements and professionalisation of auditing have been necessary, this may also equally have brought it to the current point, where regulators are inclined to intervene through increasing legislation and providing more intensified oversight over the profession (Teck-Heang and Ali, 2008).

The introduction of the MAFR is considered to be a response to the “perceived” decline in the independence of auditors which is at the core of the auditing function (IRBA,



2017a). The IRBA CPC puts the independence of auditors at the centre of the auditing profession as a fundamental “must have” in order to be able to conduct an audit as required (IRBA 2009a; Tanlu *et al.* 2003; Quick 2012; Hussey 1999; Dezoort & Taylor 2015). In the long history of the development of auditing, including changes in objectives from the traditional role of testing conformance, to the more recent enhancing, value adding and convergence roles, independence requirements and expectations have also changed and will continue to do so in future as the auditing profession and practice evolve (Teck-Heang & Ali 2008; Church *et al.* 2015)

### **2.2.1 Role Conflict Theory**

Role ambiguity, which arises when people are not certain about the exact expectations within a certain role is the main cause of the role conflict theory. This theory represents the level of congruence, harmony or consistency as well as the lack thereof to the requirements or expectations for the performance of a particular role, for example, that of an auditor. The theory developed by Rizzo *et al.* (1970) judges the said congruence, harmony or consistency in relation to a conventional standard or conditions that have an effect on the performance of the role. According to the theory, there are different types of conflicts, including conflict arising from having numerous authorities and professional values or expectations (Rizzo *et al.* 1970 ; Teck-Heang & Ali 2008).

The inter-sender role conflict (one type of role conflict theory) refers to two or more sources creating different expectations and organisational demands as a result of mismatched policies, disagreeing requests from others and dissenting assessment standards. The inter-sender role conflict theory is one that potentially affects the independence of the auditor (which has been noted by the IRBA as the main reason for the introduction of the MAFR rule) as auditors have to meet the expectations of various parties (management, investors, government agencies, regulators, professional values, their firm performance requirements and the public), with the possibility of meeting those of some at the expense of others. (Rizzo *et al.* 1970; Teck-Heang & Ali 2008 & Sie *et al.* 2012; Edwards, J.R. Anderson, M. Chandler 1993).

### **2.2.2 The auditor expectation gap**

The role conflict theory contributes to the auditor expectation gap which has been researched about (initially from the 1970s) and still does not have a commonly accepted definition (Mat Daud 2007). The expectation gap, is suggested to have existed since the 1800s. It was only formally recognised and defined in 1974 as the difference between the performance level envisioned by the auditor and the users of the audited financial statements, with the consideration of the public per the Cohen Commission (AICPA 1978 ; Humphrey *et al.* 1992). Humphrey *et al.* (1992) extended the definition to include other key matters such as the suitability of auditing standards and the quality of audits.

The criticism of auditors that has led to an intensified focus on the auditing profession and resulting in the instigation of rules such as the MAFR could well be as a result of the expectation gap. The recent deliberations by auditing regulators and the profession regarding MAFR has come about as a result of the perceived complacency of auditors in the conduct of their work as expected and required. However, the audit expectation gap suggests that there may be ambiguity in the role and definition of an audit between users of audited financial statements, the public and auditors. For example, if users and the public were to be asked whether “the role of an auditor was to detect fraud?,” they may answer “yes” (Ojo, 2006). Perhaps the historical view of the need to make an effort to create awareness regarding the role of auditors as suggested by Ojo (2006) is no longer valid, considering the well-publicised audit or reporting failures of the likes of WorldCom and Enron combined with the impact these have had on the auditing profession. As the profession “reflects” on its future, it may be worthwhile to direct some focus on reimagining audit including its objectives, which have always evolved to respond to the needs of the public, although there is usually a time delay from the auditing profession (Byrnes *et al.* 2012; Teck-Heang & Ali 2008).

### **2.2.3 Economic theories of regulation**

There are two broad views with regards to economic theories of regulation which can be considered in the context of the introduction of the MAFR rule, the public and private interest theories. Developed based on the work of Arthur Cecil Pigou, central to public interest theory is a market failure and the assumption that regulator involvement will achieve an efficient and effective solution. The public interest theory considers regulation to be made in an effort to protect and benefit the public. The IRBA is of the

view that the MAFR rule will protect investors as well as other stakeholders of organisations (including the public) from auditors who may not act independently in the conduct of audits. Issues in this regard and non-compliance with the requirements of the IRBA CPC can result in the failure of corporations and can negatively affect society in various ways, hence the need for regulation (IRBA, 2017a). According to the public interest theory, regulators will regulate in the interest of the public, having all the necessary information and knowledge, acting benevolently with the aim of benefiting the public (Hertog 2000; Hantke-domas 2003; Hertog 2010; Posner 1974).

The private interest theory overlaps with the public choice theory which argues that while market failures may exist, intervention through regulation is not necessarily the most suitable solution as regulators (just like normal human beings) will also be motivated by their interests (e.g. their prestige, public standing, power, interest groups, etc.). According to the theory, in contrast to the public interest theory, regulators have insufficient information about organisations and in their control or regulation of organisations or society, will not necessarily be able to act in the interest of the public. The private interest theory further suggests that a regulating agent will pursue their own self-interests (or interests of other groupings) which may or may not include the interests of the public (Hertog, 2010).

Regulation may not at all times suitably consider the economic theory at the core of the audit services market and thus, in the regulation of this market, it is likely that the positive results regulation yields may be offset by unintentional negative consequences (Knechel, 2016). Furthermore, the public interest theory has been widely criticised and questioned as an actual regulatory theory, with claims that it is not validated by imperial research. The IRBA does, however, in any case have a legitimacy risk with regards to its regulatory role of the auditing function in South Africa resulting from perceptions in its regulation of the audit market (IRBA, 2017a). The capture theory, developed on the premise that regulation is developed in the interest of the public, ensues when a regulatory body, whose role is to regulate in the public interest, in its place advances the interests of particular groups dominating the sector. The IRBA faces the risk of being considered to be “captured” by the very auditing profession they are tasked with regulating should they be seen by the public to be advancing the interests of the profession rather than regulating it (Hertog 2000; Hantke-domas 2003; Hertog 2010).

There is no static definition of regulation, but it can be considered to be the use of legal instruments to implement social-economic policy goals. Economic regulation is applied in the regulation of monopolies, market structures and on the imperfect competition with the aim of contrasting any damage caused by the behaviour of the dominant firm(s) (Hertog 2010). The MAFR rule (IRBA, 2017d) introduced by the IRBA constitutes a form of regulation. According to the IRBA, the MAFR rule (or regulation) has been introduced, mainly because of the need to strengthen the independence of auditors (IRBA 2017a ; IRBA 2017c), which has declined over time due to some factors Hodge (2003) and is in the interest of the public. It is debatable, however, whether the regulation is indeed underpinned by public or private interest theories as some are of the opinion that the regulation is not the correct solution to the problem (if there is indeed a problem) (SAICA 2017; SAICA Indaba 2016; Center for Audit Quality 2012; Harber 2016; Ottaway 2013; Asian 2012; AICPA 2017). The regulation of the auditing profession is not straight forward. It is dynamic and is not necessarily the exclusive responsibility of governments and regulators. The profession to an extent, regulates its operation.

#### **2.2.4 The existing law of auditing in relation to its living law**

The auditing profession follows the free market economies approach, functioning largely independently, as an authority unto itself, only soliciting contributions from governments (IAASB, 2014). The International Auditing and Assurance Standards Board (IAASB), describing itself as “an independent standard-setting body that serves the public interest by setting high-quality international standards for auditing, assurance, and other related areas, and by facilitating their adoption and implementation”, has the responsibility of issuing international auditing and assurance standards used by auditors, coordinating the auditing practice and ultimately enhancing confidence in the auditing profession (IAASB, 2014).

The living law concept is about the philosophical quest of wisdom about the law, legal systems, and justice. The concept came from the discipline of jurisprudence and was developed by Eugen Ehrlich (Murphy *et al.* 2013; O'day 1966; Nelken 2008). It is the law that dominates a particular situation, even where it has not been enshrined in legal propositions and is maintained by the public through associations and the like. Similar to customary law, it is a moral custom containing the set of those ways of acting that,

in a specific community, are respected and considered suitable to common types of circumstances and in the broader community (Murphy *et al.* 2013; O'day 1966).

The independence of auditors and other auditor responsibilities are at the very foundation of the auditing profession (Tanlu *et al.* 2003; Quick 2012; Hussey 1999; Dezoort & Taylor 2015). South African law (the Companies Act No. 71 of 2008 and Auditing Profession Act No. 26 of 2005) refers to independence and other auditor requirements (RSA APA 2006; RSA Companies Act 2009). However, at the core of the functioning of the auditing profession is its living law, where the profession through the IFAC's IAASB, sets its own rules of operation and practice for implementation in the world's economies.

Ehrlich's living law has been interpreted in various ways since introduction as the "law beyond the law", the "law without the government" and "order without law" (Nelken, 2008). The answer to the question of regulating auditors may not be in regulations (such as MAFR) but back to its living law of auditor professionalism, oath of public service and setting of the tone by leaders (Edwards, 2014). The profession in itself primarily through the IAASB (and to an extent regulators such as the IRBA) in practical terms is more of the guardian and advocate for auditor independence and proper conduct in performing an audit, than the actual law. Furthermore, it should be noted that the MAFR rule has been introduced as an amendment to the IRBA CPC and not a legal proposition in the form of legislation or law (IRBA 2017d; IRBA 2009a).

## **2.3 Empirical evidence**

The accountancy and auditing profession has over time developed into one of the most influential sectors of the world's economies. The International Federation for Accountants (IFAC) is the "mother body" of the profession and outlines its primary reason for existence as strengthening organisations and advancing the world's economies (IFAC, 2018). While the development of the profession has taken place over some decades, the professionalisation of accountancy is more recent in comparison to the existence of accountants and auditors. Early developments in the professionalisation of accountancy took place in the United Kingdom and the United States where the professionalisation strategy originated, and the accountants' use of

the public interest argument in order to advance and guard their financial self-interests grew (Lee 1989).

This is an indictment to the accountancy and auditing profession who are generally accepted as primarily serving in the interests of the public (Lee 1989; IRBA, 2009a). Following the collapse of companies like Enron and WorldCom in recent history together with their auditors Arthur Anderson, there has been a particular closer look at the auditing profession (Matthews, 2006). There has further been increasing criticism of the profession by various stakeholders which has resulted in different reform attempts and debates. Regulators in some jurisdictions including the Financial Reporting Council (FRC – UK), European Commission (EC – Europe) and the IRBA, amongst others have been part of the critics of the profession (Church *et al.* 2015; The Guardian, 2015; FRC, 2018; IRBA, 2018; Humphrey *et al.*, 2011; Edwards 2014). Regulators are also concerned about auditors failing quality inspections of work performed (IFIAR, 2015). As a result, these regulators are amongst those that have resorted to taking steps towards some form of regulatory reforms particularly for the auditing profession (Church *et al.*, 2015). One of the widely debated of these reforms is MAFR (Stern, 2015), now proposed by the IRBA. Accounting firms, SAICA and other organisations are not clearly in favour of the implementation of MAFR (Harber and West, 2017)

Deliberation over MAFR is nothing new and has been ongoing for over five decades around the world. Opponents of the policy argue, amongst other things, that new auditors (appointed after the mandatory rotation) might lack client and industry know-how, which might result in increased audit fees, particularly for early engagements and a bigger occurrence of problems and even lower quality audits in the initial years of a new engagement. Proponents of MAFR, who are usually regulators, on the other hand, argue that the implementation of MAFR will enhance auditor independence, quality and professional scepticism through the fresh eyes of new auditors (Kwon, Lim and Simnett, 2014).

Regulators, who are usually the proponents of MAFR, agree about the general audit cost drivers for MAFR, being set-up costs for new auditors to understand their clients and costs for client management to support the new auditors. While some studies have

found that MAFR decreases audit costs, some have found that audit costs can increase by approximately 20 per cent up to 128 per cent (K. Said and Khasharmeh, 2014). The IRBA has been monitoring the audit fees of JSE listed companies and notes that costs do not rise significantly, either remaining similar or showing a minor increase on appointment of a new audit firm (IRBA, 2017b).

According to Said and Khasharmeh (2014), professional auditors concur that a substantial relationship exists between MAFR and audit costs, which is in line with prior research on the matter. Said & Khasharmeh (2014) also found that just over 45 per cent of the respondents believed that MAFR would enhance the independence of auditors and were in favour of its implementation. Additionally, 36.4 per cent responded that it would work if the rotation period is long enough and 33.3 per cent indicated their agreement with MAFR. The study indicates that while costs may be affected, auditors are in favour of the implementation of MAFR due mostly to the positive impact on auditor independence it will have.

Furthermore, in a study of perceptions on earnings quality (one proxy for the measure of audit quality) and auditor independence by investors (who are not professionals), motivated by the concerns of the Securities and Exchange Commission's (SEC) of the United States, Hodge (2003) found validity in the concerns then expressed by the SEC. The results suggested that while the use of audited financial statements had increased, the perception of investors is that (earnings) quality and the independence of auditors had dropped over time resulting in the perceived decline in the reliability of audited financial statements (Hodge, 2003).

The rotation of audit partners (rather than the firm) is a current requirement in South Africa in terms of the Companies Act as well as the IRBA CPC. Opponents of MAFR consider this rotation as being sufficient to mitigate concerns raised by supporters of MAFR. Audit partner rotation has its draw backs, for example, in assessing the effect of audit failure on audit partners, He *et al.* (2016) found that audit partners suffered reputational damage from the demise of Zhongtianqin (ZTQ), once the largest Chinese audit firms. The audit failure followed the fraudulent exaggeration of earnings of a client which was not reported on by the auditors. The study found that the damage was not only limited to the complicit partners who were associated with the audit, but

extended to partners that were not involved in the audit, affecting their reputation, employability, earnings, perceived audit quality, and audit fees.

The audit partner rotation rule does, however, provide benefits, and results in a significant upsurge in material restatements in financial statements as the new partner provides a fresh eye on audits (PWC, 2017). The implementation of mandatory audit partner rotation results in enhanced quality (Monroe and Hossain, 2013). In contrast to this, however, Litt *et al.*, (2014) found that the quality of audits to be lesser in the early years subsequent to the rotation of a partner, which was more prevalent in larger audit clients. The initial three years following the rotation presents audit challenges for partners in Big Four firm and these last for up to seven years for those not in these firms (Litt *et al.*, 2014).

On the overall, there is an assumption by regulators that the implementation of MAFR will contribute to the prevention of corporate failures and damage to audit firms which is far more expensive than the audit fee increases that might result from the implementation of MAFR. This is why, according to IRBA in their assessment of G20 (an international forum for the governments and central bank governors of 19 countries and the European Union) and International Forum of Independent Audit Regulators (IFIAR) member countries, 30 out of 52 members have or will implement MAFR towards the objective of protecting investors (IRBA, 2017a). The independence of regulators supports their goal of acting in the public interest (IRBA, 2017a).

### **2.3.1 Auditor independence**

The IRBA CPC establishes the fundamental principles of ethical conduct and provides a conceptual framework that helps registered auditors in conforming with the ethical requirements and meeting their duty to act in the public interest IRBA (2009a). The IRBA CPC identifies familiarity with the audit client as one of the threats to compliance by the auditor with the fundamental principles. Yet, there seems to exist a premise ensuing from the concept of risk based auditing outlined in the International Auditing Standards that, familiarity with the audit client may be needed in order for the auditor to understand the client well enough to plan and execute a proper and well-organised audit (Bamber and Iyer, 2007).



Familiarity can threaten the independence of an auditor, where the two (the auditor and the client) identify with each other (Bamber & Iyer 2007). From the perspective of social incentives for the auditor and their identification with the client, social incentives play a role in the judgments made by auditors. While client identification is less than their professional identification, there exists a concern as client identification can impair the objectivity of auditors. This is, however, mitigated by the auditor's professional identity as well as some evidence found that an audit firm's tenure (amount of years an entity engages an auditor) is linked with greater auditor objectivity, and not less, which is contrary to the views of the proponents of MAFR (Bamber & Iyer 2007). In support of MAFR, concerns were raised about the "cosy" relationship between Enron and its Arthur Anderson auditors, who seemingly became too familiar, leading to the well documented failure of both (Arel, Brody and Pany, 2005).

