University of Antwerp

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The Auditor Selection Process: Institutional and Interpersonal Dynamics

PhD thesis submitted for the degree of Doctor of Applied Economics at the University of Antwerp to be defended by Jonas Vandennieuwenhuysen

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Prof. dr. Marie-Laure Vandenhaute

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English Abstract

Every audit engagement once started with an audit client selecting an auditor. Despite the auditor selection process being a crucial mechanism for ensuring auditor independence and enhancing audit quality, an understanding of *how* companies select an auditor was lacking before this dissertation. This dissertation investigates the auditor selection process employing a multi-methodological approach. The study synthesizes existing literature, analyzes archival data to explore audit partner-client alignment, and conducts qualitative research on eight large Dutch companies' auditor selection processes. This study reveals the importance of audit partner-client alignment when studying audit quality, auditor tenure, and auditor changes. Moreover, the findings indicate that despite regulatory efforts to standardize the selection process and enhance transparency, audit clients continue to prioritize relational factors over formal criteria. Additionally, the intended reduction of managerial influence on the selection process appears to be unsuccessful, as management remains significantly involved in every step of the process. Finally, this study highlights the importance of trust, cooperation, and commitment in auditor-client relationships, demonstrating how audit clients demand these qualities and how auditors strive to meet these expectations throughout the selection process. It suggests that mandatory audit firm rotation may introduce relational costs and reduce client-specific knowledge. These insights underscore the need for a balanced approach to regulation that considers both independence and relational dynamics. The dissertation offers insights for regulators, audit clients, and auditors and identifies avenues for future research on auditor selection behaviors and their implications.

NEDERLANDS ABSTRACT (DUTCH ABSTRACT)

Het Auditor Selectieproces: Institutionele en Interpersoonlijke Interacties

Elke auditopdracht begon ooit met een onderneming die een auditor selecteert. Hoewel het selectieproces van auditors een cruciaal mechanisme is voor het waarborgen van de onafhankelijkheid van auditors en het verbeteren van de kwaliteit van audits, ontbrak voor dit proefschrift een goed begrip van hoe ondernemingen een auditor selecteren. Dit proefschrift onderzoekt het auditor selectieproces door middel van een multi-methodologische aanpak. Het onderzoek synthetiseert bestaande literatuur, analyseert het aligneren van auditors en ondernemingen en voert kwalitatief onderzoek uit naar de selectieprocessen van auditors van acht grote Nederlandse ondernemingen. Deze studie toont het belang van het aligneren aan tussen de expertise van de auditor en de eigenschappen van de onderneming bij het bestuderen van auditkwaliteit, de lengte van de overeenkomst en de kansen op verandering van auditor. Bovendien geven de bevindingen aan dat ondanks pogingen van regelgevers om het selectieproces te standaardiseren en de transparantie te vergroten, ondernemingen nog steeds voorrang geven aan relationele factoren boven formele criteria. Daarnaast blijkt de beoogde vermindering van de invloed van managers op het selectieproces onsuccesvol, gezien het management aanzienlijk betrokken blijft bij elke stap van het selectieproces. Tot slot benadrukt dit onderzoek het belang van vertrouwen, betrokkenheid en coöperatie in de relatie tussen auditor en onderneming, waarbij aangetoond wordt hoe ondernemingen deze behoeften uitdrukken en hoe auditors proberen aan deze verwachtingen te voldoen gedurende het selectieproces. Deze bevindingen suggereren dat verplichte rotatie van auditkantoren relationele kosten met zich mee kan brengen en onderneming-specifieke kennis kan verminderen.

SUMMARY

The role of financial auditors is to gather and evaluate evidence about financial information to assess and report on its alignment with applicable financial reporting frameworks. This process results in an audit report communicating the auditors' opinion on whether the financial statements present a true and fair view to shareholders and stakeholders. For an audit to be valuable, it must be conducted by a competent and independent auditor. Yet, auditors are engaged by the company and its management, which creates an inherent conflict of interest. Regulators have implemented various measures to enhance auditor independence that directly impact the auditor selection process, such as ensuring a more independent auditor selection by the audit committee and introducing mandatory audit firm rotation.

Every audit engagement begins with an audit client selecting an auditor. Despite the importance of the auditor selection process as a crucial mechanism for ensuring auditor independence and enhancing audit quality, an understanding of how companies select an auditor was lacking before this dissertation due to limited public disclosure about how companies select and appoint their auditors.

Chapter 1 presents a systematic literature review that reveals a fragmented landscape, with archival studies focusing on observable characteristics and field studies emphasizing intangible criteria and dynamics. In this study, I develop a conceptual framework to organize the literature on the auditor selection process and summarize a variety of avenues for future research, which guide the three subsequent chapters.

Chapter 2 investigates the audit partner-client matching process, for which a new measure is developed that matches an audit partner's prior audit experiences to certain client characteristics. Using this measure, this chapter presents some evidence that alignment between audit partners and clients is associated with higher audit quality. This alignment benefits the auditor-client relationship, leading to longer tenure and a lower likelihood of auditor changes. The study indicates that within-firm partner rotations result in lower alignment, whereas audit firm-induced rotations do not affect audit partner-client alignment.

Finally, Chapters *3* and 4 go into the field and study how auditor selection processes at large companies are actually conducted. *Chapter 3* examines the auditor selection process from an institutional perspective. The study reports evidence of isomorphic tendencies in the auditor selection process, driven by regulatory uncertainty and external pressures from regulatory bodies, investors, and the media. These pressures lead clients to set up a legitimate process in the front end, relying on best practice guidelines issued by audit firms and other accounting

regulations. However, the most interesting dynamics occur in the “backstage” of the auditor selection process. Audit clients often decouple their decision-making criteria from standardized processes, focusing on interpersonal fit and the auditor’s ability to enhance a productive working relationship. Management’s daily involvement with auditors often makes them significant influencers in the selection process, with the audit committee’s role being limited. Scorecards are used more to formalize the process than as binding decision-making tools. *Chapter 4* investigates the process from an interpersonal level and finds that the perceived quality differences among tender participants are negligible, and the level of audit effort needed is unknown. Consequently, clients rely on credibility signals, such as a strong auditor-client relationship, which can enhance audit quality through better communication and more efficient working environments. Auditors and audit clients engage in social exchanges to build trust and commitment, which is crucial for winning bids and ensuring high-quality audits.

Overall, this dissertation provides a comprehensive overview of the auditor selection process, examines regulatory implications, and suggests avenues for future research on auditor selection and the impact on audit quality and independence.

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SOME INTRODUCTORY NOTES

This dissertation, even though there are many different kinds of audits, discusses the subject of financial auditing by the external auditor. Therefore, when mentioning the audit and the auditor, this is about the financial audit and the external auditor. Furthermore, in this dissertation, the term “firm” is used to refer to the audit firm, and the terms “client” and “company” are used when discussing the audit firm’s clients. The term “Big 4” audit firm refers to Deloitte, EY, KPMG, and PwC.

In the academic literature, the distinction between audit firms and audit partners is relatively clear. However, in practice, these are strongly linked together and often relatively indistinguishable. Therefore, in *Chapters 3* and *4*, I use the term “(external) auditor” for both “audit firm” and “audit partner” if either term is not specifically mentioned. I specify the most detailed level, i.e., “audit firm” or “audit partner,” when possible.

A final note is that the general sections of this PhD are written in first-person singular, as this is, of course, my own dissertation. In the individual chapters, the results are presented in first-person plural, as all of these individual chapters are a team effort.

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GENERAL INTRODUCTION

Financial auditors accumulate and evaluate evidence about financial information to determine and report on the degree of correspondence between this information and the applicable financial reporting framework (e.g., IFRS, US GAAP). The end product of this process is the audit report, which communicates the auditors' opinion about whether these financial statements give a true and fair view to financial statement users (Arens, Elder, Beasley, and Hogan 2020). To be valuable, the audit should be done by a competent, independent auditor, as stated in plenty of audit textbooks (e.g., Arens et al. 2020), regulatory documents (e.g., the European Commission (EC) 2010), and academic research. Auditor independence is seen as the cornerstone of auditing (e.g., Antle 1984; DeAngelo 1981a; Mautz and Sharaf 1961). Expanding on this, Power (1999) contended that the significance of an audit is fundamentally tied to its independence, which is crucial for the effective functioning of capital markets (DeFond, Raghunandan, and Subramanyam 2002). Auditor independence relates to the probability that the auditor will report a discovered breach in the financial reports (DeAngelo 1981a; Watts and Zimmerman 1983). Furthermore, the market evaluates auditor independence, recognizing that the value of an audit is predicated on public trust in its quality (DeAngelo 1981b; Maijoor and Vanstraelen 2012). Auditor independence is, therefore, essential both in fact and in appearance (e.g., Nelson 2006; Sutton 1997), as independence in fact ensures unbiased and objective evaluations, while independence in appearance upholds public trust and confidence in the reliability of financial reporting. In conclusion, auditors add value to their client's financial statements to the extent that financial statement users perceive audits as valuable, that is, view the auditor as competent and independent.

1. FINANCIAL STATEMENTS AS A JOINT PRODUCT

The core concept of auditor independence revolves around the auditors' role in providing assurance over a company's financial statements for the benefit of shareholders and stakeholders, despite being engaged by the company and its management (e.g., Dhaliwal, Lamoreaux, Lennox, and Mauler 2015; EC 2010; Mautz and Sharaf 1961). This creates tension, as "Regulators view auditor independence as likely compromised when management is responsible for the selection, retention, and compensation of the external auditor, as auditors may view their responsibility as serving management rather than users of the financial statements" (Dhaliwal et al. 2015, p. 577). This situation creates an inherent conflict of interest (Gavious 2007), as financial statements are a joint product of the client's and auditor's actions

(Antle and Nalebuff 1991; Gaynor, Kelton, Mercer, and Yohn 2016; Gibbins, Salterio, and Webb 2001). The central issue is whether auditors can provide objective and impartial assurance over a company's financial statements despite their close working and financial relationships with the company and its management, and whether the collaborative process between auditors and clients can coexist with the principle of independence. Traditionally, it has been argued that collaboration and independence are mutually exclusive (e.g., Bazerman, Morgan, and Loewenstein 1997; Koch and Salterio 2017). However, the auditor-client relationship is characterized by mutual dependencies, requiring both parties to work collaboratively to achieve the desired outcome, which is an accurate and reliable audit opinion (Carlisle, Gimbar, and Jenkins 2023; Daoust and Malsch 2020; Guénin-Paracini, Malsch, and Tremblay 2015; Knechel et al. 2020). According to this latter stream of research, this collaboration does not necessarily compromise independence but can enhance the accuracy and reliability of the audit. Thus, the balance between maintaining auditor-client relationships and ensuring objective auditing presents a fundamental tension in preserving auditor independence (Bazerman et al. 1997; van Brenk, Renes, and Trompeter 2020).

2. Regulations Impacting Auditor Independence

Although auditor independence was initially recognized as a fundamental principle in auditing in the 19th century and has continually developed since then (Berryman 1983), it became a focal point of concern for regulators more recently. For instance, in 1996, the EC published a Green Paper highlighting concerns about auditors' independence, noting criticisms that commercialism had supplanted professionalism within the audit function. In response to the major accounting scandals at the turn of the century, the United States (US) enacted the Sarbanes-Oxley Act in 2002, followed by similar measures in Canada (CSA 2004) and in the European Union (EU) with the Statutory Audit Directive (2006/43/EC). These measures, mainly aimed at listed companies and sometimes other public interest entities (PIEs), included increased audit committee requirements and limitations on non-audit services provided by audit firms. The objective was to strengthen auditor independence both in fact and in appearance. Specifically, these regulations mandate that the selection of the external auditor for PIEs be the responsibility of the company's audit committee, which has to represent the investing public and engage an independent auditor (Fiolleau et al. 2013). The audit committee's auditor selection should be based on its assessment of the auditor's qualifications, expertise, resources, the effectiveness of the proposed audit process, and the auditor's independence (e.g., ecoDA 2011). Furthermore, mandatory audit partner rotation was instituted, stipulating a five-year rotation period in the US starting in 2002, and a seven-year rotation period in the EU beginning in 2006. Finally, in most jurisdictions, the annual general meeting of shareholders appoints the auditor. For details about the effects of such regulations, I refer to *Chapter 1*.

Despite these measures, accounting scandals have persisted, as the global financial crisis further underscored the critical role of accounting and auditing practices (for more information, see EC 2010; Humphrey, Loft, and Woods 2009), with the Wirecard scandal serving as a prominent recent example.[1] Consequently, there has been an additional increase in regulatory emphasis on auditor independence to reinstate trust in the public audit (Zerni, Haapamäki, Järvinen, and Niemi 2012). The EC, for example, stated, “It is important to stress that auditors have an important role to play and are entrusted by law to conduct statutory audits. This entrustment responds to the fulfillment of a societal role in offering an opinion on the truth and fairness of the financial statements of audited entities. **The independence of auditors should thus be the bedrock of the audit**” (EC 2010, p. 3, emphasis added). As a result, regulations concerning auditor independence have been further tightened in the EU (e.g., Cameran, Prencipe, and Trombetta 2016; de Jong, Hijink, and in ‘t Veld; EC 2010, 2014a, 2014b; Fiolleau, Hoang, Jamal, and Sunder 2013; PCAOB 2011). Specifically, the EU enacted the new Audit Regulation in 2014, which came into effect in 2016 and introduced significant reforms to enhance auditor independence. One key component of these reforms is mandatory audit firm rotation for public interest entities (PIEs), as the EC argued that “situations where a company has appointed the same audit firm for decades seem incompatible with desirable standards of independence” (EC 2010, p. 11). Mandatory audit firm rotation in the EU requires that companies change their auditor after a legally set period of time by establishing a maximum duration of the audit engagement of an auditor or an audit firm in a particular audited company at 10 years. Interestingly, the Public Company Accounting Oversight Board (PCAOB) ultimately chose not to implement mandatory audit firm rotation in the US despite it being under serious consideration, relying on strong audit committees instead (PCAOB 2011). The debate on mandatory audit firm rotation and retendering highlights potential benefits, such as enhanced auditor independence and new perspectives, but also concerns about increased costs, reduced expertise, and auditor susceptibility to management pressure (Allam, Ghattas, Kotb, and Eldaly 2017).

[1] The interested reader may be interested in the Netflix documentary ‘Wirecard: The Billion Euro Lie (2021).’

In conclusion, the fundamental premise of these regulations is that they enhance audit quality by weakening the economic and relational bonds between auditors and their clients (Fiolleau et al. 2013), thereby improving independence in fact and in appearance.

3. The Auditor Selection Process

It is clear that among numerous aspects of the auditor-client relationship, the process of selecting auditors is an important mechanism for ensuring auditor independence and the overall quality of the audit (e.g., Adelopo 2012; ICAS 2017; Regulation (EU) No 537/2014). In response to the previously discussed regulatory changes and market demands, companies around the globe are switching auditors more frequently than in the past (FEE 2016). Companies in the EU changed auditors at twice the rate in 2016-2017 as they did in 2013-2014 (Willekens, Dekeyser, and Simac 2019), making research on this topic especially relevant. Despite the alleged importance of the auditor selection and appointment process in the production of audit quality, audited companies are currently not required to publicly disclose information on the manner in which they select and appoint their auditor (SEC 2015; Gold et al. 2018). Moreover, although we know a lot about the demand for auditing, the causes and consequences of auditor switches, and the characteristics of the auditors hired (see reviews by DeFond and Zhang 2014; Habib, Wu, Bhuiyan, and Sun 2019; Stefaniak, Robertson, and Houston 2009), a systematic understanding of *how* companies select an auditor is currently lacking.

For a comprehensive discussion of the literature on auditor selection processes, I refer to *Chapter 1*, in which I present a systematic literature synthesizing the fragmented evidence about the auditor selection process, creating a comprehensive synthesis, and identifying research gaps. The few field studies on clients' tender processes show that intangible criteria and audit partner-client relationships are crucial in the auditor selection process, an emphasis unmentioned in evaluation practice guidelines, regulatory discussions, and archival research. The research gaps identified in this systematic literature review serve as the building blocks of my empirical analysis in *Chapters 2*, *3*, and *4*.

One of the conclusions of the literature review is that there is limited research on the importance of the engagement partner in the auditor selection process, even though the importance of the audit partner's identity for audit quality has been confirmed by archival-based studies (e.g., Gul et al. 2013; Hardies et al. 2016; Knechel et al. 2015; Zerni 2011). Furthermore, research is beginning to recognize the assortative matching aspects of audit partner-client alignment. This alignment considers both parties' collective and simultaneous supply and demand preferences (Cook, Kowaleski, Minnis, Sutherland, and Zehms 2019). However, "There is almost no evidence relating to the partner-client matching process" (Lennox and Wu 2018, p. 24). Therefore, in *Chapter 2*, I explore whether there is a pairing between clients and auditors, meaning clients selectively opt for audit partners best suited to their audit needs, and auditors take on clients they are most capable of auditing effectively. Specifically, I explore whether and how audit partners' *prior* experiences with other clients are associated with *current* matching to new clients. I find that within-firm partner rotations reduce auditor-client alignment, while audit firm rotations do not impact this alignment, possibly due to audit firms' strategic partner assignments and client scrutiny, highlighting the complexity of the auditor selection process. Furthermore, audit partner-client alignment is associated with lower income-decreasing accruals.

The combination of my archival findings and the identified gaps in the literature necessitated a deeper investigation into the auditor selection process, leading me to conduct an in-depth field study. In *Chapters 3* and *4*, I present my field study, in which I collected data from semi-structured interviews and documentary analyses of eight auditor selection processes at large Dutch clients. In these studies, I combine perspectives from client management, audit committee members, and audit partners, supplemented by client documents informing about, for instance, process setup, decision-making processes, and scorecards. I applied two different perspectives when analyzing the field study data. In *Chapter 3*, by applying an institutional theory lens, I dive deeper into the impact of regulations surrounding the auditor selection process on how clients organize their process in this particularly interesting institutional setting. Taking full advantage of the detailed information about our respondents' auditor selection processes, in *Chapter 4*, I use social exchange theory to closely investigate the interpersonal interactions happening during the auditor selection process.

In my concluding chapter, I address the research gaps resolved by my dissertation, linking my empirical findings to these gaps and to each other. Additionally, I discuss the broader implications of my results, the limitations of this study, and potential avenues for further research.

CHAPTER 1. A SYSTEMATIC LITERATURE REVIEW ON COMPANIES' AUDITOR SELECTION PROCESSES

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Abstract

We provide a systematic review of the literature on companies' auditor selection process (through which they evaluate prospective external auditors and hire one). Drawing from regulations, practice guidelines, and researched topics, we organize studies into a framework: inputs, process steps (company tendering, audit proposals, auditor presentations, and company deliberation and recommendation), and outputs. We consider research findings in light of practice guidance. By focusing on evidence of process steps, we identify key actors, activities, decision factors, and expectations during auditor selection. This process consumes substantial resources and plays an important role in auditor-client matching. We find that most studies use archival data to infer aspects of the selection process from associations between publicly observable auditor and company characteristics and auditor appointment outcomes. We suggest promising directions for conducting future research with complementary methods. Our review provides valuable insights for academics and practitioners interested in companies' auditor selection practices and auditor-client relationship dynamics.

Keywords: auditor selection; audit firm selection; auditor choice; audit firm tendering; systematic review; synthesis; research opportunities.

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1. INTRODUCTION

We systematically review the academic literature on the auditor selection process, that is, the process through which companies select and hire their external auditor.[2] Asserting that this process strengthens auditor independence, regulators have targeted it by, for example, expanding the role of audit committees or introducing mandatory audit firm rotation. In response to regulatory changes and market demands, companies are switching auditors more frequently than in the past (FEE 2016). For instance, companies in the European Union (EU) changed auditors at twice the rate in 2016-2017 compared to 2013-2014 (Willekens, Dekeyser, and Simac 2019).

The academic literature offers a detailed understanding of what happens before and after the auditor selection process (e.g., the demand for auditing, causes and consequences of auditor switches, and characteristics of the auditors hired; see reviews by DeFond and Zhang 2014; Habib, Wu, Bhuiyan, and Sun 2019; and Stefaniak, Robertson, and Houston 2009).[3] This body of research shows that the demand for auditing and audit quality stems from client incentives (e.g., agency costs and regulations). As a result, various institutional factors (e.g., the level of investor protection) and client characteristics (e.g., ownership structure, board characteristics) are associated with the hiring of particular auditors (e.g., Big N auditors, industry specialists). Furthermore, changes in incentives lead to auditor switching, and market participants (e.g., investors) react to such changes. Overall, substantial convergent evidence exists on why companies switch and choose auditors.

In contrast, a systematic understanding of *how* companies select an auditor is currently lacking, despite the increasing relevance of this question. Our review aims to increase understanding of the *process* by which companies select their auditor, as distinct from their initial decision to hire an auditor, switch to a new auditor, or which particular auditor to hire. This auditor selection process encompasses decisions on who to involve in the selection, what procedures to follow, how to structure auditor-client interactions, and the decision-making

[2] We use the terms "(external) auditor" and "audit firm" interchangeably when discussing research at the audit firm-level. We use the term "audit partner" when discussing research considering the audit partner in companies' auditor selection.

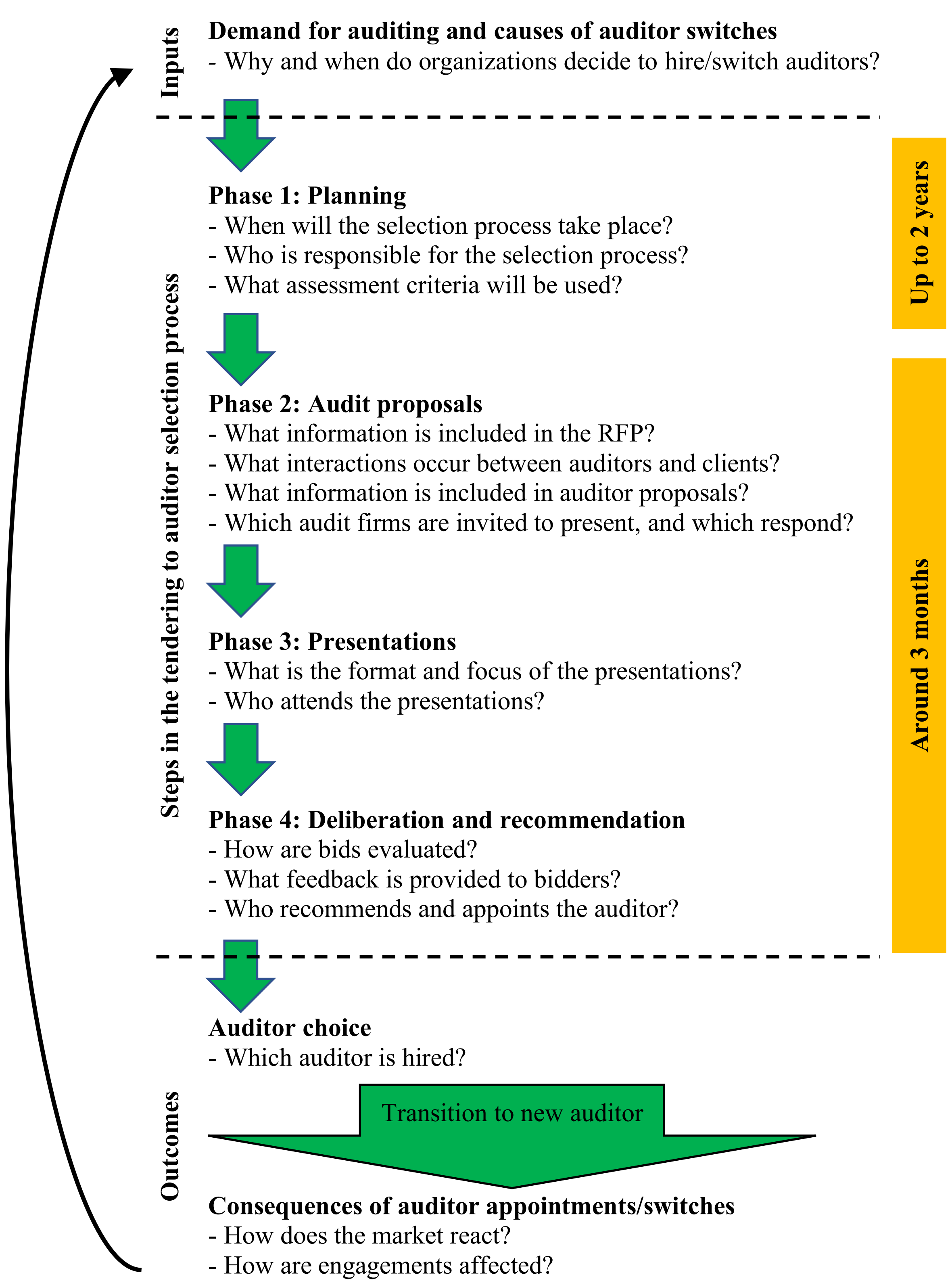
[3] Specifically, DeFond and Zhang (2014) reviewed the archival literature on audit demand. Habib et al. (2019) reviewed the archival literature on the determinants of auditor choice. Their reviews show that variations in client incentives, client characteristics, institutional differences, and regulations explain auditor choice (e.g., the hiring of Big N or industry specialist auditors). Stefaniak et al. (2009) reviewed the causes of auditor switching, distinguishing auditor-initiated from client-initiated changes, and its consequences (e.g., market reactions, financial reporting quality).

process of which auditor to hire. Through this process, companies try to specify and satisfy their demand for auditing.

Applying broad search criteria (see Section 2 for details), we identified 91 empirical studies with evidence relevant to the auditor selection process published from 2000-2022. This substantial number of studies, primarily published in leading auditing and accounting journals, illustrates the importance of the topic. Further, parallel to rotation and tendering processes becoming more common in recent years with regulatory scrutiny, academic interest in the topic has increased, with 39 of these studies published during the last five years (2018-2022). We respond to this trend by offering a systematic review of the auditor selection process. Systematic reviews significantly contribute to the literature by surveying evidence from a comprehensive set of research studies rather than the results of the largest or most recent study to inform decision-making (Hardies, Ohlrogge, Mentens, and Vandennieuwenhuysen 2024).

Our main contributions lie in collecting the fragmented evidence about the auditor selection process, creating a comprehensive synthesis, and identifying promising areas for future research. Given the absence of specific theories in the academic literature on how companies select their auditors, this paper is structured around our conceptual framework presented in Figure 1.1. This framework is derived from regulations, best practice guidelines, and synthesized topics from existing literature. Figure 1.1 shows that companies go through four steps when selecting their auditor. First, in the planning step, companies prepare for the selection process by deciding on the timing, actors to be involved, and assessment criteria by which auditors will be evaluated. In the next step, companies issue a request for proposals (RFP), auditors submit their proposals, and clients decide which auditors to invite for presentation. Companies and auditors then interact during the presentation step. Finally, in the deliberation and recommendation step, companies evaluate the different prospective auditors and recommend which auditor to hire. Our framework also illustrates how the current review is linked with and differs from existing reviews that have focused on what happens before (the inputs) and after (the outputs) the auditor selection process. We employ this framework to synthesize the existing literature, and for each step, we identify potential avenues for future research where the literature has yet to address pertinent topics.

FIGURE 1.1
Conceptual Framework for the Auditor Selection Process



This framework outlines the organization of our research synthesis. Our review does not encompass the inputs and outcomes of the auditor selection process, but relates to the 'Steps in the tendering to auditor selection process.'

The scope of our review is relatively broad. How companies select and appoint their auditor is not part of the public record, so our review includes all studies that report empirical evidence that enhances our scant understanding of this topic, including studies from specific settings such as governmental audits.[4] We also discuss if practice, as evidenced by existing empirical research, aligns with best practice guidelines for the auditor selection process. Based on these findings, we identify under-researched areas and suggest areas for future research. Our review is of value to researchers interested in topics related to auditor selection and auditor-client relationships.

2. Method and Sample Description

To obtain a comprehensive sample of the relevant literature on the auditor selection process, we examined accounting and auditing journals rated as either an A* by the Australian Business Deans Council (ABDC) or 4* or 4 by the Chartered Association of Business Schools (ABS), or jointly at least an A by the ABDC and a 3 by the ABS.[5] We added the *International Journal of Auditing* and *Managerial Auditing Journal* because they are relevant auditing journals. This resulted in identifying 25 journals (Table 1.1, Panel A). To search through these journals, we used the Web of Science (WoS) database using the strings noted in Table 1.1, Panel B.[6] After searching for published documents, we conducted subsequent searches for unpublished studies in SSRN (the Social Science Research Network) to identify working papers. Our approach follows existing guidelines and best practices for conducting systematic literature reviews in accounting (see Andiola, Bedard, and Hux 2017; Hardies et al. 2024) and is similar to that of recent reviews (e.g., Aghazadeh, Brown, Guichard, and Hoang 2022; Andiola, Downey, and Westermann 2020; Simnett, Carson, and Vanstraelen 2020).

2.1. Literature Search Strategy

We searched for all research studies that examined auditor selection and considered their relevance to the question: *How do companies select their external auditor?* As illustrated in Figure 1, this process encompasses four steps: (i) planning, (ii) proposals, (iii) presentations,

[4] Due to the specific nature of governmental audits, the generalizability of some of these results is unknown. Nonetheless, these unique settings are useful to study because they exemplify ideal auditor selection practices, such as high levels of accountability and transparency, and formalized procurement and tendering policies.
[5] Our review protocol, describing our methodological and analytical approach in detail, is publicly available at: https://osf.io/fudvg/?view_only=5baf4e1d0d174a1488ae6c6684309e72.
[6] We used the WoS database because not all journal databases have the same "advanced search" option. The WoS database allows searching through different journals by using the search string SO="journal name".

and (iv) deliberations and recommendation, which ultimately results in the company selecting their auditor from a set of prospects.

TABLE 1.1
Search Strategy

Panel A: Journals	
Abacus	
Accounting Horizons	
Accounting and Business Research	
Accounting, Auditing & Accountability Journal	
Accounting, Organizations and Society	
Accounting Review	
Auditing: A Journal of Practice & Theory	
Behavioral Research in Accounting	
British Accounting Review	
Contemporary Accounting Research	
Critical Perspectives on Accounting	
European Accounting Review	
Financial Accountability and Management	
International Journal of Accounting	
International Journal of Auditing	
Journal of Accounting & Economics	
Journal of Accounting and Public Policy	
Journal of Accounting Auditing and Finance	
Journal of Accounting Literature	
Journal of Accounting Research	
Journal of Business Finance & Accounting	
Journal of Management Accounting Research	
Management Accounting Research	
Managerial Auditing Journal	
Review of Accounting Studies	
Panel B: Search strings and limiters	
WoS (Core Collection)	**Search string:** (TS=(audit* AND “[Search term]”) OR AB=(audit* AND “[Search term]”) OR TI=(audit* AND “[Search term]”) AND (SO=journal) AND PY=(2000-2022) **Limiters:** Document type: Article, Review Article
Panel C: Search terms	
Select*	
Rotat*	
Tender	
Choice	
Switch*	
Chang*	
Auditor-client	
Hir*	
Appoint*	
Procure*	
Request for proposal	
RFP	
Ratif*	
Bid*	

This table reports the search strategy used in this systematic literature review.

We excluded papers if they did not report directly informative evidence about the selection process. For example, substantial literature examines various factors associated with why companies initiate an auditor selection process (e.g., mandatory rotation, auditor-client disagreements) and which auditors they select (e.g., Big N, industry specialist). While such inputs and outputs may correlate with the auditor selection process (i.e., *why* a company is undertaking an auditor selection process may influence *how* it selects its auditor), we only included research articles that contained empirical evidence about the auditor selection process itself. We excluded papers that merely linked auditor or client characteristics with auditor choice, switching decisions, or the consequences thereof, which existing reviews already cover (see DeFond and Zhang 2014; Habib et al. 2019; Stefaniak et al. 2009).

2.2. Search Method

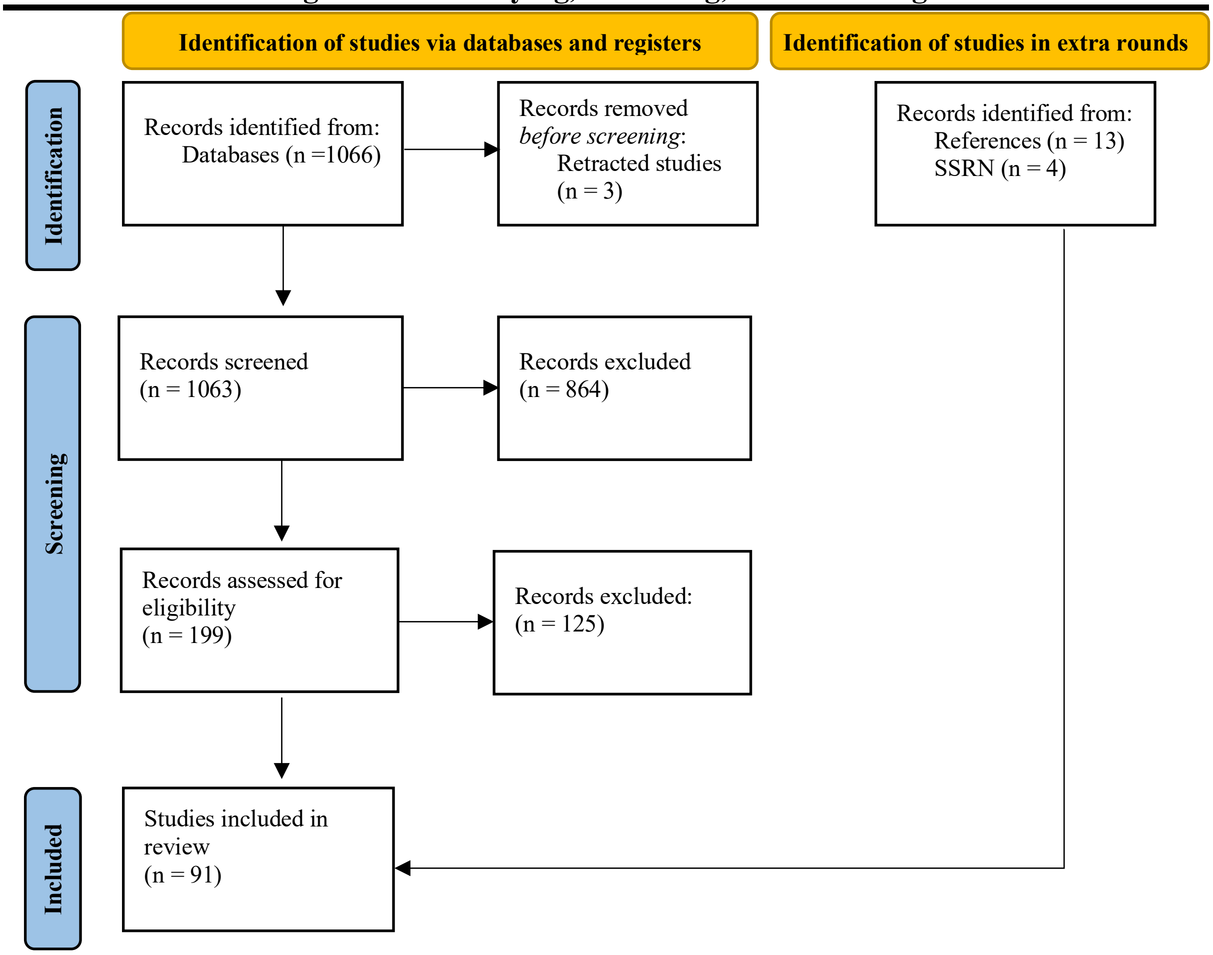
We determined relevant search criteria upfront and updated them iteratively while reviewing the literature. Table 1.1 (Panel C) shows our search terms. Because "process" is a generic term that lacks specificity, we did not use "process" as a search term. Instead, we used our judgment when reading the title and abstract of papers to determine if a paper potentially contained empirical evidence on the auditor selection process. Because we used broad terms, we initially restricted our search to the papers' titles, abstracts, and keywords. We also restricted our sample to papers from 2000-2022 because bibliographic databases do not have full-text search capabilities for publications before 2000. After deleting duplicates, a total of 1,066 unique, accessible papers remained. We finalized the searches in August 2022.

2.3. Paper Inclusion

One author screened the titles and abstracts of the 1,066 identified papers to determine their relevance. This first screening led to deleting 864 papers from our sample for not investigating the auditor selection process.[7] The topics of excluded papers were primarily: audit firm characteristics, audit fees, and audit market competition. The screening author iteratively discussed the relevance of paper topics and individual papers with the team throughout this initial screening process. If there was doubt about a paper's eligibility, it was retained in the sample at this stage of the screening process. We also excluded three retracted papers.

[7] Many papers were irrelevant to our review beyond any discussion. For instance, our initial search criteria led to the inclusion of papers that contain the words *audit** and *change* but are not about *auditor change* (e.g., Hodge, Martin, and Pratt (2006) about the effect of accounting choices on financial statement users' perceptions) or the words *audit** and *select* but are not about *auditor selection* (e.g., Doyle, Ge, and McVay (2007) on accruals quality and internal controls – the abstract contains the term "self-selection bias").