Regulators have expressed concerns over the independence (or lack thereof) of auditors in the conduct of audits, and continue with efforts or intentions to introduce appropriate safeguards, such as MAFR (Church *et al.*, 2015). Current and past directors or managers have a significant influence on the appointment of auditors (Dhaliwal *et al.* 2015; Hussey (1999). The directors consider their relationships (chemistry) with the auditors to be the most important criterion when deciding on auditor appointment. The majority of the directors, however, classify their relationship with the auditors as "professional and amicable". The familiarity threat is more powerful at the auditor appointment stages, where directors (including former) have influence over decisions. The performance of non-audit work does not have as significant an impact on the familiarity threat as is commonly perceived (Dhaliwal *et al.* 2015; Hussey (1999).

Auditor objectivity is one of the fundamental principles enshrined in the IRBA CPC (IRBA 2009a). It is also one of the principles that underlie the reliability and credibility of the work of auditors and the audit reports that culminate from this work. According to this principle, auditors registered with the IRBA should not compromise their judgment as a result of bias, conflict of interest or unjustified influence (IRBA 2009a). While there has been a spread of conflict of interests and independence concerns in the general accounting profession in recent years, Arya & Glover (2014) stresses that

the design, nature and structure of the auditing function supports far more than other accounting roles (such as tax accountants or consultants), the principle of independence.

As noted in the International Standards on Auditing (ISA), and the IRBA Code of Professional Conduct, it is a critical requirement that auditors, in the performance of an audit, are independent both in mind and appearance so as to be able to perform their work and produce credible and reliable reports for stakeholders Harber (2016). The need for auditor independence is foundational to auditing, (Tanlu *et al.* 2003; Quick 2012; Hussey 1999; Dezoort & Taylor 2015). There has been, however, in recent years a growing concern over the conduct and independence of auditors. This is due to an increase in corporate and audit failures which have seen the closure of a major international accounting and audit firm, Arthur Anderson, following the Enron scandal as well as recent attention on audit firm fines and bans issued by country audit regulators, (Firth *et al.* 2012; Shoa 2017; Mundy 2018; Crotty 2018).

The concern over the conduct and independence of auditors results in regulators considering ways in which auditor regulation can be improved. In 2011, the PCAOB issued a concept note on Independence and Audit Firm Rotation (PCAOB, 2011), inviting stakeholders to comment on the matter. Based on the 2010 Green Paper *“Audit Policy: Lessons from the Crisis”*, the European Commission (EC) on the other hand, issued some regulatory proposals relating to the role of auditors, their independence and market. The European Union formally adopted the implementation of MAFR rules (one of the numerous measures proposed by the EC to improve the independence of auditors) emanating from the green paper (Tysiac 2014).

In a review study, Tanlu *et al.* (2003) analyse the cognitive, structural, statutory and political causes to the failure of auditor independence and determines that given the corporate and audit failures as well as the different causes of the failure of auditor independence, auditor independence requires a more radical overhaul. In the public interest, the costs that would be incurred in the creation of “true independence” would be worth-while. Two possible solutions are put forward by the authors: (1) eliminating the regulatory requirement for publicly traded companies to be audited, instead requiring the purchase of insurance by these companies against the risk of being sued

for erroneous financial statements being issued and (2); improvement in the regulation of the audit-client relationships through five recommendations which are; providing audit services only, MAFR, auditors not being allowed to take up jobs with companies they audit, conducting more independent assessments and lastly, the selection of the audit firm being done by the audit committee and management not playing any role in this.

While the concept of independence is important to the auditing profession, it is inconsistent and unclear (Church et al. 2015; Malsch *et al.* 2015; Tepalagul & Lin 2015) Furthermore, as the current set up is such that the client must financially compensate its auditors, true and complete independence is rendered virtually impossible Dezoort & Taylor (2015). The auditors' working independence (the fitness to work thoroughly and effectively in order to identify material irregularities) is not only unsettled in practice, but it is also uncertain, often ignored (over institutional independence) and not easy to attain (Malsch, Tremblay and Gue, 2015).

There is more for auditors and regulators to be concerned about than just independence. The view by regulators and stakeholders that independence is the ultimate goal is not sufficient and rather, the Reliability Framework (simply the reliability of auditors) which includes independence amongst other constructs such as integrity and expertise is a more holistic approach to validate the public interest view for the existence of auditors. Such a shift from a primary focus on independence, however, would mean a revised view on these constructs that culminate in reliable auditors, given the shifting public interest views of the profession.

Said and Khasharmeh (2014) examined auditor perceptions on matters that affect auditor independence in the emerging market of Bahrain. They found that most of the auditors concur that MAFR could protect the independence of auditors (a substantial relationship between MAFR and independence exists). Auditors, however, have an incentive to protect their reputation. This leads to their issue of a going concern modified opinion Ruiz-Barbadillo *et al.* (2009). This, compared to the view that they would sacrifice their independence in long tenure audit engagements to issue modified audits opinions (other than going concern modification) while having their reputation and profession compromised (Garcia-Blandon and Argiles, 2015).

Recently and following international developments regarding the issue of fines and sanctions by regulators, the South African regulator (IRBA) has also moved to make changes to legislation relating to auditors. In recent years, the accounting and auditing profession as a whole has faced criticism over the conduct of some of the large auditing firms. Harber (2016), however, found that according to senior audit partners in South Africa, it is only the perception of the public that independence is compromised and to which the IRBA is presumably responding. This, according to the study, is not necessarily the same as the reality of the state of independence, which the study concludes should be responded to through improved corporate governance practices (not MAFR).

Anis (2014), however, concurs with Said and Khasharmeh (2014) in a survey of auditors in Egypt regarding the effects of mandatory auditor rotation. He found that generally, auditors agree that mandatory rotation would improve both the independence of the auditor in mind and appearance. This supports a previous study by Pearson (1987) who surveyed United States CPAs practising as independent auditors (both in the then Big eight and non-Big eight firms) about their perceived and actual independence impairment and deficiencies by CPA auditors. Pearson (1987) identified and linked to independence five typical reasons for audit failures (scope limitations; incompetence; auditing by discussion; not critically assessing transactions and an absence of objectivity and scepticism) which form the basis of the auditor survey. The results of this study indicated that auditors believed independence had been impaired with some admitting to personal experiences.

The percentages of auditors that perceived the matters to be occurring frequently or occasionally were: 29% - significant client scope restriction; 46% - of engagements are completed with no appropriate training or experience; 64% - acceptance of the word of management without independent verification; 25% - do not critically evaluate significant client transactions and 45% - make the effort to keep the client contented, compromising objectivity and scepticism) (Pearson 1987). Regarding actual independence impairment, utilising random response technique (RTT), Pearson (1987) found that virtually no auditor acknowledges client imposed scope restrictions or failure to evaluate significant transactions, although the auditors remarked that

these occur in practice and are not isolated. On the other hand, 10% answered yes to efforts to keep the client happy (i.e. honouring client requests that should not be); 22% admitted to completing engagements with no appropriate levels of training and experience, and 30% admitted to acceptance of the word of management without independent verification (Pearson 1987).

Long audit tenure has an adverse effect on the independence of auditors and auditor rotation has a positive one. This means that auditor rotation improves the independence of auditors. The size and age of the auditee, as well as the reputation of the auditors, have no influence on the independence of auditors (Junaidi *et al.*, 2016). MAFR regulation helps maintain independence and quality and is needed. An artificial rotation of auditors (conceptual change of auditors with the relationship in actual fact continuing) as experienced in Indonesia has a significant negative impact on auditor independence (Junaidi *et al.*, 2016).

An analysis of investor and market reaction to the prospects of the introduction of MAFR demonstrates negativity towards the proposal (Reid and Carcello, 2017). However, non-professional investors perceive auditor independence to have declined over time, resulting in the perceived drop in the reliability of audited financial statements, although their use had increased (Hodge 2003). Furthermore, investors perceive auditor independence to be impaired (specifically) as a result of a lengthy audit tenure (without rotation) and thus support the argument for the introduction of MAFR but highlight the importance of industry-specific knowledge in order to maintain adequate audit quality (Hohenfels, 2016). This is in contrast to the perception of investment consultants according to whom MAFR leads to no improvement in auditor independence (Aschauer and Quick, 2018).

Bank loan officers also support a voluntary audit firm rotation policy according to Daniels & Booker (2011). The officers believe that rotation increases auditor independence although they were not too concerned by the period of rotation and do not associate it with any improvement in quality (Daniels & Booker 2011).

### 2.3.2 Audit quality

There are a number of different proxies used in the measure of audit quality. These proxies include audit opinions; the going concern opinion; audit failures; client accrual accounting behaviours (earnings quality/management). There are also those that are miscellaneous which include for example inspections, reporting on fraud, quality control reviews, likelihood of restatement, likelihood to issue a qualified opinion, auditor size, auditor specialisation and audit report timeliness (Ewelt-Knauer *et al.* 2013; González-Díaz *et al.* 2015; Habbash & Alghamdi 2017).

There was no clear, significant positive impact on quality brought about by the introduction of the policy in South Korea (Kwon *et al.* 2014). Furthermore, there is a negative relationship between MAFR and quality (Chika Onwuchekwa *et al.* 2012; Adeniyi & Mieseigha 2013). MAFR did not yield the desired outcomes in the Korean audit market, resulting in lower quality when compared to the audit partner rotation and voluntary audit firm rotation alternatives (Choi, Lim and Mali, 2017). However, investors in South Korea, which has previously implemented, abolished and has announced the re-introduction MAFR, perceive auditor independence to be enhanced as a result of mandatory rotation (Minkim and Heun Lee, 2018). MAFR also produces better quality information and decreases the cost of equity capital. (Minkim and Heun Lee, 2018).

The Italian case study presents what could be amongst the best scenarios for the study of MAFR and its impact as the auditor rotation policy has been applicable in the country since 1975 (Cameran *et al.* 2015). Data from the Italian market shows that outgoing auditors do not neglect audit quality, instead the quality of earnings in the initial three years of the new auditor's post rotation is lower, increasing in years after that (Cameran *et al.* 2015). No significant change in quality was found where the company was audited by a Big Four firm following rotation, while quality improved after firm rotation for entities that were audited by a non-Big Four firm (Corbella *et al.* 2015; Bell *et al.* 2015).

A study on the perceptions on quality (earnings quality) by non-professional investors, Hodge (2003) found that investors perceive audit quality to have declined over time,

resulting in the perceived decline in the reliability of audited financial statements. This being the case, Kwon *et al.* (2014) who also used the client accrual accounting behaviours (earnings or accrual management) as a proxy found that there was no clear, significant positive impact on quality brought about by the introduction of the policy in South Korea. Kwon *et al.* (2014) were only able to conclusively find that the policy increased audit fees which were found to be discounted by incoming auditors.

Ghosh *et al.* (2005) studied the perception of two participants in the capital markets (investors and intermediaries) on the impact of longer audit tenure on audit quality and found that, the longer the auditor is not changed, the better the quality of their work, and note an unintended increase in audit costs that may be caused by mandatory rotation of audit firms.

This perceived improvement in quality is contradicted by Cameran *et al.* (2016) in a study of the impact of MAFR on audit quality in Italian audit market conducted while the MAFR rule was applicable. Cameran *et al.* (2016) found the rule to have a positive impact on the quality as it increased in the last three years of the maximum nine-year tenure allowed in terms of the Italian MAFR policy (which allows three-year appointments, up to three times). The three years where quality increased represent the last possible extension (of the engagement period) for the firm before the mandatory rotation. The study concludes that the auditor has an incentive to improve the quality of their work towards the end of their engagement period or term. This is because the auditor is still eyeing re-appointment in the initial periods (first two three years) and thus quality would be lower and where there is no possible reappointment, the auditor becomes conservative, with audit quality increasing as a consequence of this (Cameran, Prencipe and Trombetta, 2016).

In support of this, professional auditors perceived the rotation of auditors to have a positive effect on quality in a study conducted in the Egyptian audit market. While the study found that mandatory audit firm/partner rotation would have a negative impact on client-specific knowledge, it also found that a long audit tenure causes a decline in audit quality and that mandatory rotation would lead to an increase in quality, particularly due largely to industry specialisation as this will effectively offset any negative effect of mandatory rotation on quality (a view mainly amongst auditors

working in big audit firms). Motivated by concerns of the financial press and policy makers regarding allegations of earnings management, Gul *et al.* (2009) also find that where industry specialists conduct audits, a short audit tenure will not lead to lower audit quality. In the study, Gul *et al.* (2009) also considered and did not find results that support the often cited relation between low balling and audit quality (that auditors quote and charge lower audit fees earlier in audit engagement periods, compromising on audit quality in order to keep audit clients for longer, recouping losses incurred in the earlier engagement years in the long run).

According to investment consultants, however, MAFR does not positively impact the perceived quality of audits (Aschauer and Quick, 2018). Investors perceive audit quality to change over time during the audit tenure period. Using the perceived earnings quality, investors perceive audit quality to be lower at early and later stages of the client-auditor relationship. More specifically, quality was considered to be higher in medium (4-10 year) tenures, peaking in 8-9 year relationships. Consistent with concerns over both the frequent changing of audit firms and also long audit tenures, quality was found to be at its lowest in the first three years of auditing a client and also low for audits where the relationship is over ten years (Hohenfels, 2016). Hodge (2003), however, studied the perception of investors on earnings quality and auditor independence and found that consistent with concerns raised, earnings quality and the independence of auditors had declined over time resulting in the perceived decline in the reliability of audited financial statements.

Using internal firm quality assessment information from a Big Four audit firm, Bell *et al.* (2015) examined the impact tenure has on quality. The study found that lowballing does occur. However, new engagements (especially those that are large, complex and listed), involve a notable learning curve and require great effort from the auditor. The study finds that generally, audits are likely to achieve a lower quality rating in their first year, improving considerably after that. There is also evidence that quality decreases where the tenure is too long in non-listed company audits. This is supported by the United States Centre for Audit Quality (CAQ) who concede that independence, objectivity and professional scepticism are important for the performance of high-quality audits. The CAQ cautions, however, that the implementation of MAFR would



have significant unintended consequences that would likely harm the quality of audits (Centre for Audit Quality, 2012).

González-Díaz *et al.* (2015) considered a unique and uncommon standpoint in the assessment of the relationship between tenure and quality and found that a lengthier tenure decreases quality. This came from a public sector perspective where no mandatory rotation is required. The Spanish General Comptroller of the State Administration (IGAE) has responsibility for public sector audits which include state-owned foundations meeting particular criteria. The IGAE can only conduct the audit of the foundations. Using the likelihood to issue a qualified audit report as proxy, the study finds that audit quality decreases in the long term as in the initial years (up to five) of the tenure, the auditor is likely to issue a qualified audit opinion and that the longer the relationship, the more the likelihood of a clean audit outcome.

It is worthwhile to note that there is little difference in actual quality delivered by Big Four auditors in comparison to non-Big Four auditors. However, there is a noticeable difference in perceived quality (Sawan and Hamuda, 2014). This implies that given the opportunity, for example through MAFR, non-Big Four audit firms could produce audits of quality standards that are similar to Big Four firms.

### **2.3.3 Other considerations**

Evidence currently available on stakeholder perceptions on MAFR, its pros and cons, benefits and disadvantages, is mixed and therefore does not clearly support its implementation or not (Ewelt-Knauer *et al.* 2013; Junaidi *et al.* 2016). Audit client and shareholder views vary while regulators are in favour of rotation, wishing to improve independence and quality. The introduction of MAFR leads to an increase in independence of fact; a positive response by the financial markets; an increase in audit quality; prevention of large scale corporate collapse; prevention of damages to auditing firms and affording smaller audit firms a chance to grow (Ewelt-Knauer *et al.* 2013; Burke 2010; IRBA 2017b).

MAFR, however, also has the potential to increase market concentration (rotations amongst the Big Four firms) as well increase set up costs for both auditors and

management. It obstructs the establishment of effective working relationships; increases the risk of audit failures (which often happen in the early years of the tenure); decreases independence as long tenure leads to less reliance on management; discourages investment in development and specialisation; and leads to pressure on audit fees and low-balling (Harber 2016; AICPA 2017; SAICA 2017; SAICA Indaba 2016; Center for Audit Quality 2012; Ottaway 2013; Asian 2012) . MAFR will also not result in the transformation of the auditing profession or address audit market concentration. (Harber & West 2017; Harber 2016).

In the audit of South Korean listed entities, the introduction of the MAFR policy resulted in an increase in audit costs for audit firms, audit fees for clients without an accompanying increase in audit quality (Kwon, Lim and Simnett, 2014). MAFR can also result in lowballing (higher audit hours but the discounted fee in the first year) by new auditors, is costly and decreases the quality of audits (Cameran *et al.* 2015). The mandatory rotation audit fee increases are greater than voluntary rotations before the introduction of the policy which makes the MAFR not worthwhile. For these reasons, South Korea was correct to abandon the MAFR policy as the increased audit costs do not provide a clear positive impact on audit quality (Kwon *et al.* 2014). MAFR results in bringing lowballing (higher audit hours but the discounted fee in the first year) by new auditors, is costly and decreases the quality of audits. In studies of the Italian market, Corbella *is.* (2015) and Bell *et al.* (2015) also used data collected from the market over a number of years and found that audit fees were lower where a Big Four firm had rotated in, and remained the same where a non-Big Four firm had come in as a result of the rotation.

In an attempt to respond to audit quality concerns, no evidence could be found that supports the notion that auditors quote and charge lower audit fees earlier, on audit engagement periods (Gul *et al.* 2009). Evidence also could not be found that they compromise audit quality in order to keep audit clients for longer, in turn recouping losses incurred in the earlier engagement years in the long run, which is often cited by auditor rotation critics (Gul *et al.* 2009). Audit firms can have long tenures or relationships with their clients, some extending over 100 years, which leads to an impairment of independence (IRBA, 2017a). The compromised independence, however, is only the perception of the public and not an actuality. It is this perception

that the IRBA is presumably responding to (Harber 2016). Audit firms are able to create close connections with their clients without being subjected to any pressure that results in a real threat auditor independence (Fontaine and Letaifa, 2012). Rather, the existence of a good auditor-client relationship is so important that the primary reason for changing audit firms is a breakdown in this relationship. It is not because of high audit fees. This places more importance for auditors on audit *service* quality over just audit quality (Fontaine, Letaifa and Herda, 2013).

Closely relatable to MAFR is audit partner rotation, where the individual auditor in charge is rotated after five years. This type of rotation is required by section 92 of the South African Companies Act of 2008 (SA Government 2009). The consideration of audit partner rotation is important not only because MAFR brings automatic rotation of the audit partner, but also because the dynamics that come with the partner-client relationship are important to the auditor rotation question and audit partner rotation is often cited as a sufficient response to the threat to independence and quality. Manry *et al.* (2008) found no substantial connection between partner tenure and quality in the audit of large companies and short tenure audits of small companies. Quality was found to increase with long tenures for small companies. Bandyopadhyay *et al.* (2014) found that in the first three years post audit partner rotation, there is an improvement in audit quality. They found this more noticeable where there were better legal structures and less audit market concentration, and not in jurisdictions where legal resolutions were more developed and/or where audit markets had a high concentration (dominated by a few large firms).

Observing changes of both audit firms and partners in large corporations in financial distress in Spain and using the likelihood of the issuance of a going concern opinion as an audit quality proxy, Gómez Aguilaris *et al.* (2017) found that the rotation of the audit partner does not affect audit quality. Furthermore, the audit firm rotation on its own or combined with the rotation of the partner does not impact audit quality and thus the increased costs and fees the market is subjected to (through mandatory rotations) could not be proved to yield any positive impact on audit quality (Gómez Aguilar, Biedma López and Ruiz Barbadillo, 2017).

A close relationship between an audit partner and client impairs audit quality (Su & Wu 2016). In cases where an audit client followed an audit partner into a new audit firm (where there is no regulatory restriction and no mandatory rotation), audit quality is impaired as partners at the new firm are not only less likely to issue a qualified audit report but also favourably treat the clients that had followed them. This demonstrates the risks presented by familiarity between auditors and their clients, fuelled by managers and directors having a significant influence on the appointment of auditors (Dhaliwal et al. 2015; Hussey (1999). This influence is disputed by EY, (2016), who considers audit committee chairpersons as having the most influence on audit firm selections. While audit committee' and auditors' ties can be advantageous to the audit process, there is evidence that the relationship impairs audit quality He *et al.* (2017).

In a review, major banks in the Malaysian banking industry did not rotate auditors in over ten years, indicating that auditor rotation (voluntary in this case) was not favoured or considered necessary (Dandago and Binti Zamro, 2012). This view is supported by the Banking Association of South Africa (BASA) who in their response to the IRBA voiced their concerns about unintended consequences that MAFR would bring, proposing that alternative audit reform options be followed. One of these is that rotation be considered by the audit committee as is currently the case, when the audit firm no longer serves company and shareholder interests (BASA, 2017).

Audit committees in South Africa are correctly constituted (Marx, 2009). They also have the necessary and resource which enable their effective discharge of responsibilities (Marx, 2009). Members of audit committees are also decisively opposed to MAFR primarily as it threatens the audit committee authority as well as working autonomy granted by shareholders (Marx, 2009; Fontaine, Khemakhem and Herda, 2016). Members understand the objective of MAFR to strengthen auditor independence, however, they believe that there are other (more) effective auditor independence safeguards. Accounting bodies and firms agree with this (Burke 2010; Harber & West 2017; SAICA 2017). Audit committee members believe that through discussions, professional judgement and relationships established with both management and the auditors, they provide a better solution to independence concerns, even better than audit partner rotation as a solution (Fontaine, Khemakhem and Herda, 2016).

Professional auditors are in support of this and believe that the enhancement of auditor independence should not rely on a regulatory approach at the auditor level as intended by MAFR, but rather by improvements in oversight over the audit function through the use of structures such as the audit committee (Williams and Wilder, 2017). This regulatory shift would mean progressing focus from individual auditors to client level focus (Williams and Wilder, 2017).

Audit committee members prefer audit partner rotation as compared to MAFR (Fontaine, Khemakhem and Herda, 2016). They concede that relationships with individual audit partners may impair independence and that audit partner rotation rectifies this while maintaining the relationship and accumulated knowledge (Fontaine, Khemakhem and Herda, 2016). These members do not identify the costs associated with MAFR as the “primary” issue, rather the considerable time and effort that would be required in a change of audit firm (Fontaine, Khemakhem and Herda, 2016). The views of audit committee members may need to be taken with a pinch of salt as managers have significant influence over the selection of auditors and the responsibility given to audit committees for auditor appointments is unjustified (Dhaliwal *et al.*, 2015). Furthermore, the relationships that exist between auditors and the audit committee through previous university connections or employment affects the effectiveness of audit committees. These historical ties which can be beneficial to the audit process and oversight can also impair audit quality (He *et al.* 2017).

The implementation of MAFR would have significant unintended consequences that would likely harm the quality of audits and increase costs. In addition to decreasing audit quality, MAFR would limit regulatory audit committee authority, lead to loss of institutional knowledge, limit auditor specialisation, create pressure on resources, lead to problems with talent recruitment and management and increase market concentration, amongst others. MAFR will also present new risks around accounting estimated and judgements (EY, 2016). Alternatives to MAFR such as enhancing the effectiveness of audit committees and their oversight role, human resource practices, transparency, standard setting and the root cause of failures of audit files in audit quality inspections by regulators (Center for Audit Quality 2012; Harber 2016; Ottaway 2013; Asian 2012; (AICPA, 2017) are worth considering.

The fresh auditor eyes and “watchdog” approach brought about by auditor rotation reduce familiarity between auditors and the client, improving independence in appearance, but the negative impact far outweighs the benefits. For this reason, the re-tendering model (in favour of MAFR, the lottery and insurance models) is a better alternative for audit reform to solve the issues faced by the auditing profession (Ottaway, 2013).

As there is a negative relationship between MAFR and quality (Adeniyi & Mieseigha 2013), alternative measures should be sought or explored and implemented in an effort to improve the quality of audits (Chika Onwuchekwa *et al.* 2012). Business and Law University students have an opposing view to this, however, and consider MAFR to improve confidence in the reported information. The future participants in the world of business and law perceive MAFR as having a positive impact on audited financial statements and audit quality. Where an organisation exhibits robust corporate governance practices, there is a great incremental benefit where there is a MAFR policy in place, in comparison to an audit partner or no rotation policy at all (Gates *et al.* 2006).

## **2.4 Conclusion**

In this chapter, literature relating to MAFR and its potential benefits and disadvantages was reviewed. There is no clear consensus in the MAFR discourse as current stakeholders (and available literature) are seemingly equally for and against its implementation. Various methodologies and measures over the years have not provided an answer on whether or not MAFR should be implemented and whether if implemented, benefits stand to be gained or negative consequences would be suffered. There are different views on the impact of MAFR on auditor independence, quality as well as other outcomes that may result from its introduction.

There is no common view on the impact of a long lasting relationship between the auditor and a client and this has resulted in audit regulators taking different standpoints on whether or not to accept the (potential) long audit tenures. As an example of the opposing views that currently exist on this audit reform, the United States (US) House of Representatives chose to reject MAFR, while the European Union (EU) adopted it.

The different opinions by the US and the EU demonstrate the complexity that surrounds the auditor rotation debate.

Despite this together and other objections and reservations from many stakeholders, the South African Independent Regulatory Board for Auditors (IRBA) is going ahead with the introduction of the MAFR rule in 2023 in South Africa. Interestingly, future business participants (a different stakeholder) who are university students (studying MBA and Law) were found to believe that a MAFR policy would yield a positive impact. While different stakeholders have weighed in on the MAFR rule through responses to the IRBA consultation process and in literature, amongst the audit teams that will be implementing the rule in 2023 are current university auditing students, whose perception on MAFR has to the knowledge of the researcher, not been studied.

In the next chapter, the research methodology followed in the study of the perception of current university students on the MAFR rule and its impact is discussed.

## **CHAPTER 3: METHODOLOGY**

### **3.1 Introduction**

Chapter 2 explored the different views on the impact of Mandatory Audit Firm Rotation (MAFR), determining that there is no agreement on whether or not its introduction leads to the enhancement of independence, audit quality or other benefits (such as competitive audit fees, audit specialisation, transformation of the profession, etc.).

The objective of this study is to determine whether according to current students studying auditing at university, the introduction and implementation of MAFR in South Africa will lead to an enhancement of auditor independence, an improvement of the quality of audits and other potential benefits. Alternatively, the study will seek to determine whether no such benefits would be reaped, rather there could be potential negative unintended consequences suffered. This chapter discusses the methodology followed to attain the objective.

The chapter places the study in the appropriate paradigm and outlines the approach followed. Thereafter, the population as well as the sampling of this population is discussed. The chapter then narrates the method of collecting data, including the instrument used in this collection, its analysis, validity and reliability.

### **3.2 Research approach/paradigm**

In conducting a research study, a researcher should express his or her own paradigm (Creswell, 2007). This is the researcher's conception of the world or way of thinking which is brought into the research study (Creswell 2007; Kivunja & Kuyini 2017). The researcher's ontology (researcher's beliefs about what is real or the nature of reality), informs their epistemology (how they come to know the reality) which will lead to a logical and systematic investigation (the methodology) for a study (Barbara 2012). With adequate ethical considerations for the study (axiology), the researchers' philosophical way of thinking is assembled (Barbara 2012). Research methodology and the researcher's paradigm work together to form a research study (Creswell 2007; Mackenzie & Knipe 2006; Kivunja & Kuyini 2017; Barbara 2012).



### **3.2.1 Choosing an approach and paradigm**

In this study, the researcher follows a post-positivist research paradigm which accordingly, informs the quantitative approach in addressing the objectives. Using this scientific method of research, the researcher will be able to use empirical data to arrive at an impartial and general conclusion on the perceptions of students regarding MAFR. The post-positivist (rather than positivist) paradigm has been selected as absolute certainty would not be realised based on the nature of the aims of the study, rather great probability or approximation (Mackenzie & Knipe 2006). As the study seeks to determine the perceptions regarding the possible outcomes of the implementation of MAFR by university students, the interpretivist/constructivist (which accepts multiple realities due to subjectivity), critical/transformational (which addresses matters of social fairness), and pragmatic (the use of whichever workable notion) paradigms have not been used. This as the implementation of MAFR would either stand to benefit or disadvantage the auditing function and profession. The perceptions of university students thereof would either be in agreement or disagreement with this (Creswell 2007; Mackenzie & Knipe 2006; Kivunja & Kuyini 2017; Barbara 2012).

### **3.2.2 Why a quantitative approach?**

Post-positivist research predominantly (but not exclusively) makes use of quantitative methods of research (Mackenzie and Knipe, 2006). A research method refers to the researchers' way of considering the thesis statement. The researcher chooses or designs a method that is most appropriate to their work and that will yield the most reliable results (Hofstee, 2006). While there are two research approaches available for the study, namely quantitative and qualitative research, the study will follow the quantitative (confirmatory) approach to test the thesis statement. The purpose of the study is to test student perspectives on the effects of the MAFR rule to be implemented in 2023, and make predictions based on findings. A quantitative approach will allow the researcher to do this, gauging where the future auditors (university students) stand on MAFR. The quantitative research method is suitable in studies that indicate trends and explain relationships between variables (Creswell, 2014).

Quantitative research methods make use of measurements to prove or refute an existing hypotheses (Runciman, 2002). In a quantitative study, the researcher uses different techniques in the collection of data which can include interviews, surveys, questionnaires, case studies, action research, secondary analysis or content analysis amongst others. The chosen instrument allows the researcher to ask specific questions to obtain answers which will be used as data in a statistical analysis and interpretation of the responses. The outcomes of this analysis are thus objective and without any influence from the researcher, which is in line with the research paradigm of this study (Creswell, 2014). Quantitative methods place emphasis on objective measurements and data analysis using computational means (statistical or numeric analysis). Quantitative research is centred on the assembly of mathematical data and generalizing it or to explain a particular occurrence Mccrindle (2008).

A distinguishing factor between quantitative and qualitative research is the type of data collected, where data that is directly measurable results from quantitative research, while data that is recordable (e.g. audio) will result from qualitative research. Although measurement can also be applied to audio (qualitative research), the focus in qualitative research is more on context than counts (Bacon-Shone 2015). Qualitative methods are flexible and do not necessarily ask participants the same questions in the same order (Creswell, 2014). An advantage provided by the more structured and inflexible quantitative approach, is that meaningful comparisons can be conducted on collected information (Collector & Module 2011). A quantitative approach will specifically allow the researcher to work with a larger sample of students to determine the perspectives of students on MAFR, which can be generalised. The approach will enable an objective conclusion on whether students perceive the prospective to have positive or negative outcomes on auditor independence, quality and other factors. The approach is considered appropriate as the study does not seek in-depth interpretations by the student on the subject of MAFR.

### **3.2.3 Advantages and disadvantages of a quantitative approach**

The use of a quantitative approach is beneficial in this study as it involves the measurement of the perceptions of groups of students (numbers) on MAFR. It enables the researcher to include a greater number of students and improves the

generalisability of the outcomes, in an objective and statistical manner. To ensure there is no bias or undue influence on the participants, the researcher is able to distance themselves by employing an assistant unknown to the participants to administer the collection of data. The method enables easy replication and predictions, so the study can be conducted with students at different institutions and be effortlessly comparable (Creswell, 2014).

Quantitative research has its own disadvantages. It is inflexible and is not considered suitable in the study of human behaviour or studies that seek to obtain great insights on a matter (which are not the case in this study of MAFR). The instrument used in the collection of data is susceptible to errors for example in the measurements used and also in sampling techniques. Another disadvantage is that some topics may not be appropriate for quantitative research, particularly those that do not require the incorporation of numbers. Data collected is narrow and can be considered shallow. The outcomes of a quantitative study provide statistical rather than narrative descriptions, and thus inherently have less of the human factor. Lastly, the approach is conducted in a controlled context with pre-set questions and answers which may not necessarily be representative of the views of the participants, thus potentially causing structural bias in the study (Creswell, 2014).

### **3.2.4 Other references**

A researcher should sensibly consider choices available when deciding on the approach and in selecting methodologies that underlie auditor independence studies in order to appreciate the context and meaning of the results of the study Church *et al.*, (2015). Said & Khasharmeh (2014) and Anis (2014) follow a quantitative approach to source data through the use of survey questionnaires to solicit the perceptions of auditors regarding MAFR. This has been adopted for this study whose participants are future auditors. Some researchers use quantitative survey research (through questionnaires) in the study of MAFR and its impact on independence, although others use analytical and archival research methods, as determined by the context of the study K. Said and Khasharmeh (2014) while Fontaine *et al.* (2017) followed a qualitative approach in the survey of audit committee members on MAFR. Given the context and nature of the study, whose participants are current university students, a quantitative approach through questionnaires has been followed.

### **3.3 Research method**

The decision over a method is important in a research study. The selection is dependent on the context of the study, considering the topic, characteristics of the participants and availability of resources (Floyd and Fowler, 2009). Put differently, a research method is the way in which the research approach selected by the researcher is applied, to accomplish the researcher's objectives (Hofstee, 2006). This section addresses aspects of the methodology that include the population, sampling, the collection and analysis of data, the research instrument, as well as procedures employed to ensure that the data are trustworthy.