FIGURE 1.2
Flow Diagram of Identifying, Screening, and Including Studies



After initial screening, we assessed 199 papers for eligibility against our inclusion and exclusion criteria.[8] We first articulated these criteria in a guiding document and referred to them throughout our screening process (see Table 1.2 for key criteria). All four authors took part in this eligibility screening. First, each author independently screened an assigned number of papers for eligibility. Second, to reduce bias and errors, all instances where there was any uncertainty about a paper's eligibility were discussed in a group meeting with the entire author team. Based on this screening, we deleted 125 papers, leading to an initial sample of 74 papers. We identified 4 additional working papers on SSRN and 13 additional published papers by reviewing the reference lists of frequently cited papers in our sample.[9] Figure 1.2 gives an overview of this selection process.

[8] For example, we excluded papers only looking at determinants of Big 4 choice (e.g., Basu and Liang 2019) or auditor dismissals (e.g., Sankaraguruswamy and Whisenant 2004).
[9] Papers may be unidentified as they are sometimes absent from electronic databases, inaccurately indexed, or not indexed at all. Additionally, studies themselves may lack information (e.g., do not have the most informative titles or abstracts).

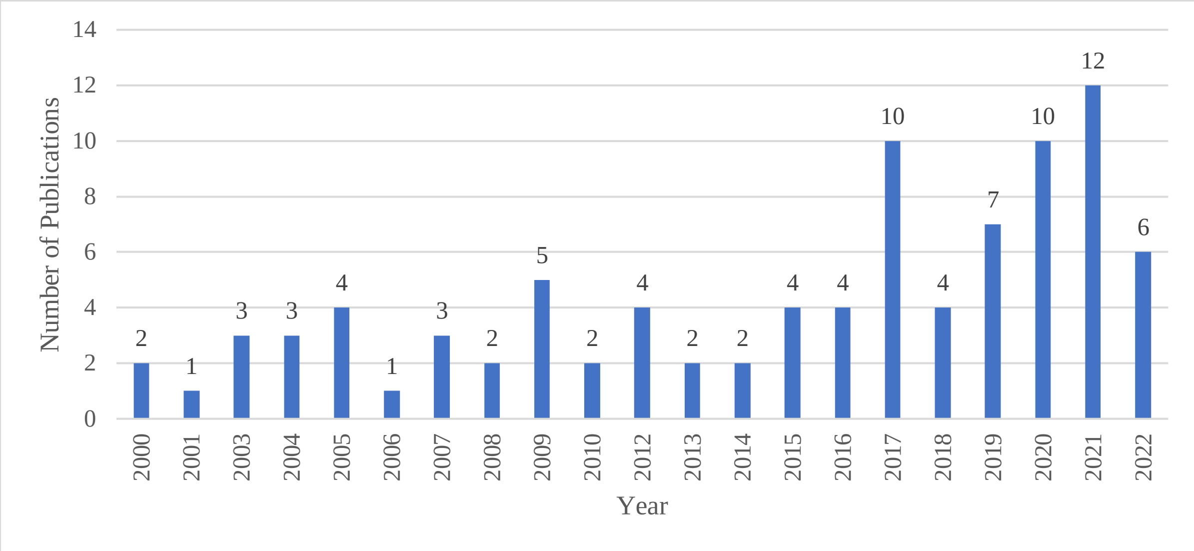
TABLE 1.2
Eligibility Criteria for Review of Literature on the Auditor Selection Process

Category	Inclusion	Exclusion	Justification
Review question	Studies relevant to the question: *How do companies select their external auditor?*	Studies not providing direct evidence on *how* companies select their auditors *	We restrict the scope of our review to studies on *how* companies select their auditors.
Study design	Empirical studies	Theoretical papers Review studies	Our focus is on synthesizing empirical evidence on the steps in the tendering to auditor selection process, so we exclude all non-empirical papers.
Publication status	Studies published in relevant accounting and auditing journals (Table 1, Panel A), plus high-quality unpublished papers	Studies published in other journals Books and book chapters	We consider studies in a broad set of journals to minimize the potential for bias and obtain a comprehensive sample of the relevant literature. We include unpublished studies to avoid publication bias.
Publication year	2000-2022	Publications before 2000	Bibliographic databases typically do not have full-text search capabilities for publications before 2000.
Language	English	Languages other than English	We focus on studies in English because of resource constraints that do not allow translations from articles in other languages.

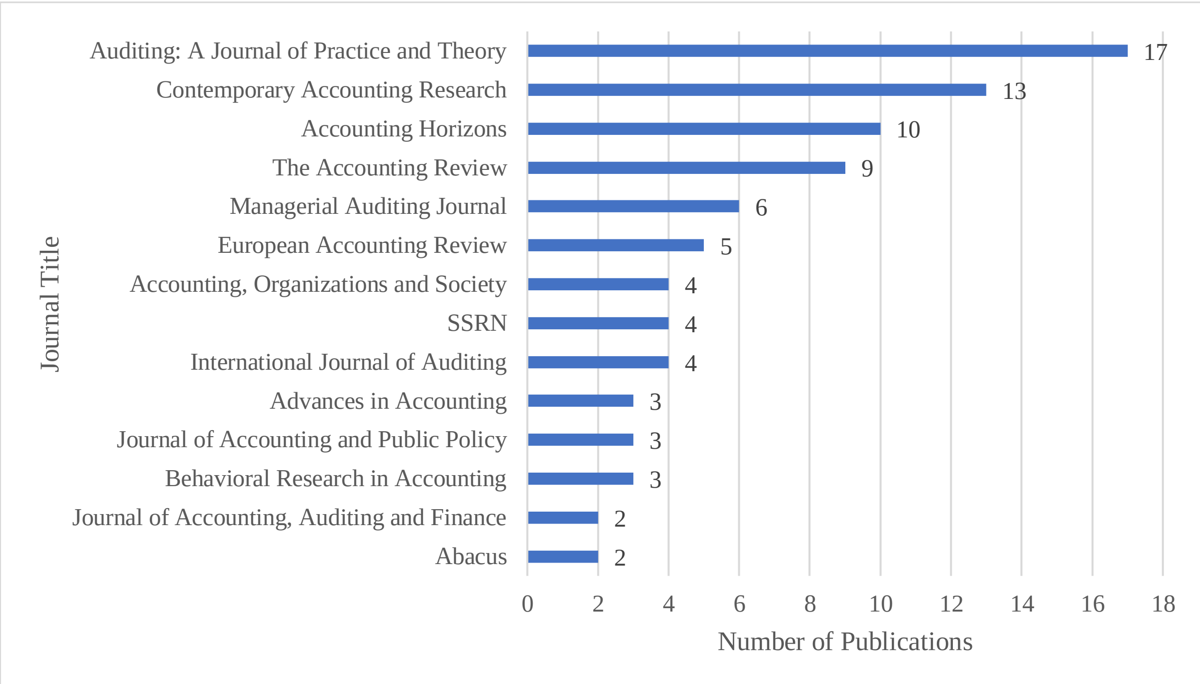
This table reports the inclusion and exclusion criteria used throughout the screening process.

FIGURE 1.3
Sample Overview

Panel A: Publications per year



Panel B: Publications per journal



Journals with only one publication included Accounting, Auditing & Accountability Journal, Journal of Accounting and Economics, Journal of Accounting Research, Journal of Business, Finance & Accounting, Review of Accounting Studies, and The International Journal of Accounting.

Figure 1.3 shows the yearly distribution of relevant papers (Panel A) and the number of papers included by the journal (Panel B). Most papers (81%) involved quantitative data: 64% relied exclusively on archival data, 12% reported experimental results, and 6% combined archival and survey data. Only 17% relied exclusively on qualitative data and 2% combined quantitative and qualitative data. Appendix A summarizes the main characteristics of our final sample of 91 studies.

3. Research on Companies' Auditor Selection Processes

Our review of the literature on the auditor selection process is organized around the four steps identified in Figure 1.1, which companies follow after deciding to hire or switch auditors: (i) planning, (ii) audit proposals, (iii) presentations, and (iv) deliberation and recommendation. We only include papers that primarily examine the inputs and outputs of the process if it informs us about how companies select their auditor. We acknowledge that the reasons for hiring or changing auditors may itself affect companies' practices in selecting auditors because a company dissatisfied with some characteristic of its incumbent auditor will seek a new auditor satisfying that characteristic (Brown and Knechel 2016). For example, companies experiencing disagreement with their auditor might be eager to hire a more cooperative auditor (Ayres, Neal, Reid, and Shipman 2019) and thus want to involve management in the selection process to assess the cooperativeness of a potential new auditor. Or, companies interested in creating a more transparent image might want to hire higher-quality auditors (Aobdia 2018) and set up a more transparent selection process. Similarly, we only include papers that primarily examine client characteristics or institutional factors if the reported evidence informs us about the auditor selection process (e.g., Abbott and Parker 2000; Lennox and Park 2007). For example, while we expect all companies to go through the four steps of the selection process, best practice guidelines suggest that the tendering process may be less exhaustive for smaller than for larger and for private than for listed entities (e.g., ICAS 2017, 2018).

3.1. Planning

Best practice guidelines suggest that the key features of a robust procurement process are thorough preparation regarding timing, the actors responsible for managing the process, and the means of evaluating prospective auditors and final decision-making (e.g., AICPA 2018; Deloitte 2016; KPMG 2018). A successful auditor procurement process should result in the company hiring an auditor that meets its needs and satisfies the reasons for hiring an auditor.

3.1.1. Timing

Best practice guidelines mention both the timing of the selection process and its timeline (e.g., Deloitte 2016; FRC 2017; ICAS 2018; KPMG 2018). In these guidelines, the time needed to complete a typical audit tender process is estimated to be around three months, although the preparation leading up to the tender may take several months or years. Guidelines also suggest that the timing affects process efficiency, especially the ease of transition to a new auditor. Companies not only need to consider regulations such as mandatory rotation and independence requirements, but also potential changes in their own business (e.g., changes in the board or management, system changes).

Audit firm and partner changes are known to be disruptive to the audit in the early years of tenure by lowering audit quality and reducing efficiency (Bell, Causholli, and Knechel 2015; Cameran, Francis, Marra, and Pettinicchio 2015; Daugherty, Dickins, Hatfield, and Higgs 2012; Gipper, Hail, and Leuz 2021). For example, partners interviewed by Daugherty et al. (2012) reported a two- to three-year familiarization period before becoming fully effective on new engagements. The successful timing of the selection process may thus be critical to ensure a smooth transition to a new auditor. Indeed, Deloitte (2016) identified "minimizing transition risk" as the number one concern among large United Kingdom (UK) companies that influence decisions around the timing of their tendering.[10] Consequently, it makes sense for audit firms to dedicate resources to minimize disruptions around initial appointments and carefully manage rotations (Dodgson, Agoglia, Bennett, and Cohen 2020; Gipper et al. 2021).[11]

Existing research further shows that companies' timing varies in the initiation of their auditor selection process and its conclusion relative to the fiscal year-end. Gipper et al. (2021) document the occurrence of early rotations of partners (before the tenure clock lapses) and audit firms among publicly listed companies in the United States (US). Pacheco-Paredes, Rama, and Wheatley (2017) find that most auditor changes happen 6 to 10 months before the fiscal year-end. The appointment of a new CEO or CFO during the fiscal year influences this timing, suggesting that client executives play a significant role in the auditor hiring process. Auditor changes closer to the year-end are associated with longer reporting lags and lower audit quality. Mande, Son, and Song (2017) report that delays in appointing successor auditors

[10] The disruptiveness of rotations also helps explain why client companies may follow their audit engagement partner when that partner changes to another audit firm (Blouin, Grein, and Rountree 2007; Chen, Su, and Wu 2009; Chang, Choy, Lin, and Koo 2019).

[11] Recent studies by Dodgson et al. (2020) and Gipper et al. (2021) explore how audit firms manage auditor transitions in the context of partner rotations. Auditor transitions are an output of the auditor selection process and, therefore, largely beyond the scope of our review.

following resignations are associated with higher audit fees, negative stock market responses, and a lower likelihood of being accepted by Big N auditors. Furthermore, Cassell, Hansen, Myers, and Seidel (2020) find late auditor changes (i.e., during or after Q4) associated with lower audit quality, likely because auditors have insufficient time to perform adequate work. These findings suggest that companies should intentionally plan the timing of their selection process, as suggested by best practice guidelines. Starting the selection process too late likely results in appointing a lower-quality auditor or one that lacks sufficient time to perform good work.

3.1.2. Actors

Both practitioners and academics debate who should have auditor hiring power, as this could influence client companies' auditor selection. The selection of an adequate auditor is an important signal from the board to outsiders about their prioritization of transparency and financial reporting quality. Practitioner guidance identifies the board as responsible for audit committee appointment, process oversight, and final auditor recommendation for the shareholder meeting (FEE 2013; ICAS 2017; KPMG 2018). Further, the audit committee is recommended to be the key, or even sole, decision-making body (Deloitte 2016; FRC 2017; ICAS 2017; KPMG 2018). A growing number of jurisdictions require audit committees, comprised of independent directors, to be directly responsible for appointment, compensation, retention, and oversight of the company's auditor (e.g., Canada, the EU, the UK, the US).[12] Audit committee requirements, which apply to listed companies and sometimes other public interest entities, were introduced in 2002 for the US with the Sarbanes-Oxley Act, but only in 2006 for the EU with the Statutory Audit Directive, and even later in some other jurisdictions (e.g., in 2009 in India with the Companies Bill). Regulations and guidelines also require at least one financial expert to serve on the audit committee.[13]

Management should be involved only where appropriate, that is, in an advisory role, to achieve an auditor selection that is 'fit for purpose' (FEE 2013; FRC 2017; KPMG 2018). Audit committees should consider the weight given to management's assessment of the audit

[12] Independence in this context is typically understood along the lines of being 'free of material conflict of interest' (EU Recommendation, Feb. 15, 2005). Davies and Hopt (2013) characterize independence in the context of corporate boards as complex and controversial.

[13] Many jurisdictions require this, including the US, the EU member states, the UK, Australia, China, and India. Hermanson, Hurley, and Obermire (2023) provide a recent review of the research on audit committees. There is some overlap in our discussion of the role of the audit committee in auditor selection and theirs. Our reviews, however, also substantially diverge because our review is more comprehensive than the role of the audit committee, while they discuss the role and functioning of audit committees in more governance areas than only in relation to auditor selection (e.g., overseeing financial reporting, internal auditors, and internal control).

teams (FRC 2017). Key influencers could, for example, be the CFO, the controller, and the head of internal audit (Deloitte 2016; FRC 2017; ICAS 2017; KPMG 2018). Guidance suggests setting up an auditor selection panel to lead and oversee the whole process and then recommending either one audit firm or a shortlist to the board. The board then recommends an auditor for appointment, and finally, the shareholders vote (FEE 2013; ICAS 2017).

Overall, practice guidelines and regulations stress the importance of the audit committee in decision-making and describe the involvement of various other stakeholders in selecting an auditor. We now turn to discuss the academic literature examining the roles of these different actors in the auditor selection process.

3.1.2.1. Board of Directors and the Audit Committee

The relationship between the characteristics of the board of directors, the audit committee, and the external auditor is complex (Cohen, Krishnamoorthy, and Wright 2004). Strong internal corporate governance mechanisms can act as determinants and/or substitutes for high-quality auditing (Abbott and Parker 2000; Hay, Knechel, and Ling 2008; Jin, Jin, Tian, and Xuan 2021; Srinidhi, He, and Firth 2014). There is substantial empirical evidence that various indicators of strong governance influence choosing a higher-quality auditor (for a review, see Habib et al. 2019). For example, much evidence shows a positive relationship between board independence and a demand for high-quality auditing (e.g., Beasley and Petroni 2001; Chen and Zhou 2007; Lee, Mande, and Ortman 2004).

Although evidence indicates that corporate governance mechanisms influence the auditor selection process, there is a remarkable lack of research on how directors influence the auditor selection process. Likewise, little is known about the mechanisms underlying many of the associations between board characteristics and auditor choice (i.e., how such characteristics affect companies' auditor selection). There is some evidence indicating that board members draw from their experiences and network to recommend the appointment of specific audit firms and audit partners to reduce the uncertainty involved in auditor selection and to protect their reputation capital (Fredriksson, Kiran, and Niemi 2020; Kacanski, Lusher, and Wang 2021).

Contrary to best practices and regulations, considerable evidence suggests that audit committee members are heavily influenced by management (e.g., Gendron and Bedard 2006; Dodgson et al. 2020). Although the audit committee is ultimately responsible for the auditor selection decision, audit committee independence and influence do not appear to be focal points of concern in practice (Gendron and Bedard 2006). One respondent in Gendron and Bedard (2006) even mentioned that the audit committee is not involved in the selection process, but this study took place before the introduction of the aforementioned regulations and guidelines increasing audit committee power. Other respondents in their study described that audit committee members act as liaisons to the overall board and actively influence auditor selection.

Audit committee involvement and oversight may also vary across different firm types. Jenkins, Pyhoza, and Taylor (2019) report that audit committees of investment companies substantially oversee audit firm retention and hiring decisions. Conversely, audit committees of public companies perform a less significant role. Nonetheless, some evidence indicates that firms with an audit committee select industry specialist lead partners with a large number of clients, positively impacting audit quality (Kao, Shiue, and Teng 2021). Furthermore, audit committees appear to increase their involvement and become more active in the first year of an audit engagement (Kalelkar 2016). Additionally, audit committees provide positive signals to investors when given high appointment power (Gold, Klynsmit, Wallage, and Wright 2018), but this appears only to be the case when mandatory rotation or tendering is present.

According to Habib et al. (2019, p. 316), '[v]ery little research has been done on the impact of independence, financial expertise, and the interlocking of audit committee members on the appointment of high-quality auditors.' Nevertheless, some evidence links audit committee characteristics to auditor choice. For example, audit committee independence, size, and active involvement are associated with the demand for high-quality auditing, as evidenced by the company's hiring of Big 4 (Chen and Zhou 2007) and industry specialist auditors (Abbott and Parker 2000). Moreover, some evidence also shows that independence reduces the effect of social ties (Abbott, Brown, and Higgs 2016; Lennox and Park 2007; see Dhaliwal, Lamoreux, and Mauler 2015 for contrasting evidence) and influences shareholder ratification actions (Raghunandan and Rama 2003). Arguably, this is due to more independent audit committees being 'more likely to exert greater effort working with the firm's auditor, thus reducing hidden audit risks' (Lee et al. 2004, p. 143). Related to audit committee effort, busy and foreign audit committee members are more likely to hire non-Big 4 auditors (Almaqoushi and Powell 2021).

Downes, Draeger, and Sadler (2021) investigate voluntary disclosures and show that audit committee activity and involvement in the audit partner selection process lead to selecting more rigorous partners, resulting in higher audit quality. Further, audit committees with female directors choose higher-quality auditors, especially when these directors are independent or more financially experienced (Lai, Srinidhi, Gul, and Tsui 2017; Oradi and Izadi 2019). Finally, there is much evidence to support the regulatory demand for financial expertise in the audit committee, with financial expertise being associated with a host of positive outcomes related to auditor selection and retention (Abbott, Buslepp, and Notbohm, 2018; Blouin et al.

2007; Chen and Zhou 2007; Krishnan and Ye 2005). A recent paper by Baugh, Hallman, and Kachelmeier (2022) shows that audit committees without Big 4 working experience are more likely to engage physically attractive audit partners. Their results suggest that an important mechanism through which audit committees influence the auditor selection process is by bringing knowledge and experience to the table that allows the selection committee to differentiate auditors based on competence (e.g., auditing philosophy, experience), mitigating the reliance on superficial cues (e.g., attractiveness).

Putting the audit committee in charge of the auditor selection generally leads to companies choosing higher-quality auditors and signaling higher objectivity, even when management is heavily involved. Gold et al. (2018, p. 84) note that "[T]he auditor selection process and audit committee appointment power are considered complements, not substitutes in enhancing audit quality." Although some evidence suggests the audit committee's role to be largely ceremonial, their mere presence may incentivize management to put more effort into the auditor selection process.

3.1.2.2. Managerial Influence

Substantial evidence shows that management is the most influential body in the auditor selection process (Beasley, Carcello, Hermanson, and Neal 2009; Cohen, Krishnamoorthy, and Wright 2010; Dhaliwal et al. 2015; Fiolleau, Hoang, Jamal, and Sunder 2013; Gendron and Bedard 2006; Taminiau and Heusinkveld 2017). Specifically, CFOs have substantial power over auditor selection (Dao, Raghunandan, and Rama 2012) and may even control auditor negotiation interactions (Beck and Mauldin 2014). As a respondent in Jenkins et al. (2019) mentioned, management must make the call because "management works with them on a day-to-day basis." Overall, management is heavily involved in auditor selection decisions (Cohen et al. 2010; Fatemi 2012). In group audit scenarios, the parent company's management influences the subsidiary company's auditor selection (Branson and Breesch 2004), as does the parent company's auditor (Downey and Westermann 2021). In contrast to the preceding studies, Jenkins et al. (2019) found that the influence of management only holds in public companies, not investment companies. Further, their results suggest that this effect is more significant when the CEO plays a dominant role on the board. While there is a dearth of research on tendering by private companies, Esplin, Jamal, and Sunder (2018) examined 11 Canadian private companies that had recently hired an auditor and found that in all cases, top management (usually the CEO) selected the auditor.

Abundant evidence indicates that shifting auditor hiring decision authority toward management lowers audit quality. This can be due to the desire for flexibility in reporting (Hurley, Mayhew, Obermire, and Tegeler 2021) or the reduction in audit committee independence (Berglund, Draeger, and Sterin 2022). In an experimental setting, Bowlin, Hobson, and Piercey (2015) found that in a mandatory rotation setting, auditors' opportunity to interact informally with management reduced audit effort and made them less skeptical about management representations (e.g., explanations for unusual fluctuations observed during analytical review). Additionally, managers are more likely to appoint auditors with whom they were formerly affiliated (Dhaliwal et al., 2015) or are currently connected (Yu, Kwak, Park, and Zang 2020).[14] Yu et al. (2020) noticed a decrease in audit quality when hiring connected auditors. Furthermore, some evidence suggests that governmental interventions limiting management influence on auditor selection can improve audit quality (Chi, Lisic, Long, and Wang 2013). The evidence on audit quality effects remains mixed, as Dhaliwal et al. (2015) found that companies hiring affiliated auditors are less likely to receive going-concern opinions but are no more likely to meet or beat analyst forecasts or have higher abnormal accruals.

In conclusion, substantial evidence highlights the significant influence management exerts over the auditor selection process, particularly through the roles of CFOs and CEOs, which can lower audit quality due to potential conflicts of interest and reduced auditor skepticism. However, interventions that limit management's influence show promise in enhancing audit quality, although the overall impact remains mixed across different studies.

3.2. Audit Proposals and Presentations[15]

When procuring a new auditor, companies typically undergo a formal tendering process and invite audit firms to submit their bids (also described as a Request for Proposal [RFP] process). These phases of the selection process involve the following key activities: Issuing the RFP with specific selection criteria; providing necessary access to information, personnel, and the company site for firms to prepare their bid; identifying the auditors to invite; deciding the practical modalities of the presentations; and interacting with the bidding firms.

[14] The terms *affiliation* and *connection* refer to any situation in which there are network ties between an auditor and a firm. Such ties can exist, for example, because of former employment (e.g., a manager who previously worked for an audit firm), corporate experiences (e.g., a director of a firm serving as an outside director for another firm), or shared backgrounds and experiences (e.g., school ties, family ties).

[15] Our conceptual framework discerns audit proposals and presentations as two distinct phases companies go through when selecting an auditor. Because there is only a small body of research that provides insight in these phases of the selection process, we discuss them together here.

3.2.1. Request for Proposals

Fiolleau et al. (2013) investigated how company management, the audit committee, and the bidding auditors acquired and communicated information to evaluate each other after the company's RFP issuance. The notable features of that companies' RFP process were: the VP Finance was the single point of contact responsible for providing access to and distributing information between the selection committee and the bidding auditors; the information exchanged and used for evaluation emphasized cultural fit (e.g., rapport, chemistry, attention to needs) rather than expertise and risk; and, even though the audit committee chair was active in the process and met with all of the bidding firms to provide insights about the CFO, the audit committee viewed their role as monitoring rather than driving the process. Fiolleau et al. (2013) highlighted several inconsistencies between the company's stated objectives for the RFP and the new auditor that the company ultimately selected. Notably, the company chose the lowest-priced bid despite asserting that pricing was not a primary motivation for the RFP, suggesting potential misalignment between stated goals and actual decision-making criteria

Formal tendering is less common among private companies going through an auditor selection process. However, in most respects, the RFP processes in private companies documented by Esplin et al. (2018) were similar to the one documented by Fiolleau et al. (2013). Notably, four out of 11 companies studied by Esplin et al. (2018) used an RFP.

Based on interviews and client evaluations from a Big 4 firm in the Netherlands, Taminiau and Heusinkveld (2017) conclude that the RFP is a dynamic process during which interactions between auditors and clients intensify, so expectations and criteria become clearer and more specific. Although practice guides portray a relatively standardized, formal RFP process, these field studies suggest substantial variation in how individuals involved interact, share information, and make decisions. Guidance suggests providing sufficiently detailed information that allows bidding audit firms to understand the entity's business (e.g., AICPA 2018; FRC 2017; ICAS 2017).

Several archival studies examine US governmental audit settings where policies for auditor procurement were introduced to strengthen internal controls over fiscal spending and increase service quality. In these settings, mandatory tendering includes policies such as issuing RFPs every five years with audit committee oversight and periodic state inspections (Elder and Yebba 2020). Elder and Yebba (2020) report that the introduction of a formal RFP process in the New York school district audit market led to a more concentrated audit market (due to small, nonspecialized firms leaving), increased hiring of specialist audit firms associated with higher quality, and higher audit fees. Boon, Crowe, McKinnon, and Ross (2005) and Butcher, Harrison, and Ross (2012) report similar findings about the Australian market for governmental audits, where competition increased after the introduction of mandatory tendering.

In summary, a limited number of field studies study and find some variation in RFP processes despite practice guides depicting a relatively standardized and formal procedure. Furthermore, archival studies of US and Australian governmental audit settings show that mandatory tendering policies, such as periodic RFP issuance and audit committee oversight, lead to a more concentrated market, higher quality specialist firm hiring, and increased audit fees

3.2.2. Audit Proposals

From the auditor's perspective, an RFP is the start of a competitive bidding process through which they may win new business – important to ensure profitability and long-term survival. The auditor's bid must reflect the expected costs of the engagement, adjusted for associated risks, and a reasonable profit (Blankley, MacGregor, and Mowchan 2021). When partaking in a bidding process, auditors also must avoid suffering the winner's curse: being worse off due to winning the bid (e.g., earning lower than expected profits or incurring reputational damages) because the engagement is awarded to the auditor most optimistic about its costs and risks (Blankley et al. 2021; Hobson, Marley, Mellon, and Stevens 2019).

Experimental evidence from Hobson et al. (2019) suggests that the winner's curse may drive low-balling in the market for audit services.[16] That is, auditors' low-balling arises due to their failure to correctly estimate the true costs and risks of the engagement (i.e., their bidding strategy is suboptimal). Of course, low-balling can also be a deliberate pricing strategy of auditors, trying to undercut one another to attract clients. In Fiolleau et al.'s (2013) case study, prospective auditors differentiated their proposals by offering a range of fees, and the client company ultimately selected the lowest fee proposal, despite management and the audit committee explicitly claiming that lowering the fee was not their priority. Goddard and Schmidt (2021) report that competing auditors commonly engage in low-balling, thus, many board members expect audit fees to decrease when changing auditors, even though they perceive initial fee discounts as negative for audit quality.[17] In contrast to speculations by the PCAOB (2011), Cameran et al. (2015) also found that even under mandatory rotation, auditors

[16] The term low-balling refers to the practice of offering fees below costs in the initial year of an engagement (DeAngelo 1981).

[17] A recent paper by Barua, Lennox, and Raghunandan (2020) argues that findings of audit fee discounting in initial year audits in the US are attributable to measurement error and that there is no evidence for low-balling.

engage in low-balling. Conversely, Elder and Yebba (2020) report that the introduction of a formal RFP process in the New York school district audit market led to the emergence of additional industry specialists who could charge higher fees. In governmental audit settings, mandatory tendering policies often restrict auditors from providing fee information in their bids (Hackenbrack, Jensen, and Payne 2000; Jensen and Payne 2005). With bid restrictions, Big 4 firms participated in the US governmental audit market, and audit fees and audit quality were high. Without the bid restrictions, the Big 4 left the market, but non-Big 4 specialization emerged, and quality was unchanged (Hackenbrack et al. 2000; Jensen and Payne 2005).

In a working paper, Baumann, Ratzinger-Sakel, and Tiedemann (2019) examined the other temporal end of the auditor-client relationship, namely when incumbent auditors face a tender in the upcoming period. They find that incumbent auditors (particularly Big 4 auditors) facing a tender charge higher audit fees but do not provide higher quality. In contrast, examining incumbent versus competing auditor behaviors for publicly listed companies, Hallman, Kartapanis, and Schmidt (2022) find incumbents perform higher quality audits and reduce their fees modestly during bidding years.

Auditors interact intensively with clients during this step of the selection process, so they can adapt their proposals to the specificities of the clients (Taminiau and Heusinkveld 2017). That is, auditors use their knowledge to tailor their proposals to suit the specific needs and preferences of the client. RFPs are customarily written in general terms, making relational activities between auditors and clients necessary to clarify expectations and selection criteria (Taminiau and Heusinkveld 2017). First and foremost, this includes understanding the reason behind the company's motives for starting a tender process, but also relates to the broader contextualization of the RFP (e.g., background information on the company, the [potentially contradictory] expectations within the selection committee, and important project issues). Fiolleau et al. (2013) report that the auditors, in their case, tried to convey a commitment to the client in their proposals (e.g., by signaling a willingness to relocate audit personnel). They also report that all auditors made extensive attempts to convey distinct expertise in their proposals, but management and the audit committee perceived no differences (see also Free et al. 2021), despite depth of expertise being the main attribute driving their search for a new auditor. In the context of US government audits, Chang and Stone (2019) found some evidence that increased readability of auditors' proposals improved their likelihood of winning the engagement. There is also some evidence that Big 4 auditors can potentially distinguish themselves from non-Big 4 auditors through their more extensive PCAOB inspection expertise, which appears to dominate managers' evaluations of auditors during a selection process (Bhaskar, Carlisle, Hux, and Zimmerman 2021).

There is limited evidence on the specific content of audit proposals and the criteria used for their evaluation. Some studies indicate that auditors attempt to differentiate themselves through their proposals by highlighting their expertise or commitment and by adopting strategic pricing approaches. However, it appears that companies often struggle to effectively distinguish between these proposals. Additionally, there is some evidence that the proposals' readability can favor their reception and evaluation.

3.2.3. Presentations

After auditors have submitted their proposals, clients must decide which auditors to invite for presentation and the practical modalities of these presentations (e.g., format, identifying attendees). Best practice guidelines stress the importance of these presentations and suggest they are used to assess auditors' technical competence, ethics and independence, and ability to challenge management, among other things (e.g., Deloitte 2016; FRC 2017; ICAS 2018; KPMG 2018). They also suggest that the whole audit committee be present during presentations. Further, they acknowledge that the format of such presentations may vary or that firms may even choose not to hold formal presentations at all but instead use Q&A sessions or other alternatives such as workshops.

There currently exists very little research on the presentation step of the auditor selection process. In Fiolleau et al.'s (2013) case study, all Big 4 auditors submitted a bid and were subsequently invited for presentations. Taminiau and Heusinkveld's (2017) field study does not provide any evidence on clients' choice of which prospective auditors to invite, but it does give some insight into clients' expectations and what they pay attention to. This seems to be mostly "qualitative" factors, such as work relationships and the auditors' "fit" with the client. This also highlights that presentations, even more so than audit proposals, offer opportunities for impression management (Taminiau and Heusinkveld 2017).

Further, these two field studies suggest that presentations are typically organized on a single day and last around 90-120 minutes (including Q&A). In Fiolleau et al.'s (2013) case, all audit committee members attended presentations – consistent with best practices – as did the other selection committee members. Taminiau and Heusinkveld (2017), however, report variation in the people attending, with at least the chairman of the AC, the CFO, the chief controller, and the head of procurement attending. Taminiau and Heusinkveld (2017) also suggest that many clients find it important that the entire audit team is present, which typically would entail the lead engagement partner, the senior manager(s), and potentially an IT or CSR auditor. In Fiolleau et al.'s (2013) case, the national CEOs of the nonincumbent firms were also present to gesture their priority treatment to the client.

Overall, very little is known about the presentation phase, which is notable given that a small number of field studies provide evidence on the perceived equivalence of audit firms, highlighting the importance of focusing on the individual partner and other audit firm personnel.

3.3. Deliberation and Recommendation

Best practice guidance suggests that auditors' proposals and subsequent presentations should be evaluated objectively and well-documented. After deliberation, the selection committee makes a recommendation to the board, who in turn present their decision to the shareholders. It is also recommended that feedback be provided to the bidders about the decision made.

3.3.1. Evaluation of Prospective Auditors

Auditor evaluation criteria may be explicit, in the form of scorecards, or implicit in that they are not formally stated but heavily weighted in the minds of individual decision-makers. Best practice guidelines suggest that companies establish, prioritize, and apply relevant criteria for determining whether prospective auditors fulfill their needs and preferences. Although extensively researched in the auditing literature, fees should never be the primary decision factor; practice guidelines advise considering a fair price for the quality delivered (AICPA 2018; Deloitte 2016; FEE 2016; FRC 2017; KPMG 2018). Although not mentioned in most evaluation practice guidelines, field studies report on the importance of work relationships and specific audit partners' organizational "fit" (Dodgson et al. 2020; Esplin et al. 2018; Fiolleau et al. 2013; Free et al. 2021). Research on auditor choice identifies several client and auditor characteristics (e.g., ownership structure, industry expertise) that influence whether a company selects a particular auditor (Habib et al. 2019). Recall that we are interested in the consideration given to such criteria in the auditor selection process. Thus, we do not discuss papers that merely associate auditor or client characteristics with auditor choice, absent examination of the auditor selection process. Next, we synthesize the literature on the following relevant auditor selection criteria: (1) pricing and expertise and (2) attributes of the engagement partner and organizational "fit."

3.3.1.1. Pricing and Expertise

Historically, relatively high audit fees were an important driver of companies' decisions to hire and switch auditors (Stefaniak et al. 2009). However, fee importance may be lower for larger companies and may have declined over time. Some evidence suggests that companies do not consider audit fees an important decision-making criterion (e.g., Almer, Philbrick, and Rupley 2014; Taminiau and Heusinkveld 2017). Further, using more sophisticated procurement processes is associated with a lower likelihood of Portuguese municipalities focusing only on price (Marques and Pinto 2019). Yet, auditors adopt pricing strategies when competing for clients, such as pricing the audit to correspond with planned engagement efforts (Johnstone, Bedard, and Ettredge 2004).

Companies frequently cite auditor expertise (i.e., having experienced personnel, specialists, or a critical mass of expert personnel) as the reason for initiating an auditor selection process (Stefaniak et al. 2009). Expert auditors can help companies compensate for weaknesses in their accounting personnel. For example, Jensen and Payne (2003) find that companies that do not hire internal auditors tend to compensate by selecting external auditors with relatively high industry expertise. Although many studies find an association between auditor choice and auditor expertise, there is little evidence on how companies evaluate this expertise or how auditors distinguish their expertise from others. Audit partners indicate that they sometimes need to relocate to maintain industry expertise and continue serving clients in the same industry (Daugherty et al. 2012). Jensen and Payne (2005) report that when entities focus on expertise rather than fees, they are more likely to select a specialist auditor.

Research has also examined the alignment between companies' auditor choices and comparable companies' choices as a signal of specialized expertise. One consideration for companies is the risk of information spillover between rival firms, where the auditor could be the conduit, which leads companies to avoid selecting the auditor of their rival (Aobdia 2015). This finding contrasts with evidence that more similar peer companies have a greater propensity to select the norm auditor (i.e., the auditor engaged by the greatest proportion of a company's peers) (Li, Sun, and Ettredge 2017) and to share the same auditor (Bills, Cobabe, Pittman, and Stein 2020), suggesting that the benefit of auditor expertise outweighs the risk of information spillover in relevance to evaluating prospective auditors. Research further supports that companies value auditor knowledge of related companies, showing that companies align with their main supplier's Big 4 auditor choice (Corten, Steijvers, and Lybaert 2018).

Substantial evidence links client and auditor characteristics to auditor choice, though there is limited research on how companies evaluate these factors during selection (Habib et al. 2019). Additionally, some evidence suggests that fees are not the primary criterion in the auditor selection process.