#### **3.3.1 Defining the target population**

A population refers to a group of people that have the same characteristics, such as a group of university students (Creswell, 2014). The population of this study is comprised of current university students registered for an accounting and auditing qualification and specifically, an auditing courses, who are referred to as the population units and will be the source of data (Blair, Czaja and Blair, 2014). The individual university student is the single entity or element in the population of the study (Alvi, 2016). Often, in specific and practical research terms, a researcher may not study the whole population due to various reasons such as the inability to obtain lists or identify individuals to be studied (Creswell, 2014).

A boundary has been set for the population of the study using geographic locations and considering the practicality and effectiveness of the research. It is important to set specific effective terms for a study so they are clearly identifiable (Blair, Czaja and Blair, 2014). The university auditing student population used in the study is determined as students at the undergraduate and postgraduate level of study of their qualification at a traditional university in the KwaZulu-Natal province of South Africa. Students at traditional universities (throughout the country, including those in KwaZulu-Natal) are gradually working through formal competency-based academic education (an academic programme) in preparation to write the Initial Test of Competence (ITC) of SAICA. The academic programmes follow the competency framework provided by the

institute (SAICA, 2016). While students may not be at the exact same levels of knowledge and understanding throughout the process (as this depends on the level of study and the delivery of the programme by their university), their exit level is similar. On completion of the academic programme (on obtaining the Certificate in the Theory of Accounting – CTA), and thus fulfilling the competency requirements of the SAICA academic programme, students write the same ITC examination.

Auditing students currently completing the academic programme, who are the potential respondents of interest in this study, represent primarily young individuals who are being trained in various competencies including governance and assurance of organisations. This competency requirement includes the students' understanding of the legal and regulatory environment responsibilities, functions and qualities by students, which includes the Auditing Profession Act of 2005, and the Companies Act (as applicable to the auditor and the IRBA Code of Conduct amongst others (SAICA, 2016). These laws or regulations and code of conduct have a direct or indirect relatability or relationship to the topic of MAFR. The academic programme includes the teaching and learning at different proficiency levels of auditing and assurance topics that include auditor ethics, independence, rotation and quality.

Ethical behaviour and professionalism is one of the competencies that students completing the academic programme need to develop as part of the pervasive qualities and skills to be acquired. This competency requires that students keep up-to-date with trends, developing issues and new rules and regulations, thereby embracing an attitude of life-long learning (SAICA, 2016). The announcement by the IRBA regarding the intended implementation MAFR forms a significant development in the accounting and auditing sector and its regulatory and professional framework that students would have become aware of. Students are able to deal with issues and answer questions that are central to the MAFR debate as they have a thorough conceptual knowledge which enables them to further explore and comprehend complexities, as suggested by the competency framework (SAICA, 2016).

A target population, refers to a group that has shared characteristics that can be recognised by the researcher and then studied. This is the group from which a sample will be selected and is made up of the sampling units or elements (Alvi, 2016). The

researcher selects a sample through sampling units or elements within the target group (Creswell, 2014). The target population has been determined as the following for this study:

- Students registered for the auditing course at the appropriate level (a level which enables them to respond to questions on MAFR) as part of their registered accounting academic qualification, at a public residential university (traditional and comprehensive) in KwaZulu-Natal. The registered qualification follows the SAICA accounting programme and provides access for the student to register with the IRBA as a Registered Auditor (RA) in future.

KwaZulu-Natal has two (2) of the nineteen (19) public (traditional) universities in South Africa (DHET, 2018). These are; the University of Zululand (UNIZULU) and the University of KwaZulu-Natal (UKZN). Both universities are accredited by SAICA to offer the accounting programme and thus follow the SAICA academic programme. Distance and independent or private institutions offering the accounting programme have been excluded from the target population as the student body at these institutions may have different characteristics. Students at both universities do not take an auditing course in their first year of study and have thus, been excluded from the population. Furthermore, students at the second level of study at UNIZULU do not cover auditing topics at an appropriate level for students to be able to respond to MAFR related questions in this study, and so, they have also been excluded. Students, however in their second year of study at UKZN, cover auditing topics and MAFR (including a class project on it) at a level considered appropriate to be able to respond to the question of the study and resultantly have been included in the population.

### **3.3.2 Identifying the sampling frame**

The sampling frame refers to the actual detail of the target population (e.g. lists), consisting of the population units which in this study are the students (Bacon-Shone, 2015). The researcher selects a sample within the sampling frame (Creswell 2014; Blair et al. 2014). The sampling frame for this study was determined as follows:

For UNIZULU, the following groups of students form part of the sampling frame and the sizes have been determined using the university enrolled student management system (UNIZULU, 2018)

- Auditing 3: 230
- Auditing 4: 52

For UKZN, the following groups of students form part of the sampling frame and the sizes have been determined using the university enrolled student management system - Institutional Intelligence Reports (UKZN, 2018):

- Auditing 200: 498
- Auditing 3: 444
- Advanced Auditing: 395

The sampling frame for the study is therefore comprised of 282 students at UNIZULU and 1337 students at UKZN. The sum for the study is thus 1 619 (281 plus 1 337)

### **3.3.3 Determining the sample size**

A sample is a detachment of a population (Lohr, 2010) and a good sample is a “scaled-down” version of the population, and is thus representative of the characteristics of the population (Lohr, 2010). The researcher is then able to generalise the results from the sample to the target population (Creswell, 2014). The appropriateness of a sample is determined by the evaluation of the way it was selected and not the results or its characteristics (Floyd and Fowler, 2009). The selection of a sample entails the determination of the sampling frame (individuals that have a chance of being selected) that represents the population, the use of an appropriate sampling technique and a sampling design and size that approximates the characteristics of the entire population (Floyd and Fowler, 2009).

A confidence interval approach has been followed in the determination of the sample size for this study. This approach is based on the relationship between a sampling error and a sample size (Etikan, 2016). The mean of a sample generally only approximates that of the population, and does not equal it. A sampling error is used to

express the probabilities that the results of the sample fall within a particular range of figures for the population.

The sample size has been computed using the following formula:

$$\text{Sample size} = \frac{\frac{z^2 \times p(1-p)}{e^2}}{1 + \left( \frac{z^2 \times p(1-p)}{e^2 N} \right)}$$

Where:  
N = population size  
e = Margin of error (percentage in decimal form)  
z = z-score

A sample size of 439 was determined using the above formula, with the margin of error at 4% and a confidence level of 95%. A total of 413 completed questionnaires were received, representing a response rate of 94%.

### 3.3.4 Selecting the sample and participants

Researchers use either probability or nonprobability sampling, depending on the nature of their research study (Creswell, 2014). Probability sampling is a rigorous sampling form which applies some form of random selection where all units of the population have a chance of being selected (Lohr, 2010). This technique was not used in this study due to the nature of the study and the participants being students. A non-probability sampling technique has been used to select a sample of participants. Non-probability sampling is used where the researcher exercises judgement and a non-random approach to sampling (Blair, Czaja and Blair, 2014). Units in the population do not necessarily get an equal chance of being selected for participation in the study as the selection is made on the basis of subjective judgment of the researcher Alvi (2016).

Convenience and purposive sampling have been used to select the sample. Convenient sampling is often used in quantitative studies. It implies the selection of participants that are easy or convenient to approach (Alvi 2016 ; Etikan 2016). The researcher is an auditing lecturer at one of the universities in KwaZulu-Natal and so auditing students are reasonably readily available. Purposive sampling refers to an approach to sampling with a prior purpose in mind, having predefined the units of the



population to be included in the study (Alvi 2016 ; Etikan 2016). The sample for the study includes auditing students who are all registered for the auditing course (be it at different levels and universities).

The sample is comprised of students who were in attendance during a pre-selected auditing lecture slot. To limit bias, students were not informed prior to conducting the research of the intention. The selection of the lecture period was random and dependent only on logistical arrangements and availability of time immediately before or after the period. The use of nonprobability sampling in the study is beneficial as it requires less effort, less time to work on the research and is not costly (Alvi 2016 ; Etikan 2016). The sampling technique may not, however, be completely free from bias and the selected participants might not be representative of all the students registered for the course (Alvi 2016 ; Etikan 2016). The use of this approach yielded 413 respondents (which is above the sample size of 311). All questionnaires completed by students were considered in the data analysis.

### **3.3.5 Procedures for collecting data from selected participants**

Once participants have been selected and identified, appropriate permission, which includes ethical approval and access to participants needs to be obtained prior to collecting data (Creswell, 2014). Ethical clearance was received from the Humanities and Social Sciences Research Ethics Committee of the University of KwaZulu-Natal and authorisation to access the participants from the Registrar of each university before data were collected. The signing of the informed consent form was compulsory for participants and the confidentiality of the information they have provided for the study is assured.

A survey-based research approach to collect data has been used, through the use of a questionnaire. Data sources and collection need to lead the researcher to reliable and well-argued conclusions (Hofstee, 2006). Data was collected from students at the two higher education institutions (UKZN and UNIZULU), who are currently registered for an auditing course (or module) in the Bachelor of Accounting, Bachelor of Accounting Science or the Postgraduate Diploma in Accounting (PGDA).

Arrangements were made with the academic staff members responsible for the auditing classes at the different levels to hand out the questionnaire for completion immediately before or after the lecture. Students registered for PGDA at UKZN had completed their academic programme during the data collection stage and could not be reached together in one venue. Efforts were, therefore, made to collect data from students that were available on campus during and after the examination period.

A research assistant who collected data during some of the lecture slots was utilised during the data collection period where appropriate (e.g. from the class lectured by the researcher – ensuring the limitation of any influence). Data that were collected from participants was secured through sealed envelopes and locked away in a secure location. No person other than the researcher and the assistant have had access to this data. The data were captured to convert it into an electronic format (Microsoft Excel) which is password protected. A backup of this data is also stored external of the main computer used for the study.

### **3.3.6 Research instrument**

A researcher may conduct a survey-based research to elicit data from participants using whichever instrument that is considered appropriate for the study (Hofstee, 2006). A researcher should, dependent on the purpose of the study as well as the target groups, select and plan for the use of an appropriate data collection instrument before actually constructing it. A pilot study should then be conducted to evaluate the appropriateness of the instrument and the necessary revisions effected (Creswell, 2014). For this quantitative study, for which a statistical analysis is performed to examine the perceptions of students on the impending MAFR, a research questionnaire has been selected, developed based on literature reviewed, sent out in a pilot study, amended as necessary and used for data collection. All participants completed the same questionnaire.

Said & Khasharmeh (2014) and Anis (2014) sourced data through the use of survey questionnaires to solicit the perceptions of auditors regarding MAFR while Fontaine et al. (2017) used interviews in the survey of audit committee members (who could provide in-depth insights) on MAFR. Given the context and nature of the study, whose participants are current university students, a structured questionnaire is appropriate.

The design of the questionnaire and the collection of data should be such that participants respond to the research questions of the study (Creswell, 2014). This involved particularly the use of structured questionnaires in which students provide their perspectives on MAFR, in response to the research questions (Hofstee, 2006). The research instrument focuses specifically on the research questions of the study. These questions seek to determine whether perceptions of students on the introduction and implementation of MAFR in South Africa are that auditor independence and audit quality would be improved; and whether any other benefits can be reaped or if instead, negative unintended consequences may be suffered.

The first section (General information) of the questionnaire requires participants to complete their biographic information such as age, gender, race, level of study, etc. and comprises a total of six (6) questions. The second section (MAFR questionnaire) relates to the research questions and is informed by literature. The second section is divided into three core parts in alignment to the research questions. The first part contains five (5) questions relating to the impact of MAFR on independence, the second part contains six (6) questions relating to the impact on audit quality and the last part contains seventeen (17) questions on other areas of potential impact. Though a structured form of data collection, questionnaires may include open questions (Hofstee, 2006). An open question has been included in the second section of the questionnaire, which requires participants to mention any potential impact of MAFR not mentioned in the questionnaire. From this open question, the researcher identified common themes from the responses of participants. The questionnaire thus has a total of thirty six (36) questions.

Respondents are required to answer the questions in the second section, which respond to the research questions using a five-point Likert scale (rating scale) between 1 – strongly disagree (SD) and 5 – strongly agree (SA). The use of a Likert scale is common practice (Creswell, 2014) and was also used by for example K. Said and Khasharmeh (2014); Aschauer and Quick (2018); Quick and Schmidt (2018) in their studies. The data collection instrument (the questionnaire) is attached as an appendix to this dissertation.

### 3.3.7 Data reliability and validity

A research instrument that reports reliable and valid data should be chosen by a researcher and the researcher ought to show how reliability and validity was achieved. An instrument containing clear questions and response options reduces measurement error as it encourages respondents to provide appropriate answers (Creswell, 2014). Data were collected through a consistent questionnaire responded to by participants, who are the primary source for this study, in an effort to arrive at a reliable conclusion. Validity refers to the measure of the degree to which the test scale serves its intended purpose. From the data analysis and based on observations during the data collection process, students were able to respond to the research questions correctly, with no issues noted. Students were observed discussing views on the different MAFR issues, illustrating their ability to respond to the survey questions, thus increasing confidence in the degree to which the study measures the perceptions of students on MAFR (Creswell 2014; Saunders *et al.* 2009).

Reliability amounts to the measure of consistency. To ensure reliability, the basis of the research instrument was the research questions as well as applicable literature. The survey questions centred on the research questions and the same instrument was handed out to all participants, which had consistent scores to ensure stability and consistency. A number of suggestions by Creswell (2014) to ensure reliability of data have been implemented in this study. The survey questions are clear, supported by literature and comparable to those used by other researchers. The questionnaire administration procedures during data collection up to recording were standardised. The questionnaire was reviewed by members of staff in the Department of Accounting and Auditing at UNIZULU (including the Head of the Auditing Discipline). A pilot study was conducted with ten fourth year auditing students who serve as tutors in the auditing discipline at UNIZULU. The reviewer provided valuable feedback regarding the study and the survey questions. This review of content also tests validity. Their suggested corrections were effected in the final questionnaire (Coughian *et al.* 2007; Creswell 2014).

Furthermore, the questionnaire was administered during auditing lecture periods which were all scheduled in the morning. No students were observed to be exhausted, or likely to misinterpret questions or end up guessing answers. Students were also

under no influence and were not observed to be nervous. The questionnaire was administered by a research assistant in the class lectured by the researcher to ensure that there is no undue influence on the students. Lastly, the questionnaire used the common Likert-scale (Creswell, 2014). Measures were applied to ensure the integrity of data provided by students including restricting access, careful handling, and the employment of an appropriate analysis strategy (Coughian *et al.* 2007; Saunders *et al.* 2009).

To test for internal consistency, the coefficient alpha (Cronbach's alpha) has been calculated to determine the reliability of the instrument. Cronbach's alpha is able to measure the consistency of scores, which may not be possible for a "naked eye" (Creswell, 2014). The following formula has been used to determine the alpha:

$$\alpha = \frac{N \cdot \bar{c}}{\bar{v} + (N-1) \cdot \bar{c}}$$

Where:

N = the number of items.

$\bar{c}$  = average covariance between item-pairs.

$\bar{v}$  = average variance.

When evaluating reliability, as a rule of thumb, an alpha range less than 0.6 is considered to be poor, while that greater than or equal to 0.9 is considered to be excellent. An alpha between 0.6 to and 0.7 is moderate, 0.7 to less than 0.8 is good and from 0.8 to less than 0.9 is very good (Hair *et al.*, 2007). The alpha calculated for the study is 0.82 which is considered to be good, thus indicating that a reliable instrument has been used.

Validity has a complex relationship with reliability as both are sometimes complementary or overlap and at times, they can be mutually exclusive. A valid instrument is always reliable, but a reliable instrument does not need to be valid. Reliability thus leads to (greater) validity (Creswell, 2014). Validity is about the genuineness of the research, in that it measures what was intended. It is a measure of the scores, and not the actual instrument (Creswell, 2014). Its concern is whether the findings or conclusions are truly about what they seem to be about (Saunders, Lewis and Thornhill, 2009).

A researcher should be concerned with both internal (degree to which the instrument measures what it is supposed to) and external (the degree to which results are generalisable) validity (Saunders, Lewis and Thornhill, 2009). To develop internal

validity in this study, the research has referred to face and content validity. The contents of the instrument were piloted with students (who work as tutors in the auditing discipline at UNIZULU) and reviewed by members of staff in the Department of Accounting and Auditing at UNIZULU, which included the leader of the Auditing discipline. The pilot and review provided constructive and positive feedback that produced an instrument measuring what it is intended to, with reference to the research question and the instrument's coverage of MAFR contents (Price et al. 2015; Kumar 2012; Saunders et al. 2009).