3.3.1.2. The Individual Engagement Partner and "Fit"

Some qualitative studies have examined the intangible qualities of organizational fit or alignment between the proposed audit partner and the client company. Audit committees generally consider audit firms, especially the Big 4, broadly equivalent, shifting much of their evaluation from the audit firm to the individual partner (Almer et al. 2014; Beasley et al. 2009; Free et al. 2021). Dodgson et al. (2020) found that management's preferences for audit partner "chemistry" dominate client-partner matching evaluations.[18] Perhaps surprisingly, not just management but also the audit committee heavily values the quality of the relationship with the audit partner (Free et al. 2021). Fiolleau et al. (2013) report that the audit committee chair spoke with references to gain insights into specific audit partners' working styles, and the bidding firms sought to align engagement team characteristics with the CFO. Research also suggests that audit firms remove an engagement partner with a poor working relationship with the client and replace them with one who is a better match for the client (McCracken, Salterio, and Gibbins 2008). Consistent with focusing on the individual audit partner, Pittman, Wang, and Lu (2022) find that in mandatory partner rotations, partners who have stronger connections with the incumbent are more likely appointed as successors, and strong-connection successors are associated with equal or higher audit quality. This focus on "fit" seems even stronger in the context of private companies' auditor selection (Esplin et al. 2018).

In conclusion, there is some evidence that audit committees view audit firms, particularly the Big 4, as broadly equivalent, shifting their focus to the individual audit partners. Relatedly, some studies show the importance of a good working relationship between management and the audit partner and specific audit partners' organizational "fit."

3.3.2. Shareholder Voting

Experimental evidence suggests that permitting investors a greater say in auditor selection increases the demand for and likelihood of high-quality auditing. Specifically, transferring the

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[18] A related stream of research examines the matching of audit partners and clients based on homophilous preferences (i.e., people's tendencies to associate with similar others). Such research shows that the selection of specific audit partners increases if they share certain attributes with the client's top managers and directors, such as ethnicity (Berglund and Eshleman 2019) and gender (Lee, Nagy, and Zimmerman 2019).

power to hire and fire the auditor from managers to investors reduces objectivity violations (Fatemi 2012; Mayhew and Pike 2004), suggesting increased auditor independence. Replacing auditors' economic accountability to managers with psychological accountability to investors also increases audit quality (Hurley, Mayhew, and Obermire 2019).

In the EU, Directive 2006/43/EC delegated final responsibility for appointing the auditor to the shareholders (or members of the general meeting for private companies). In the US, no such legal requirement exists, but it is considered good corporate governance practice to ask shareholders to ratify the auditor selected by the audit committee. Shareholder ratification is a monitoring mechanism, increasing auditors' accountability towards shareholders by expanding the latter's role in the auditor selection process (Dao et al. 2012; Krishnan and Ye 2005). Consistent with the earlier discussed experimental evidence, Dao et al. (2012) provide evidence from the US audit market that shareholder ratification is associated with audit quality, namely lower abnormal accruals, and fewer restatements.

Shareholder voting on auditor ratification has become common among US public companies (ACAP 2008; Cunningham 2017). Companies are more likely to seek shareholder ratification when they are larger, have more financial expertise on their audit committee, have a Big 4 auditor, purchase more non-audit services, are audited by the same auditor for longer periods, and when shareholder satisfaction with the board is higher (Dao et al. 2008; Krishnan and Ye 2005; Tanyi and Cathey 2020). When companies seek shareholder approval on auditor selection, shareholders rarely vote against the recommended auditor.[19] Raghunandan and Rama (2003) attribute this to large audit firms' strong reputations, shareholders' lack of ability to distinguish auditors from one another, and shareholders' belief that their actions will not make much of a difference. This may seem to suggest that shareholder voting on auditor ratification is inconsequential. However, research shows that even small increases in the proportion of votes against ratification lead to questions from the audit committee (Dao, Mishra, and Raghunandan 2008), subsequent auditor dismissals (Barua, Raghunandan, and Rama 2017; Tanyi and Roland 2017), and subsequent auditor effort and audit quality (Tanyi, Rama, Raghunandan, and Martin 2020). Further, there is evidence that the proportion of votes against the auditor increases with the ratio of non-audit fees (Raghunandan 2003; Raghunandan and Rama 2003; Mishra, Raghunandan, and Rama 2005; Tanyi and Cathey 2020), longer auditor

[19] Research reports that, on average, the rate of shareholders voting against the auditor is only around 2-3% (Barua et al. 2017; Cunningham 2017; Dao et al. 2008; Raghunandan and Rama 2003). Some anecdotal evidence, however, suggests that the proportion of votes against auditor ratification is on the rise, with some instances where 25% or more of the shareholders voted against (Audit Analytics 2021; The Wall Street Journal 2022).

tenures (i.e., 15 or more years) (Dao et al. 2008; Dunn, Lundstrom, and Wilkins 2021; Tanyi and Cathey 2020; Tanyi, Rama, and Raghunandan 2021a), when the auditor is a non-Big 4 firm (Tanyi and Cathey 2020), when there are signs of poor audit quality (e.g., restatements) (Hermanson, Krishnan, and Ye 2009; Liu, Raghunandan, and Rama 2009; Tanyi and Cathey 2020; Tanyi, Rama, and Raghunandan 2021b), and when proxy advisors recommend voting against (Cunningham 2017; Tanyi and Cathey 2020). Recommendations by proxy advisors are mainly driven by concerns about auditor independence and audit quality (Cunningham 2017).

Overall, there is strong evidence that shareholder voting increases audit quality. Additionally, research suggests that votes against auditor ratification mainly stem from concerns about auditor independence and poor audit quality, suggesting that these “against votes” contain useful information.

3.3.3. Government and State Decision Authority

Regulatory reforms have moved towards reducing management’s influence on the auditor selection process by empowering audit committees and shareholders. However, auditors continue to be hired and paid by the companies they audit, which “creates an inherent conflict of interests” (Gavious 2007, p. 451). Some academics propose resolving this tension through a system in which the hiring and firing of auditors is taken away from companies (e.g., Dontoh, Radhakrishnan, and Ronen 2004; van Brenk, Renes, and Trompeter 2020).

Two archival studies have exploited specific institutional settings to examine what happens if auditors are not appointed by their auditees. Specifically, the regulatory authority designates auditors for firms that are deemed “problematic” (i.e., firms with strong incentives and/or high potential for opportunistic earnings management) in Korea and for state-owned enterprises ultimately controlled by the central government (CSOEs) in China. Firms with designated auditors are associated with lower discretionary accruals in Korea (Kim and Yi 2009) and China (Chi et al. 2013). Although both studies used relatively large samples, they provide only indirect evidence on the potential benefits of limiting management’s influence over the auditor selection process because they rely on data from particular subsets of firms. A quasi-experimental study by Shim, Pae, and Choi (2020) provides corroborating evidence that auditor designation by the Korean regulator leads to less aggressive auditor decisions. Similarly, an experiment by Tang, Ruan, and Yang (2017) among Chinese auditors shows that regulatory designation of auditors improves their independence.

Conversely, Ruhnke and Schmidt (2016) find that German management representatives and supervisory board members do not expect auditor appointments by an independent regulator to increase the benefits of audits, such as client-specific expertise and knowledge, professional competence and expertise, independence, professional skepticism, and reputation. This casts light on different views in different regulatory regimes. In addition, governments may have political ties with companies, and some evidence suggests that auditor selection is influenced by the termination of corporate political connections (He, Pan, and Tian 2017), governmental shareholdings (Bagherpour, Monroe, and Shailer 2014), and militarily-connected directors (Harymawan 2020).

In conclusion, there is some evidence that governmental auditor designation increases audit quality. However, most research on this topic comes from stringent regulatory environments, so it is unclear if the findings generalize to other institutional settings. Governments can also influence the auditor selection process through other ways, such as political connections, shareholdings, and militarily connected auditors. Due to the limited number of studies on this topic and the specificity of their research settings, one should be careful to generalize these results.

4. Commentary on the Literature and Future Research Opportunities

Table 1.3 summarizes the main findings from our literature review and formulates potential research questions to be explored by future research. It is clear from our review that some aspects of the auditor selection process have been studied much more extensively than others. In this section, we first offer some broad comments on this literature and then proceed to discuss some more specific opportunities for future research relating to the different features of the auditor selection process.

4.1. Tendering and Auditor Independence

In some jurisdictions, audit retendering is mandatory after a specified tenure period has elapsed with the incumbent auditor, while in others, tendering is voluntary and occurs as needed or desired.[20] Debates on mandatory rotation and retendering highlight potential benefits from greater auditor independence and a "fresh pair of eyes" performing audit work, while concerns include increased audit costs, reduced expertise, and auditor susceptibility to pressure from management (Allam, Ghattas, Kotb, and Eldaly 2017).

[20] Examples of jurisdictions with an audit tendering requirement (or retendering, where the incumbent auditor is eligible to be reappointed) include the EU and the UK, with mandatory tendering for public-interest entities.

Overall, the existing research evidence makes us skeptical that regulatory interventions in the auditor selection process have been successful in increasing auditor independence. Practitioners and regulators suggest the audit committee should be the most important or even sole decision-maker in the auditor selection process (FEE 2013; FRC 2017; KPMG 2018; SOX 2002). Evidence suggests that managerial influence is associated with lower audit quality and that "good" audit committees improve audit quality. However, experimental evidence by Gold et al. (2018) suggests that investors consider audit committees' hiring power only as relevant when it is mandatory for companies to periodically consider their auditor appointment (i.e., mandatory rotation or tendering). Under voluntary tendering, investors seem to anticipate that the incumbent auditor will be reappointed. In practice, however, management appears to be the key player driving the auditor selection process, both for public companies (e.g., Cohen et al. 2010) and for private companies (Esplin et al. 2018). Audit practitioners and academics also caution that routine tendering can incentivize audit firms to dedicate efforts to compete for prospective clients (PwC 2011) and may not increase auditor independence (Fiolleau et al. 2013). Weighing the costs and benefits of mandatory tendering is challenging because they depend on particular stakeholder groups' interests. Board members perceive the tendering process as costly (Goddard and Schmidt 2021). Furthermore, while institutional investors support mandatory tendering because of expected benefits in auditor independence and audit quality, auditors (especially the Big 4) tend to refute this claim (Allam et al. 2017).

Hence, future research should investigate ways to increase audit committee involvement, and how to overcome the adverse effects of management influence while considering management's input to achieve a well-coordinated auditor-client relationship. It remains unclear what drives audit committee involvement, how limited involvement is justified (by audit committee members themselves and by management) against the backdrop of regulatory requirements and best practice guidelines, or how disagreements between and within different parties are resolved. Shareholder involvement also seems to improve audit quality, so exploring when and how shareholders have the most impact on auditor selection seems worthwhile. Field studies and experiments can shed light on relevant conditions. Further, more research is needed on the potential benefits of moving auditor selection out of companies' decision authority. It is currently unclear if these benefits are due to the peculiarities of the Chinese and Korean settings or if they generalize to less strictly regulated markets.

TABLE 1.3

Summary of Main Findings and Questions for Future Research

		Key findings from existing literature	**Suggested research questions for future research**
Demand for auditing and causes of auditor switches *Triggers the selection process*		* Extensive research on institutional and client factors associated with the hiring of particular auditors (see reviews by DeFond and Zhang 2014; Habib et al. 2019; Stefaniak et al. 2009). * Substantial evidence that demand for auditing stems from client incentives and changes in incentives lead to auditor switching.	* How do reasons for hiring/switching auditors affect subsequent procurement procedures (e.g., selection criteria, timing, participation of the incumbent auditor)?
	Steps and timeline of the selection process		
Several months to up to two years	**1. Planning**		
	When will the selection process take place?	* Some evidence of variation in the initiation of the auditor selection process. * Some evidence that timely processes improve chances of selecting a high-quality auditor.	* How does timing affect the selection process? *For example: How much time do companies need to allocate to selecting an auditor, when should they initiate this process? Does it affect auditor-client misalignment?*
	Who are the key decision-makers? ○ Audit committee (chair) ○ CFO / head of accounting / …	* Extensive research on all parties involved in the auditor selection process. Fairly good understanding of the characteristics that make up a good audit committee and the characteristics of management that matter. * Substantial evidence that management is still the most influential body in the auditor selection process, contrary to best practices and regulations. * Some evidence that board members influence the selection process by bringing knowledge and experience to the selection committee. * Audit committee involvement and oversight may vary across different firm types, but the bulk of research examines large, public companies.	* How do characteristics of different actors exactly shape the auditor selection process? *For example: In what way does the auditor selection process change due to specific characteristics such as board size or audit committee financial expertise.* * What role do audit committees play in curtailing opportunistic auditor switching? * What drives audit committee involvement in the auditor selection process? *For example: Can audit committee involvement be increased? Can the negative effects of management influence be overcome?* * How is limited audit committee involvement justified (by audit committee members themselves and by management)? * How does management exercise its influence on the auditor selection process and how does this affect auditors' ability to challenge management and remain independent? * How does government involvement affect the auditor selection process? *For example: Under what circumstances does auditor selection by a (semi-)governmental body improve audit quality?*

	Which auditors to invite for tender? ○ Independence, non-audit service providers ○ Group/subsidiary considerations ○ "Pre-selection" of partners	* Scant research about which auditors are invited for tender. Preliminary evidence on interaction and relationship building before the RFP. * Investors expect the incumbent auditor to be reappointed when tendering is voluntary. * Some evidence that the parent company's management and their auditor influence the auditor selection of their subsidiaries.	* What role does audit partner rotation play in the auditor selection process? * How do regulatory requirements shape the auditor selection process through their effects on auditor-client relationship dynamics? *For example: Cooling-off requirements, restrictions on non-audit services.*
	2. Audit proposals		
	What information is included in the RFP? What information is included in audit proposals? ○ Information about entity and engagement ○ Transparent objectives and criteria ○ Key dates and events (e.g., presentations) ○ Access to information (e.g., data room) ○ Access to management/company personnel	* Small number of field studies suggest variation in RFP, although practice guides portray a relatively standardized, formal process. * Companies aim to balance audit service quality needs and costs, which requires open competition, access to relevant information, and a well-specified process. * Scant evidence on content of proposals or how they are evaluated. * Some evidence that auditors try to differentiate themselves through their proposals – conveying expertise or commitment – and adopt pricing strategies. However, companies may be unable to differentiate. * Evidence for favorable effects of proposals' readability.	* How do companies develop and implement their procurement procedures? *For example: To what extent do selection committees consult and tailor best practice guidelines?* * What factors increase the chances of an auditor winning a bid? *For example: How much variation is there in bid documents between and within audit firm? To what extent do decision-makers attend to and process the presence/absence of information in the bid documents?*
Around three months (ranging from about two to six months)	**3. Presentations**		
	○ Format and focus (e.g., technical issues) ○ Audit firm personnel to attend - Lead audit partner - Specialists - Other key team members ○ Client firm personnel to attend - Audit committee members - CFO, …	* Almost no evidence on the presentation phase of the selection process. * Small number of field studies report evidence on the perceived equivalence of audit firms, necessitating focus on the individual partner (and other audit firm personnel).	* What strategies do decision-makers and auditors employ in interpersonal interactions? * How are the pre-defined criteria tested during interviews and presentations?
	4. Deliberation and recommendation		
	○ Assessment criteria - Quality (industry knowledge, independence, reputation …)	* Substantial evidence that links client and auditor characteristics to auditor choice (see Habib et al. 2019).	* How do companies decide on criteria to evaluate prospective auditors and implement their process to select a new auditor? *For example: How do different decision-makers translate*

	- Fees - People/working relationship (‘fit’) - Other: audit approach, added value (e.g., data analytics, network connections), … o Assessment procedure - Scorecard, matrix, rank	Much less literature on how such factors are evaluated by companies during their selection process. * Some evidence that fees are not an important criterion. * Some evidence for the importance of work relationships and specific audit partners’ organizational “fit”.	*concerns about audit quality into selection criteria and hiring decisions, especially if they hold different conceptions of audit quality? Do companies consider subtle cues of audit quality in their evaluation of auditors, or do they only attend to and process vivid signals of low quality? Do criteria differ between different parties in the firm, and how are such differences reconciled?* * To what extent are prospective auditors evaluated at the firm, team, and partner level? * How do companies explicitly and explicitly evaluate prospective auditors? *For example: How are different attributes weighted and different criteria applied by decision-makers? How do decision-makers consider subjective criteria versus objective criteria?* * Does auditor independence play a more prominent role in some cases than others? *For example: Is there heightened scrutiny by audit committees or shareholders in cases where the process is initiated because of auditor-client disagreements?*
	o Approval by the board of directors o Shareholder voting o Feedback to bidders	* Strong evidence that shareholder voting increases audit quality. * Some evidence that votes against auditor ratification mainly stem from concerns about auditor independence and poor audit quality.	* How do different actors involved in the selection process resolve disagreements about how to evaluate prospective auditors? *For example: Disagreement among members of the audit committee or between management and the audit committee.*
	Outcomes and consequences of hiring/switching auditors o Auditor characteristics o Market reactions o Transition to new auditor	* Extensive research on consequences of auditor hiring, choice, and switching (see reviews by DeFond and Zhang 2014; Stefaniak et al. 2009). * Strong evidence that transitions are disruptive.	* Which audit procurement procedures ease the transition to the new auditor? * What are the effects of using formal tendering processes? *For example: On audit quality, on audit fees, on auditor-client misalignment.* * Do specific features of the auditor selection process affect auditors’ subsequent behavior and audit outcomes? * How does management involvement in the selection process affect the power dynamics in audit-client interactions after appointment? * How do audit partners maintain their independence if “fit” and good working relationships were important considerations during the selection process?

This table provides an overview of the main findings and identified research questions, organized by the framework from Figure 1.1.

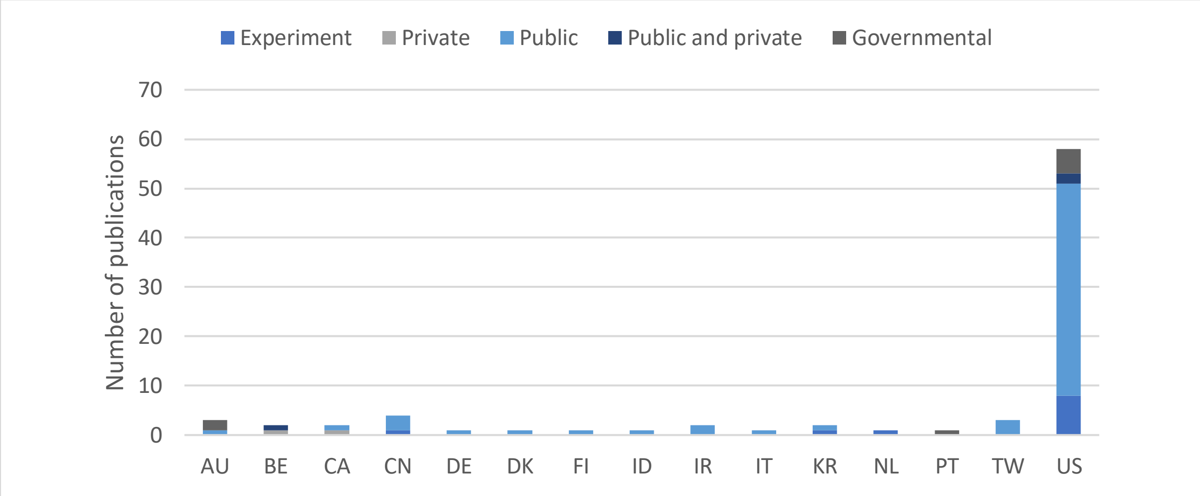
4.2. The Predominant Focus on Listed Companies and US Data

We identify a few interesting observations about the context in which most of the research on the auditor selection process has been conducted, as shown in Figure 1.4. First, most studies on the auditor selection process have focused on public companies (59 out of 83 studies that specified their setting [71%], see Figure 1.4: Panel A). While there is considerable literature on audit demand in private firms (for a review, see Vanstraelen and Schelleman 2017), there is a dearth of research on tendering by private companies, as only five studies (of the 83 that specified their setting, see Figure 1.4: Panel A) used data on private companies, and only two focused exclusively on the private company setting. Likewise, we have been unable to identify any research related to the auditor selection process as practiced by non-profit organizations, despite specific attention by practitioners to auditor selection by non-profits (e.g., ICAS 2018).

Second, the majority of studies originate from the US (67%, see Figure 1.4: Panel B). Prior research shows that cross-cultural differences (e.g., collectivism, religiosity, and societal trust) and environmental factors (e.g., the legal environment and auditing standards) influence individuals' behavior and decisions (e.g., Bik and Hooghiemstra 2018; for a review, see Nolder and Riley 2014). Therefore, cross-cultural research to ascertain if prior findings generalize beyond the US seems a fruitful avenue for future research. Third, studies on the US audit market have relied predominantly on archival data (45 out of 61 [74%] partly or exclusively). At the same time, 12 out of 30 (40%) of the studies conducted outside of the US have employed other data and study methods (e.g., field studies, experiments). This suggests that there may be research opportunities for archival researchers to pursue outside of the US. For further insights into the auditor selection processes conducted by US-listed companies, the most promising opportunities will likely come from access to proprietary data such as audit firms' bid documents and presentations.

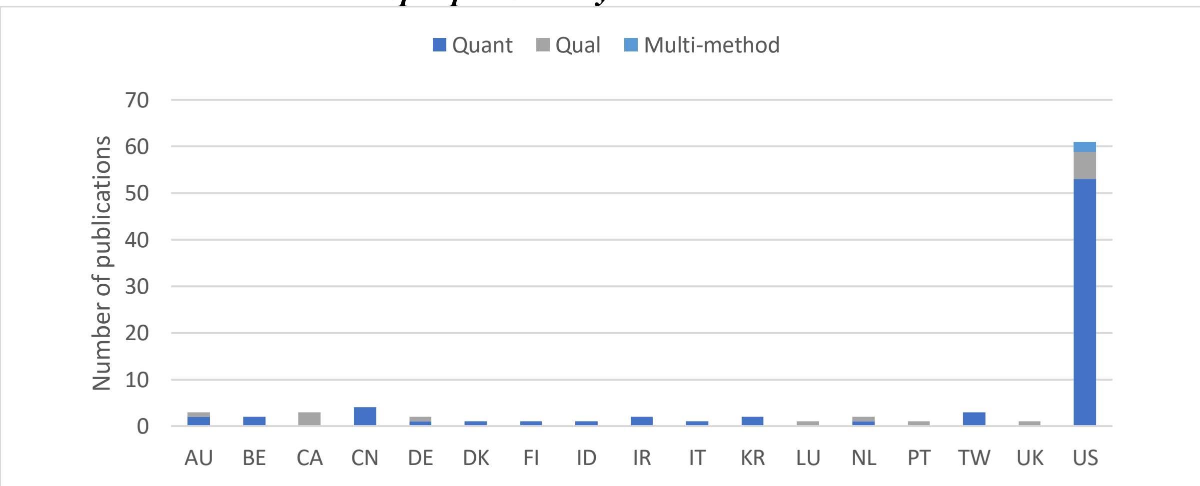
FIGURE 1.4
Overview of Research Methods and Setting

Panel A: Research Settings Split per Country



Setting	AU	BE	CA	CN	DE	DK	FI	ID	IR	IT	KR	NL	PT	TW	US	Total
Experiment	0	0	0	1	0	0	0	0	0	0	1	1	0	0	8	11
Private	0	1	1	0	0	0	0	0	0	0	0	0	0	0	0	2
Public	1	0	1	3	1	1	1	1	2	1	1	0	0	3	43	59
Public & private	0	1	0	0	0	0	0	0	0	0	0	0	0	0	2	3
Governmental	2	0	0	0	0	0	0	0	0	0	0	0	1	0	5	8
Total	3	2	2	4	1	1	1	1	2	1	2	1	1	3	58	83

Panel B: Research Methods Split per Country



Method	AU	BE	CA	CN	DE	DK	FI	ID	IR	IT	KR	LU	NL	PT	TW	UK	US	Total
Quantitative	2	2	0	4	1	1	1	1	2	1	2	0	1	0	3	0	53	74
Qualitative	1	0	3	0	1	0	0	0	0	0	0	1	1	1	0	1	6	15
Multi-method	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	2	2
Total	3	2	3	4	2	1	1	1	2	1	2	1	2	1	3	1	61	91

Panel A shows the different research settings studied split per country. We excluded studies that did not specify the particular setting. Panel B shows the research methods split per country in our sample. The country codes used are: Australia (AU), Belgium (BE), Canada (CA), China (CN), Denmark (DK), Finland (FI), Germany (DE), Indonesia (ID), Italy (IT), Korea (KR), the Netherlands (NL), Portugal (PT), Taiwan (TW), the United Kingdom, and the United States (US). Both panels are sorted alphabetically.

Fourth, it is quite remarkable that the existing research on auditor selection has paid little to no attention to parent-subsidiary considerations, despite the importance of (multinational) business groups and the challenges of global group audits (e.g., Downey and Westermann 2021). There is only little evidence that the management of a parent company, as well as its auditor, influences their subsidiaries' auditor selection (e.g., Branson and Breesch 2004; Downey and Westermann 2021). Furthermore, we have not been able to identify any studies that have focused on the auditor selection process with a clear focus on business groups and how companies and auditors navigate such additional complexities. There seem to be ample opportunities for future research to explore parent companies' influence on their subsidiaries' auditor selection process.

4.3. Specific Opportunities for Future Research

We do not intend to offer a detailed discussion of all opportunities for future research, which we summarize in Table 1.3; we aim to elaborate on issues that demand particular attention. First, several studies improve our understanding of companies' assessment criteria to evaluate prospective auditors (e.g., pricing, expertise, certain intangible or social qualities). Some studies also show that companies do not always closely follow their stated priorities when evaluating auditors. However, very few studies offer insights into how decision-makers use audit proposals and presentations to try to differentiate between auditors or into the interplay between different evaluation criteria in auditor selection. There is also an absence of evidence on the relative weight of different criteria for auditor selection or how management and audit committees deal with disagreements during this process. For example, do management and audit committee members explicitly account for and communicate about their preferences for intangible criteria such as "fit" or "chemistry," or does this affect the selection process unconsciously? How are such considerations incorporated in formal decision-making (e.g., evaluation scorecards)?

Second, few studies have examined audit proposals and, even less so, presentations – despite their central role in the selection process. Therefore, several important questions remain unanswered, and we urge future research to gain more insights into these aspects of auditor selection. For example, research indicates that auditors respond to client preferences in their bids, but we have very little insight into auditors' strategic considerations or communication strategies (e.g., impression management). Consequently, we do not know if such factors help auditors win proposals. A potential avenue for archival analysis is to obtain a sizeable sample of these proposals, as they are documented and managed by audit firms' business development personnel in their national offices. We also know very little about the micro-level interactions that take place between auditors and clients during these steps of the selection process.

5. CONCLUSION

Reflecting the long-lasting debate about who should have the power to appoint the auditor, there is relatively extensive literature on the different parties involved in the auditor selection process and the characteristics of these parties. The overall evidence suggests that the involvement of audit committees, shareholders, and governments in the selection process leads to the appointment of higher-quality auditors. At the same time, these actors perceive little differentiation between auditors, especially among the Big 4 firms. These observations raise questions about how their involvement in the selection process shapes the timing, procedures, and decision-making processes that eventually lead to the appointment of the auditor.

A smaller body of evidence, primarily from field studies, has investigated clients' RFP processes. Results of these studies show significant discrepancies between tangible, "objective" criteria identified by archival studies as essential inputs of the auditor selection process and more intangible, "subjective" criteria described in field studies. Specifically, field studies highlight that the focus during the auditor selection process is often on the individual audit partner rather than the audit firm. This is remarkable because this emphasis is typically left unmentioned in evaluation practice guidelines and regulatory discussions. Moreover, recent research suggests that such intangible criteria also continue to play a role after appointing a new auditor. They are an essential feature of the auditor-client relationship, a relationship that audit firms carefully plan and manage.

Synthesizing the evidence about the auditor selection process is challenging due to the vast and fragmented research on auditor selection. Archival studies rely on observable auditor and company characteristics to make inferences about auditor selection but offer relatively few insights into how companies select their auditors. Field studies and a few experiments provide more detailed descriptions of selection processes. However, they are rare and often limited in scope or focused on particular settings (e.g., governmental audits), potentially limiting generalizability. Hence, despite its importance, we know relatively little about the process by which companies select their auditor, especially compared to what we know about what happens before and after auditor selection (e.g., determinants of auditor choice). Investigating the auditor selection process is complex because client companies are not required to publicly disclose information on how an auditor is selected (Gold et al. 2018). Therefore, researchers may have to rely on proprietary data or indirect inferences. However, throughout this review, we developed research questions about different features of the auditor selection process that we believe will advance our knowledge about this topic.

Our study is subject to the following methodological limitations. Although we followed best practices to minimize the potential for bias in our research synthesis, we applied judgment throughout our review in determining our search criteria, study relevance, and evidence strength. Some relevant studies may not be included in our review because, for example, they were published in other journals or were not returned by our search terms.

CHAPTER 2. AUDIT PARTNER-CLIENT ALIGNMENT

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Abstract

This study investigates audit partner-client alignment and its effects on audit quality, audit partner tenure, and audit partner changes. We measure audit partner-client alignment as the degree to which an audit partner's prior experiences match specific client characteristics, including (i) size, (ii) financial risk, (iii) IFRS application, (iv) public trading status, and (v) industry. Additionally, we differentiate between alignment in the context of new-client acceptance decisions and existing-client rotations. Analyzing 152,272 company-year observations in Belgium from 2008 to 2019, we find evidence that higher alignment is associated with less income-decreasing total accruals, longer audit partner tenure, and a lower likelihood of audit partner changes. Our results show that audit partner changes, particularly those stemming from within-firm partner rotations, decrease alignment, whereas audit firm-induced rotations do not have such an effect. This study contributes to understanding how audit partner-client alignment influences key audit outcomes and provides insights relevant to regulations concerning audit partner and audit firm rotation and the consequences for audit quality.

Keywords: audit firm portfolio management; audit partner assignment; auditor selection; auditor rotation; audit quality.

Data Availability: The data are publicly available from the sources we identify.

1. INTRODUCTION

We examine the alignment between audit partners and their clients from the perspective of an assortative matching market (Gale and Shapley 1962), whereby both parties interact to reach collectively attractive alignment decisions.[21] In this study, audit partner-client alignment refers to the extent to which an audit partner's prior audit experiences match a prospective client's relevant characteristics, including (i) size, (ii) financial risk, (iii) IFRS application, (iv) public trading status, and (v) industry. Essentially, alignment measures the degree of compatibility between the audit partner's past experiences and the client's profile. Audit firms actively manage their client portfolios (Johnstone and Bedard 2004), consider client preferences when making decisions about partner assignment (Fiolleau, Hoang, Jamal, and Sunder 2013; McCracken, Salterio, and Gibbins 2008), and may assign their "best" partners to their riskiest clients (Kinney 2015). Individual audit partners control alignment as they solicit new clients and negotiate pricing and financial reporting choices (Beattie, Fearnley, and Brandt 2000; Brown and Johnstone 2009; Gibbins, Salterio, and Webb 2001; Ittonen, Johnstone, and Myllymäki 2014; Keune and Johnstone 2012). Clients likely have preferences for specific partners, just as they have preferences for particular audit firms (e.g., Brown and Knechel 2016; Khurana and Rama 2004). These preferences may reflect actual or perceived quality differences across partners (e.g., Gaver and Utke 2019; Gul, Wu, and Yang 2013; Knechel, Vanstraelen, and Zerni 2015) and/or factors such as partner personality, social ties, and industry specialization (e.g., Christensen, Glover, and Wood 2018; Gaver and Utke 2019; Guedhami, Pittman, and Saffar 2014; Lennox and Park 2007).

Understanding audit partner-client alignment is important because it affects audit partners' ability to perform high-quality audits (Guan, Su, Wu, and Yang 2016; Hsieh and Lin 2016). For example, alignment may occur based on risk profile (Amir, Kallunki, and Nilsson 2014) or interpersonal preferences (Fiolleau et al. 2013), both of which may have adverse consequences for audit quality. Specifically, alignment based on risk can result in partners being more tolerant of aggressive accounting (Amir et al. 2014), while organizational fit may impair auditor independence (Fiolleau et al. 2013). Furthermore, users make inferences about financial reporting quality based on auditor reputation (Balsam, Krishnan, and Yang 2003), and audit firm survival depends on

[21] We use the term "(external) auditor" interchangeably to refer to both "audit firm" and "audit partner." However, whenever possible, we specify the most detailed level by using "audit firm" or "audit partner" explicitly. Similarly, we use the terms "client" or "company" to refer to the client company.

prudent client acceptance and continuance decisions (e.g., consider the Andersen-Enron debacle). Some recent research is beginning to recognize the assortative matching aspects of audit partner-client alignment, whereby both parties' collective and simultaneous supply and demand preferences are relevant (Cook, Kowaleski, Minnis, Sutherland, and Zehms 2019). However, Lennox and Wu (2018, p. 24) note that "There is almost no evidence relating to the partner-client matching process" due to a lack of data availability.

We examine audit partner-client alignment for 152,272 company-year observations in Belgium during 2008–2019. We explore whether and how audit partners' *prior* experiences with other clients are associated with *current* matching to new clients. Specifically, we measure alignment as the degree of matching by audit partners possessing prior experience with clients that are large, financially risky, require IFRS expertise, are publicly traded, and are active in specific industries, and clients possessing those characteristics or requiring such expertise. We report evidence that higher audit partner-client alignment is associated with less income-decreasing accruals, longer audit tenure, and a lower likelihood of audit partner changes.[22] Moreover, we find that alignment is lower after audit partner changes induced by within-firm audit partner rotations but not necessarily by audit firm-induced rotations, which do not result in significantly higher or lower audit partner-client alignment.

While prior research on audit firm portfolio management broadly characterizes the nature of how audit firms choose clients, such research generally does not view these choices at the individual audit partner level (an exception is Johnstone (2000) in an experimental context), despite recent recognition regarding the value of doing so (Lennox and Wu 2018). Further, we extend prior research on individual audit partners by illustrating important elements of both the development and application of their expertise in risk assessment and portfolio management (e.g., Knechel et al. 2015; Low 2004). Most notably, the associations are different for audit partner-client alignment involving new-client acceptance compared to existing-client partner rotation, as new-client acceptance does not lead to significantly higher or lower alignment. These results are interesting for discussions about mandatory firm and partner rotation because they suggest an underlying mechanism (audit partner-client alignment) influencing auditor choice, client acceptance, and auditor change decisions. Our findings are particularly relevant because we find some evidence

[22] We use the term audit partner change to refer to all audit partner changes. These changes include within-firm audit partner changes and audit partner changes that result from an audit firm change, which are also separately analyzed.

that audit partner-client alignment is associated with higher audit quality, which offers insights into the ongoing debate of auditor rotations and their audit quality effects. Finally, the results of our study provide insight into the potential importance of endogeneity for studies conducted at the partner level. Endogeneity can be problematic for such studies if the matching between partners and clients is not random (Lennox and Wu 2018).

2. LITERATURE REVIEW AND HYPOTHESES

Audit portfolio management is critical to ensure audit quality and firm reputation. DeAngelo (1981b, p. 197) asserts that auditors' quasi-rents provide 'an incentive to design their client portfolios' through disciplined client acceptance and continuance decisions (e.g., Bell, Bedard, Johnstone, and Smith 2002). Auditing standards support this idea, requiring that auditors only agree to engage clients for whom they can reasonably provide quality services (e.g., IAASB ISA 220). Early work on these decisions reveals that audit firms are strategic in client acceptance and retention, making pricing and personnel resource allocation decisions to yield deliberate client portfolio outcomes. Using archival data, Shu (2000) finds that auditors are more likely to resign as their litigation exposure related to the client increases. Bell, Landsman, and Shackelford (2001) use survey data from a single audit firm and report that auditors adapt to client-related risks by billing for additional effort. Johnstone and Bedard (2003, 2004) use proprietary data to test models of portfolio management decisions, including those relating to client acceptance, continuance, and pricing. Hackenbrack and Hogan (2005) show that an audit firm's inability to charge adequate realization rates is associated with a greater likelihood of resigning from the client. The introduction of the Sarbanes-Oxley Act and the PCAOB's AS5 introduced new dynamics in auditor portfolio management, with a shift towards mitigating misreporting risks (Landsman, Nelson, and Rountree 2009; Schroeder and Hogan 2013) and earnings management more generally (Kim and Park 2014).[23]

Clients themselves have unique preferences for specific auditor characteristics. In the context of auditor-client negotiations around financial accounting choices, a field study by McCracken et al. (2008) reveals that clients have preferences for certain audit partners and that audit firms take such preferences into account when assigning those partners. In another field study, Fiolleau et al.

[23] See also the research on litigation (Krishnan and Krishnan 1997; Venkataraman, Weber, and Willenborg 2008), auditor dismissals (Johnson and Lys 1990; Haskins and Williams 1990), and regulation (Duguay, Minnis, and Sutherland 2018; Ferguson, Pinnuck, and Skinner 2018) with respect to audit firm portfolio management.