Where internal validity is limited, external validity would also be limited as there would be no point generalising the results. However, generalisability is not certain even if internal validity has been achieved (Ferguson, 2004). The concern in relation to external validity in this study is the extent to which the findings of the study could be applicable to the target population (auditing students at UNIZULU and UKZN) and auditing students at other universities in South Africa and in other parts of the world. Cook & Campbell (1979) distinguish between generalizing to a population (population validity) and *across* subpopulations (from one group to another – ecological validity) (Ferguson, 2004). The threat to external (population) validity is decreased by the use of a target population (as compared to an accessible population) (Ferguson, 2004) to select the sample, which is opposed by the use of the convenience sampling technique. The manner of selection of participants, however, was based on students who were in attendance during lectures on a randomly pre-selected day and no other prior arrangements were made with students. This makes it possible to generalise the findings.

Generalisation to and across populations involves inferences and the making of broad statements, using particular data such as that in the sample of the study (Ferguson, 2004). Generalisability across other institutions of higher learning would be a challenge if the two universities covered by this study are considered to have unique characteristics which may not be applicable at other universities (Saunders, Lewis and Thornhill, 2009). The more the sample is representative of the population, the more (in theory) it allows for generalisation (Ferguson, 2004). The convenience sampling technique has primarily been relied on in the study. However, the selection of participants was by chance as it depended solely on students who attended the lecture on the day that the questionnaire was administered. This in turn increases the

likelihood of a sample that represents the population of university students, and thus allowing for generalisation of findings.

Auditing university students (who constitute the population for this study) at traditional universities (particularly throughout the country, similarly to those in this study) are gradually working through formal competency-based academic education (in South Africa, a SAICA academic programme). The SAICA academic programme is navigated in a similar manner by different universities and ultimately, students exit at competency levels that are the same (SAICA, 2016). Determining the student profile, background and personality traits of auditing students of the different universities would be complex. However, it is not unreasonable to assume that there is a fair amount of diversity and representation at each institution. First time entering students who wish to pursue accounting and auditing studies usually select from fifteen (15) public residential universities, or may choose a distance learning institution or a private provider, accredited by SAICA (SAICA, 2018). These students make their choice of universities based on many variable reasons and come from different backgrounds to study at the institutions. Once registered, they then follow the relevant academic programme. Although their worldviews may be different, the knowledge gained from the academic programme is similar. It is also possible that any student may end up registering at any of the institutions accredited by SAICA and thus, the participants of this study likely represent the population of other university students.

### **3.3.8 Data coding and analysis**

According to (Hofstee, 2006), data needs to be turned into evidence and information, through performing statistical or textual analysis or a combination of the two. Once complete and accurate data for the study are collected, the researcher performs an analysis to explain data and make inferences by using appropriate statistical techniques (descriptive and inferential) or econometrics models (Kumar, 2012). The calculation of statistics is part of a bigger process in the analysis of data. The researcher then identifies trends and creates a summary of the data. An analysis involves preparing data to be analysed (coding), conducting the analysis, reporting findings, and discussing these (Creswell, 2014).

Data in preparation for a quantitative analysis should be assigned and recorded using a unique numerical codes (Ferguson, 2004). In the preparation of data, each questionnaire was assigned a unique number which followed a sequence. The use of a sequential numbering system allows for ease of reference from the electronic (captured) data back to the course, which would be the questionnaire. All data were captured on a Microsoft Excel spreadsheet which was coded according to the unique numbers allocated to the questionnaires (and response options) and the data were prepared for analysis. Each question in the questionnaire was also allocated a number for the analysis and to ensure effective coding.

The coded data were uploaded on a statistical software for analysis. From the data, a researcher conducts an analysis that is sufficient to provide necessary explanations and conclusions as required by the objectives of the study. The dawn of many statistical analysis software packages aids researchers in the analysis of data (Kumar, 2012). Researchers generally make use of a statistical software to analyse data (Creswell, 2014). The IBM SPSS Statistics 25 or Statistical Package for the Social Sciences 25 (SPSS25) has been used for coding and capturing data in this study. The use of the SPSS software makes the analysis part of the research project easier for the researcher (Kumar, 2012). According to Field (2009), SPSS is “the best of the commercially available statistical packages and is commonly used in many universities”. There were no identified errors in the data and missing data were so negligible (a few participants did not answer a particular question for unknown reasons). Outcomes are reported on excluding a response not provided by a participant.

The following descriptive statistical analysis techniques have been used in this study:

#### **3.3.8.1 Frequency distribution**

Frequency distribution depicts, in a summarised format, data of one variable, outlining how commonly it occurs. Frequency distribution tables show the number of respondents that chose each answer to a survey question. It is a descriptive statistical instrument which can be used to provide information about the demographic particulars of the research participants, as well as the simple results of individual questions in the questionnaires. The approach followed in the study was the identification of the largest (and second largest groups - necessitated by significance)



scores by participants to highlight these and then report on them with possible explanations and corresponding literature (Saunders *et al.* 2009; Creswell 2014; Patel 2009).

### **3.3.8.2 Central tendency and dispersion**

Measures of central tendency are summary figures from collected data that denote a single value in a distribution of scores from respondents. They are expressed in three ways: the mode (the most frequent score), the median (the middle of a set of scores) and the mean (the average score). Researchers may report all three in a quantitative study, with the mean being the most popular of the three. Only the mean has been reported in this study. In contrast to analysing the central tendency, a researcher may also describe how data values have been dispersed around the central tendency. In this study, the standard deviation (which measures the average distance of each value away from the sample mean) has been used to describe as well as compare the difference between the mean and values provided by respondents (Saunders *et al.* 2009; Creswell 2014).

### **3.3.8.3 Correlation – Relationships and association**

To assess the relationship between two variables, a researcher uses Pearson's correlation. This parametric statistical technique is possible in this study as the collected samples are normally distributed. The calculation of a correlation coefficient enables the measure of the strength of the linear relationship between two ranked or numerical variables. The Pearson correlation coefficient ( $r$ ) can be any number between -1 (negative relationship) and +1 (positive relationship). A coefficient of -0.3 and 0.3 are considered to be weak and a 0 represents perfect independence of the variables. The correlation is used to respond to the research questions in this study (Saunders *et al.* 2009; Creswell 2014).

### **3.3.8.4 Reporting data**

In providing explanations and supporting arguments made in a research project, a researcher may use non-textual material (such as charts, tables and other graphics) (Hofstee, 2006). This part of the project is arguably one of the most challenging but

also rewarding, as it contains the culmination of all the work performed. The researcher presents and discusses specific results of the statistical analysis. The results reporting section of the study contains tables (which summarise statistical information), figures (charts) and detailed explanations of the result and supporting literature (Creswell 2014).

In reporting data, the researcher should respond to the research questions of the study (Creswell 2014). To ensure this, as part of the presentation of the results, a link has been made to the research questions as outlined in chapter 1. Following the reporting and explanation of results, to enable a conclusion to the study, a summary of the key findings is provided by summarising the major results of the research project. (Creswell 2014).

### **3.4 Ethical considerations**

This section details what the researcher has done to make sure that the work adheres to the applicable ethical guidelines (Hofstee, 2006). Ethical clearance for the study was obtained from the Human and Social Sciences Research Ethics Committee of the University of KwaZulu-Natal in line with the guidance of the university. In addition, the supervisor who directed the researcher through the research process was qualified and experienced. To ensure the integrity of data, it were kept in sealed envelopes and locked away in a safe location. To protect the confidentiality of the participants (who are students), their identification was not collected, ensuring their anonymity. There were no significant ethical concerns that needed to be addressed in this research study.

### **3.5 Chapter summary**

This chapter has discussed the methodology. The chapter commenced with a brief introduction before outlining the research approach/paradigm for the project, with the approach followed being quantitative, outlining reasons for selecting this approach. The chapter then described the population for the study, which comprises of auditing students at the two universities in the province of KwaZulu-Natal, as well as the

sampling of the population, thereafter the procedures followed and instrument (questionnaire) used in the collection of data from participants.

The chapter concluded by discussing the ethical considerations, elaborating on the coding of data collected from participants and the statistical analysis performed on the data and discussing how the researcher has ensured the reliability and validity. Chapter 4 presents and discusses the findings which are based on the analysis of data obtained from the structured questionnaires handed out to research participants.

## **CHAPTER 4: PRESENTATION AND ANALYSIS OF DATA**

### **4.1 Introduction**

The preceding chapter provided details on the methodology of the study by describing the quantitative approach selected and providing detail on the research method. The chapter described the population, method used to select a sample, as well as the collection of data, its management, analysis and presentation. The measures employed to ensure the reliability and validity of the study were also dealt with. The chapter concluded with a discussion relating to the ethical considerations.

Chapter 4 presents an analysis and discussion of the data as well as findings. A research questionnaire was used in order to collect data, in an effort to realise the research objectives. In this chapter, the method of analysis and presentation will be discussed. Furthermore, the results of a diagnostics test and the actual presentation of results in line with the research questions (that is auditor independence, audit quality and other considerations) are also presented. The brief discussion of the reliability and validity of data is followed by the analysis.

### **4.2 Method of data analysis and presentation of data**

This chapter presents and discusses the analysis and findings from 413 questionnaires completed by auditing students at the Universities of Zululand and KwaZulu-Natal during the 2018 academic year. A sample size of 439 was determined for the study, using 4% margin of error and a confidence level of 95%. This represents a response rate of 94%. The questionnaires were handed out to students during or around the time of their auditing lectures at their respective universities. The objective of the study was to examine the perception of auditing students regarding the imminent implementation of MAFR in South Africa and the impact it will have on auditor independence, audit quality and other parts of the audit profession and practice.

In analysing the data, descriptive and inferential statistics were used to identify frequencies, percentages of responses to questions and the general perception of respondents. The measure of central tendency (expressed as: a mean) and the variability measure (the standard deviation) have been used in the analysis. The data

and findings are discussed according to the following sections which is in line with the questionnaire used to collect data as well as the research questions:

- Personal (Biographical) data
- Impact on auditor independence
- Impact on audit quality
- Other potential impact
- Further data analysis
- Additional comments by students

### **4.3 Diagnostics Test Results**

The research instrument utilised throughout the study (refer to appendix A) is consistent, based on literature and contains clear questions and response options. Based on the data analysis (and observations during the data collection process), students were able to respond to the research questions correctly, with no issues noted. Furthermore, students were observed discussing views on the different MAFR issues, illustrating their ability (and interest) to respond to the survey questions. The researcher is confident that the study has met its objectives. The questionnaire was reviewed by members of staff in the Department of Accounting and Auditing at UNIZULU (including the Head of the Auditing Discipline) and with feedback received from Auditing tutors from the same department following a pilot study. These initial reviews ensured the development of internal validity for the study.

To test for internal consistency, the coefficient alpha (Cronbach's alpha) has been computed to determine the reliability of the instrument. Cronbach's alpha is able to measure the consistency of scores, which may not be possible for a "naked eye" (Creswell, 2014). The alpha calculated for the study is 0.82 which is considered to be good, thus indicating that a reliable instrument has been used (Hair *et al.*, 2007).

Regarding sample selection, the approach followed was based on students who were in attendance during auditing lectures on a randomly pre-selected day (no prior arrangements were made with students). This makes it possible to generalise the findings.

## 4.4 Descriptive analysis

### 4.4.1 Personal (biographic) data – age, race, university, etc.

This section covers the respondents' age, race, gender, university of study, level of study and qualification registered for. Though not central to the study, this section helps contextualise the results by providing a profile of the respondents.

<b>Table 4.1 – Total respondents for the study</b>						
	<b>Age</b>	<b>Race</b>	<b>Gender</b>	<b>University of study</b>	<b>Qualification registered</b>	<b>Level of study</b>
Valid	404	412	413	413	413	413
Missing	9	1	0	0	0	0
Total	413	413	413	413	413	413

Respondents were asked their age, gender, university of study, qualification registered for as well as level of study. Tables 4.2 to 4.7 depict this information.

<b>Table 4.2 – Age</b>		
<b>Age Category</b>	<b>Frequency</b>	<b>Percentage</b>
18 – 21	276	68.3
22 – 25	115	28.5
26 - 30	13	3.2
Total	404	100

<b>Table 4.3 – Gender</b>		
<b>Gender</b>	<b>Frequency</b>	<b>Percentage</b>
Male	196	47.5
Female	217	52.5
Total	413	100.0

<b>Table 4.4 – Race</b>		
<b>Race</b>	<b>Frequency</b>	<b>Percentage</b>
African	314	76.2
Coloured	9	2.2
Indian	83	20.1
White	5	1.2
Other	1	0.2
Total	412	100.0

<b>Table 4.5 – University of study</b>		
<b>University</b>	<b>Frequency</b>	<b>Percentage</b>
University of Zululand	150	36.3
University of KwaZulu-Natal	263	63.7
Total	413	100

<b>Table 4.6 – Qualification registered at university</b>		
<b>Qualification Name</b>	<b>Frequency</b>	<b>Percentage</b>
UNIZULU - Bachelor of Accounting Science	72	17.4
UNIZULU - Bachelor of Accounting	78	18.9
UKZN - Bachelor of Accounting	237	57.4
UKZN - Postgraduate Diploma in Accounting	26	6.3
Total	413	100.0

<b>Table 4.7 – Level of study</b>		
<b>Level of study</b>	<b>Frequency</b>	<b>Percentage</b>
<b>2 (UKZN)</b>	137	33.2
<b>3 (UKZN and UNIZULU)</b>	214	51.8
<b>4 (UNIZULU NON-CTA)</b>	36	8.7
<b>4 (UKZN CTA)</b>	26	6.3
<b>Total</b>	<b>413</b>	<b>100.0</b>

Section A of the questionnaire revealed that out of the 413 respondents to the study, most are: between the ages of 18 and 21 (68.3%), female (52.5%), African (76.2%), registered at the University of KwaZulu-Natal (63.7%), registered (at UKZN) for the Bachelor of Commerce (Accounting) degree (57.4%) and in their third year of study (51.8%).

#### **4.4.2 The impact of MAFR on independence**

This section of the questionnaire reveals the responses of students on questions relating to the perceived effect of MAFR on independence. The questions were answered by students using the Likert scale (between one and five).

**Table 4.8 – Responses relating to MAFR impact on auditor independence**

Statements relating to the perceived impact of the implementation of MAFR on independence.	Strongly disagree (SD)	Disagree (D)	Neutral/No change (N)	Agree (A)	Strongly agree (SA)	Mean	Standard Deviation
<b>Q7.</b> A long audit tenure (term), where an audit firm audits a client longer than ten years without rotating leads to the familiarity threat to the independence of the auditor.	2.9	1.2	2.7	24.5	68.8	4.55	.851
<b>Q8.</b> A long audit tenure (term), where an audit firm audits a client longer than ten years without rotating leads to the compromise of the professional scepticism of the auditor.	1.7	4.6	11.7	40.4	41.6	4.16	.921
<b>Q9.</b> A long audit tenure (term), where an audit firm audits a client longer than ten years without rotating will cause the auditor to be sympathetic to the position of the audit client.	3.2	3.9	15.3	34.5	43.1	4.19	.923
<b>Q10.</b> A long audit tenure (term), where an audit firm audits a client longer than ten years without rotating leads to the compromise of the objectivity of the auditor.	1.9	4.1	10.9	39.6	43.4	4.11	1.01

<b>Q11.</b> The implementation of MAFR will lead to the enhancement of the independence of auditors when conducting an audit.	2.7	1.2	5.8	28.3	62.0	4.46	.871
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Students responded positively (agree or strongly agree) to all five questions relating to the impact of MAFR on auditor independence (with an average mean above 4).

When asked if long audit tenures (over 10 years) lead to the familiarity threat to auditor independence, the majority of students (93.3%) affirmed, with a mean of 4.55 and standard deviation of 0.851 which confirms this view. This result is in line with the IRBA CPC which identifies long association with audit clients as a threat to independence (IRBA, 2009a). This finding is also consistent with (Hussey, 1999) who found that a longer audit term does threaten independence.

The majority of respondents (82%) affirmed when asked if a long audit tenure leads to the compromise of the professional scepticism of the auditor. This was confirmed by a mean of 4.16 and a relatively low standard deviation of 0.921. On long tenures resulting in auditors being sympathetic to the position of their client, the majority (78.5%) affirmed, with a mean of 4.19 and a standard deviation of 0.923. Garcia-Blandon & Argiles (2015), consistent with these results found that auditors were more inclined to sacrifice their independence and scepticism in long tenure audit engagements. Bamber & Iyer (2007) states that auditors indeed identify with their clients in varying levels. However, auditors do consider their professional identity as important. Svanberg & Öhman (2015) also found that auditors are inclined to identify with their clients, and when they do, there could be compromised scepticism and preferential treatment.