(2013) report that a partner's perceived "fit" with a client was essential in the client's selection of their new auditor. The audit partners in their study were often also unwilling to probe the client for information that might improve their risk assessment before accepting the engagement. Chen, Peng, Xue, Yang, and Ye (2016) show that clients can exert pressure on audit firms to assign audit partners they prefer, especially when the client is economically important to the firm, and that such assignments yield subsequent detriments to earnings quality. Li, McNichols, and Raghunandan (2018) report auditor-client matching in IPO markets based on reporting quality. Research also suggests that audit firms consider the preferences of high-profile clients when making partner rotation decisions, and audit firms strategically resign from riskier clients (for recent examples of the latter, see Financial Times 2019). This body of research focuses on audit firm portfolio management at the *firm-level* and does not acknowledge the vital role of audit *partner-level* decision-making. Nonetheless, Lee, Nagy, and Zimmerman (2018) reveal that top management' demographics (gender diversity and experience) are associated with audit partner demographics (gender and experience), suggesting that the partner-client matching process is not random. Collectively, this body of research reveals that clients and audit firms strategically "choose" each other. The current study contributes to the literature by investigating audit partner-client alignment across multiple characteristics: (i) size, (ii) financial risk, (iii) IFRS application, (iv) public trading status, and (v) industry.

We expect that audit partner-client alignment, based on audit partner-specific prior audit experiences and client characteristics, is associated with audit quality. This expectation is supported by a large body of research demonstrating a positive association between audit partner expertise and audit quality (e.g., Bedard and Wright 1994; Chi and Chin 2011; Goldman, Harris, and Omer 2019; Gunn and Michas 2018; Johnstone, Li, and Luo 2014; Owhoso, Messier, and Lynch 2002). Moreover, audit offices with extensive experience managing distressed clients exhibit a significantly lower likelihood of going-concern opinion misclassifications (Beck, Constance, and Li 2024).

In conclusion, we expect audit partners to be better positioned to address audit challenges and mitigate risks when they are well-matched with their clients regarding industry expertise and risk assessment capabilities, thereby improving the overall quality of the audit. We refer to such matching as "audit partner-client alignment," which is the degree of similarity between an audit partner's prior audit experiences and specific client characteristics. As auditor experience is associated with higher audit quality, we expect a similar result for clients engaging with audit partners matching their particular needs.

This discussion leads us to predict the following hypothesis:

H1: Higher audit partner-client alignment is positively associated with higher audit quality.

Additionally, higher domain-specific expertise is related to longer auditor tenure and less auditor switching (Brown and Knechel 2016). Fiolleau et al.'s (2013) investigation of an audit firm rotation resulting from a "bad fit" illustrates that "bad" matches reduce auditor tenure. Furthermore, when there is a mismatch between a client and an auditor, the likelihood of the client replacing the auditor increases (Brown and Knechel 2016; Gerakos and Syverson 2015). An audit engagement is more likely to end early due to poor compatibility. We measure audit partner-client fit with our audit partner-client alignment measure. If a company values an audit partner's specific expertise, having an audit partner whose skills match the company's needs should result in less frequent audit partner changes and longer working relationships. Therefore, we expect that:

H2(a): Higher audit partner-client alignment is positively associated with longer audit partner tenure.
H2(b): Lower audit partner-client alignment is positively associated with a higher likelihood of changing audit partners.

Finally, we advance the literature by studying auditor portfolio management decisions from the perspective of the individual audit partner during new-client acceptance and continuing-client partner rotations. An early example of research adopting this perspective includes Johnstone (2000), who reports the results of an experiment using partners making client acceptance decisions under conditions of varying levels of audit risk, client business risk, and auditor business risk. The results reveal that partners can reliably assess these types of risks, but they have difficulty determining how to adjust their audit planning accordingly. Hsieh and Lin (2016) use publicly available data from Taiwan to show that audit partners with industry expertise are less likely to accept new clients who present either heightened audit risk or client business risk. Amir et al. (2014) show that audit partners' personal risk tolerances affect the composition of their client portfolios; those with criminal convictions have clients with higher financial, governance, and reporting risks than partners without convictions. These studies show evidence of auditors' strategic client acceptance and retention decisions. Complementing these findings, we also know that clients change auditors when there is an auditor-client mismatch (Brown and Knechel 2016; Fiolleau et al. 2013) and that clients often follow their audit partner when the partner moves to a new audit firm (Blouin, Grein, and Rountree 2007; Chang, Choy, Lin, and Koo 2019). Overall, this suggests that the auditor-client matching process is not random. Hence, we expect clients to search for an audit partner with the right expertise and audit firms to assign partners who match the client well. Therefore, we predict that:

H3(a): Audit partner-client alignment is stronger after an audit partner change.

Motivations for audit *partner* rotation include facilitating independence and improving audit quality (Brody and Moscove 1998; Carey and Simnett 2006; Fargher, Lee, and Mande 2008). Of course, such rotations also have costs (e.g., gaining client familiarity across partners within the same firm [Bedard and Johnstone 2010]). Audit *firm* rotations are another means of facilitating these benefits, but they come with even more significant costs (e.g., gaining familiarity for the partner and the entire engagement team, along with assessing and planning responses to unknown risks for which there exists considerable information asymmetry) (Carcello and Nagy 2004). Audit firm rotation may occur voluntarily due to client preferences or involuntarily because of a regulatory firm rotation mandate (Kohler, Quick, and Willekens 2016) or because the prior audit firm resigned. For partner rotations as a consequence of an audit firm rotation, one would expect particularly careful scrutiny about whether or not the new audit firm and its available partners can reliably provide a high-quality audit. Audit firm rotations are perceived as especially costly (Allam, Ghattas, Kotb, and Eldaly 2017; Goddard and Schmidt 2021) and disruptive to the audit in the early years of tenure by lowering audit quality (Cameran, Francis, Marra, and Pettinicchio 2015). Based on this discussion, we expect the relative cost-benefit calculus of partner rotations due to new client acceptance to be more stringent than for within-firm partner rotation decisions. Therefore, we expect that:

H3(b): Audit partner-client alignment is stronger after an audit firm rotation than after a within-firm partner rotation.

3. METHODS

3.1. Institutional Setting

Belgium follows all EU directives regulating the movement of capital, labor, and goods and services and, therefore, has accounting and auditing regulations that are very similar to those in other EU member states (Hardies, Vandenhaute, and Breesch 2018; Vanstraelen and Willekens 2008). Companies in Belgium must obtain an audit of their financial statements by a registered auditor if they meet specific size criteria.[24] Audit firms in Belgium have to comply with International Standards on Auditing (ISAs), including ISQC 1, which requires that they establish a quality control system that, among other things, ensures that the engagement partner has the appropriate competence, capabilities, and authority. ISQC 1 further explains that audit firms should consider whether an individual is suitable to perform the functions of the audit engagement partner, including evaluating knowledge and understanding about (i) the client's industry, (ii) specific subject matters, (iii) the nature and complexity of the engagement, and (iv) regulatory or reporting requirements.

Following approval by the board of directors, the general assembly of shareholders appoints the auditor. For public interest entities, the audit committee makes recommendations to the general assembly for appointing the auditor. Appointments are for renewable three-year periods (Vanstraelen and Willekens 2008). After a maximum of six years, audit partner rotation is required for public-interest entities (Directive 2006/43/EU), with a two-year cooling-off period before the partner can return to the engagement. Client size influences the audit firm-client legal relationship, whereby companies with more than 100 employees must have a works council, a form of governance that implements social legislation. For such clients, the audit partner meets with the works council to discuss economic information and the audit report (de Beelde and Leydens 2002; Vanstraelen and Willekens 2008). The works council also decides whether to approve the (re)appointment of the auditor.

[24] During the first period of our study (2008–2015), these criteria were met if a company exceeded at least two of the following thresholds: (1) turnover (excluding VAT) > 7,300,000 euros; (2) total assets > 3,650,000 euros; and (3) number of employees (yearly average) > 50. In 2016, these criteria changed to (1) turnover (excluding VAT) > 9,000,000 euros; (2) total assets > 4,500,000 euros; and (3) number of employees (yearly average) > 50. If the company belongs to a group that publishes consolidated statements or if the company is a holding or a listed company, these criteria had to be considered on a consolidated basis. Listed companies and companies with more than 100 employees were always considered large.

3.2. Measuring Alignment

We measure audit partner-client alignment with binary similarity coefficients, where higher values generally indicate greater alignment (for an overview, see Brusco, Cradit, and Steinley 2021). This approach assumes that clients select audit partners who share similar attributes and that audit firms allocate partners to clients based on these shared attributes. Specifically, we examine alignment by assessing whether a partner has expertise with a particular client attribute and whether the client possesses this attribute. This leads to four potential outcomes, *a*, *b*, *c*, and *d*, detailed in Table 2.1: Panel A.

We focus on five characteristics on which audit partners and clients can align: client size, financial condition, public-trading status, industry, and IFRS application. The size of the client is a critical factor influencing audit pricing and staffing decisions (e.g., Simunic 1980; O'Keefe, Simunic and Stein 1994). Larger clients are generally more complex and bring about coordination and communication challenges (e.g., Smith et al. 1994). In addition, they may require specialized expertise because of legal and regulatory requirements that apply only to larger companies (Zerni 2012). In our analysis, a client is classified as large (*LARGE* = 1) if it ranks within the top decile of the market in year *t* in terms of size (measured using *LTA*, the natural logarithm of total assets). Correspondingly, a partner possesses expertise in auditing large clients (*LARGE_EXPERTISE_90* = 1) if, in period *t-1*, the partner audited a number of large clients that place the partner within the top 10 percent of all audit partners in that period by the number of large clients audited. Next, we consider financial risk, measured by the *DSCORE*, a bankruptcy score whereby lower values indicate that the company is at a greater risk of bankruptcy. Prior research has shown that audit offices with extensive experience in managing financially distressed clients are associated with delivering higher-quality audits (Beck et al. 2024). A client is financially risky (*FIN_RISK* = 1) if the client is in the top decile of the financially riskiest clients in the market in year *t*. A partner is an expert in auditing financially risky clients (*FINRISK_EXPERTISE_90* = 1) if, in period *t-1*, the partner audited a number of financially risky clients that place the partner within the top 10 percent of all audit partners in that period by the number of financially risky audited. The public listing status of a client (*LIST* = 1) denotes if the client is publicly traded in year *t*. *LIST_EXPERTISE_90* equals one if the partner audited a number of large clients in period *t-1*, which places the partner within the top 10 percent of all audit partners in that period by the number of listed clients audited. Partners develop expertise in auditing such clients, which is associated with enhanced audit quality

(Ittonen et al. 2014). Adopting International Financial Reporting Standards (*IFRS* = 1) is the fourth characteristic we consider. Accordingly, in our main analysis, a partner is an IFRS expert (*IFRS_EXPERTISE_90* = 1) if, in period *t-1,* the partner audited a number of clients preparing their financial statements in accordance with IFRS, placing the partner within the top 10 percent of all audit partners in that period based on the number of IFRS clients audited. Specialized knowledge concerning IFRS is a reasonable expectation for any partner assigned to a client applying IFRS.[25] Finally, we include industry expertise as industry audit specialists provide higher-quality audits (e.g., Balsam et al. 2003; Bell, Causholli, and Knechel 2015; Chin and Chi 2009), and industry expertise is a fundamental characteristic along which audit partners specialize themselves (e.g., Zerni 2012; Goodwin and Wu 2014). A partner classifies as an industry expert (*INDUSTRY_EXPERTISE_90* = 1) if the partner audited a number of clients in a particular industry in period *t-1* that places the partner within the top 10 percent of all audit partners in that period by the number of clients audited in a particular industry.

In Panel A of Table 2.1, we delineate outcomes *a*, *b*, *c*, and *d*. Specifically, outcome *a* signifies the sum of positive matches, corresponding to the number of characteristics that a client possesses and for which the partner has expertise. Outcome *b* indicates the sum of mismatches where the audit partner possesses expertise in a characteristic that the client does not have, reflecting scenarios in which the audit partner has “excessive” experience that is not relevant to the client’s needs. In contrast, *c* represents the sum of mismatches where the client possesses a characteristic in which the audit partner is not an expert, highlighting a lack of necessary expertise on the part of the audit partner and potentially compromising audit quality. Finally, *d* denotes the sum of negative matches, representing the number of characteristics where the partner lacks expertise, and the client does not possess that characteristic. These situations are less informative as they do not indicate a genuine alignment or mismatch in attributes. The outcomes are utilized to calculate the similarity between the audit partner and the client for each observation by employing similarity coefficients.

This study focuses predominantly on asymmetric similarity coefficients because shared presences in are often more informative than shared absences (Brusco, Cradit, Steinley 2021). That is, we are not interested in alignment that occurs because neither the partner nor the client possesses a particular feature, as this does not necessarily indicate a genuine similarity in attributes. The

[25] At the audit firm level, prior research finds that IFRS expertise yields audit fee premia (Lin and Yen 2016; Wieczynska 2016).

empirical analyses incorporate a spectrum of co-occurrence coefficients, as elaborated by Brusco et al. (2021), excluding and including negative matches to ensure robustness in our findings.

Table 2.1: Panel B provides a summary of the alignment variables employed. Our main analysis focuses on the Dice2 coefficient (Dice 1945). This variable represents the ratio of positive matches to the sum of the positive matches (*a*) and negative mismatches where the client attributes equal one (*c*), that is, *a/(a+c)*.[26] Values of the Dice2 coefficient range from 0 to 1, with higher values indicating greater similarity (i.e., higher audit partner-client alignment).

In additional analyses, we also explore other widely recognized co-occurrence coefficients. Further, we categorize a partner as an expert if they rank within the top decile in terms of experience with specific client characteristics relative to their peers; that is, the audit partner audited more clients with that characteristic than ninety percent of all partners in that year. The variables are displayed as *AlignmentVariable_X*, with the alignment variable being one of the variables shown in Table 2.1: Panel B and *X* being the percentage cut-off for partner expertise. Therefore, our main analyses use *DICE2_90* as our alignment variable. We also explore alternative, more lenient, and stringent criteria for defining expertise in sensitivity analyses, with cut-off points at 50 percent, the median, 70 percent, 80 percent, and 95 percent. Table 2.2: Panel A gives an overview of the variables used to create the alignment variable.

[26] As a hypothetical example, *IFRS_EXPERTISE* = 1 and the client uses IFRS (*IFRS* = 1), *LARGE_EXPERTISE* = 1 and the client is not large (*LARGE* = 0), and *FINRISK_EXPERTISE* = 0 while the client is financially risky (*FIN_RISK* = 1), but for the other two characteristics, *LIST* and *INDUSTRY*, the partner is not an expert in a characteristic that the client does not possess. In this case, *a*, *b*, and *c* equal one, and *d* equals two. In this case, the value of the Dice2, calculated by *a/(a+c)*, is 1/(1+1), or 0.5.

TABLE 2.1
Alignment Variables

Panel A: Binary Similarity Matrix		
	$\boldsymbol{Client\ Attribute_j\ is\ equal\ to\ 1}$	$\boldsymbol{Client\ Attribute_j\ is\ equal\ to\ 0}$
$\boldsymbol{Partner\ \ Expertise_i\ is\ equal\ to\ 1}$	$a = number\ of\ positive\ matches$ $a = \sum(PA_i = 1\ \&\ CA_j = 1)$	$b = number\ of\ mismatches\ (PA\ occurence)$ $b = \sum PA_i = 1\ \&\ CA_j = 0$
$\boldsymbol{Partner\ \ Expertise_i\ is\ equal\ to\ 0}$	$c = number\ of\ mismatches\ (CA\ occurence)$ $c = \sum PA_i = 0\ \&\ CA_j = 1$	$d = number\ of\ negative\ matches$ $d = \sum PA_i = 0\ \&\ CA_j = 0$
Panel B: Alignment Variables		
Coefficient Name	**Calculation**	
DICE 2	$Similarity_j = \frac{a}{a+c}$	
JACCARD	$Similarity_j = \frac{a}{a+b+c}$	
GLEASON	$Similarity_j = \frac{2a}{2a+b+c}$	
DRIVER AND KROEBER	$Similarity_j = \frac{a}{\sqrt{(a+b)(a+c)}}$	
SOKAL AND SNEATH 1	$Similarity_j = \frac{a}{a+2b+2c}$	
SORGENFREI	$Similarity_j = \frac{a^2}{(a+b)(a+c)}$	
EUCLIDIAN DISTANCE	$Similarity_j = \sqrt{\sum(PA_i - CA_j)^2}$	

Table adapted from Brusco, Cradit, and Steinley (2021). All similarity variables, i.e., the alignment variables, can take on values between 0 and 1, with higher values indicating a better match. Only the Euclidian Distance variable is a dissimilarity distance variable, meaning that a higher value indicates a worse match. We study these variables because they are the co-occurrence coefficients that do not incorporate negative matches (Brusco et al. 2021). However, we exclude the Driver and Kroeber and the Sorgenfrei coefficients in the analysis because many observations would be deleted resulting from a 0 in the denominator.

TABLE 2.2
Variable Definitions

Panel A: Matching Variables	
Client Attributes (CA)	
LIST	Dummy variable: *LISTED* = 1, in case company *i* is listed in year *t*, and 0 otherwise.
IFRS	Dummy variable: *IFRS* = 1, in case company *i* applies IFRS in year *t*, and 0 otherwise.
FIN_RISK	Dummy variable: *FIN_RISK* = 1, in case company *i* is in the top 10 percent of the riskiest clients in the market (measured using *DSCORE*) in year *t*, and 0 otherwise.
LARGE	Dummy variable: *LARGE* = 1, in case company *i* is in the top 10 percent of the largest clients in the market (measured using *LTA*) year *t*, and 0 otherwise.
INDUSTRY	Dummy variable: *INDUSTRY* = 1, in case company *i* is active in a specific industry (using the NACE two-digit codes) in year *t*, and 0 otherwise.
Partner Attributes (PA)	
LIST_EXPERTISE_X	Dummy variable: *LIST_EXPERTISE_X=1*, in case audit partner *i* audited more listed clients than X% of all partners in that year, and zero otherwise.
IFRS_EXPERTISE_X	Dummy variable: *IFRS_EXPERTISE_X=1*, in case audit partner *i* audited more IFRS applying clients than X% of all partners in that year, and zero otherwise.
FINRISK_EXPERTISE_X	Dummy variable: *FINRISK_EXPERTISE_X=1*, in case audit partner *i* audited more financially risky clients than X% of all partners in that year, and zero otherwise.
LARGE_EXPERTISE_X	Dummy variable: *LARGE_EXPERTISE_X=1*, in case audit partner *i* audited more large clients than X% of all partners in that year, and zero otherwise.
INDUSTRY_EXPERTISE_X	Dummy variable: *INDUSTRY_EXPERTISE_X=1*, in case audit partner *i* audited more clients in the client's specific industry (using the NACE two-digit codes) than X% of all partners in that year, and zero otherwise.
Panel B: Audit Quality Analysis	
Dependent Variables	
GCO	Dummy variable: *GCO* =1 if company *i* receives a going-concern opinion in year *t*, 0 otherwise.
$\|TA\|$	The absolute value of company's *i* total accruals. Total accruals are calculated as follows: $TA_{it} = \Delta CA_{it} - \Delta CL_{it} - \Delta CASH_{it} + \Delta STD_{it} - DEP_{it}$, where $\Delta CA_t$is the change in current assets ($CA_t - CA_{t-1}$), ΔCL_t is the change in current liabilities ($CL_t - CL_{it-1}$), $\Delta CASH_t$ is change in cash ($CASH_t - CASH_{t-1}$), STD_t is the change in the current portion of long-term liabilities ($STD_t - \Delta STD_{t-1}$), and DEP_t is the depreciation and amortization expense. $\|TA_{it}\|$ measures the absolute values of TA_{it}.
Panel C: Tenure, Change and Alignment Analysis	
Dependent Variables	
CHANGENXTYR	Dummy variable: *CHANGENXTYR* = 1 if company *i* changes audit partner in year *t+1*, 0 otherwise.
REALENGAGEMENT	Dummy variable: *REALENGAGEMENT* = 1 if in the placebo analysis, the audit partner-client combination is a real combination.
TENURE3YRS	Dummy variable: *TENURE3YRS* = 1 if company *i*'s audit tenure is longer than three years in year *t*, 0 otherwise.

Panel D: Independent Variables

Test Variables	
ALIGNMENT_VARIABLE (DICE2_90)	Degree of alignment in year t between client and audit partner using similarity coefficients as shown in Table 2.1. In the main analyses, we use *DICE2_90*.
CHANGE	Dummy variable: *CHANGE* = 1 if company *i* changes audit partner in year *t*, 0 otherwise.
NEW	Dummy variable: *NEW* = 1 if company *i* changes audit partner because of an audit firm change in year t, 0 otherwise.
PARTNERROT	Dummy variable: *PARTNERROT* = 1 if company *i* changes audit partner because of a within-audit firm change in year *t*, 0 otherwise.
Auditor-specific Control Variables	
BIG4	Dummy variable: *BIG4* = 1, in case company *i*'s auditor is a Big 4 auditor in year *t*, and 0 otherwise.
CAREER	Number of years since company *i*'s audit partner was certified in year *t.*
CLIENT_IMP_FIRM (CIF)	Ratio of company *i*'s audit and nonaudit fees to audit firm's total fees from all clients in year *t.*
CLIENT_IMP_PARTNER (CIP)	Ratio of company *i*'s audit and nonaudit fees to the individual auditor's total fees from all clients in year *t.*
EXPERIENCE	Number of years since company *i*'s audit partner was certified in year *t.*
FEERATIO	Ratio of company *i*'s audit and nonaudit fees to the auditor year *t.*
LAF	The natural logarithm of company *i*'s audit fees paid in year *t.*
LNAS	The natural logarithm of company *i*'s non-audit fees paid in year *t.*
MALE	Dummy variable: *MALE* = 1, in case company *i*'s audit partner is a male audit partner in year *t.*
OFFICE_SIZE	Number of registered audit partners in the office where company *i*'s audit partner is affiliated in year *t.*
PORTFOLIO	The natural logarithm of company *i*'s audit partner's total audited total assets in year *t.*
TENURE	The number of years the audit partner has audited the client as of period *t.*
Client-specific Control Variables	
AGE	Age of company *i* in year *t* measured in years.
CONSOL	Dummy Variable: *CONSOL*=1 if the company prepares consolidated group accounts; = 0 otherwise as of period *t.*
CURRENT	Company *i'*s current assets over current liabilities in year *t.*
DSCORE	General discriminant score (D-score) of company *i* in year t, measured by using a standardized bankruptcy prediction model developed for Belgian companies (Ooghe, Joos and De Bourdeaudhuij 1995). A higher score indicates a healthier company.
GROWTH	Company *i*'s total assets less beginning total assets, divided by beginning total assets in period *t.*
IRISK	The sum of company *i*'s inventories and receivables scaled by total assets in year *t.*
LEV	Company *i*'s total liabilities deflated by total assets in year *t.*
LIST	Dummy variable: *LISTED* = 1, in case company *i* is listed in year *t*, and 0 otherwise.
LOSS	Dummy variable: *LOSS* = 1, in case company *i* experienced a loss in year *t.*
LTA	The natural logarithm of company *i*'s total assets in year *t.*

MAO	Dummy variable: *MAO* = 1, in case company *i* received a modified audit opinion in year *t*.
OCF	Company *i*'s operating cash flows scaled by total assets in year *t-1*.
PPE_GROWTH	Company *i*'s percent change in gross property, plant and equipment from year *t-1* to year *t*.
PRIOR_GCO	Dummy variable: *PRIOR_GCO* = 1, in case company *i* received a going-concern opinion in year *t-1*, and 0 otherwise.
ROA	Company *i*'s net income divided by total assets in year *t*.
SALES_GROWTH	Company *i*'s percent change in sales from year *t-1* to year *t*.
STD_OCF	The logarithm of the standard deviation of company *i*'s operating cash flow from operations from year *t-2* through year *t*.
STD_SALES	The logarithm of the standard deviation of a company *i*'s sales from year *t-2* through year *t*.
TA_LAG	Company *i*'s absolute value of total accruals in year *t-1*, scaled by total assets in year *t-2*.
WORKSCOUNCIL	Dummy Variable: *WORKSCOUNCIL*=1 if the company has more than 100 employees; = 0 otherwise as of period *t*.

Panels A, B, and C present the dependent variables used in the different analyses. Panel D provides an overview of the test variables and control variables.

3.3. Estimation Models

3.3.1. Audit Quality Models

We test whether audit partner-client alignment is associated with audit quality using two widely used measures: the propensity to issue going-concern opinions (*GCO*) and total accruals (*TA*). We use the following specifications to test our hypotheses. Following prior research (e.g., Hardies et al. 2018; Knechel and Vanstraelen 2007), we estimate the association between audit partner-client alignment and *GCO* for financially distressed firms using Equation [1]:

$$GCO_{it} = \beta_0 + \beta_1 ALIGNMENT\_VARIABLE_{it} + Auditor\ controls_{it} + Client\ controls_{it} + Industry\ and\ Year\ FE + \varepsilon_{it} [1]$$

GCO is a binary variable equal to one if a company received a going-concern opinion. We include client-specific and auditor-specific controls found to be related to the propensity of an auditor to issue a GCO in prior studies (see Carson, Fargher, Geiger, Lennox, Raghunandan, and Willekens 2012).

For our total accruals (*TA*) analysis, we use Equation [2] to calculate the *TA* for each company year. *TA* is the change in non-cash current assets minus the change in current liabilities, excluding the current portion of long-term debt, minus depreciation and amortization, ΔREV_{it} is the revenues in year t minus the revenues in year t-1, ΔREC_{it} is the net receivables in year t minus the net receivables in year t-1, PPE_{it} is the gross property, plant, and equipment in year t, and ROA_{it-1} is the return on assets in year t-1. Recent research argues that modeling accruals with a two-step approach generates biased coefficients and standard errors (Chen, Hribar, and Melessa 2018). Following Chen et al. (2018), we therefore add to the model all the regressors of the following performance-adjusted modified Jones model and the interaction variables between these regressors and industry-year effects:

$$TA_t = \alpha_1 \left(\frac{1}{A_{t-1}}\right) + \alpha_2(\Delta REV_t - \Delta REC_t) + \alpha_3 PPE_t + \alpha_4 ROA_{t-1} + \varepsilon_t \; [2]$$

We control for client-and auditor-related characteristics found to be related to total accruals (e.g., Causholli, Chambers, and Payne 2014; Goodwin and Wu 2015) and estimate the regression in Equation [3], using the absolute value of the total accruals:

$$|TA_{it}| = \beta_0 + \beta_1 ALIGNMENT\_VARIABLE_{it} + Auditor\ controls_{it} + Client\ controls_{it} + Industry\ and\ Year\ FE + Jones\ Model\ Regressors\ x\ Industry - Year\ FE + \varepsilon_{it} \; [3]$$

Table 2.2: Panel B provides variable definitions for the dependent variables of our audit quality models, while Table 2.2: Panel D provides variable definitions for the test and control variables. ε_{it} is the regression error term. In all our models, unless specifically mentioned otherwise, we use robust standard errors adjusted for clustering by company to correct for heteroscedasticity and serial dependence (Petersen 2009). We winsorize all continuous variables at the 1 percent and 99 percent levels. Furthermore, our models include industry (based on two-digit NACE codes) and year-fixed effects.[27]

3.3.2. Tenure and Change Models

Our tenure model is estimated using Equation [4]. *TENURE3YRS* is a dichotomous variable equal to one if tenure exceeds three years. Given that audit mandates in Belgium last for three years, we expect that if a client wants to change audit partners, the client will do so after the first mandate of three years rather than reappointing the audit partner for another three. Similarly, we estimate our audit partner change model using Equation [5]. We expect that lower alignment in the current year leads to an audit partner change the year after. We use auditor and client controls that

[27] NACE is the industry standard classification system used in the EU.

prior literature shows to relate to auditor tenure and auditor changes (e.g., Blouin et al. 2007; Stefaniak et al. 2009).

$$TENURE3YRS_{it} = \beta_0 + \ \beta_1 ALIGNMENT\_VARIABLE_{it} + Auditor\ controls_{it} + Client\ controls_{it} + Industry\ and\ Year\ FE + \varepsilon_{it} \ [4]$$

$$CHANGE_{it+1} = \beta_0 + \ \beta_1 ALIGNMENT\_VARIABLE_{it} + Auditor\ controls_{it} + Client\ controls_{it} + Industry\ and\ Year\ FE + \varepsilon_{it} \ [5]$$

Table 2.2: Panel C delineates the dependent variables used in the tenure, change, and alignment models. Table 2.2: Panel D provides variable definitions for the test and control variables.

3.3.3. Alignment Models

Finally, we estimate Equation [7] to determine whether an audit partner change leads to a better match between the audit partner and the client. We calculate the difference in alignment between the current year and the previous year to measure changes in partner-client alignment in Equation [6]:

$$DIFF\_ALIGNMENT\_VARIABLE_t = ALIGNMENT\_VARIABLE_t - ALIGNMENT\_VARIABLE_{t-1} \ [6]$$

The control variables for Equation [7] and [8] are the same as those for Equation [5]:

$$DIFF\_ALIGNMENT\_VARIABLE_{it} = \beta_0 + \ \beta_1 CHANGE_{it} + Auditor\ controls_{it} + Client\ controls_{it} + Industry\ and\ Year\ FE + \varepsilon_{it} \ [7]$$

Finally, we estimate Equation [8] with separate variables for within-firm partner rotations and partner rotations resulting from an audit firm change to test whether audit partner—client alignment is more pronounced for new client acceptance decisions than for within-firm partner rotation decisions (H3b). *NEW* equals one if the client is new to the audit firm's portfolio and zero if the client is a continuing client from the prior year. *PARTNER_ROTATION* equals one if the partner change is a within-firm partner change:

$$DIFF\_ALIGNMENT\_VARIABLE_{it} = \beta_0 + \ \beta_1 PARTNER\_ROTATION_{it} + \ \beta_1 NEW_{it} + Auditor\ controls_{it} + Client\ controls_{it} + Industry\ and\ Year\ FE + \varepsilon_{it} \ [8]$$

4. Data and Sample Selection

We gathered financial statement data from the electronic database *Bel-First* from *Bureau Van Dijk*. We obtained additional data on audit firms and audit partners from the public register of auditors in Belgium, and we obtained data about the use of IFRS or the requirement to prepare consolidated group accounts from the National Bank of Belgium.

We start our sample with 227,706 company-year observations from Belgian companies audited from 2008 to 2019. Our sample period begins in 2008 because partner identities became widely disclosed from that point onward. Our sample ends in 2019 because this is the last year we have all the necessary data. The full sample includes 762 unique audit partners and 24,361 companies. We eliminated 18,391 observations for joint audits (i.e., engagements with more than one audit partner). We eliminated 18,902 observations from the financial and public administration industries. Finally, missing or invalid values for calculating our alignment variables account for another 18,580 deleted observations, yielding a total of 152,272 company-year observations.

For our GCO analyses, we only retain observations from financially distressed companies. Following DeFond et al. (2002), we define financially distressed companies to be companies that report either (1) an operational loss, (2) a bottom line loss, (3) negative retained earnings, or (4) negative working capital (Hopwood, McKeown, and Mutchler 1994). After excluding observations with missing data, we have a sample of 64,804 company-year observations for the GCO analyses. For the accrual analysis, we have 92,952 company-year observations. Finally, the tenure, change, and alignment analyses use samples of 115,073, 118,166, and 125,054 complete company-year observations, respectively. Table 2.3 gives a full overview of the sample selection process for all models.

TABLE 2.3
Sample Selection Process

	Total
Full sample company-years	227,706
Minus joint audits	18,391
Minus less than one partner in firm	19,561
Minus financial and public administration industries	18,902
Minus missing or invalid values for calculating strategic variables	18,580
Final sample	**152,272**

	GCO analyses	**Accruals analyses**	**Tenure analyses**	**Change analyses**	**Alignment analyses**
Minus observations of non-financially distressed companies	72,584	0	0	0	0
Minus observations of missing data on the dependent variable	14,519	30,354	27,498	23,447	23,579
Minus observations of missing data on the control variables	364	28,966	9,701	10,659	3,639
Final Sample	**64,805**	**92,952**	**115,073**	**118,166**	**125,054**

Sample used in the placebo analysis	
Company-years	11,623,280
Minus missing data on control variables	702,826
Final sample used in the placebo analysis	**10,920,454**

This table reports the sample selection steps for the samples of analysis.

4.1. Descriptive Statistics

Table 2.4 provides descriptive statistics for all variables used in this study. Panel A shows that for the GCO analysis, the probability of an audit partner issuing a GCO to a financially distressed client is about 27 percent, which is comparable with prior studies using Belgian data (e.g., Hardies, Breesch, and Branson 2015; Knechel and Vanstraelen 2007). Panel B shows the descriptive statistics for the total accruals model, and the mean for $|TA|$ is 0.14. Panel C presents the descriptive statistics for the tenure analysis and shows that, on average, 59 percent of the clients have an audit tenure longer than three years. Panel D demonstrates that, on average, 13 percent of the clients change audit partners. Panel E details that 8 percent of all observations (62 percent of all partner changes) were within-audit firm partner rotations, while 5 percent (38 percent of all partner changes) were due to audit firm rotations.

Across our samples, the mean audit partner-client alignment is between 0.10 and 0.11 (*DICE2_90*). A reason why not all audit partners and clients highly align can be explained by field studies showing the importance of work relationships. Beyond measurable prior experiences, the organizational "fit" of the audit partner with the client might also be of importance in the auditor-client matching decision (Dodgson, Agoglia, Bennett, and Cohen 2020; Fiolleau et al. 2013; Free, Trotman, and Trotman 2021). The descriptive statistics for the control variables for all samples are consistent with prior research conducted in the Belgian setting (e.g., Hardies et al. 2015). Untabulated results show considerable differences within the partner portfolios. The mean number of large clients in a given partner's portfolio per year equals about eight, and the mean number of clients in financial distress is about seven. Listed companies and those that use IFRS are less common in our setting, with few partners having any listed clients or clients using IFRS. Further, untabulated results show that at the 90 percent cut-off level for partner expertise, IFRS matches exist in 0.3 percent of our observations, public company matches in 0.2 percent of our observations, while matches on firm size exist in 1.6 percent of the cases. Financial risk matches happen in 1.1 percent of our sample, and industry matches in 9.5 percent of our observations.[28]

Table 2.5 presents the equality of means test for the *DICE2_90* variable in the GCO, tenure, and change analyses. The mean alignment is higher ($p < 0.01$) for the clients receiving a GCO and for longer tenure. These results indicate that better audit partner-client alignment is related to a higher likelihood of receiving a GCO and with longer audit tenure. We also compare the alignment scores between clients who changed audit partners and those who did not change. The lower mean ($p = 0.003$) for our audit partner change group indicates that lower audit partner-client alignment is associated with a higher likelihood of an audit partner change. In additional analyses, we control for auditor- and client-specific characteristics to reduce potential confounding other differences in measuring the relationship between audit partner-client alignment and our other variables of interest.

[28] While we also take industry into account to measure alignment between client and partner, the wide array of categories within this variable precludes us from reporting the average number of clients per industry in the audit partner portfolio per year.

TABLE 2.4
Descriptive Statistics

Panel A: Descriptive Statistics GCO Model (N=64,805)

Variables	Mean	SD	Min	p25	Median	p75	Max
GCO	0.27	0.45	0.00	0.00	0.00	1.00	1.00
DICE2_90	0.11	0.30	0.00	0.00	0.00	0.00	1.00
LTA	15.68	2.07	10.00	14.43	15.71	16.92	21.20
LOSS	0.53	0.50	0.00	0.00	1.00	1.00	1.00
ROA	-0.04	0.32	-2.17	-0.03	0.01	0.05	0.77
IRISK	0.44	0.34	0.00	0.11	0.43	0.74	1.00
LEV	0.99	1.99	0.00	0.42	0.74	0.93	17.58
CURRENT	15.42	83.68	0.01	0.57	0.97	1.70	719.17
DSCORE	-2.54	18.42	-158.48	-0.49	0.49	1.58	5.22
LIST	0.01	0.09	0.00	0.00	0.00	0.00	1.00
IFRS	0.01	0.12	0.00	0.00	0.00	0.00	1.00
AGE	22.78	19.78	1.00	8.00	18.00	30.00	98.00
CONSOL	0.05	0.22	0.00	0.00	0.00	0.00	1.00
WORKSCOUNCIL	0.12	0.33	0.00	0.00	0.00	0.00	1.00
FEERATIO	0.09	0.18	0.00	0.00	0.00	0.06	0.80
MALE	0.88	0.32	0.00	1.00	1.00	1.00	1.00
CAREER	17.49	6.91	3.00	12.00	17.00	23.00	34.00
CIP	0.02	0.04	0.00	0.00	0.01	0.02	0.27
PORTFOLIO	21.81	1.62	17.85	20.62	22.04	23.01	24.90
OFFICE_SIZE	8.63	7.91	1.00	3.00	5.00	12.00	32.00
BIG4	0.54	0.50	0.00	0.00	1.00	1.00	1.00
PRIOR_GCO	0.24	0.43	0.00	0.00	0.00	0.00	1.00

Panel B: Descriptive Statistics Total Accruals Model (N=92,952)

Variables	Mean	SD	Min	p25	Median	p75	Max
$\lvert TA \rvert$	0.14	0.19	0.00	0.03	0.07	0.16	0.95
DICE2_90	0.11	0.29	0.00	0.00	0.00	0.00	1.00
LTA	15.98	1.82	11.27	14.90	15.94	17.03	21.08
LOSS	0.28	0.45	0.00	0.00	0.00	1.00	1.00
ROA	0.05	0.18	-0.94	0.01	0.04	0.11	0.66
IRISK	0.52	0.32	0.00	0.24	0.55	0.80	1.00
LEV	0.67	0.64	0.00	0.35	0.62	0.83	5.16
CURRENT	6.32	26.90	0.02	0.93	1.34	2.37	232.77
DSCORE	0.45	5.40	-41.18	0.26	1.13	2.38	5.60
LIST	0.01	0.08	0.00	0.00	0.00	0.00	1.00
IFRS	0.01	0.11	0.00	0.00	0.00	0.00	1.00
AGE	26.64	18.80	4.00	13.00	22.00	35.00	93.00
TA_LAG	-0.03	0.23	-0.95	-0.10	-0.02	0.04	0.89
OCF	0.06	0.23	-0.95	-0.01	0.05	0.15	0.82
SALES_GROWTH	1.40	12.21	-1.00	-0.09	0.01	0.11	118.88
PPE_GROWTH	0.62	5.09	-1.00	-0.16	-0.04	0.04	48.48
LSTDSALES	13.52	2.13	6.76	12.34	13.70	14.91	18.25
LSTDOCF	13.52	1.89	8.50	12.36	13.47	14.61	18.93
MAO	0.36	1.21	0.00	0.00	0.00	0.00	7.00
MALE	0.89	0.32	0.00	1.00	1.00	1.00	1.00
CAREER	17.65	7.09	3.00	12.00	17.00	23.00	34.00

CIP	0.03	0.04	0.00	0.00	0.01	0.03	0.29
PORTFOLIO	21.74	1.62	17.77	20.56	21.89	22.95	24.84
OFFICE_SIZE	8.34	7.85	1.00	3.00	5.00	11.00	32.00
BIG4	0.52	0.50	0.00	0.00	1.00	1.00	1.00
CONSOL	0.04	0.21	0.00	0.00	0.00	0.00	1.00
WORKSCOUNCIL	0.16	0.36	0.00	0.00	0.00	0.00	1.00
FEERATIO	0.09	0.17	0.00	0.00	0.00	0.08	0.77

Panel C: Descriptive Statistics Tenure Model (N=115,073)

Variables	Mean	SD	Min	p25	Median	p75	Max
TENURE3YRS	0.59	0.49	0.00	0.00	1.00	1.00	1.00
DICE2_90	0.10	0.28	0.00	0.00	0.00	0.00	1.00
LTA	15.98	1.83	11.00	14.92	15.97	17.05	20.97
LOSS	0.26	0.44	0.00	0.00	0.00	1.00	1.00
IRISK	0.52	0.32	0.00	0.24	0.55	0.81	1.00
LEV	0.67	0.65	0.00	0.34	0.62	0.83	5.33
ROA	0.05	0.19	-1.02	0.01	0.05	0.11	0.65
CURRENT	7.67	35.01	0.02	0.96	1.36	2.40	304.55
DSCORE	0.51	5.65	-43.75	0.32	1.21	2.47	5.75
LIST	0.01	0.08	0.00	0.00	0.00	0.00	1.00
IFRS	0.01	0.10	0.00	0.00	0.00	0.00	1.00
CONSOL	0.04	0.20	0.00	0.00	0.00	0.00	1.00
WORKSCOUNCIL	0.15	0.36	0.00	0.00	0.00	0.00	1.00
LAF	8.98	0.98	6.91	8.31	8.91	9.58	11.74
LNAS	2.22	3.77	0.00	0.00	0.00	6.22	11.25
GROWTH	0.07	0.41	-0.76	-0.07	0.01	0.13	2.62
BIG4	0.52	0.50	0.00	0.00	1.00	1.00	1.00
MALE	0.87	0.34	0.00	1.00	1.00	1.00	1.00
CAREER	17.70	7.32	0.00	12.00	18.00	23.00	44.00
CIF	0.00	0.01	0.00	0.00	0.00	0.00	0.06
CIP	0.03	0.04	0.00	0.00	0.01	0.03	0.29
PORTFOLIO	21.76	1.58	17.86	20.60	21.88	22.94	24.89

Panel D: Descriptive Statistics Change Model (N=118,166)

Variables	**Mean**	**SD**	**Min**	**p25**	**Median**	**p75**	**Max**
CHANGENXTYR	0.13	0.34	0.00	0.00	0.00	0.00	1.00
DICE2_90	0.10	0.29	0.00	0.00	0.00	0.00	1.00
LTA	15.99	1.82	11.06	14.93	15.97	17.04	21.00
LOSS	0.26	0.44	0.00	0.00	0.00	1.00	1.00
IRISK	0.52	0.32	0.00	0.24	0.55	0.80	1.00
LEV	0.65	0.58	0.00	0.35	0.62	0.82	4.62
ROA	0.05	0.18	-0.91	0.01	0.05	0.11	0.63
CURRENT	7.17	32.28	0.02	0.96	1.36	2.37	280.28
DSCORE	0.65	4.75	-35.50	0.31	1.19	2.43	5.64
LIST	0.01	0.08	0.00	0.00	0.00	0.00	1.00
IFRS	0.01	0.11	0.00	0.00	0.00	0.00	1.00
CONSOL	0.04	0.21	0.00	0.00	0.00	0.00	1.00
WORKSCOUNCIL	0.16	0.36	0.00	0.00	0.00	0.00	1.00
LAF	8.98	0.99	6.91	8.30	8.91	9.61	11.75
LNAS	2.37	3.86	0.00	0.00	0.00	6.83	11.31
GROWTH	0.08	0.41	-0.73	-0.07	0.01	0.13	2.70

BIG4	0.52	0.50	0.00	0.00	1.00	1.00	1.00
MALE	0.88	0.33	0.00	1.00	1.00	1.00	1.00
CAREER	17.54	7.18	0.00	12.00	17.00	23.00	43.00
CIF	0.00	0.01	0.00	0.00	0.00	0.00	0.06
CIP	0.03	0.04	0.00	0.00	0.01	0.03	0.29
PORTFOLIO	21.76	1.60	17.79	20.58	21.92	22.94	24.85

Panel E: Descriptive Statistics Alignment Model (N=125,054)

Variables	Mean	SD	Min	p25	Median	p75	Max
DIFFDICE2_90	-0.00	0.36	-1.00	0.00	0.00	0.00	1.00
CHANGE	0.13	0.33	0.00	0.00	0.00	0.00	1.00
NEW	0.05	0.22	0.00	0.00	0.00	0.00	1.00
PARTNERROT	0.08	0.26	0.00	0.00	0.00	0.00	1.00
LTA	15.96	1.84	10.94	14.89	15.96	17.04	20.98
LOSS	0.26	0.44	0.00	0.00	0.00	1.00	1.00
IRISK	0.52	0.32	0.00	0.24	0.55	0.80	1.00
LEV	0.67	0.66	0.00	0.34	0.62	0.83	5.49
ROA	0.05	0.19	-1.02	0.01	0.05	0.11	0.66
CURRENT	7.84	35.83	0.02	0.96	1.36	2.41	310.12
DSCORE	0.48	5.85	-45.72	0.31	1.20	2.46	5.75
LIST	0.01	0.08	0.00	0.00	0.00	0.00	1.00
IFRS	0.01	0.10	0.00	0.00	0.00	0.00	1.00
CONSOL	0.04	0.20	0.00	0.00	0.00	0.00	1.00
WORKSCOUNCIL	0.15	0.36	0.00	0.00	0.00	0.00	1.00
LAF	8.97	0.98	6.91	8.29	8.89	9.58	11.74
LNAS	2.24	3.78	0.00	0.00	0.00	6.32	11.25
GROWTH	0.07	0.41	-0.76	-0.07	0.01	0.13	2.63
BIG4	0.52	0.50	0.00	0.00	1.00	1.00	1.00
MALE	0.87	0.33	0.00	1.00	1.00	1.00	1.00
CAREER	17.76	7.22	0.00	12.00	18.00	23.00	44.00
CIF	0.00	0.01	0.00	0.00	0.00	0.00	0.06
CIM	0.03	0.04	0.00	0.00	0.01	0.03	0.28
PORTFOLIO	21.77	1.57	17.90	20.61	21.89	22.93	24.85
TENURE	4.30	2.51	1.00	2.00	4.00	6.00	11.00

We define all variables in Table 2.2.

TABLE 2.5
Mean Differences Alignment Variable

	GCO Sample		*Tenure Sample*		*Change Sample*	
Group	***GCO***	***No GCO***	***Tenure > 3 years***	***Tenure < 3 years***	***Change***	***No change***
N	17,671	47,134	68,044	47,029	15,400	102,766
Mean *Dice_90*	0.116	0.105	0.104	0.094	0.096	0.104
Diff	0.011		0.010		-0.007	
Se	0.001		0.002		0.003	
***t*-stat**	4.30		5.85		-3.05	
***p*-value**	0.000***		0.000***		0.003***	

This table includes the equality of means tests for the GCO, tenure, and change samples. We compare the mean value of our alignment variable (Dice2_90) for the GCO versus non-GCO observations, for the observations with tenure longer and shorter than three years, and observations with and without an audit partner change.

5. RESULTS

5.1. Audit Quality Analyses

Table 2.6 presents the correlation matrices for the audit quality analyses. The alignment variable (*DICE2_90*) is weakly positively correlated with both *GCO* and |*TA*|. The highest variance inflation factor (VIF) is 4.01, indicating that multicollinearity is not a problem.

5.1.1. Hypothesis 1

To investigate the association between audit partner-client alignment and audit quality, we estimate Equations [1] and [3]. Table 2.7 reports the results of these analyses. The likelihood ratio for the GCO analysis is statistically significant ($p < 0.01$), and the Pseudo R-squared is 38 percent. The estimated coefficient for audit partner-client alignment (*DICE2_90*) is not statistically significant ($p = 0.12$). Next, we estimate the total accrual analysis using the absolute value of total accruals because both positive and negative accruals could signal earnings management. The R-squared for this model is 22 percent. The coefficient for *DICE2_90* is negative and significant ($p = 0.07$). Regarding economic magnitude, the predicted value of |*TA*| is 0.1394 for *DICE2_90* at the 10th percentile and 0.1363 for *DICE2_90* at the 90th percentile.

We also analyze the positive and negative accruals separately in Table 2.8.[29] In this analysis, we identify a positive and statistically significant effect of audit partner-client alignment on the negative accruals ($p < 0.01$), indicating that a better match is associated with higher audit quality. In the negative accruals subsample, the predicted values of $|TA|$ at the 10^{th} and 90^{th} percentiles of *DICE2_90* are 0.1426 and 0.1360, respectively. This result could be expected in our setting, as taxes in Belgium are calculated based on profit. Therefore, companies have incentives to keep their profits low, to which income-decreasing accruals (i.e., larger negative total accruals) can help. In the positive accruals subsample, we identify no statistically significant effect of audit partner-client alignment on the income-increasing accruals ($p = 0.10$). We argue that the audit quality effect is driven by our finding that higher alignment is associated with less extreme negative accruals, i.e., lower income-decreasing accruals.

[29] For these analyses, we decompose the total accruals into their constituent positive and negative components and subsequently calculate the absolute values of each.

TABLE 2.6
Pearson's Correlation Coefficients Audit Quality Analysis

Panel A: GCO Analysis

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22
1 GCO	1.00																					
2 DICE2_90	**0.02**	1.00																				
3 LTA	**-0.23**	**0.01**	1.00																			
4 LOSS	**0.26**	**0.01**	**-0.20**	1.00																		
5 ROA	**-0.23**	-0.01	**0.26**	**-0.39**	1.00																	
6 IRISK	**0.10**	-0.00	**-0.18**	**0.08**	**-0.05**	1.00																
7 LEV	**0.21**	0.01	**-0.33**	**0.12**	**-0.39**	**0.05**	1.00															
8 CURRENT	**-0.06**	0.00	0.00	**-0.04**	**0.03**	**0.05**	**-0.08**	1.00														
9 DSCORE	**-0.18**	-0.00	**0.34**	**-0.11**	**0.38**	**-0.05**	**-0.86**	**0.03**	1.00													
10 LIST	**-0.03**	**0.03**	**0.13**	**-0.01**	0.00	**-0.06**	**-0.02**	**-0.01**	-0.00	1.00												
11 IFRS	**-0.05**	**0.04**	**0.20**	**-0.04**	**0.02**	**-0.08**	**-0.03**	-0.00	**0.02**	**0.60**	1.00											
12 AGE	**-0.11**	**-0.03**	**0.20**	**-0.05**	**0.07**	**0.04**	**-0.07**	0.01	**0.05**	**0.08**	**0.10**	1.00										
13 CONSOL	**-0.09**	0.01	**0.25**	**-0.10**	**0.05**	**-0.16**	**-0.06**	**-0.02**	**0.04**	**0.31**	**0.51**	**0.08**	1.00									
14 WORKSCOUNCIL	**-0.06**	-0.00	**0.35**	**-0.04**	**0.05**	0.01	**-0.05**	**-0.06**	**0.06**	**0.06**	**0.10**	**0.18**	**0.09**	1.00								
15 FEERATIO	-0.01	**0.01**	**0.17**	**-0.02**	0.01	**-0.06**	**-0.03**	**-0.03**	**0.02**	**0.10**	**0.10**	**0.02**	**0.15**	**0.08**	1.00							
16 MALE	-0.01	**0.02**	**0.01**	-0.01	0.00	**-0.03**	**-0.02**	0.01	**0.01**	0.01	0.01	**0.01**	0.01	0.00	**0.02**	1.00						
17 CAREER	**-0.03**	**-0.06**	0.01	**-0.02**	**0.03**	-0.00	**-0.02**	-0.01	**0.02**	-0.01	**-0.01**	**0.06**	**0.03**	-0.01	**-0.02**	**0.07**	1.00					
18 CIP	**-0.04**	**-0.12**	**0.27**	**-0.04**	**0.04**	-0.00	**-0.05**	**-0.06**	**0.05**	**0.18**	**0.19**	**0.16**	**0.18**	**0.22**	**0.20**	**-0.03**	**0.03**	1.00				
19 PORTFOLIO	-0.01	**0.22**	**0.13**	**0.01**	**-0.02**	**-0.02**	**0.02**	**0.05**	**-0.04**	**0.03**	**0.07**	**-0.02**	0.01	**0.09**	**0.03**	**0.07**	**-0.13**	**-0.39**	1.00			
20 OFFICE_SIZE	**-0.02**	**0.05**	**0.09**	**0.03**	**-0.02**	**-0.02**	**0.02**	**0.04**	**-0.03**	**0.04**	**0.06**	**-0.03**	**-0.01**	**0.07**	**0.02**	**-0.04**	**-0.15**	**-0.06**	**0.41**	1.00		
21 BIG4	-0.01	**0.18**	**0.09**	**0.03**	**-0.03**	-0.00	**0.04**	**0.05**	**-0.05**	**0.01**	**0.05**	**-0.03**	**-0.04**	**0.11**	**0.04**	**-0.01**	**-0.26**	**-0.21**	**0.67**	**0.55**	1.00	
22 PRIOR_GCO	**0.61**	**0.02**	**-0.20**	**0.12**	**-0.13**	**0.08**	**0.22**	**-0.06**	**-0.20**	**-0.02**	**-0.04**	**-0.09**	**-0.08**	**-0.05**	-0.01	**-0.02**	**-0.02**	**-0.05**	**0.03**	0.01	**0.03**	1.00

Bolded values are significant at .01-level. All variables are defined in Table 2.2.
N = 64,805

TABLE 2.6
Pearson's Correlation Coefficients Audit Quality Analysis

Panel B: TA Analysis

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24	25	26	27	28
1 |TA|	1.00																											
2 DICE2_90	**0.02**	1.00																										
3 LTA	**0.04**	**0.02**	1.00																									
4 LOSS	**-0.17**	**0.01**	**-0.13**	1.00																								
5 ROA	**0.28**	**-0.01**	**0.09**	**-0.53**	1.00																							
6 IRISK	**0.17**	**0.01**	**-0.17**	**-0.06**	**0.04**	1.00																						
7 LEV	**-0.19**	**0.02**	**-0.24**	**0.25**	**-0.31**	**0.05**	1.00																					
8 CURRENT	**0.06**	0.01	**-0.03**	-0.00	-0.00	0.01	**-0.18**	1.00																				
9 DSCORE	**0.11**	**-0.01**	**0.26**	**-0.27**	**0.36**	**-0.06**	**-0.77**	**0.04**	1.00																			
10 LIST	0.00	**0.03**	**0.12**	**0.01**	**-0.01**	**-0.07**	**-0.02**	**-0.01**	**-0.01**	1.00																		
11 IFRS	**-0.03**	**0.03**	**0.19**	-0.00	-0.00	**-0.09**	**-0.03**	0.00	0.00	**0.60**	1.00																	
12 AGE	0.00	**-0.03**	**0.20**	**-0.05**	**0.03**	-0.00	**-0.12**	-0.00	**0.09**	**0.07**	**0.09**	1.00																
13 TA_LAG	**-0.03**	**0.01**	**0.05**	**-0.09**	**0.09**	**0.13**	**-0.17**	**0.06**	**0.12**	0.00	0.00	0.01	1.00															
14 OCF	**-0.26**	**-0.02**	**0.03**	**-0.23**	**0.40**	**-0.19**	**-0.15**	**-0.03**	**0.20**	-0.00	0.01	**0.02**	**0.07**	1.00														
15 SALES_GROWTH	-0.00	**0.01**	**-0.05**	**0.05**	**-0.02**	**-0.01**	**0.03**	**0.08**	**-0.07**	-0.01	-0.00	**-0.04**	**-0.02**	**-0.04**	1.00													
16 PPE_GROWTH	**-0.04**	0.01	**-0.02**	**0.01**	-0.01	**-0.01**	-0.00	-0.00	-0.00	-0.00	0.00	**-0.05**	**0.02**	-0.00	**0.15**	1.00												
17 LSTDSALES	**0.01**	0.01	**0.52**	**-0.07**	**0.04**	**0.19**	**-0.01**	**-0.20**	**0.07**	**0.05**	**0.08**	**0.13**	0.00	**0.03**	**-0.10**	**-0.01**	1.00											
18 LSTDOCF	**0.02**	**0.02**	**0.75**	**-0.06**	**0.04**	**-0.05**	**-0.07**	**-0.05**	**0.07**	**0.10**	**0.16**	**0.13**	**0.01**	**0.04**	**-0.04**	-0.00	**0.56**	1.00										
19 MAO	**-0.01**	**0.02**	**-0.04**	**0.09**	**-0.08**	**0.03**	**0.09**	**-0.02**	**-0.09**	0.00	-0.01	**-0.02**	**-0.01**	**-0.04**	0.01	0.00	**0.01**	**-0.01**	1.00									
20 MALE	-0.00	**0.01**	**0.01**	**-0.01**	0.01	**-0.03**	**-0.02**	0.00	**0.02**	0.01	0.00	**0.01**	-0.00	0.01	0.01	0.00	**0.01**	0.01	0.00	1.00								
21 CAREER	**-0.01**	**-0.07**	**-0.02**	-0.00	0.00	**-0.02**	**-0.01**	-0.01	**0.01**	**-0.01**	**-0.02**	**0.05**	-0.01	**0.02**	**-0.01**	-0.01	**-0.02**	**-0.04**	-0.00	**0.09**	1.00							
22 CIP	-0.00	**-0.12**	**0.25**	**-0.02**	**0.01**	**-0.02**	**-0.03**	**-0.07**	**0.04**	**0.14**	**0.16**	**0.14**	-0.00	**0.01**	**-0.04**	**-0.02**	**0.22**	**0.20**	**-0.02**	**-0.03**	**0.02**	1.00						
23 PORTFOLIO	**0.01**	**0.21**	**0.15**	**0.04**	**-0.01**	**-0.02**	0.01	**0.05**	**-0.05**	**0.03**	**0.07**	**-0.04**	**0.01**	**-0.02**	**0.04**	**0.02**	**0.06**	**0.17**	-0.00	**0.07**	**-0.12**	**-0.42**	1.00					
24 OFFICE_SIZE	**0.01**	**0.02**	**0.11**	**0.03**	**-0.01**	**-0.02**	**0.01**	**0.04**	**-0.03**	**0.04**	**0.06**	**-0.03**	**0.01**	**-0.02**	**0.02**	0.01	**0.04**	**0.12**	-0.00	**-0.05**	**-0.16**	**-0.06**	**0.41**	1.00				
25 BIG4	0.01	**0.15**	**0.11**	**0.05**	**-0.01**	-0.00	**0.01**	**0.05**	**-0.05**	**0.01**	**0.05**	**-0.04**	**0.01**	**-0.02**	**0.03**	**0.02**	**0.04**	**0.14**	**-0.01**	**-0.03**	**-0.26**	**-0.21**	**0.67**	**0.55**	1.00			
26 CONSOL	**0.01**	0.01	**0.24**	**-0.03**	**0.01**	**-0.17**	**-0.07**	**-0.01**	**0.04**	**0.30**	**0.50**	**0.07**	**0.01**	**0.01**	-0.01	**0.02**	**0.06**	**0.18**	**-0.02**	-0.00	**0.02**	**0.16**	**0.02**	0.01	**-0.01**	1.00		
27 WORKSCOUNCIL	**-0.02**	-0.00	**0.40**	**-0.03**	**0.02**	**-0.03**	**-0.04**	**-0.07**	**0.05**	**0.05**	**0.10**	**0.15**	**-0.02**	**0.04**	**-0.04**	**-0.03**	**0.38**	**0.34**	**-0.02**	0.00	**-0.02**	**0.19**	**0.11**	**0.08**	**0.12**	**0.10**	1.00	
28 FEERATIO	0.01	0.00	**0.17**	0.00	0.00	**-0.06**	**-0.02**	**-0.03**	0.01	**0.09**	**0.10**	**0.03**	-0.00	0.01	-0.00	**0.02**	**0.12**	**0.16**	**-0.01**	**0.02**	**-0.03**	**0.19**	**0.05**	**0.04**	**0.06**	**0.14**	**0.09**	1.00

Bolded values are significant at .01-level. All variables are defined in Table 2.2.
N = 92,952

TABLE 2.7
Audit Quality Analysis

Variables	***GCO***			***|TA|***		
	Beta	*zstat*	*p-value*	*Beta*	*tstat*	*p-value*
Intercept	-1.225***	-4.03	0.00	0.237***	9.97	0.00
DICE2_90	0.063	1.56	0.12	-0.004*	-1.82	0.07
LTA	-0.102***	-13.15	0.00	-0.041***	-52.40	0.00
LOSS	1.202***	42.64	0.00	0.013***	7.86	0.00
ROA	-0.649***	-12.54	0.00	0.016**	2.21	0.03
IRISK	0.444***	11.08	0.00	-0.046***	-15.53	0.00
LEV	0.099***	6.67	0.00	0.032***	12.53	0.00
CURRENT	-0.001***	-6.07	0.00	0.000***	4.79	0.00
DSCORE	0.007***	4.72	0.00	-0.002***	-5.40	0.00
LIST	0.035	0.65	0.51	-0.012	-1.46	0.15
IFRS	-0.210	-0.94	0.35	0.012*	1.80	0.07
AGE	-0.006***	-7.59	0.00	-0.000***	-5.71	0.00
TA_LAG				-0.030***	-7.21	0.00
OCF				-0.027***	-4.58	0.00
SALES_GROWTH				0.001***	9.81	0.00
PPE_GROWTH				0.002***	13.00	0.00
LSTDSALES				0.002***	3.63	0.00
LSTDOCF				0.032***	48.94	0.00
MAO				0.000	0.81	0.42
MALE	-0.036	-0.90	0.37	0.002	0.90	0.37
CAREER	-0.006***	-3.51	0.00	0.000	0.00	1.00
CIP	0.471	1.24	0.22	0.002	0.13	0.90
PORTFOLIO	0.013	1.12	0.26	0.003***	4.01	0.00
OFFICE_SIZE	-0.009***	-4.74	0.00	-0.000	-0.02	0.99
BIG4	-0.192***	-4.97	0.00	0.017***	8.62	0.00
CONSOL	-0.221***	-3.06	0.01	-0.019***	-6.38	0.00
WORKSCOUNCIL	0.047	1.07	0.28	-0.007***	-3.80	0.00
FEERATIO	0.106	1.45	0.15	0.032***	7.98	0.00
PRIOR_GCO	3.115***	104.60	0.00			
Observations		64,800			92,952	
Year FE		YES			YES	
Industry FE		YES			YES	
LR-Ratio (χ^2)		14,788.37***				
F-statistic					31.15***	
Pseudo R-squared		0.38				
R-squared					0.22	
Jones Model regressors and their interaction with industry-year fixed effects					YES	

*Statistical significance based on two-tailed tests at the 1%, 5%, and 10% levels are denoted by ***, **, and * respectively. All variables are defined in Table 2.2. To correct for heteroscedasticity and serial dependence, the statistical significance is calculated using robust standard errors adjusted for clustering by company (Petersen 2009).*

TABLE 2.8
Total Accruals Additional Analysis

Subsample	***Positive TA***			***Negative TA***		
Variables	***|TA|***			***|TA|***		
	Beta	*tstat*	*p-value*	*Beta*	*tstat*	*p-value*
Intercept	0.172***	5.15	0.00	0.251***	16.09	0.00
DICE2_90	0.005	1.67	0.10	-0.008***	-3.46	0.00
LTA	-0.026***	-24.54	0.00	-0.036***	-51.63	0.00
LOSS	0.061***	18.15	0.00	-0.004**	-2.49	0.01
ROA	0.428***	34.33	0.00	-0.237***	-49.89	0.00
IRISK	-0.021***	-5.32	0.00	-0.085***	-33.65	0.00
LEV	-0.029***	-6.45	0.00	0.072***	42.76	0.00
CURRENT	0.000*	1.80	0.07	0.000	1.19	0.23
DSCORE	-0.007***	-12.72	0.00	0.001***	4.90	0.00
LIST	-0.016	-1.14	0.26	-0.010	-1.01	0.31
IFRS	0.011	1.09	0.28	0.011	1.31	0.19
AGE	-0.000***	-4.97	0.00	-0.000**	-2.42	0.02
TA_LAG	-0.089***	-15.48	0.00	0.005*	1.66	0.10
OCF	-0.309***	-37.41	0.00	0.189***	51.55	0.00
SALES_GROWTH	0.001***	5.61	0.00	0.001***	19.34	0.00
PPE_GROWTH	0.001***	5.38	0.00	0.004***	26.46	0.00
LSTDSALES	0.002**	2.46	0.01	0.001*	1.82	0.07
LSTDOCF	0.021***	26.00	0.00	0.026***	42.49	0.00
MAO	0.001*	1.88	0.06	-0.001	-1.64	0.10
MALE	-0.002	-0.78	0.44	0.003*	1.66	0.10
CAREER	0.000**	2.10	0.04	-0.000	-0.99	0.32
CIP	-0.027	-1.33	0.18	0.021	1.16	0.25
PORTFOLIO	0.002**	2.01	0.04	0.003***	5.04	0.00
OFFICE_SIZE	0.000	1.17	0.24	-0.000	-0.56	0.58
BIG4	0.013***	4.82	0.00	0.014***	6.78	0.00
CONSOL	-0.014***	-3.26	0.00	-0.021***	-5.59	0.00
WORKSCOUNCIL	-0.009***	-3.53	0.00	-0.003	-1.62	0.11
FEERATIO	0.029***	5.22	0.00	0.024***	6.14	0.00
Observations		36,083			56,869	
Year FE		YES			YES	
Industry FE		YES			YES	
F-statistic		25.11***			428.16***	
R-squared		0.36			0.28	
Jones Model regressors and their interaction with industry-year fixed effects		YES			YES	

*Statistical significance based on two-tailed tests at the 1%, 5%, and 10% levels are denoted by ***, **, and * respectively. All variables are defined in Table 2.2. To correct for heteroscedasticity and serial dependence, the statistical significance is calculated using robust standard errors adjusted for clustering by company (Petersen 2009).*

5.2. Audit Partner Tenure and Audit Partner Change Analyses

The audit partner tenure analysis examines if improved alignment between audit partners and clients increases the likelihood of engagements extending beyond a first three-year audit mandate. We removed the first three years in our sample to remove confounding effects because our data only started in 2008. We calculated which client-audit partner engagements last longer than three years (*TENURE3YRS* = 1). Additionally, we investigate whether alignment in year *t* is associated with an audit partner change in year *t+1* (*CHANGENXTYR* = 1). Table 2.9 presents the correlation matrices. As expected, *DICE2_90* is positively associated with *TENURE3YRS* and negatively associated with *CHANGENXTYR*. This suggests that a better match is associated with longer tenure and a lower likelihood of changing audit partners. The highest VIF for both analyses is 2.74, indicating that multicollinearity is not a problem.

5.2.1. Hypothesis 2

Table 2.10 presents the results of estimating Equations [4] and [5]. Both analyses' likelihood ratios are statistically significant ($p < 0.01$). The Pseudo R-squared is 9 percent and 4 percent in the tenure and auditor change analyses, respectively. The results support Hypothesis 2. That is, better audit partner-client alignment is positively associated ($p < 0.01$) with a higher likelihood that clients retain their audit partner for longer than a single three-year mandate (i.e., longer tenure) and with a lower likelihood ($p < 0.01$) of an audit partner change. In terms of economic magnitude, the predicted probability of an engagement lasting longer than three years (one mandate) is 59.11 percent at the 10^{th} percentile of *DICE2_90* and 62.81 percent for an engagement at the 90^{th} percentile of *DICE2_90*.[30] The predicted probability of an audit partner change occurring is 13.03 percent at the 10^{th} percentile of *DICE2_90* and 11.79 percent for an engagement at the 90^{th} percentile of *DICE2_90*.

[30] At the 25^{th} and 75^{th} percentiles, these values are 59.81 and 62.13 percent respectively.

TABLE 2.9
Pearson's Correlation Coefficients Tenure and Change Analysis

Panel A: Tenure Analysis

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22
1 TENURE3YRS	1.00																					
2 DICE2_90	**0.02**	1.00																				
3 LTA	**0.03**	**0.03**	1.00																			
4 LOSS	**-0.04**	**0.01**	**-0.16**	1.00																		
5 IRISK	**0.03**	-0.01	**-0.15**	**-0.08**	1.00																	
6 LEV	**-0.03**	**0.01**	**-0.25**	**0.26**	**0.04**	1.00																
7 ROA	**0.02**	**-0.01**	**0.12**	**-0.53**	**0.05**	**-0.36**	1.00															
8 CURRENT	0.01	0.01	**-0.03**	**0.02**	**0.01**	**-0.17**	-0.01	1.00														
9 DSCORE	**0.01**	-0.01	**0.28**	**-0.28**	**-0.04**	**-0.77**	**0.42**	**0.04**	1.00													
10 LIST	**-0.02**	**0.04**	**0.11**	**0.01**	**-0.06**	**-0.02**	**-0.01**	**-0.01**	**-0.01**	1.00												
11 IFRS	**-0.01**	**0.03**	**0.18**	0.00	**-0.08**	**-0.03**	-0.00	0.00	0.01	0.60	1.00											
12 CONSOL	**0.02**	**0.01**	**0.24**	**-0.02**	**-0.16**	**-0.07**	**0.01**	**-0.01**	**0.04**	**0.28**	**0.49**	1.00										
13 WORKSCOUNCIL	**0.02**	-0.01	**0.39**	**-0.05**	**-0.02**	**-0.04**	**0.03**	**-0.07**	**0.05**	**0.05**	**0.10**	**0.11**	1.00									
14 LAF	**0.02**	-0.01	**0.59**	**-0.06**	**0.06**	**-0.05**	**0.04**	**-0.15**	**0.07**	**0.13**	**0.20**	**0.18**	**0.48**	1.00								
15 LNAS	**0.04**	**0.01**	**0.25**	-0.01	**-0.04**	**-0.02**	0.01	**-0.05**	**0.02**	**0.11**	**0.13**	**0.16**	**0.19**	**0.34**	1.00							
16 GROWTH	**-0.05**	**0.01**	**0.07**	**-0.06**	0.00	**-0.02**	**0.11**	**-0.02**	**0.08**	0.00	0.00	-0.00	-0.00	**-0.04**	**0.02**	1.00						
17 BIG4	**-0.10**	**0.13**	**0.10**	**0.05**	**-0.01**	**0.01**	**-0.01**	**0.05**	**-0.05**	**0.02**	**0.06**	-0.00	**0.12**	**0.27**	**0.06**	0.01	1.00					
18 MALE	**0.06**	**0.04**	0.00	-0.00	**-0.02**	**-0.01**	0.01	0.01	**0.01**	0.00	-0.00	**-0.01**	**-0.01**	**-0.02**	**0.02**	0.00	**-0.04**	1.00				
19 CAREER	**0.30**	**-0.03**	-0.00	-0.01	**-0.02**	**-0.01**	-0.00	-0.01	0.01	-0.01	**-0.01**	**0.02**	**-0.01**	**-0.07**	**-0.03**	**-0.02**	**-0.22**	**0.06**	1.00			
20 CIF	**0.07**	**-0.10**	**0.09**	**-0.04**	0.00	**-0.01**	**0.02**	**-0.05**	**0.04**	**0.03**	**0.02**	**0.04**	**0.04**	**0.07**	**0.03**	**-0.01**	**-0.42**	0.00	**0.11**	1.00		
21 CIP	**0.02**	**-0.12**	**0.25**	**-0.03**	**-0.01**	**-0.03**	**0.02**	**-0.07**	**0.04**	**0.13**	**0.15**	**0.15**	**0.20**	**0.34**	**0.21**	**-0.01**	**-0.21**	**-0.04**	**0.02**	**0.53**	1.00	
22 PORTFOLIO	**-0.03**	**0.21**	**0.14**	**0.05**	**-0.02**	0.00	**-0.02**	**0.05**	**-0.04**	**0.04**	**0.07**	**0.03**	**0.10**	**0.18**	**0.05**	**0.01**	**0.66**	**0.06**	**-0.10**	**-0.46**	**-0.44**	1.00

Bolded values are significant at .01-level. All variables are defined in Table 2.2.
N = 115,067

TABLE 2.9
Pearson's Correlation Coefficients Tenure and Change Analysis

Panel B: Change Analysis

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23
1 CHANGENXTYR	1.00																						
2 DICE2_90	**-0.01**	1.00																					
3 LTA	**0.02**	**0.02**	1.00																				
4 LOSS	0.01	**0.02**	**-0.15**	1.00																			
5 IRISK	**-0.01**	-0.00	**-0.15**	**-0.09**	1.00																		
6 LEV	0.00	**0.02**	**-0.23**	**0.26**	**0.05**	1.00																	
7 ROA	-0.00	**-0.01**	**0.10**	**-0.54**	**0.06**	**-0.35**	1.00																
8 CURRENT	0.00	0.00	**-0.03**	**0.01**	0.01	**-0.19**	**-0.01**	1.00															
9 DSCORE	0.00	**-0.01**	**0.26**	**-0.30**	**-0.05**	**-0.75**	**0.42**	**0.04**	1.00														
10 LIST	**0.02**	**0.03**	**0.11**	**0.01**	**-0.06**	**-0.02**	**-0.01**	**-0.01**	**-0.01**	1.00													
11 IFRS	**0.02**	**0.03**	**0.18**	-0.00	**-0.08**	**-0.03**	-0.00	0.00	0.00	0.57	1.00												
12 CONSOL	-0.00	**0.01**	**0.24**	**-0.03**	**-0.17**	**-0.07**	**0.01**	**-0.01**	**0.04**	**0.29**	**0.49**	1.00											
13 WORKSCOUNCIL	**0.01**	-0.01	**0.39**	**-0.04**	**-0.02**	**-0.04**	**0.03**	**-0.07**	**0.05**	**0.05**	**0.10**	**0.10**	1.00										
14 LAF	**0.04**	-0.00	**0.59**	**-0.06**	**0.06**	**-0.04**	**0.04**	**-0.15**	**0.06**	**0.13**	**0.20**	**0.18**	**0.48**	1.00									
15 LNAS	**0.01**	0.01	**0.26**	-0.01	**-0.03**	**-0.03**	**0.01**	**-0.05**	**0.02**	**0.11**	**0.13**	**0.15**	**0.20**	**0.35**	1.00								
16 GROWTH	0.00	**0.01**	**0.06**	**-0.05**	0.00	-0.01	**0.10**	**-0.02**	**0.06**	-0.00	-0.00	-0.00	-0.01	**-0.04**	**0.02**	1.00							
17 BIG4	**0.08**	**0.14**	**0.10**	**0.05**	-0.01	**0.01**	**-0.02**	**0.05**	**-0.05**	**0.02**	**0.05**	**-0.01**	**0.12**	**0.29**	**0.07**	**0.01**	1.00						
18 MALE	**0.02**	**0.03**	0.01	-0.00	**-0.02**	**-0.01**	0.00	0.01	**0.01**	0.00	0.00	**-0.01**	-0.00	**-0.02**	**0.01**	0.00	**-0.03**	1.00					
19 CAREER	**0.08**	**-0.04**	-0.00	**-0.01**	**-0.02**	**-0.01**	0.00	-0.01	**0.02**	**-0.01**	**-0.01**	**0.02**	**-0.01**	**-0.08**	**-0.03**	**-0.02**	**-0.24**	**0.07**	1.00				
20 CIF	**-0.03**	**-0.10**	**0.08**	**-0.04**	0.01	**-0.01**	**0.02**	**-0.05**	**0.04**	**0.03**	**0.02**	**0.04**	**0.04**	**0.05**	**0.02**	**-0.01**	**-0.42**	0.00	**0.11**	1.00			
21 CIP	**0.03**	**-0.12**	**0.25**	**-0.03**	**-0.01**	**-0.03**	**0.02**	**-0.07**	**0.04**	**0.13**	**0.16**	**0.15**	**0.19**	**0.33**	**0.21**	**-0.01**	**-0.23**	**-0.04**	**0.01**	**0.53**	1.00		
22 PORTFOLIO	**0.03**	**0.21**	**0.14**	**0.04**	**-0.02**	0.00	**-0.02**	**0.05**	**-0.05**	**0.03**	**0.07**	**0.02**	**0.11**	**0.21**	**0.06**	**0.02**	**0.67**	**0.07**	**-0.10**	**-0.46**	**-0.44**	1.00	
23 TENURE	**0.04**	**-0.01**	**0.07**	**-0.06**	**0.04**	**-0.04**	**0.03**	-0.01	**0.03**	**-0.03**	**-0.01**	**0.02**	**0.04**	**0.04**	**0.03**	**-0.04**	**-0.11**	**0.03**	**0.32**	**0.07**	**0.04**	**-0.03**	1.00

Bolded values are significant at .01-level. All variables are defined in Table 2.2.
N = 118,164

TABLE 2.10
Tenure and Change Analysis

Variables	***TENURE3YRS***			***CHANGENXTYR***		
	Beta	*zstat*	*p-value*	*Beta*	*zstat*	*p-value*
Constant	-2.797***	-12.69	0.00	-3.089***	-13.39	0.00
DICE2_90	0.219***	8.36	0.00	-0.149***	-4.65	0.00
LTA	0.018***	2.65	0.01	-0.003	-0.49	0.62
LOSS	-0.137***	-6.70	0.00	0.038	1.56	0.12
IRISK	0.203***	6.76	0.00	-0.061**	-2.04	0.04
LEV	-0.125***	-5.86	0.00	0.033	1.39	0.17
ROA	0.145***	2.85	0.00	-0.016	-0.26	0.79
CURRENT	0.001***	2.91	0.00	-0.000	-0.29	0.77
DSCORE	-0.016***	-6.17	0.00	0.006**	2.11	0.03
LIST	-0.684***	-5.39	0.00	0.488***	4.47	0.00
IFRS	-0.334***	-3.03	0.00	0.029	0.25	0.80
CONSOL	0.227***	4.06	0.00	-0.228***	-3.88	0.00
WORKSCOUNCIL	0.050*	1.67	0.10	-0.122***	-4.23	0.00
LAF	0.042***	2.91	0.00	0.040***	2.85	0.00
LNAS	0.028***	11.79	0.00	-0.006**	-2.23	0.03
GROWTH	-0.234***	-14.09	0.00	0.022	1.01	0.31
BIG4	-0.218***	-7.96	0.00	0.772***	27.53	0.00
MALE	0.216***	7.87	0.00	0.186***	6.30	0.00
CAREER	0.090***	69.08	0.00	0.043***	30.34	0.00
CIF	11.396***	7.94	0.00	-14.637***	-9.89	0.00
CIP	-1.070***	-3.50	0.00	4.143***	15.43	0.00
PORTFOLIO	0.034***	3.79	0.00	-0.056***	-6.33	0.00
TENURE				0.037***	8.66	0.00
Observations	115,067			118,164		
Year FE	YES			YES		
Industry FE	YES			YES		
LR-Ratio (χ^2)	6,789.15***			3,485.24***		
Pseudo R-squared	0.09			0.04		

*Statistical significance based on two-tailed tests at the 1%, 5%, and 10% levels are denoted by ***, **, and * respectively. All variables are defined in Table 2.2. To correct for heteroscedasticity and serial dependence, the statistical significance is calculated using robust standard errors adjusted for clustering by company (Petersen 2009).*

5.1. Alignment Analyses

Table 2.11 presents pairwise correlations for our alignment analyses after a partner change. Interestingly, our variable of interest, *DICE2_90,* negatively correlates with audit partner changes, suggesting such changes correlate with lower audit partner-client matching.