Respondents were asked if a long audit tenure leads to compromised auditor objectivity. The majority (83%) affirmed with a mean of 4.11 and a standard deviation of 1.01. This is consistent with the findings of Garcia-Blandon and Argiles-Bosch (2017), that tenure has an effect on auditors identifying with clients, a factor and which impairs auditor objectivity. When asked the direct question of the impact of the implementation of MAFR on independence, the majority of the respondents (90.3%) responded positively that its implementation will lead to enhanced auditor independence. The mean confirms the strength of the positive response (mean = 4.46) with a standard deviation of 0.871. This is consistent with (Junaidi et al. 2016;



Hohenfels 2016) who found a positive relationship between audit firm rotation and auditor independence.

#### 4.4.3 The impact of MAFR on quality

**Table 4.9 – Responses relating to MAFR impact on audit quality**

Statements relating to the perceived impact of the implementation of MAFR on quality. ( <i>Refer to Annexure A for the detailed questions</i> )	Strongly disagree (SD)	Disagree (D)	Neutral/No change (N)	Agree (A)	Strongly agree (SA)	Mean	Standard Deviation
<b>Q12.</b> A long audit tenure (longer than ten years), leads to a decline in quality of audit work.	4.4	9.7	19.9	41.2	24.9	3.73	1.07
<b>Q13.</b> A new audit firm (less client specific knowledge) may not detect material misstatements during the initial year(s).	5.6	23.2	20.3	36.8	14.0	3.31	1.13
<b>Q14.</b> Audit failure risk increases as the audit tenure period increases due to the level of comfort between the auditors and client management together with the desire to maintain the relationship.	1.5	7.7	17.9	52.5	20.3	3.83	0.89
<b>Q15.</b> Audit failure risk is higher in the initial stages of the audit tenure period due to a lack of specific client knowledge and experience by the incoming auditors.	4.6	20.8	24.7	35.6	14.3	3.34	1.10
<b>Q16.</b> The implementation of MAFR, leading to the competitiveness in audit fees, will cause the auditor to aspire to decrease audit costs by being efficient in the conduct of the audit which will result in a decrease in the quality of audit work.	6.1	18.9	33.7	32.0	9.4	3.20	1.05
<b>Q17.</b> The implementation of MAFR will lead to an increase in the quality of the work performed by auditors when conducting audit due to fresh eyes looking at client records.	1.9	5.1	14.8	46.1	32.0	4.01	0.92

Students generally responded positively to questions relating to the impact of MAFR on audit quality.

When asked if long audit tenures (over 10 years) lead to a decline in the quality of audit work, the majority of students (66.1%) affirmed, with a mean of 3.73 and standard deviation of 1.07. On whether the implementation of MAFR would lead to an improvement in the quality of the work performed by auditors when conducting audit due to fresh eyes looking at client records, the majority of respondents (78.1%)

agreed. The mean was 4.01 which confirms support by students that MAFR would lead to improved audit quality. The standard deviation was determined as 0.92. This is consistent with Hodge (2003) and Gul *et al.* (2009) who found that investors and auditors recognise audit quality declines over time, resulting in a perceived deterioration in the reliability of audited financial statements. Bell *et al.* (2015) found that audit quality decreases where the audit tenure (increases following rotation) is too long for non-listed company audits. Cameran *et al.* (2016) and Monroe & Hossain (2013) also found the rule to have a positive effect on audit quality.

Just over half (50.4%) of the respondents affirm that a new audit firm with a smaller amount client specific knowledge would not be able to identify material misstatements in the financial statements during the first few years of the audit tenure with a mean of 3.31 and a standard deviation of 1.13. This concern is consistent with (Hohenfels 2016; Gul *et al.* 2009) who highlight the importance of both client and industry-specific knowledge in order to maintain adequate audit quality, notwithstanding the impact MAFR may have on the audit quality.

When asked if the risk of an audit failure increases as the audit tenure period increases due to the establishment of a “comfortable relationship”, the majority (72.8%) either agree or strongly agree. The mean for this question was 3.83 with a standard deviation of 0.89. This finding is supported by Church *et al.* (2015) who found that continuing auditor-client relationships can lead to auditor complacency and undue trust of the client. Furthermore, concerns were raised regarding the “cosy” relationship between Enron and its Arthur Anderson auditors, who seemingly became too familiar, leading to the well documented failure of both (Arel, Brody and Pany, 2005).

Just under half (49.6%) of the respondents, with a mean of 3.34 and a standard deviation of 1.10, either agree or strongly agree that during the initial years of an audit tenure, the risk of an audit failure is higher as a result of the absence of specific client knowledge and experience by the new auditors. This is consistent with the finding by Hohenfels (2016), who highlights concern over the frequent changing of audit firms as quality was found to be at its lowest in the first three years of auditing a client. Bell *et al.* (2015) also found that new engagements (especially those that are large, complex and listed) involve a notable learning curve that generally, these audits are likely to achieve a lower quality rating in their first year and improve considerably after that.

The finding is also consistent with the opinion of the United States Centre for Audit Quality (CAQ) (Centre for Audit Quality, 2012).

When asked if the implementation of MAFR would result in the decrease of the quality of audit due to possible increased competitiveness in audit fees (resulting in pressure to reduce audit costs in an effort to achieve audit efficiency), 41.4% of the respondents affirmed while 33.7% were neutral on the question with a mean of 3.20 and a standard deviation of 1.05. This result does not represent an overwhelming affirmation by students. Ghosh et al. (2005) note an unintended increase in audit costs that may be caused by mandatory rotation of audit firms, while some studies have found that MAFR decreases audit costs (K. Said and Khasharmeh, 2014). Kwon *et al.* (2014) found in a study that where an increase in audit costs for audit firms occurs, audit fees also increase for clients without an accompanying increase in audit quality.

#### 4.4.4 Other potential impact of MAFR

**Table 4.10 – Responses relating to other potential impact of MAFR**

Statements relating to the perceived impact of the implementation of MAFR on other factors. ( <i>Refer to Annexure A for the detailed questions</i> )	Strongly disagree (SD)	Disagree (D)	Neutral/No change (N)	Agree (A)	Strongly agree (SA)	Mean	Standard Deviation
<b>Q18.</b> The implementation of MAFR will lead to an improvement in the <b>transformation</b> of the auditing profession in South Africa.	1.0	2.9	14.6	50.6	30.6	4.07	0.81
<b>Q19.</b> The implementation of MAFR will lead to an improvement in competition in the South African audit market	1.2	5.3	23.1	49.5	20.9	3.84	0.86
<b>Q20.</b> The implementation of MAFR will lead to a decrease in the market concentration, particularly concentration in the Big Four Firms.	1.0	10.7	34.7	31.6	22.1	3.63	0.97
<b>Q21.</b> The implementation of MAFR will lead to an increase in the protection of investors as a result of enhanced auditor independence and audit quality.	1.2	2.2	17.7	47.2	31.7	4.06	0.83
<b>Q22.</b> The implementation of MAFR will lead a decrease of the possibility of auditors subconsciously advocating for the point of view of the audit client.	0.7	6.1	33.8	43.6	15.7	3.67	0.84
<b>Q23.</b> The implementation of MAFR will lead to an improvement in the financial stability of companies under audit.	1.7	9.5	32.4	42.3	14.1	3.58	0.91

<b>Q24.</b> The implementation of MAFR will lead to an improvement in the financial stability of the economy of South Africa.	1.2	8.5	34.5	41.1	14.6	3.59	0.88
<b>Q25.</b> The implementation of MAFR will lead to an increase in audit costs due to the auditors need to understand new clients.	2.9	17.0	29.4	40.6	10.0	3.38	0.98
<b>Q26.</b> The implementation of MAFR will cause inefficiencies for client personnel and management who will have to explain how the company operates to new auditors after the rotation period.	6.8	30.3	27.4	28.2	7.3	2.99	1.07
<b>Q27.</b> The implementation of MAFR will lead to competitive audit fees being offered to audit clients.	3.2	12.1	31.3	43.0	10.4	3.45	0.94
<b>Q28.</b> The implementation of MAFR will lead to a decrease in audit fees due to the competitiveness brought about by the periodic rotations.	4.4	24.8	36.2	27.7	7.0	3.08	0.99
<b>Q29.</b> The implementation of MAFR, leading to the competitiveness in audit fees, will cause the auditor to decrease audit costs by making an effort to be efficient in the conduct of the audit.	3.9	25.1	37.2	28.7	5.1	3.06	0.95
<b>Q30.</b> The implementation of MAFR will lead to a more rigorous and transparent process for the appointment of auditors.	1.7	3.9	19.9	48.9	25.7	3.93	0.87
<b>Q31.</b> A sense of advancement of the public interest will be created, because the requirements apply all registered auditors equally in relation to public interest entities (PIEs).	0.0	2.9	20.7	53.3	23.1	3.97	0.75
<b>Q32.</b> MAFR will serve as a way of addressing concerns that those charged with governance do not always attain the required balance between public and entity interests.	1.2	8.0	31.2	48.7	10.9	3.60	0.83
<b>Q33.</b> The engagement of a new audit firm will ensure that the attention of management and those charged with governance is continuously refocused.	0.2	2.5	17.5	54.9	24.9	4.02	0.74
<b>Q34.</b> MAFR will encourage smaller, mid-tier and established audit firms to invest (or invest more) in expanding their staff and resources.	0.5	3.6	22.9	47.0	26.0	3.95	0.82
<b>Q35.</b> MAFR will discourage audit firms from investing in the development of expertise and specialisation (e.g. Insurance industry specialisation) for the firm due to the required periodic rotation.	10.7	27.3	35.0	17.3	9.7	2.88	1.12

This part of the questionnaire contained various questions on the potential impact of MAFR in South Africa.

IRBA initially described the transformation of the audit profession and addressing market concentration (Big Four domination) as the secondary objective of MAFR, later withdrawing this and advising that these would be addressed through complementary initiatives (IRBA, 2017b). IRBA and the accounting profession concede that the audit market in South Africa needs to be transformed to be in line with the demographics of the country and that the market is currently concentrated (particularly dominated by Big Four firms). There is no clear consensus, however, between the two on how the transformation, competition and concentration issues should be resolved (Harber and West, 2017; IRBA, 2017a). When asked whether the implementation of MAFR will lead to an improvement in the transformation of the auditing profession in South Africa, improve competition and decrease concentration amongst the Big Four firms, students seem to agree with the original position of the IRBA. The majority are of the opinion that MAFR could address these issues of transformation (81.2%, mean=4.07, standard deviation=0.81), competition (70.4%, mean=3.84, standard deviation=0.86) and concentration (53.7%, mean=3.63, standard deviation=0.97).

When asked if the implementation of MAFR will lead to an increase in the protection of investors (as a result of enhanced independence and quality), the majority (78.9%) of respondents agreed with a mean of 4.06 and standard deviation of 0.83. On whether MAFR will lead to a decrease of the possibility of auditors subconsciously advocating for the point of view of the audit client, 59.3% affirmed with a mean of 3.67 and a standard deviation of 0.84. This is in line with responses provided for research questions on the impact on independence and quality as described above.

Considering the current criticism labelled against the auditing profession (The Guardian, 2015; FRC, 2018; IRBA, 2018; Humphrey et al., 2011), when assessing the respondents' current views on the audit function and profession, particularly whether MAFR would have a positive effect on the financial stability of companies and the economy, the majority of respondents affirmed (74.7%, mean=3.58, standard deviation=0.91 and 55.7%, mean= 3.59, standard deviation=0.88 respectively). The results are supported by Gates, Jordan Lowe and Reckers (2006) who found that even where good controls and governance practices are in place, MAFR increases the confidence of investors in capital markets and IRBA who have the same view and intend protecting investors (IRBA, 2017b).

When asked whether MAFR would lead to increased audit costs due to the auditors needing to understand new clients, 50.6% of respondents affirmed with a mean of 3.38 and a standard deviation of 0.98. The lower mean is comparable to that of question 16 (3.20) on the impact of MAFR on audit fees, costs and quality (with only 41.4% affirming that quality would decrease as a result of competitive fees). Furthermore, 55.6% of respondents affirm that MAFR would cause inefficiencies, however with a (lower) mean (2.99) and a standard deviation of 1.07 which is consistent with the findings of (K. M. Said and Khasharmeh, 2014).

The majority of respondents (53.4%) affirm that MAFR will lead to competitive audit fees, with a mean of 3.45 and a standard deviation of 0.94. This is consistent with the finding of Grant, Harber and Minter (2018), who found evidence of audit fee discounting due to increased competition. MAFR leads to pressure on audit fees, but further to this, there is an unintended negative consequence of low-balling as a result of the competition and pressure (Harber 2016; Huang *et al.* 2015). Interestingly, the majority of respondents (36.2%) were neutral when asked if MAFR will lead to a decrease in audit fees due to the competitiveness brought about by the periodic rotations (only 34.7% affirming and 29.2% in disagreement). The mean for this question was 3.08 and the standard deviation 0.99.

Furthermore, when asked if MAFR, as a result of competitive audit fees, will cause the auditor to decrease audit costs by making an effort to be efficient in the performance of the audit, the majority of respondents (37.2%) were neutral on the question (33.8% affirming and 29% in disagreement), with a mean of 3.06 and a standard deviation of 0.95. This result confirms the complexity of the discussion on, and the relationship between between audit fees, costs and quality. It is in line with other research which has found that MAFR would not lead to a decrease in audit fees (Kwon, Lim and Simnett, 2014) and the mixed results of research on MAFR and its impact (Ewelt-Knauer *et al.* 2013; Junaidi *et al.* 2016).

The majority of respondents (74.6%) believe that MAFR will lead to a more rigorous and transparent process for the selection of auditors. The mean for this question was 3.93, confirming the view of respondents with a standard of 0.87. Current and past directors or managers have a significant influence on the appointment of auditors. These results are consistent with Dhaliwal *et al.* (2015) and Hussey (1999), who call

into question the selection and appointment of auditors by audit committees, concluding that relationships with management play a role (inappropriately so) in the process. Furthermore, 59.6% of respondents (mean of 3.60 and a standard deviation of 0.83) believe that MAFR will serve as a means of addressing concerns that a suitable balance between public and entity interests may not always be accomplished by those charged with governance (which include the audit committee). This supports the findings of Dhaliwal *et al.* (2015), that the responsibility given to audit committees for auditor appointments is unjustified as they are influenced by management.

According to the public interest theory, regulators regulate in the interest of the public (Hertog 2000; Hantke-domas 2003; Hertog 2010; Posner 1974). This is in line with the findings of this study. When asked whether MAFR would create a sense of promotion of the public interest, as the requirements apply all registered auditors equally in relation to public interest entities (PIEs), 76.4% of the respondents responded positively, with a mean of 3.97 and a standard deviation of 0.75. This is consistent with Lee (1989), who discusses the professionalisation strategy for accountants and the accountants' use of the public interest argument in order to advance and protect their financial self-interests.

The majority of respondents (79.8%) conceded that the engagement of a new audit firm will ensure that the attention of management (including senior) is continuously refocused, and thus ensure that financial reporting is improved. This was confirmed by the mean of 4.02 and a relatively low standard deviation of 0.74. The result is consistent with the theoretical reasoning that with new auditors, less likely to act in favour of the client, management need to continue reinventing and improving their reporting (Quick and Schmidt, 2018). This result is in line with the response provided for questions on independence and quality, where increased objectivity and rigour by auditors will have an effect on the work of management, including reporting.

Lastly, with a mean of 3.95 and a standard deviation of 0.82, the majority of respondents (73%) affirmed when asked if MAFR will create an incentive for small, medium and (even) bigger firms to invest (more) in growing their personnel and resources. This is consistent with the results for questions 19 and 20, where respondents affirmed that MAFR would address the issue of market concentration, particularly amongst the big four firms. Respondents, however, responded with a

mean of 2.88 (standard deviation of 1.12) when asked whether MAFR will discourage audit firms from investing in the development of expertise and specialisation, with 35% answering that there will be no change (neutral), 27% affirming, but 38% disagreeing. According to (Gul, Fung and Jaggi, 2009), it is difficult to predict at which point the auditor has learnt sufficiently about the client or industry but estimate it to be between four-eight years. This finding is contrary to the ones made by other outcomes Harber (2016); AICPA (2017); SAICA (2017); SAICA Indaba (2016); Center for Audit Quality (2012); Ottaway (2013); Asian (2012); EY (2016), that MAFR discourages investment in development and specialisation and can lead to problems with talent recruitment and management.

## 4.5 Inferential analysis

### 4.5.1 The impact of MAFR on independence

**Table 4.11 Pearson's correlation - association between variables relating to the impact of MAFR on independence**

Statements relating to the perceived impact of the implementation of MAFR on independence.	Q7	Q8	Q9	Q10	Q11
Q7.	1				
Q8.	.556**	1			
Q9.	.584**	.459**	1		
Q10.	.467**	.446**	.587**	1	
Q11.	.459**	.287**	.351**	.186	1

\*\* . Correlation is significant at the 0.01 level (2-tailed).