5.1.1. Hypothesis 3

To test Hypotheses 3a and 3b, we estimate Equations [7] and [8]. Table 2.12 presents the results of these analyses. The model is statistically significant overall ($p < 0.01$), but the R-squared is very low (0.5 percent). The highest VIF is 2.68, indicating that multicollinearity is not a problem. Interestingly, in contrast to our expectation, we find that audit partner changes (*CHANGE*) are negatively associated ($p < 0.01$) with the yearly difference in audit partner-client alignment. This suggests that after an audit partner change, the audit partner-client alignment is worse than before the change. The predicted value of *DIFF_ALIGNMENT_VARIABLE* is 0.0018 if no audit partner change occurred the year before, while the predicted value is -0.0132 when an audit partner change occurred the year before.

Analyzing audit partner changes in within-firm partner rotations (n = 9,466) and audit-firm rotations (n = 6,189) separately, results in Table 2.12 show a negative statistically significant result for within-firm partner rotations (*PARTNERROT*, $p < 0.01$). In terms of economic magnitude, the predicted value of *DIFF_ALIGNMENT_VARIABLE* is 0.0019 when within-firm audit partner change occurred the year before, while the predicted value is -0.0237 when a within-firm audit partner change happened in the year before.

Conversely, partner rotations stemming from audit firm rotations (*NEW*) are not associated with a difference in audit partner-client alignment ($p = 0.76$). Contrary to Hypothesis 3a, these results suggest that partner-client alignment is lower after an audit partner change. However, consistent with Hypothesis 3b, these results are driven by within-firm partner rotations. Compared to within-firm partner rotation, partner-client alignment is better for new clients.

TABLE 2.11
Pearson's Correlation Coefficients Alignment Analysis

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24	25
1 DIFFDICE2_90	1.00																								
2 CHANGE	**-0.01**	1.00																							
3 NEW	0.01	**0.60**	1.00																						
4 PARTNERROT	**-0.02**	**0.76**	**-0.07**	1.00																					
5 LTA	**0.01**	**0.03**	**0.02**	**0.02**	1.00																				
6 LOSS	0.00	**0.01**	**0.01**	0.00	**-0.16**	1.00																			
7 IRISK	-0.00	**-0.01**	**-0.01**	**-0.01**	**-0.15**	**-0.08**	1.00																		
8 LEV	-0.01	-0.00	**-0.01**	0.00	**-0.25**	**0.25**	**0.04**	1.00																	
9 ROA	0.00	-0.00	-0.00	-0.00	**0.12**	**-0.53**	**0.05**	**-0.36**	1.00																
10 CURRENT	0.00	0.00	-0.01	0.01	**-0.03**	**0.02**	**0.01**	**-0.17**	-0.01	1.00															
11 DSCORE	0.01	0.01	**0.01**	0.00	**0.28**	**-0.28**	**-0.04**	**-0.77**	**0.42**	**0.04**	1.00														
12 LIST	0.00	**0.02**	0.00	**0.03**	**0.11**	**0.01**	**-0.06**	**-0.02**	**-0.01**	**-0.01**	**-0.01**	1.00													
13 IFRS	0.00	**0.02**	0.00	**0.02**	**0.18**	-0.0	**-0.08**	**-0.03**	-0.00	0.00	0.01	**0.56**	1.00												
14 CONSOL	0.01	0.00	-0.00	0.01	**0.24**	**-0.03**	**-0.16**	**-0.07**	**0.01**	**-0.01**	**0.04**	**0.28**	**0.49**	1.00											
15 WORKSCOUNCIL	0.00	**0.02**	**0.01**	**0.01**	**0.39**	**-0.05**	**-0.02**	**-0.04**	**0.03**	**-0.07**	**0.05**	**0.05**	**0.10**	**0.11**	1.00										
16 LAF	0.00	**0.04**	**0.02**	**0.03**	**0.59**	**-0.07**	**0.06**	**-0.05**	**0.04**	**-0.15**	**0.07**	**0.13**	**0.20**	**0.18**	**0.48**	1.00									
17 LNAS	0.00	**-0.03**	**-0.04**	0.00	**0.25**	**-0.01**	**-0.03**	**-0.02**	**0.01**	**-0.05**	**0.02**	**0.11**	**0.13**	**0.16**	**0.19**	**0.34**	1.00								
18 GROWTH	**0.01**	0.00	0.00	0.00	**0.07**	**-0.06**	0.00	**-0.02**	**0.11**	**-0.02**	**0.08**	0.00	0.00	-0.00	-0.00	**-0.03**	**0.02**	1.00							
19 BIG4	-0.01	**0.07**	**0.02**	**0.08**	**0.10**	**0.05**	**-0.01**	**0.01**	**-0.01**	**0.05**	**-0.05**	**0.02**	**0.06**	-0.01	**0.12**	**0.27**	**0.06**	**0.01**	1.00						
20 MALE	0.00	**-0.03**	**-0.01**	**-0.04**	0.00	-0.00	**-0.02**	**-0.01**	**0.01**	0.01	**0.01**	0.00	-0.00	**-0.01**	**-0.01**	**-0.02**	**0.01**	-0.00	**-0.03**	1.00					
21 CAREER	0.00	**-0.19**	**-0.07**	**-0.17**	-0.01	**-0.01**	**-0.02**	**-0.01**	0.00	-0.01	**0.01**	**-0.01**	**-0.02**	**0.02**	**-0.02**	**-0.08**	**-0.03**	**-0.01**	**-0.23**	**0.07**	1.00				
22 CIF	-0.00	**-0.04**	**-0.01**	**-0.04**	**0.09**	**-0.04**	0.01	**-0.01**	**0.02**	**-0.05**	**0.04**	**0.03**	**0.02**	**0.04**	**0.04**	**0.07**	**0.03**	**-0.01**	**-0.42**	0.00	**0.12**	1.00			
23 CIP	**-0.01**	**0.02**	-0.00	**0.02**	**0.26**	**-0.04**	**-0.01**	**-0.03**	**0.02**	**-0.07**	**0.04**	**0.13**	**0.16**	**0.15**	**0.20**	**0.34**	**0.22**	**-0.01**	**-0.22**	**-0.04**	**0.03**	**0.53**	1.00		
24 PORTFOLIO	**0.02**	**0.03**	**0.02**	**0.02**	**0.14**	**0.04**	**-0.02**	0.00	**-0.02**	**0.05**	**-0.04**	**0.04**	**0.07**	**0.03**	**0.10**	**0.19**	**0.05**	**0.02**	**0.66**	**0.06**	**-0.12**	**-0.46**	**-0.44**	1.00	
25 TENURE	-0.00	**-0.46**	**-0.29**	**-0.34**	**0.06**	**-0.06**	**0.04**	**-0.04**	**0.03**	-0.01	**0.02**	**-0.03**	**-0.02**	**0.02**	**0.04**	**0.04**	**0.03**	**-0.04**	**-0.13**	**0.04**	**0.34**	**0.09**	**0.04**	**-0.05**	1.00

Bolded values are significant at .01-level. All variables are defined in Table 2.2.
N = 125,047

TABLE 2.12
Alignment Analysis

Variables	***DIFF_ALIGNMENT_VARIABLE (1)***			***DIFF_ALIGNMENT_VARIABLE (2)***		
	Beta	*tstat*	*p-value*	*Beta*	*tstat*	*p-value*
Intercept	-0.173***	-11.45	0.00	-0.170***	-11.23	0.00
CHANGE	-0.015***	-4.25	0.00			
PARTNERROT				-0.026***	-6.06	0.00
NEW				0.002	0.30	0.76
LTA	-0.000	-0.27	0.78	-0.000	-0.32	0.75
LOSS	0.001	0.56	0.58	0.001	0.52	0.60
IRISK	0.000	0.07	0.95	0.000	0.07	0.94
LEV	-0.002	-1.19	0.24	-0.002	-1.14	0.25
ROA	-0.001	-0.09	0.93	-0.001	-0.08	0.93
CURRENT	0.000	0.71	0.48	0.000	0.75	0.45
DSCORE	0.000	0.50	0.62	0.000	0.51	0.61
LIST	0.011	1.49	0.14	0.012	1.62	0.11
IFRS	-0.010*	-1.66	0.10	-0.011*	-1.72	0.09
CONSOL	0.006**	2.10	0.04	0.006**	2.13	0.03
WORKSCOUNCIL	-0.002	-1.48	0.14	-0.003	-1.56	0.12
LAF	0.002**	2.27	0.02	0.002**	2.23	0.03
LNAS	0.000	0.75	0.45	0.000	0.97	0.33
GROWTH	0.009***	3.24	0.00	0.009***	3.24	0.00
BIG4	-0.022***	-13.54	0.00	-0.022***	-13.29	0.00
MALE	0.001	0.65	0.52	0.001	0.55	0.58
CAREER	0.000	1.48	0.14	0.000	1.01	0.31
CIF	0.244***	5.82	0.00	0.230***	5.48	0.00
CIP	-0.039***	-2.93	0.00	-0.038***	-2.80	0.01
PORTFOLIO	0.009***	15.64	0.00	0.008***	15.40	0.00
TENURE	-0.002***	-6.94	0.00	-0.002***	-6.62	0.00
Observations		125,047			125,047	
Year FE		YES			YES	
Industry FE		YES			YES	
F-statistic		21.43***			21.33***	
R-squared		0.005			0.005	

*Statistical significance based on two-tailed tests at the 1%, 5%, and 10% levels are denoted by ***, **, and * respectively. All variables are defined in Table 2.2. To correct for heteroscedasticity and serial dependence, the statistical significance is calculated using robust standard errors adjusted for clustering by company (Petersen 2009). In analysis (1), we focus on all audit partner changes simultaneously, while in (2), we investigate the difference between within-firm partner changes and partner changes resulting from an audit firm change.*

5.2. Additional Analyses and Robustness Tests

5.2.1. Placebo Analysis

Our audit partner-client alignment variable assumes that audit partners and clients strategically enter audit mandates. However, because our sample only shows existing audit partner-client engagements, we cannot directly test whether both parties take each other's characteristics into account. Moreover, field studies show that the organizational "fit" of the audit partner with the client at least partly drives the auditor-client matching decision (e.g., Dodgson et al. 2020; Fiolleau et al. 2013; Free et al. 2021), rather than solely prior audit experience. To study the existence of audit partner-client alignment, we run a placebo test by creating a sample that contains all potential audit partner-client combinations during our sample period, calculating the alignment, and keeping track of the "real" audit engagements. We restrict this analysis to Big 4 clients because of the otherwise enormous amount of possible audit partner-client combinations. We think this decision is justified because audit markets are segmented, and clients audited by one of the Big 4 often only consider Big 4 firms when selecting a new auditor (e.g., Fiolleau et al. 2013).

As shown in Table 2.3, this yields a final sample of 10,920,454 client-year observations, consisting of 12,049 clients and 245 unique audit partners. Table 2.13 presents the result of the logistic regression, with *REALENGAGEMENT* being the dependent variable, which is equal to one if the audit partner-client match is the one observed in reality.

The results show that the coefficient for *DICE2_90* is positive and statistically significant ($p < 0.01$), suggesting that audit partners and clients strategically match compared to all other alternative partner-client matches. The predicted probability of being an existing audit partner-client engagement is 0.66 percent at the 10^{th} percentile of *DICE2_90*, while it is 0.84 percent at the 90^{th} percentile of *DICE2_90*.

TABLE 2.13
Placebo Analysis

Variables	***REALENGAGEMENT***		
	Beta	*zstat*	*p-value*
Intercept	-10.475***	-91.80	0.00
DICE2_90	0.283***	14.39	0.00
LTA	0.000**	2.39	0.02
LOSS	0.000	1.17	0.24
IRISK	0.000***	3.36	0.00
LEV	0.000	0.45	0.65
ROA	0.000	0.93	0.35
CURRENT	-0.000	-1.10	0.27
DSCORE	0.000	0.50	0.62
LIST	0.003***	6.12	0.00
IFRS	-1.643***	-20.73	0.00
CONSOL	0.002***	14.26	0.00
WORKSCOUNCIL	0.000	0.10	0.92
LAF	-0.000***	-4.64	0.00
LNAS	-0.000*	-1.75	0.08
GROWTH	-0.000	-0.45	0.65
MALE	0.003	0.11	0.91
CAREER	0.004***	3.18	0.00
PORTFOLIO	0.264***	51.71	0.00
OFFICE_SIZE	-0.032***	-36.68	0.00
Observations	10,919,519		
Year FE	YES		
Industry FE	YES		
LR-Ratio (χ^2)	17174.32***		
Pseudo R-squared	0.026		

*Statistical significance based on two-tailed tests at the 1%, 5%, and 10% levels are denoted by ***, **, and * respectively. All variables are defined in Table 2.2. To correct for heteroscedasticity and serial dependence, the statistical significance is calculated using robust standard errors adjusted for clustering by company (Petersen 2009).*

5.2.2. Big 4 Analysis

Our sample includes a wide range of observations, exhibiting variations in both client size and audit firm size. This is noteworthy because large clients have potentially more audit partners to choose from, and Big 4 audit firms may have more suitable candidate audit partners compared to smaller firms. Splitting the sample into Big 4 and non-Big 4 firms results in highly comparable conclusions. However, by incorporating interaction effects in Model 8 with the variables *PARTNERROT* and *NEW* interacting with *BIG4*, we observe that the interaction term between partner rotation and Big 4 affiliation is not significant (p = 0.671). This implies that the effect of partner rotation on alignment does not differ significantly between Big 4 and non-Big 4 firms, and that partner rotation is generally associated with lower audit partner-client alignment. In contrast, the interaction between *NEW* and *BIG4* is positive and significant (p < 0.01), indicating that changing audit firms to a Big 4 is associated with better audit partner-client alignment compared to non-Big 4 firms. However, the total effect of an audit firm change to a Big 4 is not significantly associated with higher or lower audit partner-client alignment (p = 0.12), while changing to a non-Big 4 is associated with lower audit partner-client alignment (p = 0.07).

5.2.3. Robustness Tests

In our main analyses, we capture audit partner expertise through specific client characteristics, defining expertise as having more experience with such characteristics than 90 percent of partners during the period. Using the top decile of partners to define expertise is restrictive. To assess the robustness of our findings relative to this design choice, we conducted additional analyses employing varying cut-off points for audit partner expertise, which resulted in changes in our alignment variable. Specifically, we used cut-off points at the 50th percentile, the median, 70th, 80th, 90th, and 95th percentiles. The results are presented in Table 2.14.

TABLE 2.14
Sensitivity Analysis

Dependent Variable	***Variable of Interest***	50%		Median		70%		80%		90%		95%	
		β	*p-value*	*β*	*p-value*	*β*	*p-value*	*β*	*p-value*	*β*	*p-value*	*β*	*p-value*
GCO	*DICE2*	0.12	0.00	0.12	0.00	0.09	0.00	0.08	0.01	0.06	0.12	0.02	0.76
|TA|	*DICE2*	0.00	0.91	0.00	0.65	-0.00	0.11	-0.00	0.02	-0.00	0.07	-0.01	0.01
TENURE3YRS	*DICE2*	0.13	0.00	0.16	0.00	0.20	0.00	0.23	0.00	0.22	0.00	0.31	0.00
CHANGENXTYR	*DICE2*	-0.03	0.17	-0.01	0.63	-0.01	0.74	-0.01	0.57	-0.15	0.00	-0.18	0.00
DICE2	*CHANGE*	-0.08	0.00	-0.09	0.00	-0.08	0.00	-0.05	0.00	-0.01	0.00	-0.01	0.00
DICE2	*PARTNERROT*	-0.12	0.00	-0.12	0.00	-0.13	0.00	-0.09	0.00	-0.03	0.00	-0.02	0.00
DICE2	*NEW*	-0.02	0.01	-0.03	0.00	-0.01	0.35	-0.00	0.92	0.00	0.76	0.00	0.03

Table 2.14 presents the sensitivity analysis for all main models. The first two columns show the dependent variables and the variables of interest. The other columns show the coefficients and p-values for the variable of interest at different definitions for audit partner audit expertise, i.e., the partner audits more clients with a particular characteristic than 50% of the partners that year, than the median of that year, 70%, 80%, 90%, and 95%.

For the audit quality analyses, we find the statistical significance of our variable of interest changes with different specifications. For example, the probability of issuing a GCO decreases with more stringent audit partner expertise cut-offs, while the negative effect on the absolute total accruals increases. These results suggest that audit partner alignment may increase audit quality, although we advise caution in interpreting these results. The effect changes at the lower cut-offs, indicating a potential non-linear relationship.

The tenure and change sensitivity analyses reveal that the more stringent the matching criteria, the more pronounced the effects we study. The alignment analyses show relatively robust results, except for the coefficient of *NEW*. This finding might be explained by the difference between Big 4 and non-Big 4 audit firm changes identified in the previous section.

Moreover, we used different alignment variables from Table 2.1 to estimate our models and obtained similar results (untabulated) to our main analysis. The considerable overlap between the different similarity variables explains the small differences across all specifications. Given that each variable has its specifications and similar small coefficients, these results reinforce the robustness of our models. Additionally, the Euclidean Distance is the only measure where a smaller number indicates a better match, yet it also yields comparable conclusions to our main analysis. The relevant coefficients are opposite but result in similar inferences to our other matching variables. Finally, our results remain robust when including audit firm fixed effects.

6. CONCLUSION

This paper provides evidence on how audit partner-client alignment links to audit quality, audit tenure, and audit partner changes. We also considered how alignment decisions differ depending on whether they relate to new-client acceptance decisions or existing-client rotations. Based on a sample of 152,272 company-year observations in Belgium from 2008 to 2019, we investigated if partners with prior experience auditing larger clients, financially risky clients, publicly listed clients, clients from specific industries, or those clients requiring IFRS expertise are more likely to match with clients with those characteristics.

Our findings suggest rather weak evidence for the association between audit partner-client alignment and improved audit quality as we only find a negative association between audit partner-client alignment and total accruals, driven by the negative association with income-decreasing total accruals. These results might be attributed to the broader range of aspects on which audit partners and clients might align beyond the characteristics we measure. For instance, Amir et al. (2014) find that riskier clients are more likely to hire risk-seeking audit partners. However, these audit partners tend to provide lower audit quality, indicating that specific types of alignment between audit partners and clients, such as those rooted in risk preference, may have adverse effects on audit quality. In addition, clients and audit partners at least partially focus on an interpersonal “fit” (e.g., Fiolleau et al. 2013; see *Chapter 4*), with potential consequences for audit quality (e.g., Yu, Kwak, Park, and Zang 2020).

Further, we find that higher audit partner-client is associated with longer audit tenure, and a lower likelihood of changing audit partners. Interestingly, alignment is weaker after an audit partner change resulting from within-firm audit partner rotations but not when resulting from audit firm rotations. In the latter case, audit partner-client alignment neither increases nor declines. The weaker alignment after a within-firm partner change may be due to audit firms’ lack of sufficiently experienced partners or clients not caring about the new partner because the audit firm, and potentially the rest of the audit team, remain. Our results show that partner-client alignment is stronger for clients new to the audit firm than for clients who experience a within-firm partner rotation. This result is consistent with the idea that audit firms scrutinize new clients more carefully than continuing clients (Johnstone and Bedard 2004). Furthermore, when participating in a tender process, audit firms may present their best-suited partners for that particular client (Fiolleau et al. 2013). Finally, our analysis reveals that partner rotations stemming from audit firm changes are associated with weaker alignment for transitions to non-Big 4 firm audit partners. However, there is no significant association observed for transitions involving Big 4 audit partners. A potential explanation for this finding is that Big 4 firms may possess greater resources to present the “best” audit partner.

Given that we find evidence that audit partner-client alignment is associated with higher audit quality, fewer changes, and longer tenure, our findings provide insights relevant to audit partner and audit firm rotation regulations. The observation that partner-client alignment involving new-client acceptance is stronger compared to existing-client partner rotations suggests that the initial alignment of a new audit partner with a new client is more advantageous in terms of partner-client alignment than rotating partners for existing clients. Furthermore, our results suggest clients may not specifically hire the highest-quality audit partner that matches their characteristics – higher audit partner-client alignment is weakly associated with higher audit quality, but audit partner changes are associated with lower alignment. Whether this is because of audit partner availability or client preferences is unclear. Future research may explore this issue further by examining how clients select their audit partners in more detail.

Our study is subject to the following limitations. Our data arise from a single country, so future research will have to establish the generalizability of our results. While the Belgian audit market is similar to many other small European audit markets, it differs in important respects from others, such as the US audit market. Audit partner-client alignment could be even more important in the US audit market because of stronger liability concerns. Such concerns make alignment more critical from a defensive auditing perspective. Future research can also attempt to draw distinctions in alignment under mandatory audit firm rotation regimes compared to voluntary audit firm rotation.

CHAPTER 3. CREATIVE COMPLIANCE: ISOMORPHISM AND DECOUPLING IN AUDITOR SELECTION PROCESSES

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Abstract

This study examines auditor selection processes from eight large companies in various stages of the process in the Netherlands from 2019 to 2022, focusing on the impact of mandatory audit firm rotation reforms. Our field study includes semi-structured interviews with 29 key stakeholders and documentary evidence. We find that clients organize their selection processes thoroughly upfront, retain formal decision-making power in the hands of the audit committee, and favor auditors with high reputations. This approach, shaped by the need for legitimacy driven by coercive, mimetic, and normative pressures (DiMaggio and Powell 1983), results in isomorphic process organization. Client idiosyncrasies and the necessity for a robust auditor-client relationship lead to decoupling, creating a disconnect between the clients' formal structures, policies, and processes and their actual practices (Bromley and Powell 2012). Our findings suggest that although formal auditor selection process structures are intended to maintain legitimacy in the eyes of regulators and stakeholders, practical considerations frequently result in audit clients depending on discretionary judgments and the involvement of management in the decision-making.

Keywords: auditor selection; audit regulation; auditor-client relationship; institutional theory; case study.

1. INTRODUCTION

The auditors' role is to provide assurance over a company's financial statements for the benefit of shareholders and external stakeholders, despite being engaged by the company and its management (e.g., Antle 1984; Dhaliwal, Lamoreaux, Lennox, and Mauler 2015; European Commission (EC) 2010; Mautz and Sharaf 1961). The balance between maintaining client relationships and ensuring objective auditing creates a fundamental tension in preserving auditor independence, especially in the context of management's potential influence over the audit process (Bazerman, Morgan, and Loewenstein 1997; van Brenk, Renes, and Trompeter 2020).[31] Auditor independence relates to the probability that the auditor will report a discovered breach in the financial reports (DeAngelo 1981; Watts and Zimmerman 1983) and is crucial to safeguard the value of the audit (Nelson 2006; Power 1999). Among numerous aspects of the auditor-client relationship, selecting auditors emerges as an important mechanism for ensuring auditor independence and the overall quality of the audit (Adelopo 2012; ICAS 2017; Regulation (EU) No 537/2014). Potential independence improvements include shifting the hiring power away from managers (e.g., Fatemi 2012; Mayhew and Pike 2004; van Brenk et al. 2020), increasing audit committee involvement (e.g., Beasley, Carcello, Hermanson, and Neal 2009; Chen and Zhou 2007), or introducing mandatory rotation requirements (e.g., Boon, Crowe, McKinnon, and Ross 2005; Elder and Yebba 2020). The 2014 EU Audit Reform installed such regulatory reforms to achieve independent, transparent selection processes by introducing enhanced audit committee responsibilities and mandatory audit firm rotation.

This paper reports results from a field study investigating how large companies organize their auditor selection process in this new institutional setting. Specifically, we examine how clients and auditors engage in legitimacy-creating practices in response to external pressures from undertaking an auditor selection process under new audit firm rotation requirements. Moreover, we investigate whether and how clients potentially decouple their formal processes from their actual practices for efficiency purposes.

Research on this topic is timely because the introduction of mandatory audit firms and partner rotations increases the frequency of auditor selection processes. For example, companies in the European Union (EU) switched auditors at twice the rate in 2016-2017

[31] In this chapter, we use the term "(external) auditor" for both "audit firm" and "audit partner" if either term is not specifically mentioned, as we notice that, in the auditor selection process, these terms are strongly linked together and indistinguishable for some topics. When possible, we use the most detailed level, i.e., we specifically use "audit firm" or "audit partner." The term "client" or "company" is used when discussing the client company.

compared to 2013-2014 (Willekens, Dekeyser, and Simac 2019). While rotations can provide greater auditor independence and a fresh pair of eyes performing audit work, tension arises from concerns, including increased audit costs, reduced expertise, and auditor susceptibility to pressure from management (Allam, Ghattas, Kotb, and Eldaly 2017). Notwithstanding these reforms, research indicates that management's influence over the auditor selection process remains significant when organizing a tender (e.g., Fiolleau, Hoang, Jamal, and Sunder 2013; Taminiau and Heusinkveld 2017) and with increased audit committee oversight (e.g., Beasley et al. 2009), suggesting that these regulatory efforts might be potentially ineffective. Furthermore, companies and audit firms allocate substantial resources and time – sometimes up to 18 months – to undertake extensive selection processes, indicating that such rotations are costly for auditors and clients (Fiolleau et al. 2013; Taminiau and Heusinkveld 2017). Finally, it is still unclear what clients look for when selecting an auditor, although recent research has started focusing on this topic by studying management (Christensen, Ege, Sharp, and Wilks 2024) and audit committee (Free, Trotman, and Trotman 2021) preferences. Despite the critical importance of auditor selection and its relevance to the investing public (Adelopo 2012; ICAS 2017), there is a notable lack of required public disclosure of information on these processes (Gold, Klynsmit, Wallage, and Wright 2018; SEC 2015).

Our investigation covers eight distinct cases of auditor selection processes in the Netherlands between 2019 and 2022. We leverage the recent implementation of mandatory audit firm rotation to examine a variety of auditor switches. It includes seven companies classified as Public Interest Entities (PIEs), subject to the mandatory auditor rotation regulations, and one large non-PIE. We are interested in understanding how the process was set up between the different actors, such as the client's management and AC, and also what role the auditor plays in this process. Our study includes 25 semi-structured interviews with 29 key participants, including managers, audit committee members (ACMs), and incumbent audit partners, as we tried to get as many individual points of view from multiple auditor selection processes. Furthermore, we received internal documents such as request for proposals (RFPs), scorecards, internal presentations, and Q&As, which we used to triangulate our interview findings, following best practice guidelines in field research (e.g., Malsch and Salterio 2016; Power and Gendron 2015). This methodology enables us to obtain a detailed view of auditor selection processes within this institutional setting, particularly in light of regulations aimed at increasing auditor independence.

We analyze our data using institutional theory, specifically focusing on isomorphism and decoupling, as public accounting is a highly institutionalized field (Carpenter and Dirsmith 1993; Robson and Ezzamel 2023). In this context, changing regulatory landscapes and market dynamics can significantly drive institutional change (Greenwood, Suddaby, and Hinings 2002). Organizations adapt to environmental pressures in such an environment by evolving their practices to maintain or enhance legitimacy within their field (DiMaggio and Powell 1983; Greenwood et al. 2002; Meyer and Rowan 1977). This legitimacy creation, combined with uncertainty and ambiguity of how to organize such practices, can lead to institutional isomorphism (DiMaggio and Powell 1983) and decoupling (Bromley and Powell 2012; Meyer and Rowan 1977). Our investigation considers the institutional change resulting from the European Audit Reform in 2014, which included the introduction of Directive 2014/56/EU, hereafter “the Directive”, and Regulation (EU) 537/2014, hereafter “the Regulation” (EC 2014a; EC 2014b).

We find that, to create legitimacy in their selection process – for instance, towards their shareholders, investors, and the media – clients organize their selection process thoroughly upfront, maintain the formal decision-making power in the audit committee, and choose high-reputation auditors. The need for legitimacy, together with the uncertainty and ambiguity about how to organize these selection processes, results in highly isomorphic process organization resulting from coercive, mimetic, and normative pressures (DiMaggio and Powell 1983). We focus on the interplay between coercive, mimetic, and normative institutional isomorphism in the auditor selection processes (DiMaggio and Powell 1983). However, we also notice client idiosyncrasies shaping the expectations of clients and, thus, their selection criteria and decision-making. Indeed, in accordance with the idiosyncratic needs of clients and the fact that not all companies have the same need for legitimacy, as they have different stakeholders, we find that the clients decouple their decision-making practices from this formalized process (Bromley and Powell 2012). Regulatory frameworks, such as the Regulation, mandate that audit committees lead auditor selection based on transparent, non-discriminatory criteria, minimizing management’s influence. However, empirical observations reveal that management frequently plays a pivotal role, driven by the necessity of an effective auditor-client relationship. While formal structures aim to uphold legitimacy and good governance, practical considerations rely on discretionary judgments and interpersonal dynamics, overshadowing the “transparent and non-discriminatory” criteria.

Our study adds to the literature by investigating the dynamics between audit committee auditor appointment responsibilities and the influence of management in the auditor selection process. It reveals the persistent tension between maintaining professional objectivity and managing client relationships (Bazerman, Morgan, and Loewenstein 1997; van Brenk, Renes, and Trompeter 2020), even in the stringent mandatory audit firm rotation setting. Furthermore, we add to the literature on mandatory tendering requirements and how this potentially impacts auditor independence. Utilizing institutional theory, our findings illustrate how companies organize auditor selection processes to create legitimacy. It explores the role of coercive, mimetic, and normative isomorphism in these processes (DiMaggio and Powell 1983), demonstrating how companies adapt their practices to meet external pressures and maintain legitimacy. The study's findings on isomorphic tendencies and decoupling practices provide nuanced insights into how formal processes are often separated from actual decision-making practices for efficiency and practical considerations (Bromley and Powell 2012). Finally, we outline auditor selection processes at large companies, why they are organized in a certain way, who is involved, and which criteria play a role. The inclusion of various stakeholders, such as managers, ACMs, and audit partners, enriches the practical understanding of these processes. Our research also has policy implications, given that our findings suggest that regulatory changes intended to enhance auditor independence by altering the selection process may not have achieved their desired effect. Shareholder involvement in auditor selection remains largely symbolic, while management continues to exert significant influence. Regulatory ambiguity leads to varied interpretations and standardized processes that may not fit specific client needs. The perceived lack of choice in the Dutch audit market indicates a need for regulatory bodies to promote competition and address market concentration. Decision-making often prioritizes interpersonal relationships over formal criteria, which regulators should consider, and scorecards used to evaluate auditors serve as legitimizing tools but do not reflect the final decision-making, which is based on relational factors.

We outline the regulatory changes resulting from the Regulation and the institutional setting in Section 2. Section 3 introduces the institutional theory used in our analysis, while Section 4 discusses our methodology. We present our analysis in Section 5. Finally, we discuss the results and offer a general conclusion and avenues for future research.

2. Selecting an Independent Auditor

Auditor independence relates to the probability that the auditor will report a discovered breach in the financial reports (DeAngelo 1981a; Watts and Zimmerman 1983). Yet, while their role is to provide assurance over a company's financial statements for the benefit of shareholders and external stakeholders, auditors are engaged by the company and its management (e.g., Antle 1984; EC 2010; Mautz and Sharaf 1961). This creates tension, as "Regulators view auditor independence as likely compromised when management is responsible for the selection, retention, and compensation of the external auditor, as auditors may view their responsibility as serving management rather than users of the financial statements" (Dhaliwal et al. 2015, p. 577). Furthermore, long auditor tenure can compromise auditor independence because of the development of personal relationships between client management and the audit partner (e.g., Carey and Simnett 2006; Mautz and Sharaf 1961). Among numerous aspects of the auditor-client relationship, selecting auditors emerges as an important mechanism for mitigating these issues, thereby ensuring auditor independence and the overall quality of the audit (Adelopo 2012; EC 2014b; ICAS 2017).

2.1. Measures to Safeguard Auditor Independence in the Auditor Selection Process: Literature Review

The academic literature discusses a variety of measures related to auditor selection to increase auditor independence, which mainly focuses on hiring power and mandatory rotation and tendering requirements. First, shifting the hiring power from managers to investors increases audit quality (e.g., Fatemi 2012; Hurley, Mayhew, and Obermire 2019; Mayhew and Pike 2004). Furthermore, board and audit committee involvement positively correlates with a demand for high-quality auditing (e.g., Beasley and Petroni 2001; Chen and Zhou 2007).

Another strand of research focuses on mandatory rotation and tendering as a solution to enhance auditor independence. Overall, this body of research suggests that mandatory rotation and tendering increase competition and audit quality (e.g., Boon et al. 2005; Elder and Yebba 2020). Gold et al. (2018) find that investors consider audit committees' hiring power only as relevant when it is mandatory for companies to periodically consider their auditor appointment (i.e., mandatory rotation or tendering). Debates on mandatory rotation highlight potential benefits for greater auditor independence and a "fresh pair of eyes" performing audit work. At the same time, concerns include increased audit costs, reduced expertise, and auditor susceptibility to pressure from management (Allam et al. 2017). The underlying premise of measures regulations is that they enhance audit quality by weakening the economic and relational bonds between auditors and their clients (Fiolleau et al. 2013), thereby improving independence in fact and appearance. However, limited research has been performed on the effects of mandatory audit firm rotation and how this impacts the auditor selection process.

2.2. Measures to Safeguard Auditor Independence: Regulations

Regulatory reforms aimed at bolstering auditor independence by increasing audit committee responsibilities have been increasingly introduced across various jurisdictions, beginning with the Sarbanes-Oxley Act in the United States (US) in 2002 and followed by similar measures in Canada (2004), the EU (2006), and India (2009) (see *Chapter 1* for an overview). Although the Public Company Accounting Oversight Board (PCAOB) opted against implementing mandatory audit firm rotation, favoring robust audit committees instead (PCAOB, 2011), the European Commission (2010, p. 11) contends that "Situations where a company has appointed the same audit firm for decades seem incompatible with desirable standards of independence." Consequently, the EU Audit Reform, influenced by the "Audit Policy: Lessons from the Crisis" Green Paper (EC, 2010), was enacted in 2014 and came into effect in 2016. This Green Paper identified critical areas for change, which include enhancing investor transparency, reducing conflicts of interest, stimulating competition within the audit market, and establishing robust public oversight. Auditor independence was perceived as crucial, as it is "the unshakeable bedrock of the audit environment" (EC 2010, p. 10).

We focus on two pivotal aspects of the 2014 EU Audit Reform for Statutory Audits, and specifically the Regulation, related to auditor selection: (1) mandatory rotation and (2) tendering requirements for PIEs. Under the Regulation, PIEs must rotate their statutory auditors or audit firms at intervals not exceeding ten years.[32] Member States have the discretion to set the minimum duration of initial engagements and the maximum total duration, which can extend to 24 years for joint audits.

2.3. The Formalized Selection Process

This section provides an overview of Article 16 of the Regulation and its impact on the auditor selection process. The selection process must encompass several steps. The audited entity is free to invite any statutory auditors or audit firms to submit proposals. The audited

[32] For non-PIE audits, no firm or partner rotation is required.

entity shall prepare tender documents that allow the auditors to understand the business and the type of audit to be carried out. Furthermore, these documents shall contain "transparent and non-discriminatory" selection criteria that the client shall use to evaluate the audit proposals, as "Quality and independence should be key selection criteria in any tendering procedure" (EC 2010, p. 16). The requirements allow for considerable discretion in the selection process, as the audited entity is free to determine the selection procedure and may conduct negotiations with interested tenderers during the procedure.

Regarding hiring authority, the Regulation stipulates that audit firms must be appointed by the annual general meeting of shareholders (AGM). This mandate reinforces the independence of the statutory auditor or audit firm from the executive members of the audited entity. The appointment procedure under Article 16 of the Regulation is executed in three stages: the audit committee organizes the tender procedure, then the evaluation is made in accordance with selection criteria predefined in the tender documents, after which a report is prepared and validated by the audit committee. The audit committee then makes a recommendation that includes at least two options for the audit engagement, and the administrative or supervisory body of the audited entity then recommends to the general meeting of shareholders. The recommended statutory auditor or audit firm must have participated in the tender procedure (EC 2014b).

Interestingly, while the Regulation stipulates specific tender requirements, there is no guidance on a timeline or specific criteria, only that the process should take place in a "fair and non-discriminatory way." The Regulation does not provide more detail on "transparent and non-discriminatory criteria." Consequently, uncertainty exists about how the process is organized and carried out (e.g., CSSF 2021). In addition, neither Article 16 nor any other article of the Regulation defines any legal consequences in case a public interest entity or an auditor fails to meet the procedure requirements under Article 16 of the Regulation.

The European Commission conducted a post-implementation review of the outcomes of the reforms. Between 2016 and 2020, approximately half of the companies changed auditors at least once, influenced by various factors, including the introduction of the rotation requirement, general corporate governance practices, corporate restructuring, and auditor performance dissatisfaction (EC 2022). This study argues that post-reform, the introduction of mandatory rotation has contributed to improved quality of the audit services and auditor independence. Additionally, it highlights that the Audit Reform did not impact competition as intended. The switch across different types of auditors has been limited, with a persistently high market share for the Big 4. The concentrated nature of the audit market and restrictions on non-audit services limit auditor choices for PIEs, typically restricting them to major competitors (EC 2022). However, this study did not report details on how the reforms influenced companies' and auditors' approach to the selection process.

2.4. The Dutch Setting

Audit regulation in the Netherlands stems mainly from the previously discussed EU legal framework (specifically Directive 2014/56/EU and EU Regulation No 537/2014) (Van Linden and Hardies 2018).[33] Under the Dutch Audit Profession Act, mandatory audit firm rotation became effective for PIEs on January 1, 2016.[34] Audit firm rotation is mandatory after ten years, without any exemptions (de Jong, Hijink, and in 't Veld 2020). There is also a four-year cooling-off period before a firm can be re-contracted for audit services. Furthermore, a one-year cooling-in period exists before the selection, prohibiting the statutory auditor from internal control-related non-audit services.

Engagement partner rotation applies after a maximum of five years in case of a statutory PIE audit. Again, the Dutch rules impose stricter auditor rotation requirements than the EU regulations, which impose partner rotation after seven consecutive years. Audit firms are set strict rules and are under thorough surveillance by the Dutch Authority for the Financial Markets (AFM) for obtaining the license to audit PIEs (AFM 2017; International Monetary Fund 2017).[35] Consequently, only six firms in the Dutch audit market are currently allowed to perform PIE audits.

[33] PIEs in the Netherlands are legal entities established in the Netherlands under Dutch law, whose securities are admitted to trading on a regulated market as referred to in Article 1:1 of the Financial Supervision Act. A bank with its seat in the Netherlands as referred to in Article 1:1 of the Financial Supervision Act to which a license has been granted under that Act; A central credit institution with its seat in the Netherlands as referred to in Article 1:1 of the Financial Supervision Act to which a license has been granted pursuant to that Act; A life insurer or non-life insurer with its seat in the Netherlands as referred to in Article 1:1 of the Financial Supervision Act to which a license has been granted pursuant to that Act; An enterprise, institution, or public body, belonging to one of the categories designated pursuant to Article 2. (NBA ALERT 27)

[34] Art. 41 Audit Regulation. As of 17 June 2020, audit engagements cannot be entered into or renewed if the auditor or audit firm has been providing audit services for 20 or more consecutive years at the date of entry into force of the Regulation. As of 17 June 2023, this applies if audit services have been provided for 11 or more but less than 20 consecutive years at the date of entry into force.

[35] The Dutch Authority for Financial Markets (AFM) is responsible for supervising the operation of the financial markets and oversees audit entities that provide auditor reports relevant to the Dutch capital markets.

3. THEORETICAL FOUNDATIONS

3.1. Legitimacy and Institutional Theory

Public accounting is a highly institutionalized field (Carpenter and Dirsmith 1993; Robson and Ezzamel 2023). In such a field, changing regulatory landscapes and market dynamics could significantly drive institutional change (Greenwood et al. 2002). Institutional theory suggests that organizations adapt to environmental pressures by evolving their practices to maintain or enhance legitimacy within their field (DiMaggio and Powell 1983; Greenwood et al. 2002; Meyer and Rowan 1977). Organizations achieve legitimacy by conforming to accepted ways of doing business, adhering to legal mandates, copying the practices of other successful organizations, or adapting widespread practices that have otherwise been legitimated within the environment (DiMaggio and Powell 1983; Meyer and Rowan 1977).

We apply institutional theory to our field study data to understand how audit firms and clients organize the auditor selection process surrounded by regulatory pressures and stakeholder pressures such as shareholders and investors. For example, clients have to be able to prove to legislators that the process was conducted in a transparent, non-discriminatory way, and the client's shareholders may care how the process was designed, as they are the ones who eventually approve the appointment. Furthermore, institutional investment organizations, such as Eumedion, provide a yearly evaluation of the significant auditor selection processes conducted in the Netherlands.[36] The development and introduction of audit reforms heightened scrutiny of practices to enhance auditor independence, including the auditor selection process. The new independence regulations introduced uncertainties for clients in the auditor selection process, including timelines, criteria, and repercussions for failing to comply, as they seek legitimacy from regulators and stakeholders. The following discussion explores how uncertainty and legitimacy-seeking are linked to institutional isomorphism.

3.2. Institutional Isomorphism as a Consequence

Organizations within a similar environment develop legitimacy-creating practices that often converge, resulting in increasingly similar practices among these organizations. This convergence, driven by mimetic, coercive, and normative pressures in their pursuit of

[36] Eumedion advocates for institutional investors in corporate governance and sustainability, focusing on improving practices in Dutch-listed companies and promoting responsible shareholding among its members. Every year, Eumedion prepares an evaluation of the season of annual reports and shareholders meetings, the AGM season. For more information, see https://www.eumedion.nl/Over-Eumedion.html).

legitimacy (DiMaggio and Powell 1983), exemplifies the process of isomorphism. The authors describe the process of isomorphism as forcing one unit in a population to resemble other units operating in similar environmental conditions. While the driving mimetic, coercive, and normative pressures are conceptually distinct, they often interconnect and overlap in practice (DiMaggio and Powell 1983). Next, we discuss the isomorphic pressures.

3.2.1. Coercive Isomorphism

Coercive isomorphism results from formal and informal pressures from entities such as government agencies or regulators and cultural expectations in their societal environment, which compel organizations to adopt specific practices (DiMaggio and Powell 1983). Specifically, the primary driver of these isomorphic changes is the need for organizations to comply with the demands of these influential external parties (Tuttle and Dillard 2007). In auditor selection, regulations prescribing audit firm rotation, independence requirements, and audit committee roles could impact the process. In addition to litigation and legal risks, these rules constrain companies' prospects for suitable auditors and shape selection processes and criteria. Moreover, legal requirements for financial disclosures can make specific auditor expertise or credentials necessary. External stakeholder pressures, such as those from shareholders and potential investors, also influence the process, potentially making criteria such as reputation, compliance, and independence more crucial.

3.2.2. Mimetic Isomorphism

Tuttle and Dillard (2007) explain that mimetic isomorphism arises either in the initial phases of a field or when major innovations induce uncertainties about effective processes and the criteria for distinguishing between superior and inferior performance. We argue that the introduction of mandatory audit firm rotation presents such a case. The challenge in defining and assessing high-quality auditing introduces uncertainty about what constitutes a competent auditor (Causholli and Knechel 2012; PCAOB 2015) and, therefore, which criteria to use when searching for an auditor. Additionally, clients are not required to publicly disclose their auditor selection process (Gold et al. 2018; SEC 2015). In such uncertain environments, organizations often mimic others (DiMaggio and Powell 1983). Confronted with unclear challenges, firms may opt for "viable" choices, leading to efficient but potentially suboptimal solutions (Cyert and March 1963). Dutch PIEs are limited to choosing from only six PIE-licensed audit firms, and this limited range of options can also drive organizational homogeneity (DiMaggio and

Powell 1983). Mimetic pressures involve benchmarking and identifying best practices and industry leaders, leading to the adoption of legitimized practices from others in the field (Tuttle and Dillard 2007).

3.2.3. Normative Isomorphism

DiMaggio and Powell (1983) define normative isomorphism as the development of a shared cognitive base among professionals through the formation of organizations, which then propagate common orientations and practices to legitimize the profession. In the context of new audit regulation, Griffith, Hammersley, Kadous, and Young (2015) describe it as the adoption of practices that become standardized through professional training and interaction. This implies that auditor selection is influenced not only by regulatory compliance but also by adherence to the standards and ethics set by accounting bodies. The educational and professional backgrounds of decision-makers can also incline the selection toward auditors or firms known for their prestige or expertise. Furthermore, cultural norms within specific industries, such as a focus on innovation, sustainability, or risk management, might steer the selection towards auditors proficient in these areas. Moreover, we expect technological progress and market trends, such as the move towards sustainability reporting in auditing, to induce isomorphism, leading to similar auditor selection processes and outcomes across organizations. The best practices promoted by audit firms and professional bodies, representing normative isomorphism, embody the standards and norms highly regarded within the professional community. While these standards are not enforced by law, there is a solid professional and ethical imperative to comply with them.

3.3. Decoupling as a Response

An important potential consequence of the external pressures driving convergence in the auditor selection process for legitimacy purposes is that isomorphic processes may not enable auditors and clients to meet their goals efficiently or effectively if the legitimized practices are inappropriate for the specific organization and task (DiMaggio and Powell 1983). In the audit setting, Causholli and Knechel (2012) suggest that the unique characteristics of each audit would not be adequately addressed with a standardized approach. Therefore, standardization does not necessarily enhance audit quality as client-specific needs and expectations are neglected in the search for uniformity in process organization (Knechel, Thomas, and Driskill 2020).

Organizations face inherent tensions between conforming to institutional expectations and addressing practical efficiency or operational needs (Bromley and Powell 2012). Consequently, conformity to external pressures does not always translate into substantive changes in organizational practices, leading to a phenomenon known as decoupling (Bromley and Powell 2012; Meyer and Rowan 1977). Decoupling refers to the disconnect between an organization's formal structures, policies, or processes, and actual practices. Decoupling allows organizations to maintain legitimacy in their institutional environment while managing internal efficiencies and practicalities that may not align with external expectations. Organizations may adapt to institutional norms, often leading to surface-level alignment with these norms while maintaining internal practices. This adaptation can result in decoupling, where formal structures and policies do not accurately reflect the actualities of auditor-client interactions (Boxenbaum and Jonsson 2008). Decoupling takes two forms: policy-practice and means-ends decoupling. Policy-practice decoupling happens when rules or policies are formally in place but are unimplemented or routinely violated. Means-ends decoupling occurs when policies are implemented, but the link between these policies and the intended outcomes remains unclear or ineffective (Bromley and Powell 2012).

In the context of auditor selection, the concept of decoupling is particularly relevant because of the complex interplay of regulatory requirements, professional norms, and market pressures. The research conducted by Fiolleau et al. (2013) brings to light how regulatory changes, despite being aimed at enhancing auditor independence, might not necessarily lead to substantive changes in how auditors are selected or function. From a service perspective, the auditor-client relationship is complex and often characterized by mutual dependencies (see Knechel et al. 2020). For instance, clients can significantly impact the audit process (Daoust and Malsch 2020). Guénin-Paracini, Malsch, and Tremblay (2015) argue that the practical achievement of auditors' operational independence cannot be readily guaranteed merely by the formulation of institutional measures. This literature suggests a potential disconnection between adopting a formal auditor selection process for legitimacy purposes, focused on independence, transparency, and non-discrimination (to comply with the requirements), and not fully implementing it in practice (to achieve the client's needs) (Boxenbaum and Jonsson 2008). Understanding these dynamics is essential for understanding the auditor selection process and addressing the challenges in attaining genuine auditor independence and high audit quality.

We examine two topics that flow from institutional theory in the context of new regulatory requirements that influence the auditor selection process. First, we examine clients' legitimacy-creating practices in response to external pressures from undertaking an auditor selection process under new audit firm rotation requirements. Second, we focus on whether and how clients decoupled their formal processes from their actual practices. Therefore, are research questions are:

RQ1: How do companies formally organize their process to select an auditor under new audit firm rotation requirements?

RQ2: To what degree do actual practices correspond to the auditor selection processes that the companies formally established?

4. Research Method and Participants

In this study, we examine eight distinct cases concerning their auditor selection process, spanning from 2019 to 2022. Within this sample, seven entities are categorized under the mandatory auditor rotation regime in the Netherlands and identified as PIEs. Among these, six companies rotated their auditor to comply with the legal mandate, while one opted for a change in auditors earlier than mandated. The non-PIE, which is not subject to mandatory auditor rotation, also voluntarily changed its auditor. Seven clients appointed a Big 4 auditor, and one client a non-Big 4 auditor. Six clients changed from one Big 4 auditor to another, one from a Big 4 to a non-Big 4, and another from a non-Big 4 to a Big 4 auditor. The involvement of these companies and their respective auditing firms was facilitated through the efforts of the Foundation for Auditing Research (FAR), which contacted the audit firms for access to their clients that had recently undertaken or were about to undertake an auditor selection process. Five different audit firms provided at least one recent audit firm rotation case. In the final two cases, we observed that the point of saturation had been reached, consistent with the principles articulated by Power and Gendron (2015) and Malsch and Salterio (2016). Specifically, the seventh and eighth cases yielded detailed and consistent information that corroborated the findings from earlier interviews, both through case-by-case analysis and cross-respondent comparisons. The quotes included in this paper are derived from all the cases studied.

4.1. Data Collection

Consistent with other qualitative studies on auditor-client interactions (e.g., McCracken et al. 2008; Cohen et al. 2010; Fiolleau et al. 2013; Dodgson et al. 2020), we employed a semi-structured interview approach. For each case, we interviewed the current audit partner, one member of the audit committee, and at least one member of the client's management involved in the auditor selection process. Table 3.1 shows a more detailed overview of the participants per case.

We conducted semi-structured interviews using pre-defined scripts, which were updated throughout the data collection to better align with our interests. We tailored two distinct interview transcripts to address the specific perspectives of different participant groups: one for audit partners and another for client interviewees (which included ACMs, CFOs, controllers, and internal audit managers). Additionally, we developed specialized subquestions for ACMs and managers, acknowledging the varying roles and responsibilities they hold in the auditor selection process. We drafted these scripts based on best practices and regulations related to auditor selection, drawing on multiple sources (e.g., SOX 2002; Deloitte 2016; KPMG 2018; EC 2014b). Additionally, we reviewed the last 20 years of literature on auditor selection in leading accounting journals, summarizing it to identify potential research avenues for this study (see *Chapter 1*). We then compiled this information into interview scripts, which the researchers on our team reviewed and refined. We identified five key topics for company members and six for audit partners. The interview scripts included open-ended, neutral, general questions and predefined sub-questions for each topic (Power and Gendron 2005). The open-ended, general questions are available in Appendix B1. Our sub-questions served as conversation guidelines, though we let respondents freely describe their selection process and explore topics in depth as they saw fit, similar to the approach by other qualitative research on auditor-client interactions (e.g., Dodgson et al. 2020; Fiolleau et al. 2013; Free et al. 2021).

We emailed participants a project summary and interview agenda, requesting written consent for their participation and the recording of interviews. Furthermore, we added a support letter from the FAR. The documents are located in Appendices B2, B3, and B4. We also invited the interviewees to provide feedback on additional items or topics for discussion, leading to a minor script update after five interviews. Our field research process was set up and executed following best practice guidelines (e.g., Malsch and Salterio 2016; Power and Gendron 2015; Yin 2014).

TABLE 3.1
Overview Case Studies

Case	Industry	Process duration	Timing Interviews	Respondent Position	Current job experience (in years)	Interview duration
1	Real estate	Seven months	One year after rotation	Audit partner	11-15	70 min
				Internal audit manager	0-5	68 min
				CFO	11-15	68 min
				ACM	0-5	67 min
2	Distribution	Three months	After selection, before rotation	Audit partner	26-30	54 min
				Internal audit manager	6-10	88 min
				Controller	6-10	90 min
				CFO	0-5	55 min
				ACM	16-20	34 min
3	Retail	Six months	After selection, before rotation	Inc. audit partner	11-15	58 min
				Controller	6-10	82 min
				ACM	6-10	70 min
				Audit partner	20-25	61 min
4	Finance	Seven months	Two years after rotation	Audit partner	11-15	64 min
				Audit senior manager	11-15	64 min
				CFO	0-5	56 min
				ACM	6-10	73 min

5	Finance	Six months	One year after rotation	Audit partner	5-10	74 min
				CFO	15-20	78 min
				Internal audit manager	10-15	78 min
				ACM	5-10	52 min
6	Services	Five months	One year after rotation	CFO	10-15	53 min
				Audit partner	5-10	23 min
7	Rental	Three months	One year after rotation	CFO	10-15	68 min
				Audit partner	10-15	51 min
8	Entertainment	Five months	3 months after rotation	CFO	0-5	32 min
				Controller	0-5	72 min
				Controller	5-10	72 min
				ACM	0-5	45 min

Table 3.1 provides an overview of all cases studied and interviews performed. The process duration column shows how long the tender process itself took. In the column 'Timing interviews', the timing of the interviews vis-à-vis the eventual rotation is shown. Abbreviations used in this table are Chief Financial Controller (CFO), Audit committee member (ACM), and Incumbent audit partner (Inc. audit partner). The respondent position is the position with respect to the specific case. We assigned broad job descriptions to the participants to mitigate identification possibilities due to specific job titles. The current job experience pertains to the number of years of experience the respondent has in their current role for the client interviewees. For the auditor interviewees, the current job experience pertains to the number of years of experience in their current role, not fixed to the current audit firm.

We conducted 20 interviews via Microsoft Teams and five in person.[37] Four interviews included two participants each, while the remaining interviews involved a single participant, resulting in a total of 29 participants. Each interview featured two team members: The first author focused on the interview's main content while the other team member (the fourth author for 22 interviews, the third author for three interviews) managed time and posed follow-up questions as needed. Interviews ranged from 23 to 90 minutes, averaging 62 minutes. Three interviews were conducted in English, the remaining 22 interviews were conducted in Dutch. Every session began with an overview of the research and our team and concluded with a review of the confidentiality agreement. We also invited respondents to share their professional backgrounds, including their expertise, experience, and role within the company being studied. To ensure the trustworthiness of our analysis, we performed member-checking (Malsch and Salterio 2016), sending a draft of the manuscript to each interviewee for commentary, and assured participants that any quotes considered for inclusion in our paper would be reviewed with them to verify accurate interpretation. Our member-checking e-mail is presented in Appendix B5. Some participants requested slight modifications to their quotes. We followed our interview scripts but departed from our protocol when responses took us down an important path (Yin 2014).

The first author transcribed the interviews, ensuring the pseudonymization of all mentioned names by assigning random codes to the interviewees.[38] This researcher utilized ten transcripts to inductively generate first-order codes, which were then aggregated into a coding scheme. This scheme encompassed topics predetermined by our review of practitioner, regulatory, and academic literature and identified through extensive discussions among the research team during and after the interviews. Each aggregated code received a concise description, enabling a second coder to analyze the interviews. We employed NVivo software to code and analyze the interview data. We regularly reread and reviewed transcripts to keep track of our insights (Kenno, McCracken, and Salterio 2017). Additionally, the first and fourth authors prepared a summary memo of observations from interviewees for each case, which all authors then analyzed. We compared each case memo against every other individual case and the collective set of cases. Throughout the project, we alternated between reviewing our data and examining

[37] Due to the COVID-19 pandemic, conducting on-site interviews was largely infeasible.

[38] Throughout the analysis, we assign a unique identifier to each respondent to denote their respective roles. The abbreviations utilized are as follows: AP for Audit Partners, CFO for Chief Financial Officers, ACM for Audit Committee Members, IA for Internal Audit Managers, and C for Controllers. To maintain anonymity and avoid potential identification, the numbering is randomized and does not correspond to any specific case studied.

theoretical concepts to test and validate our findings, as suggested by Yin (2014). From this iterative process, we noticed patterns of the interplay between institutional isomorphism and decoupling based on our observation that participants reported highly standardized, comparable auditor selection processes but varied perceptions and experiences of the outcomes. We developed a new coding scheme, as presented in Table 3.2, from the literature on institutional isomorphism and decoupling to code our interview data deductively. One author coded the data based on this scheme.

To supplement the interviews, we obtained additional documents on the selection process that participants uploaded to a digital vault.[39] These documents include inside correspondence on the selection process (e.g., presentations from the selection committee to the AC, Q&A's with the audit firms, audit proposals from winning and losing bids, outlines of the selection process, and scorecards). We use these evidence sources to clarify and validate findings from the interviews. We have also reviewed publicly available resources, including company websites and annual reports.

TABLE 3.2
Codebook Institutional Isomorphism and Decoupling

Top-level code	Description	Subcodes
Coercive isomorphism	This code relates to changes in auditor selection practices due to legal and regulatory pressures.	Regulatory compliance External pressures Adaptation to legal changes
Mimetic isomorphism	Pertains to the adoption of selection practices from other organizations, often as a response to uncertainty.	Benchmarking Modeling competitors Industry trends
Normative isomorphism	This code focuses on the influence of professional norms, education, and networks on auditor selection.	Professional standards Expert influence Educational impact
Impact of isomorphism on auditor selection	Analyzes the overall impact of isomorphic processes on the decision-making and outcome of auditor selection.	Tender process Decision-making process Selection outcomes Organizational changes
Case-specific examples of isomorphism	Captures specific instances or anecdotes from interviews that illustrate isomorphism in action.	Coercive examples Mimetic examples Normative examples
Decoupling in auditor selection	Addresses the discrepancy between formal policies and actual practices in auditor selection, highlighting how organizations may symbolically conform to external expectations while maintaining different internal practices.	Formal versus informal practices Symbolic compliance Practice-policy decoupling Means-end decoupling

Table 3.2 presents the codebook used for the final coding round of the interviews in Chapter 3.

[39] This digital vault was organized by CenterData, an independent data centre. In addition to the participant documents uploaded on the vault, the interviews were stored here as well during the transcription stages.

5. ANALYSIS

The auditor selection processes in this study are highly standardized, although there is some variety in the cases studied. For instance, management involvement varies across cases, and clients prioritize different criteria. We argue that the selection processes are well-organized responses to uncertainty, ambiguity, and the need for legitimacy. First, we elaborate on the steps towards a legitimate process and how isomorphic pressures result in similar practices (DiMaggio and Powell 1983). Then, we discuss how clients, during the auditor selection process, differentiate their external commitments from their internal operations to maintain efficiency (Bromley and Powell 2012).

5.1. Auditor Selection Process Preparation and Execution: Isomorphic Pressures in a Highly Structured Process

In light of legislative requirements, companies must rigorously structure their auditor selection process. This is especially pertinent for PIEs, where regulations are stringent and stakeholder expectations are high (EC 2014a). A well-organized and transparent selection process is a procedural necessity and a fundamental aspect of compliance while safeguarding macro-order comfort production (Pentland 1993). In the following sections, we highlight why clients engage in legitimacy-creating practices and which practices clients implement in their selection process to attain external pressures.

5.1.1. Searching for Legitimacy

The Regulation mandates that the audit committee leverages the outcomes of a mandatory selection procedure conducted by the audited entity under the audit committee's responsibility. The ultimate decision rests with the shareholders, who vote based on the audit committee's recommendation. Previous studies (e.g., Barua, Raghunandan, and Rama 2017; Cunningham 2017) suggest that shareholder voting tends to be more symbolic than substantive, with votes against the recommended auditor being a rarity. This symbolic nature is further underscored by our findings, where it is noted that the selected auditor often begins shadowing the current auditor even before the AGM, highlighting the procedural aspect of these gatherings. Shareholder voting, however, can be perceived as an effective monitoring mechanism. By expanding the shareholders' role in the auditor selection process, it enhances auditors' accountability to shareholders (Dao, Raghunandan, and Rama 2012; Krishnan and Ye 2005). In our study, respondents emphasized the necessity of a formally structured process to avoid questions at the AGM, with two CFOs specifically highlighting the process should be well-organized to avoid questions from the AGM.

Moreover, ACMs, managers, and audit partners mentioned the importance of the audit committee, not management, formally presenting the selection process results to the shareholders. While also a regulatory necessity, an audit partner mentioned, “I can imagine that if you work at a PIE, you would not want even to have the appearance of the public interest against you, that the management makes the decision” (AP6). Except for one client that could not appoint a Big 4 auditor because of independence issues, all clients studied emphasized the importance of hiring a Big 4 auditor. According to our respondents, hiring a Big 4 firm is often equated with acquiring an international network, quality, established processes, and a successful audit. External pressures, including media influence and stakeholder opinions, also play a role, as an ACM notes: “We would like to hire a Big 4, precisely because of all the reputation and the pressure from the media on the company” (ACM1). Additionally, a CFO (CFO3) noted that if negative news surfaced about the preferred candidate, they would not select that auditor, even if it were the only candidate available. The sentiment that reputation issues highly influence the process was echoed by the controller of one of the largest clients in our field study:

> In the Netherlands (…), we have about 200 listed companies, and none of them is audited by anyone outside the Big 4. We are in the top X of the highest index, so I think it wouldn’t be easy to justify choosing someone other than the Big 4. (Controller, C1)

This quote is particularly relevant because while the Regulation highlights the importance of non-discrimination in the selection process, the non-Big 4 firms are often not seen as a justifiable option to the shareholders and broader stakeholders. Interestingly, the non-PIE in our sample, a rapidly expanding organization, was under pressure because of the growing number of investors and felt the need to organize a formal selection process and hire a Big 4 auditor. Clients realize the external, mainly coercive and normative pressures by the regulators, shareholders, stakeholders, the media, and the broader public, and feel the need to formally put the audit committee in charge of the final recommendation to the board, have an upfront well-organized process, and focus mainly on the Big 4 auditors to create legitimacy surrounding the auditor process (DiMaggio and Powell 1983; Meyer and Rowan 1977). The following sections investigate how the different actors engage in these legitimacy-creating practices.

5.1.2. Uncertainty and ambiguity as predecessors for institutional isomorphism

While adhering to external pressures results in legitimacy-creating practices, "The audited entity has the discretion to determine its own selection procedure. This can include direct negotiations with interested parties during the process" (EU Regulation 537/2014, Article 16 [3e]). This creates an inherent ambiguity in how clients have to select their auditor. In addition, although this number is increasing, audit firm rotations in PIEs happen relatively infrequently. To illustrate, only 20% of the PIEs in the EU changed auditors between 2015 and 2018 (EC 2022). Moreover, some of our clients studied had never or only once changed auditors, and uncertainty exists about how to conduct this process. As a result, many clients use best practice guidelines by audit firms and institutional instances. This is particularly clear when no previous auditor selection process experience exists. In these cases, the clients almost precisely copied the existing best practice guidelines, indicating the uncertainty in executing the process, which results in falling back on best practices. These best practice guidelines suggest that the key features of a robust procurement process are thorough preparation regarding timing, the actors responsible for managing the process, and the means of evaluating prospective auditors and final decision-making (e.g., AICPA 2018; Deloitte 2016; KPMG 2018). The legislative change introducing mandatory audit firm rotation, coupled with the uncertainty stemming from a lack of previous rotations, led to increased information gathering from colleagues and competitors, particularly by ACMS. This is exemplified in the following quote: "I called a few of those friends [working at competitors]. Luckily, there were already some who had rotated [their audit firm], and we were able to take advantage of that in a way" (ACM6). Furthermore, interviewees mention using documents from their incumbent auditor, scientific documents, best practices, and regulators, as exemplified in the following quote:

> With the project team, we determined a list of request for proposals criteria. We did that based on, I think, work from our auditor, from scientific documents we have studied, where we looked at how audit quality is determined, we looked at brochures from Big 4 firms where they describe how such a process works and what the points of attention are. We looked at what the AFM focuses on in office rotations, so also how the regulator views audit quality. (Internal audit manager, IA1)

In all but one case, the management and ACMs mention using best practice guidelines to set up their process. These guidelines can even diminish the role of the ACM in the process set-up. A CFO explained, "There is so much uniform guidance on drafting an RFP document for an audit; those documents generally all look the same. There is generally little for the audit committee to add" (CFO6). In sum, the initial uncertainty and ambiguity about how to organize these processes, combined with coercive and normative pressures, appear to result in a highly institutionalized, isomorphic set-up of the auditor selection process. This set-up includes comparable selection committees, procedures, and criteria, which we discuss in the following sections.

5.1.3. Isomorphic Process Set-up

5.1.3.1. Selection Committee

All the clients studied have set up selection committees that manage the day-to-day aspects of the selection process, eventually making a recommendation to the audit committee. Although the Regulation assigns the audit committee the responsibility for the selection process, it does not specify who else is involved. Best practice guidelines suggest that "The audit committee should submit a proposal to the supervisory board for the external auditor's engagement to audit the annual accounts. The management board should play a facilitating role in this process" (Dutch Corporate Governance Code (DCGC) 2022, p. 19). Audit committees are advised to consider the management's evaluation of the audit teams (FRC 2017), with potential key influencers being the CFO, the controller, and the head of internal audit (Deloitte 2016; FRC 2017; ICAS 2017; KPMG 2018). The purchasing department was only involved in two cases. According to the controllers in these cases, their role in the process was to investigate the quotation materials and establish a line with the legal department to assess purchasing decisions.

The selection committees formed by the clients in our study typically include the audit committee chair, the CFO, and other management team members such as the controller, head of accounting, and head of internal audit. CEO involvement is relatively minimal, with only a few cases mentioning an explicit role in the process. However, it is noteworthy that the majority of the members of the selection committees are from the management team. This is surprising since the audit committee's responsibilities for appointing auditors, overseeing the selection process, and making final recommendations to the shareholders are outlined in various guidelines and regulations, including those by FEE (2013), ICAS (2017), and KPMG (2018), and the Regulation. However, these regulations often leave the audit committee's exact role during this process somewhat ambiguous. Still, practitioners suggest that the audit committee should be the primary decision-maker (e.g., Deloitte 2016, FRC 2017, ICAS 2017, KPMG 2018), which contrasts with the prevailing typical composition of a selection committee.

The ambiguity surrounding the audit committee's role and the unclear selection committee recommendations in best practice guidelines and regulations introduce further uncertainty, which, we argue, results in highly comparable selection committees. The primary overlap in all cases is the involvement of the audit committee chair and the CFO.

5.1.3.2. Inviting Firms: Timing and Constraints

Best practices indicate that completing a typical audit tender process usually takes about three months, but preparatory work may extend over several months or even years (e.g., Deloitte 2016; FRC 2017; KPMG 2018). Among our cases, the earliest initiation was two years before the rotation, the latest just six months prior. Most clients initiated their process approximately six months to a year before rotation. Interestingly, only two clients started the process more than a year in advance to account for the one-year cooling-in period. All audit partners highlighted a unique challenge in the Dutch market, where only six firms hold a PIE license. This issue is exemplified by the following quote:

> What you see now, especially in the Dutch market where only six firms have a public interest entity license (…), is that sometimes it can be very limiting. (…) The one that does it is often a Big 4 firm, especially [for] a large corporation. [The incumbent auditor] is not allowed to do it anymore, so they are out. Another Big 4 firm might be in conflict because they do a lot of advisory work, where the fee is usually higher than for the audit. So, the question ultimately is, you may rotate, but how much real choice is left? (Audit partner, AP5)

Audit firms are set strict rules and are under thorough surveillance by the AFM for obtaining the license to audit PIEs (AFM 2017; International Monetary Fund 2017). Another limitation in choice arises when the parent company engages an audit firm for certain tax services, rendering that firm ineligible for selection as the subsidiary's auditor. These coercive pressures result in a general lack of choice for clients. Intriguingly, clients can and sometimes do respond by adjusting the timing of their auditor changes based on their competitors' actions, opting for quieter market periods. One of the clients rotated early, and part of their motivation was that "At that moment, there were very few rotations in the market, so the offices were, well, I don't know if they were more eager, but you could reach them, and they were willing to take on this job as well" (Controller, C1).

In addition, while choices are limited, there is not much differentiation perceived among the Big 4 firms, as exemplified by a comment of an ACM: "These Big 4 companies, they can all conduct a good audit. You're not supposed to say that an audit is a commodity, but you can assume that they are capable of conducting a good audit" (ACM3). Despite six firms being eligible to audit PIEs, the clients studied revealed a preference for the Big 4 unless specific circumstances dictate otherwise. Coercive and normative pressures, such as liability concerns and heightened quality expectations from, among others, regulatory bodies, the public, and the media, appear to drive this phenomenon.

The resulting scarcity of options and the coercive and normative pressures on the PIE-licensed audit firms and their clients further explain the similarity in the auditor selection process. Moreover, in line with DiMaggio and Powell's (1983) expectations, isomorphic behavior is especially evident in the larger and more visible organizations we study, as they are more subject to these pressures.