\* . Correlation is significant at the 0.05 level (2-tailed).

Four correlation coefficients were assessed using Pearson's correlation for responses on the impact on auditor independence and all relationships between variables were considered to be statistically significant ( $p < 0.05$ ), indicating a positive relationship between all responses on independence by students, and confirming the general view by respondents that the implementation of MAFR will improve auditor independence. The majority of the relationships reflected can be accepted as medium with two being weak and below 0.3.



#### 4.5.2 Further data analysis - Crosstables

The following analysis provides some insights into the responses provided by different respondents. Three questions (11 - independence, 17 - quality and 18 - transformation) have been identified and selected for further analysis of responses according to the different races, age groups, university and levels of study. Questions 11 and 17 have been selected as they are most appropriate for providing the perceptions of students on the impact of MAFR on independence and quality respectively. Question 18, which relates to transformation of the sector, was selected as the transformation matter had been highlighted by the IRBA and is considered to be important in the South African context.

**Table 4.12 – Analysis of race vs MAFR enhancing auditor independence**

	SD	D	N	A	SA	Total
African	7	2	20	91	194	314
Coloured	0	0	0	4	5	9
Indian	4	3	2	19	55	83
White	0	0	2	3	0	5
Other	0	0	0	0	1	1
Total	11	5	24	117	255	412

A consistently high percentage of the different races (African: 90.8%, Coloured: 100% and Indian: 89.2%, other: 100% and White (slightly lower): 60%) agreed that MAFR would enhance auditor independence.

**Table 4.13 – Analysis of race vs MAFR improving audit quality**

	SD	D	N	A	SA	Total
African	6	14	42	143	108	313
Coloured	0	1	0	6	2	9
Indian	2	6	15	39	21	83
White	0	0	3	2	0	5
Other	0	0	0	0	1	1
Total	8	21	60	190	132	411

A consistently high percentage of the different races, with the exception of white respondents at 40% (African: 80.2%, Coloured: 89.9%, Indian: 72.2% and other: 100%) agreed that MAFR would improve audit quality.

**Table 4.14 – Analysis of race vs MAFR leading to improved transformation**

	SD	D	N	A	SA	Total
African	2	5	44	150	111	312
Coloured	0	0	1	7	1	9
Indian	2	6	13	48	14	83
White	0	1	2	2	0	5
Other	0	0	0	0	1	1
Total	4	12	60	207	127	410

A consistently high percentage of the different races, with the exception of white respondents 40% (African: 83.7%, Coloured: 89.9%, Indian: 74.7% and other: 100%) agreed that MAFR would lead to transformation of the auditing profession.

**Table 4.15 – Analysis of age vs MAFR enhancing auditor independence**

	SD	D	N	A	SA	Total
18-21	10	4	15	73	174	276
22-25	1	1	8	37	68	115
26-30	0	0	1	4	8	13
Total	11	5	24	114	250	404

A consistently high percentage of the different age groups (18-21: 89.5%, 22-25: 91.3% and 26-30: 92.3%) agreed that MAFR would enhance auditor independence.

**Table 4.16 – Analysis of age vs MAFR improving audit quality**

	SD	D	N	A	SA	Total
18-21	7	17	42	122	87	275
22-25	1	4	15	53	42	115
26-30	0	0	3	10	0	13
Total	8	21	60	185	129	403

A consistently high percentage of the different age groups (18-21: 76%, 22-25: 82.6% and 26-30: 76.9%) agreed that MAFR would improve audit quality.

**Table 4.17 – Analysis of age vs MAFR leading to improved transformation**

	SD	D	N	A	SA	Total
18-21	3	10	38	145	79	275
22-25	1	2	19	53	39	114
26-30	0	0	2	7	4	13
Total	4	12	59	205	122	402

A consistently high percentage of the different age groups (18-21: 81.5%, 22-25: 80.7% and 26-30: 84.6%) agreed that MAFR would lead to transformation of the auditing profession.

**Table 4.18 – Analysis of university of study vs MAFR enhancing auditor independence**

	SD	D	N	A	SA	Total
UNIZULU	5	0	8	49	88	150
UKZN	6	5	16	68	168	263
Total	11	5	24	117	256	413

A consistently high percentage of respondents at both universities (UNIZULU: 91.3% and UKZN: 89.7%) agreed that MAFR would enhance auditor independence.

**Table 4.19 – Analysis of university of study vs MAFR improving audit quality**

	SD	D	N	A	SA	Total
UNIZULU	4	10	16	70	50	150
UKZN	4	11	45	120	82	262
Total	8	21	61	190	132	412

A consistently high percentage of respondents at both universities (UNIZULU: 80% and UKZN: 77.1%) agreed that MAFR would improve audit quality.

**Table 4.20 – Analysis of university of study vs MAFR leading to improved transformation**

	SD	D	N	A	SA	Total
UNIZULU	0	3	22	68	56	149
UKZN	4	9	38	140	71	262
Total	4	12	60	208	127	411

A consistently high percentage of respondents at both universities (UNIZULU: 83.2% and UKZN: 80.5%) agreed that MAFR would lead to transformation of the auditing profession.

**Table 4.21 – Analysis of level of study vs MAFR enhancing auditor independence**

	SD	D	N	A	SA	Total
2	3	1	7	41	85	137
3	5	4	14	60	131	214
4	3	0	3	16	40	62
Total	11	5	24	117	256	413

A consistently high percentage of respondents at the different levels of study (2: 91.9%, 3: 89.3% and 4: 90.3%) agreed that MAFR would enhance auditor independence.

**Table 4.22 – Analysis of level of study vs MAFR improving audit quality**

	SD	D	N	A	SA	Total
2	2	6	16	66	47	137
3	4	13	38	94	64	213
4	2	2	7	30	21	62
Total	8	21	61	190	132	412

A consistently high percentage of respondents at the different levels of study (2: 82.5%, 3: 74.2% and 4: 82.3%) agreed that MAFR would improve audit quality.

**Table 4.23 – Analysis of level of study vs MAFR leading to improved transformation**

	SD	D	N	A	SA	Total
2	3	5	12	82	35	137
3	0	4	44	104	61	213
4	1	3	4	22	31	61
Total	4	12	60	208	127	411

A consistently high percentage of respondents at the different levels of study (2: 85.4%, 3: 77.5% and 4: 86.9%) agreed that MAFR would lead to transformation of the auditing profession.

## 4.6 Additional student comments

Question 36 of the questionnaire was an open one, which was aimed at allowing respondents to mention any potential impact of MAFR or comment not addressed by the questionnaire, without changing the design of the study. Comments by respondents for this question primarily emphasised their views on MAFR with some noting their reservations on its implementation. The majority of the comments were covered by the questionnaire. It is interesting to note that the comments (as summarised below), are in line with the ongoing debate and mixed research outcomes on MAFR (Ewelt-Knauer et al. 2013; Junaidi et al. 2016), as while they show support for MAFR, a notable amount of issues are raised as potential concerns, in line with current literature. From this open question, the researcher identified the following themes and comments:

MAFR will have a positive outcome as (it will):

- Safeguard against the (or decrease) familiarity threat to independence.
- Lead to improved professional scepticism, auditor independence, and audit quality.
- Improve the credibility of financial statements and investor confidence.
- Lead to more competition in the profession and create opportunities especially for new and small firms, thus enabling their growth.
- MAFR has both positive and negative outcomes (partner rotation is sufficient).
- Help combat corporate fraud.
- Lead to transformation of the audit profession.
- Will protect investors, reduce scandals in the profession and restore public faith in it.
- Improve the competence of auditors
- Increase the focus of firms and auditors on ethical behaviour and compliance with principles in the code of conduct.

MAFR will have a negative effect as it will:

- Lead to lowballing.
- Increase pressure on audit fees, leading to their decrease and a resultant decrease in audit quality.

- Result in a lack of objectivity (with new auditors trying to impress their client).
- Cause an increase in audit time (hours) as new auditors familiarise themselves with the client and its environment, resulting in increased audit costs.
- Result in audit firms losing their clients (in an unfair manner – regardless of the service provided), leading to decreases in revenues, profitability and sustainability.
- Lead to a threat to auditor confidentiality as a result of industry specialisation.
- Result in audit clients rotating only amongst the big four firms with no positive effect on small firms.
- Not result in any significant impact on independence as intended, but will lead to increased audit risk and audit fees.
- Lead to new auditors being unable to identify issues and misstatements.
- Discourage new Registered Auditors (RAs) from joining the audit profession.

Respondents also suggested that better guidance be provided to auditors in setting audit fees, to ensure consistency and eliminate the issues fees may cause. Some respondents also commented that ten years (per the MAFR rule) is still too long, suggesting that it should be reduced. One student commented, in favour of MAFR, using the “boiling frog” metaphor, suggesting that gradual change is needed. Summarily, respondents perceive MAFR as a positive initiative, however, they still have some reservations on the potential negative (unintended) effects it may have. There were also comments that MAFR does not address the major issues faced by the audit profession or function.

## **4.7 Summary of data analysis**

This chapter presented data with an analysis and discussion of the findings of the study. The chapter described the method and approach for presentation and a description of the validity and reliability tests performed. The chapter then presented the results of the study in line with the research questions (i.e. auditor independence, audit quality and other considerations). A descriptive statistical analysis was presented as well as an analysis of the Pearson’s correlation in relation to the impact on auditor independence.

The next chapter presents a summary of the study and makes conclusions on the perceptions of students regarding MAFR, discusses recommendations, suggestions for further research, limitations and delimitations for the study.

## **CHAPTER 5: SUMMARY, CONCLUSION AND RECOMMENDATIONS**

### **5.1 Introduction**

The findings of the study were presented and discussed in chapter 4. Chapter 5 presents a summary of the study and makes conclusions on the perceptions of students regarding MAFR, based on data collected and discussed in chapter 4. The chapter also discusses recommendations, suggestions for further research, limitations and delimitations for the study.

### **5.2 Summary of the Study**

As indicated in chapters 1 and 2, there is currently no consensus by different stakeholders and jurisdictions on whether or not the implementation of MAFR yields positive or negative outcomes. Current auditing students, most of whom will be amongst audit teams implementing MAFR in South Africa as future auditors, are a stakeholder in the profession. Based on this, this study identified the objectives as being to determine whether according to university students:

- The introduction and implementation of MAFR will enable the IRBA to meet the objective of improving auditor independence and whether the quality of audits would be increased.
- Any other benefits will be reaped from the introduction of MAFR, particularly those considered by the IRBA, other regulators and scholars.
- Potential negative unintentional consequences could result from the looming implementation of MAFR.

Chapter 2 discussed literature on MAFR and related issues (including independence, audit quality, audit costs and fees amongst others), highlighting the discourse that exists regarding the impact of MAFR. The chapter first placed the study in an appropriate theoretical framework, discussing the applicability of the role conflict theory, audit expectation gap, economic theories of regulation and the living law of audit.



The chapter then discussed literature on the impact of MAFR on independence, audit quality and other areas of the audit function and profession, confirming the complexity of the debate that surrounds the topic of MAFR. Lastly, the chapter noted that the MAFR rule will be implemented in South Africa from 2013 and the perceptions of future auditors (current auditing student) stakeholder would be researched in this study.

Chapter 3 described the methodology. The chapter outlined the research approach/paradigm for the project, the approach followed being quantitative, and reasons for selecting this approach. The chapter then described the population for the study, which comprises of auditing students at the two traditional residential universities in the province of KwaZulu-Natal, as well as the sampling of the population (convenience-students who were in class on the day scheduled for data collection). Thereafter the procedures followed and the instrument (questionnaire) used in the collection of data from participants were explained. The chapter also discussed the ethical considerations, elaborated on the coding of data collected from participants and the statistical analysis performed on the data. Finally, it discussed how reliability and validity would be ensured in the study.

Chapter 4 presented an analysis and discussion of the data. The chapter also described the method and approach followed for the presentation, description of the validity and reliability tests performed. The results of the study were presented in line with the research questions (i.e. auditor independence, audit quality and other considerations). A descriptive statistical analysis was presented as well as an analysis of the Pearson's correlation in relation to the impact on auditor independence.

## **5.3 Findings and conclusions**

The findings and conclusions on the perceptions of current auditing students on MAFR will be presented in line with research questions and objectives.

### **5.3.1 Impact on independence**

Based on responses to questions 7 to 11, students perceive MAFR as having a positive impact on auditor independence. Students either agreed or strongly agreed with between 78.5% and 93.3% (and an average mean for all questions of 4.29) with statements, suggesting that the introduction of MAFR would improve independence.

A total of 68.8% of students strongly agreed that a tenure of above 10 years leads to a familiarity threat to independence while 62% strongly agreed that MAFR would improve independence. Furthermore, positive moderate to strong relationships were found in the responses provided by students to all the questions relating to independence, confirming the general view by respondents that the implementation of MAFR will improve auditor independence. Students provided further comments demons

### 5.3.2 Impact on quality

Students also perceive the impact of MAFR on quality to be positive, with reservations as a result of the absence of client specific knowledge and pressure on audit fees and costs. The extent, however, to which students believe the impact will be positive is less when compared to the impact on independence, as evidenced by the lower mean determined for the questions and the standard deviation that is higher. There are also a notable amount of students that indicated that there would be no impact on quality. When asked if MAFR would lead to lower quality (due to pressure on audit fees), 41.4% of students agreed while 33.7% indicated no change. Students (50.8) also agreed that new auditors may not detect misstatements. However, when asked if audit quality would increase due to fresh eyes looking at client records, students responded positively (78.1%) with a mean of 4.01. This outcome is in line with the current debate on the impact of MAFR on audit quality as outlined in chapter 2.

### 5.3.3 Impact on “other”

The majority of students perceived MAFR as having a positive effect on the bulk of the matters included in this part of the questionnaire. The results were as follows:

**Tables 4.24 – Summary of findings on impact on other matters – positive impact**

The majority believe MAFR will have a <b>positive impact</b> on:	
Transformation	81.2%
Competition in the profession	70.1%
Market concentration	53.1%
Protection of investors	78.9%
Auditors advocating (decrease) for client positions	59.3%
Financial stability of clients or companies	56.4%
Financial stability of the SA economy	55.7%

Competitive audit fees	53.4%
Rigour and transparency to audit firm appointment	74.6%
A sense of advancing public interest	76.4%
Addressing concerns of those charged with governance balance of company and public interests	59.6%
Continuously refocusing the efforts of those charged with governance	79.8%
Incentive for small firms to invest in staff and resources	73%

**Tables 4.25 – Summary of findings on impact on other matters – negative or no impact**

The majority believe MAFR will have a <b>negative effect</b> on:	The majority believe MAFR will have <b>no impact (neutral)</b> on:
Audit costs (understanding new client) (50.6%)	Audit fees (36.2%)
Efficiencies of client personnel and management (35.5%)	Audit costs as a result of efficiencies (37.2%)
	Investment in the development of expertise and specialisation (35%)

### 5.3.4 Additional analysis and comments

Student responses were found to be consistent across racial lines, age groups, the two universities and levels of study. However, on analysis of comments provided by students on their questionnaires (through one open question), students provided positive comments as well as notable potential negative consequences of MAFR.

### 5.3.5 Conclusion

Current university auditing students perceive the introduction and implementation of MAFR as having a positive impact on the independence, quality and other matters (refer to *Table 4.24* above) relating to audits. This conclusion is consistent with (Gates *et al.* 2006) who concluded that business and law university students consider MAFR to be able to improve confidence in the reported information, as well as perceive MAFR as having a positive impact on audited financial statements and audit quality.

## 5.4 Recommendations

On the basis of the results of this investigation the following is recommended:

- Further research should be conducted on the impact of and perceptions on MAFR (refer below).

- The IRBA should proceed with the implementation of MAFR especially in an effort to improve independence, however, due and appropriate care should be exercised.
- A more comprehensive solution should be considered and implemented to increase the quality of audit work.
- Stakeholders of the accounting and auditing profession should begin to embrace the change that needs to occur in the profession.

## **5.5 Suggestions for Further Study**

On the basis of the findings of this study, these areas have been identified for further research:

- Perceptions of university auditing students at other institutions on the impact of MAFR.
- A more focused study of the perception of students on the effect of MAFR on audit quality.
- Suggestions and/or comments of students on the reform of the auditing profession and function.
- Perceptions of audit trainees currently completing their training contracts.

## **5.6 Limitations of the study**

- The study was undertaken at two universities (Zululand and University of KwaZulu-Natal), focusing on students studying in the accounting stream (with the potential of qualification as a chartered accountant (CA) and registered auditor (RA).
- This study utilised non-probability sampling, selecting students on a convenient basis who were in attendance at the lecture pre-selected for data collection.
- University students (particularly at these residential institutions) base their perceptions on theoretical knowledge and views from outside as they do not have practical auditing experience.

## **5.7 Delimitations**

- The population for the study has been restricted to auditing students at the universities of Zululand and KwaZulu-Natal (second year students from UNIZULU were excluded from the study).
- The study aimed to obtain a general perception of students on MAFR and thus asked non-specific, and broad questions (in comparison to questions that are specific and focused on one area (e.g. independence or quality)).
- Due to the aim being of obtaining a general perception on MAFR and the fact that participants may not have had sufficient insights into the practical world of auditing, a quantitative approach was selected for this study.

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## **APPENDIX A: RESEARCH INSTRUMENT** **(QUESTIONNAIRE)**

### INFORMED CONSENT DOCUMENT

Date: 11 September 2018

Dear Participant

I, Msizi Gwala, am a student who is currently registered for the Master of Accountancy degree in the School of Accounting, Economics and Finance, Westville campus, University of KwaZulu- Natal. The topic of my study is: **Mandatory Audit Firm Rotation (MAFR): A student perspective.**

I can be reached on 035 902 6519 or [gwalam@unizulu.ac.za](mailto:gwalam@unizulu.ac.za) for any queries related to the study. My academic supervisor is Bomi Nomlala, based in the School of Accounting, Economics and Finance, Westville campus, University of KwaZulu- Natal. He can be contacted on [nomlalabc@ukzn.ac.za](mailto:nomlalabc@ukzn.ac.za) or 031 260 8603 during office hours. The HSSREC Research Office can be contacted by reaching Ms Mariette Snyman on [Snymanm@ukzn.ac.za](mailto:Snymanm@ukzn.ac.za) or alternatively on 031 260 8350.

The aim and purpose of this research is to determine the perception of university auditing students in the KwaZulu-Natal Province of South Africa regarding the looming implementation of the Mandatory Audit Firm Rotation (MAFR) rule in South Africa by the Independent Regulatory Board for Auditors (IRBA) on 1 April 2023. The study seeks to bring to the fore the perspective of the potential auditors of the future, who are an important stakeholder in the profession to the fore.

The study is expected to survey senior students (level 2, 3 or 4) currently registered for an accounting qualification at the University of KwaZulu-Natal and the University of Zululand and will involve the collection of data from these students. A copy of the thesis will be available at the university's main library for accessibility to respondents based on their anonymity during the study.

Please note that your name will not be included in the report. The questionnaire does not require any personal information. The information will be seen only by me, my supervisor and the examiner and your anonymity and confidentiality is of utmost importance and will be maintained throughout the study.

Your participation in this study is voluntary. You have the right to withdraw at any time.

I appreciate the time and effort it would take to participate in this study. I would be very grateful for your participation as it would enable me to complete my thesis.

This study has been ethically reviewed and approved by the UKZN Humanities and Social Sciences Research Ethics Committee (approval number HSS/1019/018M)

**Please complete the section below:**

I ..... (*full names of participant*) hereby confirm that I understand the contents of this document and the nature of the research project, and I consent to participating in the research project. I understand that I am at liberty to withdraw from the project at any time, should I so desire.

Signature of participant.....

Date .....

## SECTION A: GENERAL INFORMATION

Please complete your age and tick the appropriate option for the remainder of the questions in this section:

**NOTE: You are free to withdraw from this research at any time without any negative or undesirable consequences to you**

1. Age:

2. Race

a	b	c	d	e
African	Coloured	Indian	White	Other

3. Gender

a	b	c
Male	Female	Other

4. University of study

a	b
UNIZULU	UKZN

5. Qualification registered

a	b	c	d
<b>UNIZULU – BCom(AccScie)</b>	<b>UNIZULU - BCom(Acc)</b>	<b>UKZN - BCom(Acc)</b>	<b>UKZN – PGDA/CTA</b>

6. Level of study

a	b	c
3	4	2

## SECTION B: MAFR QUESTIONNAIRE

**Instruction:** You are required to respond to the statements below by ticking ("X") on the most appropriate column in your view relating to MAFR and related matters. The following rating scale is used to respond to the questions:

SD	Strongly disagree	1
D	Disagree	2
N	Neutral (no change)	3
A	Agree	4
SA	Strongly agree	5

**Consider this statement in responding to the questions that follow:**

The introduction and implementation of the Mandatory Audit Firm Rotation (MAFR) rule in April 2023 for registered auditors (RAs) in South Africa will enable the IRBA to meet the primary objective of **enhancing auditor independence**.

#	Statements relating to the perceived impact of the implementation of MAFR on independence.	SD	D	N	A	SA
		1	2	3	4	5
7.	A long audit tenure (term), where an audit firm audits a client longer than ten years without rotating leads to the <b>familiarity threat</b> to the <b>independence</b> of the auditor.					
8.	A long audit tenure (term), where an audit firm audits a client longer than ten years without rotating leads to the compromise of the <b>professional scepticism</b> of the auditor.					
9.	A long audit tenure (term), where an audit firm audits a client longer than ten years without rotating leads to the compromise of the <b>objectivity</b> of the auditor.					
10.	A long audit tenure (term), where an audit firm audits a client longer than ten years without rotating will cause the auditor to be <b>sympathetic to the position of the audit client</b> .					

#		SD	D	N	A	SA
11.	The implementation of MAFR will lead to the <b>enhancement of the independence of auditors</b> when conducting an audit.					

**Consider this statement in responding to the questions that follow:**

The introduction and implementation of the Mandatory Audit Firm Rotation (MAFR) rule in April 2023 for registered auditors (RAs) in South Africa will lead to the achievement of the objective of **improving audit quality**?

#	Statements relating to the perceived impact of the implementation of MAFR on audit quality.	SD	D	N	A	SA
		1	2	3	4	5
12.	A <b>long audit tenure (term)</b> , where an audit firm audits a client for a period longer than ten years without rotating will lead to a decrease in the <b>quality of the audit work</b> performed.					
13.	There is a likelihood that a <b>new audit firm</b> (with less client specific knowledge) would <b>not detect material misstatements</b> in the financial statements during the initial year(s) of the audit tenure.					
14.	The risk of an <b>audit failure increases as the audit tenure period increases</b> due to the level of comfort between the auditors and client management together with the desire to maintain the relationship.					
15.	The risk of an <b>audit failure is higher in the initial stages of the audit tenure period</b> due to a lack of specific client knowledge and experience by the new auditors.					
16.	The implementation of MAFR, leading to the competitiveness in audit fees, will cause the auditor to aspire to <b>decrease audit costs by being efficient in the conduct of the audit</b>					

	which will result in a decrease in the quality of audit work.					
#		SD	D	N	A	SA
17.	The implementation of MAFR will lead to an <b>improvement in the quality</b> of the work performed by <b>auditors</b> when conducting audit due to <b>fresh eyes</b> looking at client records.					

**Consider this statement in responding to the questions that follow:**

The following statements represent **other potential outcomes or effects** of the implementation of Mandatory Audit Firm Rotation (MAFR) in South Africa.

Indicate your perception as follows:

- **If in agreement** with the statement, tick 4 or 5 as appropriate.
- If you have a view that there will be **no change or effect**, tick 3 to indicate neutrality.
- Where you **disagree** and consider the **impact to be rather negative** on the matter indicated by the statement, indicate this by ticking 1 or 2 as appropriate.

#	Statements relating to the perceived impact of the implementation of MAFR on other factors.	SD	D	N	A	SA
		1	2	3	4	5
18.	The implementation of MAFR will lead to an improvement in the <b>transformation</b> of the auditing profession in South Africa.					
19.	The implementation of MAFR will lead to an improvement in <b>competition</b> in the South African audit market					
20.	The implementation of MAFR will lead to a decrease in the <b>market concentration</b> , particularly concentration in the Big Four Firms.					
21.	The implementation of MAFR will lead to an increase in <b>the protection of investors</b> as a					

	result of enhanced auditor independence and audit quality.					
#		SD	D	N	A	SA
22.	The implementation of MAFR will lead a decrease of the possibility of auditors <b>subconsciously advocating for the point of view of the audit client.</b>					
23.	The implementation of MAFR will lead to an <b>improvement in the financial stability of companies</b> under audit.					
24.	The implementation of MAFR will lead to an <b>improvement in the financial stability of the economy</b> of South Africa.					
25.	The implementation of MAFR will lead to an <b>increase in audit costs due to the auditors need to understand new clients.</b>					
26.	The implementation of MAFR will cause <b>inefficiencies for client personnel and management</b> who will have to <b>explain how the company operates</b> to new auditors after the rotation period.					
27.	The implementation of MAFR will lead to <b>competitive audit fees</b> being offered to audit clients.					
28.	The implementation of MAFR will lead to a <b>decrease in audit fees</b> due to the competitiveness brought about by the periodic rotations.					
29.	The implementation of MAFR, leading to the competitiveness in audit fees, will cause the auditor to <b>decrease audit costs by making an effort to be efficient in the conduct of the audit.</b>					
30.	The implementation of MAFR will lead to a more <b>rigorous and transparent process for the appointment of auditors.</b>					



#		SD	D	N	A	SA
31.	A sense of <b>advancement of the public interest will be created</b> , because the requirements apply all registered auditors equally in relation to public interest entities (PIEs).					
32.	MAFR will serve as a means of addressing concerns that <b>those charged with governance may not always achieve an appropriate balance between the interests of the company and the public interest.</b>					
33.	The involvement of a new audit firm will ensure that the attention of <b>management and those charged with governance is continuously refocused.</b>					
34.	MAFR will create an incentive for smaller or mid-tier audit firms and even other established firms to invest (or invest more) in <b>expanding their staff and resources.</b>					
35.	MAFR <b>will discourage audit firms from investing in the development of expertise and specialisation</b> (e.g. Insurance industry specialisation) for the firm due to the required periodic rotation.					

***Provide a response to the following question as additional information only where necessary or applicable.***

**36.** The following statement(s) represent other outcomes (negative or positive) that can be expected from the implementation of the MAFR rule in South Africa. *(Use additional paper if necessary).*

No.	Statement representing potential impact or outcome

## **APPENDIX B: ETHICAL CLEARANCE CERTIFICATE**



23 August 2018

**Mr Msizi Cedric Gwala (218083995)**  
School of Accounting, Economics & Finance  
Westville Campus

Dear Mr Gwala,

**Protocol Reference Number : HSS/1019/018M**

**Project title:** Mandatory Audit Firm Rotation (MAFR) : A student perspective

### **Provisional Approval – Expedited Application**

This letter serves to notify you that your application received on 19 July 2018 in connection with the above, has been provisionally approved, subject to the following:

- Gatekeeper permission letter(s)

**This approval is granted provisionally and the final clearance for this project will be given once the above mentioned condition has been met. Note that data collection may not proceed until final ethics approval letter has been issued after the remaining conditions have been met and approved by the research ethics committee.**

Kindly submit your response to Professor Shenuka Singh: Research Office as soon as possible.

Yours faithfully

.....  
**Professor Shenuka Singh (Chair)**

/ms

Cc Supervisor: Bomi Nomlala  
cc Academic Leader Research: Professor Josue Mbonigaba  
cc School Administrators: Ms Seshni Naidoo

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**Humanities & Social Sciences Research Ethics Committee**

**Professor Shenuka Singh (Chair)**

**Westville Campus, Govan Mbeki Building**

**Postal Address:** Private Bag X54001, Durban 4000

**Telephone:** +27 (0) 31 260 3587/8350/4557 **Facsimile:** +27 (0) 31 260 4609 **Email:** [ximbap@ukzn.ac.za](mailto:ximbap@ukzn.ac.za) / [snymanm@ukzn.ac.za](mailto:snymanm@ukzn.ac.za) / [mohunp@ukzn.ac.za](mailto:mohunp@ukzn.ac.za)

**Website:** [www.ukzn.ac.za](http://www.ukzn.ac.za)



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## **APPENDIX C: GATEKEEPER LETTER – UKZN**



10 August 2018

Mr Msizi Cedric Gwala (SN 218083995)  
School of Accounting, Economics & Finance  
College of Law and Management Studies  
Westville Campus  
UKZN  
Email: [msizi.gwala@vodamail.co.za](mailto:msizi.gwala@vodamail.co.za) [Nomlalabc@ukzn.ac.za](mailto:Nomlalabc@ukzn.ac.za)

Dear Mr Gwala

### **RE: PERMISSION TO CONDUCT RESEARCH**

Gatekeeper's permission is hereby granted for you to conduct research at the University of KwaZulu-Natal (UKZN) towards your postgraduate studies, provided Ethical clearance has been obtained. We note the title of your research project is:

*"Mandatory Audit Firm Rotation (MAFR): A student perspective."*


It is noted that you will be constituting your sample by handing out questionnaires to third and fourth year Auditing students in the School of Accounting, Economics & Finance on the Westville Campus.

Please ensure that the following appears on your notice/questionnaire:

- Ethical clearance number;
- Research title and details of the research, the researcher and the supervisor;
- Consent form is attached to the notice/questionnaire and to be signed by user before he/she fills in questionnaire;
- gatekeepers approval by the Registrar.

You are not authorized to contact staff and students using 'Microsoft Outlook' address book. Identity numbers and email addresses of individuals are not a matter of public record and are protected according to Section 14 of the South African Constitution, as well as the Protection of Public Information Act. For the release of such information over to yourself for research purposes, the University of KwaZulu-Natal will need express consent from the relevant data subjects. Data collected must be treated with due confidentiality and anonymity.

Yours sincerely

  
**MR SS MOKOENA**  
**REGISTRAR**

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#### **Office of the Registrar**






Postal Address: Private Bag X54001, Durban, South Africa

Telephone: +27 (0) 31 260 8005/2206 Facsimile: +27 (0) 31 260 7824/2204 Email: [registrar@ukzn.ac.za](mailto:registrar@ukzn.ac.za)

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## **APPENDIX D: GATEKEEPER LETTER – UNIZULU**



**UNIVERSITY OF  
ZULULAND**

University of Zululand, Private Bag X1001, KwaDlangezwa, 3886

**W:** [www.unizulu.ac.za](http://www.unizulu.ac.za)

**T:** +27 35 902 6731 **E:** [DlaminiA@unizulu.ac.za](mailto:DlaminiA@unizulu.ac.za)

***Deputy Vice-Chancellor: Research and Innovation Office***

Msizi Gwala CA(SA)  
Department of Accounting and Auditing  
079 742 3202  
Per email: [gwalam@unizulu.ac.za](mailto:gwalam@unizulu.ac.za)

04 September 2018

Dear Mr. MC Gwala

**REQUEST FOR PERMISSION TO CONDUCT RESEARCH AT UNIZULU: "MANDATORY AUDIT  
FIRM ROTATION (MAFR): A STUDENT PERSPECTIVE"**

Your letter to me, refers.

I hereby grant approval for you to conduct part of your research at UNIZULU, as per the methodologies stated in your research proposal and in terms of the data collection instruments that you have submitted. I note also that the University of KwaZulu Natal, has issued provisional ethical clearance and having read the documentation, I am happy to accept that. Once the full ethical clearance is issued please submit that.

You may use this letter as authorization when you approach the appropriate persons. Please note that permission is based on the documentation that you have submitted. Should you revise your research instruments, or use additional instruments, you must submit those to us as well.

I wish you well in your research.

Yours sincerely,

  
Professor Gideon De Wet  
Chairperson: University of Zululand Research Ethics Committee  
Deputy Vice-Chancellor: Research and Innovation

# APPENDIX E: TURNITIN REPORT

2/8/2019

Turnitin

Turnitin Originality Report							
Processed on: 08-Feb-2019 12:15 PM CAT ID: 1067844687 Word Count: 33162 Submitted: 9							
MAFR Study By Msizi Gwala							
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< 1% match (Internet from 10-Dec-2016) <a href="http://www.saica.co.za/Portals/0/documents/MAFRDiscussionPaper.pdf?Reference_ID=449">http://www.saica.co.za/Portals/0/documents/MAFRDiscussionPaper.pdf?Reference_ID=449</a>							
< 1% match (Internet from 06-Sep-2017) <a href="http://theses.ubn.ru.nl/bitstream/handle/123456789/1717/16.008%20Sander%20Ricken%20mathesis.pdf?sequence=1">http://theses.ubn.ru.nl/bitstream/handle/123456789/1717/16.008%20Sander%20Ricken%20mathesis.pdf?sequence=1</a>							
< 1% match (student papers from 07-Apr-2016) <a href="#">Submitted to University of Mauritius on 2016-04-07</a>							
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