5.1.3.3. Criteria

Tender documents are expected to feature transparent and non-discriminatory criteria for evaluating proposals, as the Regulation mandates. The Green Paper mentions that quality and independence should be key selection criteria in any tendering procedure (EC 2010), but which criteria should be applied is unclear (e.g., CSSF 2021). Best practice guidelines recommend companies define, prioritize, and apply pertinent criteria to assess if prospective auditors meet their specific needs and preferences. While the auditing literature extensively discusses fees, best practices argue that these should not be the primary factor in decision-making and that the focus should be on considering a 'fair price' that reflects the quality of service delivered (AICPA 2018; Deloitte 2016; FEE 2016; FRC 2017; KPMG 2018). The ambiguous guidance (e.g., transparent and non-discriminatory criteria, a "fair price") creates further uncertainty, potentially leading to more isomorphic behavior. Client interviewees reported that fees were an important factor but not primary to their decision-making. A possible explanation is that auditors converge on a narrow range of proposed fees. Auditor interviewees described how they researched several publicly available sources to ensure the fees are comparable:

> What you often see is that we make a calculation based on a feeling of what is reasonable in the market. You already know those audit fees from everyone from a similar organization. Before us, Firm 4 was there, and they had to disclose the audit fee in the annual report, so you can take the fee that Firm 4 had. Then, we

> verify that by comparing it with our own calculations based on estimates of the sector, size, etc. If you buy a kitchen yourself, you also want a discount or at least a sharp price, so you should not just mindlessly copy [the proposed fee], but you should say, well, in this case, we ask this much. (Audit Partner, AP3)

We conducted a case-by-case analysis of the clients' requests for proposals (RFPs) and observed a high level of convergence and uniformity. Clients' RFPs commonly emphasize fees, industry experience, IT capabilities, business knowledge, and transition planning. Despite the potential need for audits tailored to unique situations (Knechel et al. 2020), the formally expressed requisites exhibit high degrees of similarity. The uniformity in the criteria, which are mainly quantifiable and, in most cases, assessed with scorecards, exemplifies a trend toward standardization resulting from isomorphic pressures where clients adopt similar practices in response to regulatory, competitive, and professional norms. The reliance on measurable and widely accepted criteria in RFPs reflects an effort to adhere to recognized standards and practices, thereby ensuring the legitimacy of the process in the eyes of stakeholders, regulatory bodies, and the market.

5.1.4. Isomorphic Process Execution

Best practice recommendations advise providing detailed information to enable audit firms to thoroughly understand the client's business (e.g., AICPA 2018; FRC 2017; ICAS 2017). Given the ambiguity in the Regulation, which states that the audited entity has the discretion to determine its own selection procedure and that this procedure can include direct negotiations with interested parties during the process (EC 2014b), it is unsurprising that clients adhere to these best practice guidelines. Clients described establishing data rooms (i.e., platforms intended for data-sharing and interacting with potential auditors) and stressed the importance of ensuring fairness and "a level playing field." For example, if one audit firm requests information, it is typically shared with all participants.

Following best practice guidelines, the clients in our study issued their RFPs, received audit proposals, and invited firms to present their bids. These presentations are considered crucial by best practice guidelines, allowing evaluation of auditors' technical skills, ethical standards, independence, and ability to engage with management critically. The guidelines recommend the attendance of the entire audit committee during these presentations (e.g., Deloitte 2016; FRC 2017; ICAS 2018; KPMG 2018). However, in practice, these presentations are often viewed as confirmatory rather than decisive, with only one client mentioning that the presentation influenced the decision. One ACM (ACM3), the only respondent to mention this, shared an experience where "We had two [options] that we scored more or less the same, and that final presentation was what made the coin fall on one side rather than the other." Throughout the selection process, clients schedule additional interviews. The number of such interviews can vary widely, ranging from none, in one case, to as many as sixteen. One client even organized workshops for a better acquaintance with the audit team, and others opted for additional Q&A sessions. Nonetheless, the process is methodically organized and documented, with evaluations often formalized in scorecards. Interviewees mentioned that the robust process results in the shareholders accepting the auditor that is proposed, and that, consequently, the topic of auditor selection is a formality in the annual general meeting.

> In terms of appointing statutory auditors, I have never come across an example of them being rejected [by the shareholders] because the process behind it is so robust. The audit committee and supervisory board are involved, the management board is involved, we have all been part of the decision-making process up until this point, (…) there is no scope for discussion, it is more a formality in the annual meeting. It is the proposal, and the annual meeting accepts the proposal. (CFO, CFO1)

This robust process is designed to assure the audit committee of the recommendation's validity, mitigate queries at shareholder meetings, and fulfill the client's perceived responsibility toward external stakeholders. The interplay of normative and coercive pressures on both auditors and clients to structure a legitimate selection process, coupled with the ambiguity in the Regulation regarding the organization of this process, has resulted in a highly isomorphic auditor selection procedure. This conformity persists despite academic literature advocating for the preservation of audits' idiosyncratic nature to ensure audit quality (e.g., Knechel et al. 2020).

5.2. Auditor Selection Decision-making: Decoupling to Maintain Operational Efficiency

Considering the highly isomorphic practices of clients and auditors, one might expect decision-making to be objective, devoid of discretion, and firmly under the audit committee's purview, driven by pressures from regulators and shareholders. However, in a field characterized by conflicting demands—external pressures emphasizing auditor independence and internal demands prioritizing efficiency through a productive auditor-client relationship—

decoupling becomes a strategic response. This approach allows organizations to minimize risk by distinguishing their external commitments from their internal operations (Bromley and Powell 2012). This decoupling, where organizations strategically align their structures with institutional pressures for legitimacy while maintaining internal operational efficiency, reflects the theoretical insights of Meyer and Rowan (1977). They define decoupling as the deliberate separation between organizational structures crafted for legitimacy and organizational practices driven by efficiency concerns. Organizing the auditor selection process in a highly structured fashion enables organizations to attain legitimacy through outward compliance with institutional norms, while internally adhering to practices that ensure operational efficiency. The subsequent sections will examine the specific decoupling strategies employed by organizations to navigate these dual demands.

5.2.1. Decision-makers

Following the selection process, the audit committee is responsible for recommending a single audit firm or a shortlist to the board. The board then suggests an auditor for appointment, which is subsequently ratified through a shareholder vote (FEE 2013; ICAS 2017). The Regulation underscores the audit committee's role in selecting a new statutory auditor or audit firm, aiming to enhance the informed decision-making of the general meeting of shareholders or members of the audited entity. It emphasizes that management's influence should be limited to being "fit for purpose." The management board should facilitate the selection process, while the audit committee retains independence in decision-making (DCGC 2022). However, there are no clear guidelines specifying what constitutes a "fit for purpose" level of management involvement. The Regulation only discusses audit committee involvement and stipulates that the audit committee should decide. Clients are free in how to organize their selection process, and we notice that all clients significantly involve management team members. Specifically, the management team members involved in the selection process perceive this as evident, since they have to work with the auditor on a day-to-day basis. This is described in the following quote:

> The audit committee makes the final decision on which party to propose to the shareholders for approval as the new auditor. The relevant management and ACMs prepare the analysis and weighting of candidates for this purpose. Since the audit committee only sees the auditor five times a year at the audit committee meeting, and we have to actively work with the new auditor, the CEO, CFO, and ACMs involved in the selection process certainly listen

> carefully to the input of the relevant management, and take this information highly into account in the decision-making. The internal audit manager has to work daily with his people, and I, with my people, with the new auditor. (Controller, C1)

In our cases, interviews were conducted mainly by management team members, with ACMs occasionally participating. In almost all cases, only one ACM was present for the final presentations. Management always emerged as the most influential entity in the auditor selection process. This observation aligns with the findings of Jenkins, Pyhoza, and Taylor (2019) and Fiolleau et al. (2013), where management is predominantly the primary decision-maker.

Interestingly, perceptions varied between the different respondent roles regarding who truly drives the decision-making: Several management team members feel in control, whereas audit committee members have differing views about their own vis-à-vis management's decision-making authority, indicating differences in perceptions of the ACM's roles (Free et al. 2021; Couchoux 2023). The rationale behind management's influence is their day-to-day interaction with the auditor. These findings further prove that the distinction between management and audit committee influence is often blurred in practice. Our ACM respondents welcome management team involvement in saving time, and they do not perceive a loss of independence in this process, as an ACM highlighted in the quote below:

> It's true that when it comes to preparation, of course, the management team does the preliminary work from a dual perspective. On the one hand, because they have to work with [the auditor] themselves, and on the other hand, because they can also be the executors of the process for us, so it's good that they spend time on it as it is very time-consuming. It's also crucial for them to be interested in working with an auditor who is good at this. But at the same time, we have also set the criteria so that management [can carry out the process]. If you have the proper selection criteria, you can shape it well. The second point is it's more than just the appointment; it's ultimately the relationship you enter into with the accountant that determines whether you can guarantee that independence. (…) At the start of the discussions around the selection and immediately after the selection, we had a large number of set moments when we spoke with the accountants. Because of that, I don't feel we would be on a leash of the management. (ACM, ACM2)

Provided that criteria are established beforehand and adhered to, ACMs generally feel comfortable with management leading the execution of the selection process. Moreover, ACMs maintain that they can assert their independence through individual interviews with the auditors, conducted in the absence of management. However, it is noteworthy that the frequency of these ACM-auditor interviews is generally quite limited.

We observe some variations in the eventual decision-making power within the selection process. In all cases, the selection committee reached decisions by consensus through discussions involving all team members. In some instances, client preferences were considered, and potential disagreements were resolved through dialogue. Notably, in one case, each selection committee member had one vote, and the audit committee's vote accounted for only a quarter of the total votes. As a result, the management team members felt they were in control. However, the relevant ACM (ACM3) argued that although the process is executed by management, ultimately, "The CFO and I sit down, and we also have a chat, just the two of us, and say, you know, do we really believe this is the right choice?"

In conclusion, while the audit committee technically should be the final decision-maker, our findings indicate that the formal audit committee recommendation to the board was significantly influenced by management team members in all cases, albeit to varying degrees. The practice of the audit committee recommendation, aimed at creating legitimacy, is decoupled from the actual selection process. The practical efficiency of management's influence appears to be more critical for the clients studied. This is not to imply that the ACM's influence is insignificant. In one instance, despite the CFO's strong preference for a specific firm, the ACM overruled this choice in favor of a higher-reputation auditor. However, such instances of the ACM overruling other participants' preferences in the selection process appear to be rare.

5.2.2. Decision-making

We argued that ambiguity in the guidance for auditor selection criteria, coupled with the need for legitimacy, has led the clients in our sample to establish highly comparable selection criteria. However, within the decision-making process, we observe a second decoupling event.

The clients in our study perceive the quality of services offered by audit firms as similar, resulting in minimal differences in terms of transparent, non-discriminatory criteria. As a CFO mentioned when discussing the evaluation of the RFP: "If I compare the two companies, they are a copy of each other, so there is no differentiation in that respect" (CFO3). In each interview, interpersonal compatibility emerged as a crucial criterion. For instance, a CFO (CFO6) highlighted the importance of personal rapport: "Whether as a person you can get along with each other, that is the most important thing, so whether you have a similar way of working.

Yes, that's mainly about personalities." Even audit committee members prioritized this fit and trust in their decision-making (see also Free et al. 2021), as indicated in the quote below:

> The most important thing for me is how the chief auditor, the team leader, comes across. What impression do they make, what kind of person are they, do you expect them to be able to work well together, are they critical enough? That is decisive for me when making a choice. And the rest is all fine; those firms are big enough for [a good audit], they have enough expertise and knowledge, etc. What is most important to me is the relationship with the team leader. (ACM, ACM5)

There are some examples of disagreements between the ACM and management team members. For example, one CFO favored a firm based on the strength of its fit, while the ACM, in that case, focused more on the auditors' reputation and capabilities. Management team members in our study appear to place more value on the auditor-client relationship than the ACM. Formal guidelines dictate transparent, non-discriminatory, criteria-based selection, yet discretionary judgments about interpersonal dynamics significantly influence the actual practice.[40] The use of scorecards further illustrates this phenomenon. In seven of our cases, clients utilized scorecards to evaluate participating auditors. These scorecards seem to function more as legitimizing tools to demonstrate objectivity and ensure all criteria are formally addressed, rather than genuinely determining the best choice objectively. According to our respondents, it is challenging to encapsulate all necessary criteria within a decision-making tool, as summarized in the following quote:

> Look, a proposal is not just a list; of course, it is a list; you ask for points and get answers on them, which you can then organize into lists, make comparisons, and so on. But it's really about the overall image of the firm, and based on that, you try to see if all the points that need to be addressed are addressed in a good way. (ACM, ACM2)

This statement illustrates that using a list or scorecard does not capture the essence of what the client is looking for in an auditor. We investigated the scorecards used by some of the clients in our study. We observed that the criteria employed were predominantly measurable, as stipulated in the RFPs, encompassing factors such as expertise, knowledge, and fees. Only a few clients included scores on "fit." This is unexpected, given that "fit" and "added value"

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[40] I explore these observations further in *Chapter 4*.

were consistently highlighted as crucial in every interview conducted. It appears that clients decouple these scorecards from the actual decision-making criteria. This is explicitly evident in two cases where the auditor with the highest rating was not selected.[41] In another case, the scorecard form stated, “While following criteria will be scored on 1-5, the selection of the winning tender participant will not be the party obtaining the largest score on the items below as some of the criteria weigh more in importance than others and other criteria will also be taken into account.” This indicates a divergence between a scorecard’s formal, objective use in evaluating auditors and a focus on other factors like compatibility, highlighting a decoupling between intended evaluation methods and actual practices.

> Because [management], of course, deal daily with the audit teams during the audit, and it’s something different from the perspective of the audit committee and CFO. Then, you’re looking at it differently from the audit committee’s viewpoint than from the CFO’s, who balances between the two. That’s what I remember as a CFO. (…) And you know, the best part is when it clicks for both. And that’s not always consistent. And that is perhaps, in this case it wasn’t so, where a difference of opinion can arise. (ACM, ACM1)

The quote above suggests a potential reason why standardized scorecards might not be the most effective tool for achieving the intended objectives, particularly in objectively selecting the ‘best option.’ Different stakeholders may have varying criteria for what constitutes the best auditor, influenced by factors such as specific needs, industry standards, and regulatory requirement (e.g., Beattie and Fearnley 1995; Knechel et al. 2013). This ambiguity can introduce uncertainty, potentially leading to further decoupling (Bromley and Powell 2012).

[41] We were unable to review all completed scorecards as some clients did not share their filled-out scorecards.

6. DISCUSSION AND CONCLUSION

This paper studies how auditor selection processes are conducted at large firms and how institutional pressures influence these processes. Our field study covers eight distinct auditor selections in large Dutch companies by combining semi-structured interviews with documentary evidence about the process.

While the Regulation places the appointment authority at the shareholder level in the AGM, we find that their role is rather ceremonial. All respondents in our study mentioned that there were barely any issues or questions the shareholders asked regarding the selection process. This finding aligns with previous studies (e.g., Barua et al. 2017; Cunningham 2017) and is reinforced by the new auditor shadowing the incumbent auditor already before the AGM formally appoints the auditor. Nonetheless, the clients in our study, specifically the ACMs, worry about potential questions if the process is not well-organized and the audit committee is not the formal decision maker. Consequently, the need for a legitimate process because of the shareholder influence may lead to more formally structured auditor selection processes. Furthermore, we notice that other external pressures, such as the media and potential investors, motivate our study's clients to produce a legitimate process on the front end. At the same time, the "backstage" may be more complex (Power 2003).

The Regulation introduces some ambiguity and freedom for clients to organize their auditor selection. For example, while the audit committee should be in charge, the Regulation does not mention who can be involved in the selection process, how the selection process should be organized, and what "transparent and non-discriminatory" criteria are. These uncertainties and ambiguity lead to auditor selection processes showing isomorphic tendencies reflected in the concepts discussed by DiMaggio and Powell (1983). Clients attach great value to the suggested process steps and selection criteria presented in best practice guidelines issued by audit firms and other accounting organizations. Consequently, clients' auditor selection processes appear to have become highly standardized. This standardization could result in each audit's idiosyncratic nature not being sufficiently considered (Causholli and Knechel 2012), as the process does not match the client's specific needs. Furthermore, within companies, the audit committee, management, and shareholders might have different perceptions of a high-quality auditor (Beattie and Fearnley 1995; Carcello, Hermanson, and McGrath 1992). Knechel et al. (2020) argue that the standardization of processes, which is at least partly the result of recent regulations, may not increase audit quality due to the idiosyncratic, interpersonal nature of auditing and the role of client inputs. In line with their discussion, given the apparent challenges in making the decision itself transparent, enhancing the transparency of the process can still be beneficial. However, the question arises whether regulation alone can ensure the selection of a competent auditor.

Our results reveal that the clients in our study decouple from these standardized auditor selection processes in the decision-making criteria, the decision-making, and the ‘real’ decision-makers. First, we notice that the standardized criteria displayed in the RFP are used as a checklist to determine the non-qualifying participants in the tender process rather than determining the ultimate winner. Most clients in the interviews mentioned that the distinctive decision-making factors are interpersonal fit and the added value of the auditor in building a good working relationship. We argue that the relationship, as contended by Dodgson et al. (2020), Knechel et al. (2020), and Guénin-Paracini et al. (2015), is not sufficiently taken into account by regulators as the focus on auditor independence ignores the operational efficiency that such a relationship may bring to the audit. Relatedly, even the ACM portrays management’s involvement in the process as crucial because management has to work with the auditors on a day-to-day basis. We find that management team members exert the most significant influence on the decision-making process. However, in one notable case involving a highly visible client, the audit committee overruled management’s decision due to concerns about the auditor’s reputation. It appears that this client, considering their own high status and level of stakeholder scrutiny, prioritized seeking higher legitimacy. While we notice ACMs displaying varying roles in the auditor selection process (Couchoux 2023), their key decision criteria are surprisingly similar to those of management. Finally, several clients in our study used scorecards to evaluate prospective audit firms, which, we argue, serve as a legitimizing tool by providing “written evidence” (Power 2003) that a transparent process has been executed.

The Green Paper on Audit Policy also focused on improving the competition in the audit market (EC 2010). However, our findings indicate that clients perceive a lack of choice in the Dutch audit market, with only six PIE-licensed audit firms remaining. Interestingly, one client rotated their auditor before reaching the maximum mandate length. This decision was partly influenced by the limited number of rotations occurring in the market at that time, making audit firms more eager and available to participate in the selection process. Despite these constraints, numerous respondents favorably perceive mandatory audit firm rotation, appreciating the "fresh look" it offers (see also Allam et al. 2017). Additionally, due to the stringent regulations, the quality of all PIE-licensed audit firms is sufficiently high, at least according to our interviewees.

To conclude, our study shows that clients organize their auditor selection to seem legitimate to stakeholders, keeping decision-making with the ACM and preferring reputable auditors. Despite Regulation (EU) No 537/2014 directing audit committee-led, transparent selections, we find a practical deviation with management often leading the process, driven by the need for a strong auditor-client relationship. The decoupling from formally organized processes reflects client-specific needs. Furthermore, this study challenges the regulatory aim of limited management influence and market competition, with the Dutch audit market being restricted to a few PIE-licensed firms.

Our research underscores the importance of further research into auditor-client relationships. Future research could focus on how auditor-client interactions influence the auditor selection process, similar to how Dodgson et al. (2020) investigated the partner rotation process. Specifically, the dynamics between the auditor, client management, and ACMs could be highly relevant to understanding how companies select their auditor, as discussed in *Chapter 4*. This research also hints at which criteria are decisive for clients when choosing their external auditor. Additional studies could help pinpoint which criteria matter most, how clients communicate them, and how auditors present themselves to win bids. In addition, how clients who use scorecards to evaluate their prospective auditors attach differential weights to particular criteria seems an exciting avenue for future research.

Our study is subject to several limitations. We report on eight distinct auditor selection cases, which facilitates comparing and contrasting findings but is insufficient to generalize to all audit firm rotation cases. Since our sample consists of smaller and larger, private and public, and voluntary and mandatory rotation firms, variation exists between our cases that might not be explained through our theoretical framework. Due to availability issues, we could not access interviewees at the same management positions at every firm. Some interviews were conducted sometime after the rotation so that some details may have faded from participants' memories. Ideally, the first interviews would have been undertaken before the selection process started, although we have documentary evidence on the process organization before the start.[42] Finally,

[42] While probably not easily feasible, a real-time study to investigate all interactions could be highly interesting.

as with all interview research, our results may be subject to participant and researcher bias. We tried to overcome this by following best practice guidelines in auditing field research, such as those suggested by Yin (2014), Malsch and Salterio (2016), and Gendron and Power (2015).

In light of our findings, we look forward to research aiming to understand further the complex interactions between auditors and clients, particularly how these interactions influence the selection process. This could offer more clarity on how regulations impact actual auditor selection practices. In *Chapter 4*, we deep-dive into these interpersonal interactions.

CHAPTER 4. AUDITOR-CLIENT RELATIONSHIP BUILDING IN THE AUDITOR SELECTION PROCESS: AN EXAMINATION OF TRUST AND COMMITMENT

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Abstract

In this paper, we examine the development of auditor-client relationships by applying constructs from social exchange theory to the interpersonal dynamics involved in auditor selection processes. Regulators have introduced requirements related to auditor selection to address the familiarity threat in long-standing auditor-client relationships. However, there are benefits to strong relationships because financial statements result from joint efforts by clients and their auditors. We conducted a field study of auditor selection processes at eight large Dutch companies from 2019 to 2022 through semi-structured interviews with 29 key stakeholders and analysis of relevant documents. Our findings reveal that clients and auditors value a cooperative auditor-client relationship. During the selection process, they evaluate the potential quality of this relationship based on observed demonstrations of trust and commitment. We find that clients and auditors use the selection process to build the relationship by engaging in interpersonal, reciprocal social exchanges that start before the tender and continue until the client selects their auditor. Clients and auditors rely on signals of credibility and compatibility to make decisions throughout the selection process. This study contributes to literature and practice by shedding light on how auditor-client relationships develop before the audit starts.

Keywords: auditor selection; auditor-client relationship; social exchange theory; case study.

1. Introduction

Familiarity between the auditor and client is typically considered a cause for concern.[43] As stated in the Green Paper "Audit Policy: Lessons from the Crisis" by the European Commission (EC), "Situations where a company has appointed the same audit firm for decades, seem incompatible with desirable standards of independence" (EC 2010, p. 11). The concern with familiarity is that the auditor may advocate for management rather than view the investing public as the client (e.g., Jamal and Tan 2010). Consequently, the EU introduced mandatory audit firm rotation and enhanced audit committee responsibilities to limit this familiarity threat through its 2014 Audit Reform. This regulatory change was motivated by the belief that prolonged auditor-client relationships could lead to a loss of auditor independence, potentially compromising the integrity of financial reporting. The assumption is that frequent rotation and limiting management's influence would introduce fresh perspectives and reduce the risk of auditors becoming too aligned with their client's interests.

Nevertheless, the audited financial statements are a joint product of the client's and the auditor's actions (Antle and Nalebuff 1991; Gibbins, Salterio, and Webb 2001). Mutual dependence characterizes the auditor-client relationship, which requires collaboration between auditors and their clients to achieve accurate and reliable audits (Carlisle, Gimbar, and Jenkins 2023; Daoust and Malsch 2020; Guénin-Paracini, Malsch, and Tremblay 2015; Knechel, Thomas, and Driskill 2020). For example, limited or poor communication can adversely affect evidence-gathering and audit quality (e.g., Saiewitz and Kida 2018). Hence, Knechel et al. (2020) argue that the professional auditor's role is much more complex, rich, and nuanced than the traditional view that considers such collaboration as threatening auditor independence. They posit that increased cooperation can even enhance independence by increasing trust and knowledge intensity. Other studies have reported that auditor selection processes involve extensive, continuous negotiations and dynamics between the auditor and the client (e.g., Dodgson, Agoglia, Bennett, and Cohen 2020; Fiolleau, Hoang, Jamal, and Sunder 2013; Taminiau and Heusinkveld 2017). However, there is a notable lack of publicly available information on how these processes actually take place (Gold, Klynsmit, Wallage, and Wright

[43] In this chapter, we use the term "(external) auditor" for both "audit firm" and "audit partner" if either term is not specifically mentioned, as we notice that, in the auditor selection process, these terms are strongly linked together and indistinguishable for some topics. When possible, we use the most detailed level, i.e., we specifically use "audit firm" or "audit partner." The term "client" or "company" is used when discussing the client company.

2018; SEC 2015). This gap in the literature leaves a critical aspect of auditor-client dynamics underexplored, particularly in the context of mandatory audit firm rotation.

The purpose of this study is to examine the interpersonal interactions during the auditor selection process that shape the auditor-client relationship. This paper examines how clients and auditors engage in interpersonal interactions during the auditor selection process. We aim to identify how decision-makers, such as CFOs and audit committee members (ACMs), pinpoint, articulate, and assess their needs during this process and auditors' responses to the resulting expectations. We also explore exchanges that indicate a compatible auditor-client match or reinforce mutual trust and commitment. Moreover, we consider how these interactions influence the subsequent auditor-client working relationship. Finally, this study is set against the backdrop of the 2014 Audit Reform in the European Union (EU), which introduced mandatory audit firm rotation and increased audit committee requirements to address familiarity threats.

Our investigation covers eight distinct cases of auditor selection processes in the Netherlands between 2019 and 2022. We study seven client companies classified as Public Interest Entities (PIEs), subject to the mandatory auditor rotation regulations, and one large non-PIE. These cases include companies at various stages of the selection process, ranging from a few weeks after finishing the selection process to two years after the rotation. We examine how clients set up their selection process and how they and their auditors engage in interpersonal interactions. We conducted 25 semi-structured interviews with 29 key participants, including managers, ACMs, and audit partners, to get various perspectives about these auditor selection processes. We triangulate our findings with documentary evidence such as request for proposals (RFPs) and scorecards – this approach follows best practice guidelines in field research (e.g., Malsch and Salterio 2016; Power and Gendron 2015).

We study the development of the auditor-client relationship by applying constructs from social exchange theory (SET) (e.g., Blau 1986; Cropanzano and Mitchell 2005; Homans 1958) to the interpersonal exchanges that occur during the auditor selection process. According to SET, relationships evolve over time into trusting, loyal, and mutual commitments through social exchanges (Cropanzano and Mitchell 2005). Such social exchange takes place in interdependent relationships in which one party's actions result in unspecified obligations from the second party in the relationship, causing a continuous series of reciprocal exchanges (i.e., exchanges that do not include explicit bargaining) between the two parties (Cropanzano and

Mitchell 2005). Such reciprocal exchanges help to build trust and commitment, which improve working relationships (Morgan and Hunt 1994). In turn, continued working relationships reinforce the trust needed for successful cooperation (e.g., de Brentani and Ragot 1996; Eriksson and Vaghult 2000).

Although the 2014 EU Audit Reform specifically aimed to weaken auditor-client relationships, our interviewees persistently highlighted the importance of collaboration, trust, and commitment in the audit. Reasons for this include the interdependent nature of the audit, the ambiguity of what a good audit is, and improved information-sharing. Moreover, to create trust and commitment, clients and auditors engage in reciprocal exchanges before and during the selection process, namely during informal conversations, interviews, and presentations (Cropanzano and Mitchell 2005). Even a negotiated exchange, such as the audit fee, can induce distrust toward the other party (e.g., an extremely low fee can result in the client doubting the auditors' motivation to provide a high-quality audit). Clients see few differences in audit capability among bidding firms, such that a foundational level of trust leads the client during the auditor selection process to rely on signals of a productive auditor-client relationship. These signals include auditor-client fit, the auditor showing eagerness to win the bid, and committing that the audit will lead to minimal disruption in the client's day-to-day business. We find that the audit committee and management make the final decision together as part of a selection committee, focusing on the prospective collaboration between the auditors and the management. More specifically, as long as the audit committee trusts management, the audit committee mainly follows the management's opinion. Finally, we find that gut feelings and demonstrations of commitment to the relationship highly influence the deliberations and the auditor selection decision.

This study adds to the literature by investigating how clients and their auditors build relationships during the auditor selection process. By examining interpersonal interactions, this study provides evidence that the auditor-client relationship documented in previous literature originates from the start of the auditor selection process and is built up throughout this process. We apply the SET and find that reciprocal exchanges between auditors and clients contribute to building and sustaining their working relationships, and that interviewees experience benefits from their actions during the selection process have important implications for auditor independence and audit quality. The SET literature suggests that these exchanges foster trust and commitment (e.g., Cropanzano and Mitchell 2005), and this trust and commitment could be beneficial for the audit, as this may improve collaboration between auditors and their clients to achieve accurate and reliable audits (Carlisle, Gimbar, and Jenkins 2023; Daoust and Malsch 2020; Guénin-Paracini, Malsch, and Tremblay 2015; Knechel, Thomas, and Driskill 2020). However, if this increased trust and commitment results in auditors feeling the need to uphold these positive reciprocal exchanges, this could lead to auditors being more concessionary in negotiations with the client over subjective financial reporting issues (Dodgson et al. 2020; Koch and Salterio 2017). Furthermore, we present evidence that even in the most stringent auditor independence settings, relationship-building between the auditor and client prevails. We add to the auditor choice literature by showing how "intangible" aspects, such as how clients and auditors gain trust and build commitment to each other due to interpersonal interactions and reciprocal exchanges, influence client preferences. We add to the literature by showing which criteria matter in the auditor selection process, how clients test these criteria, and how auditors respond to these demands. We present how the partner-client matching process unfolds, answering Lennox and Wu's (2018) calls for research. Finally, we show the nature and role of social exchanges between ACMs and management during deliberations, adding to the literature on auditor appointments.

Our study also has policy and practical implications. First, we show how relationship-building persists as the focal effort of auditor selection processes despite the introduction of mandatory audit firm rotation. Our results indicate that in selecting their auditor, clients do not only use the 'transparent and non-discriminatory criteria,' as described by Regulation (EU) No 537/2014 (hereafter, "The Regulation"), but also evaluate the more informal and intangible qualities of interpersonal interactions. Moreover, our results reveal that clients evaluate both formal criteria and informal qualities, such as interpersonal interactions and signals of commitment, when selecting an auditor. This understanding can assist auditors in better presenting themselves to prospective clients and help clients make more informed decisions.

2. AUDITOR SELECTION: BACKGROUND LITERATURE

2.1. Independence in the Auditor Selection Process

The 2014 EU Reform encompasses two crucial parts: Directive 2014/56/EU (hereafter, "the Directive") and the Regulation. The goal was to reinforce independence as an essential element when carrying out statutory audits to reinforce the credibility of the audited financial statements. Practitioners and academics have debated strengthening auditor independence by altering the auditor selection process. Proposed solutions include removing the hiring power from management and introducing mandatory audit firm selection and tender processes (e.g., Dontoh, Radhakrishnan, and Ronen 2004; van Brenk, Renes, and Trompeter 2020; Regulation (EU) No 537/2014). Such solutions are consistent with research highlighting the positive impact on audit quality of audit committee influence (e.g., Abbott, Buslepp, and Notbohm 2018; Chen and Zhou 2007; Downes, Draeger, and Sadler 2021; Krishnan and Ye 2005), investor influence (Fatemi 2012; Mayhew and Pike 2004), and mandatory rotation and tendering (e.g., Boon et al. 2005; Elder and Yebba 2020). Practitioner guidance also recommends that the audit committee be the key, or even sole, decision-making body (Deloitte 2016; FRC 2017; ICAS 2017; KPMG 2018), with management only being involved "where appropriate" (FEE 2013; FRC 2017; KPMG 2018). The board then recommends an auditor for the appointment, and finally, the shareholders vote (FEE 2013; ICAS 2017).[44]

Nonetheless, evidence suggests that management still significantly influences auditor selection (e.g., Cohen, Krishnamoorthy, and Wright 2010; Esplin, Jamal, and Sunder 2018; Fiolleau et al. 2013; Taminiau and Heusinkveld 2017). This management influence and the resulting reduction in audit committee independence are associated with lower audit quality (Berglund, Draeger, and Sterin, 2022). For example, some managers desire more flexibility in reporting (Hurley, Mayhew, Obermire, and Tegeler 2021) or are more likely to appoint affiliated auditors (Dhaliwal, Lamoraux, Lennox, and Mauler 2015; Yu, Kwak, Park, and Zang 2020).[45]

To ensure quality and independence when selecting an auditor, the Regulation further stipulates that clients should use "transparent and non-discriminatory" criteria when selecting an auditor. Research on auditor choice identifies several client and auditor characteristics (e.g., ownership structure, industry expertise) that influence whether a company selects a particular auditor (e.g., Defond and Zhang 2014; Habib, Wu, Bhuiyan, and Sun 2019). Expertise constitutes one such characteristic, and a large body of research demonstrates a positive association between auditor expertise and audit quality (e.g., Bedard and Wright 1994; Chi and

[44] As *Chapter 1* and *Chapter 3* already outline the regulatory guidelines and best practices surrounding the auditor selection process, in this paper, we only outline the regulations influencing the auditor selection process at the interpersonal level in this study.

[45] The terms *affiliation* and *connection* refer to any situation in which there are network ties between an auditor and a firm. Such ties can exist, for example, because of former employment (e.g., a manager who previously worked for an audit firm), corporate experiences (e.g., a director of a firm serving as an outside director for another firm), or shared backgrounds and experiences (e.g., school ties, family ties).

Chin 2011; Goldman, Harris, and Omer 2019; Gunn and Michas 2018; Johnstone, Li, and Luo 2014; Owhoso, Messier, and Lynch 2002). Many of these studies focus on "observable" selection criteria, which align with the "transparent and non-discriminatory" criteria outlined in the Regulation.

2.2. Mutual Dependence and Cooperation in the Auditor-Client Relationship

Mutual dependence characterizes the auditor-client relationship, with auditors and the clients needing to collaborate to achieve an accurate and reliable audit (Carlisle et al. 2023; Daoust and Malsch 2020; Guénin-Paracini et al. 2015; Knechel et al. 2020). For instance, auditees can significantly influence audit outcomes via their working relationship with their auditor (Carlisle et al. 2023; Daoust and Malsch 2020). Specifically, good working relationships facilitate auditor-client interactions by better information-sharing (e.g., Guénin-Paracini et al. 2015; Hatfield, Hoang, Ricci, and Thomas 2022) and auditor objectivity, as client commitment may decrease client leniency (Herda and Lavelle 2015, 2022). However, trust in client management can impede auditors' professional skepticism on questionable accounting issues and result in compromised objectivity (Herda and Lavelle 2015). When auditors become increasingly committed to a client through customer relationship management efforts, auditors are also less likely to scrutinize the client's aggressive accounting (Koch and Salterio 2017). In contrast to this traditional view that problematizes familiarity and auditor-client cooperation, Knechel et al. (2020) posit that cooperation can contribute to independence through increased trust and knowledge intensity.

2.3. Relationship Building, Trust, and Commitment in the Auditor Selection Process

The importance of the auditor-client relationship in auditor selection is also evident from research on the criteria clients consider when choosing their auditors (e.g., Almer, Philbrick, and Rupley 2014; Beattie and Fearnley 1998; Christensen et al. 2024; Free, Trotman, and Trotman 2021). Detailed studies on the auditor selection process are scarce (examples include Dodgson et al. 2020; Esplin et al. 2018; Fiolleau et al. 2013; Taminiau and Heusinkveld 2017). These studies report some evidence that auditor selection processes involve extensive and continuous negotiations and dynamics between the auditor and the client. The organizational fit between the auditee's management and the auditor plays a crucial role in this process. Auditees, during audit partner rotations, can seek auditors who align with their company culture and operational style (Dodgson et al. 2020). In addition, "poor" auditor-client relationships may motivate auditees to change auditors (Fiolleau et al. 2013), and audit firms appear to remove the partners who are in "poor" relationships (McCracken, Salterio, and Gibbins 2008). Research has documented the importance of auditor-client dynamics and relationship-building during the engagement, highlighting the significance of demonstrating trust and commitment to the client, although these studies focus on the audit engagement rather than the selection process (Dodgson et al. 2020; Free et al. 2021). It is not only management that emphasizes service quality and the relationship with the auditor (Christensen et al. 2024), but the audit committee also places significant importance on these aspects (Free et al. 2021).

In summary, existing studies underscore the critical nature of auditor-client relationships, characterized by trust, interaction, and commitment, mainly throughout the audit engagement, while also hinting at the potential impact of the selection process. However, there is an ongoing debate about whether these dynamics benefit or harm the auditing field (e.g., Ewelt-Knauer, Gold, and Pott 2013; Knechel et al. 2020).

3. Social Exchanges During the Auditor Selection Process

Social exchange theory (SET) helps understand enduring relationships and recurring exchanges in business contexts (Homans 1958). SET posits that the unit of analysis in social exchanges is the relationship between actors, who can be individuals or corporate groups acting as single units. These actors engage in exchanges within a social structure, learning from past experiences to maximize positive outcomes and minimize negative ones (Homans 1958; Molm 1997). While SET assumes actors to behave in ways that facilitate desired outcomes (i.e., exchanges continue when the benefits for continuation outweigh the costs), it does not always involve conscious calculations (Emerson 1976). Furthermore, exchanges occur within structures of mutual dependence, with each actor's dependence constituting a source of power for its partner (Emerson 1962). Rewards generated by relationships are at the core of SET, and these rewards can be intrinsic (e.g., the pleasure of being with someone) or extrinsic (e.g., a good or service someone can provide) (Blau 1986). According to SET, relationships evolve over time into trusting, loyal, and mutual commitments if the "rules of exchange" are followed (Cropanzano and Mitchell 2005). The two major social exchange rules are reciprocal and negotiated exchanges. Reciprocal exchanges are those where one party performs an act for another party without knowing whether or when the counter-party will reciprocate (Cropanzano and Mitchell 2005). In negotiated exchanges, both parties engage in a joint decision process, such as explicit bargaining, in which they seek agreement on the terms of the exchange (Molm 2003). Reciprocal exchanges generally produce better work relationships than negotiations and allow individuals to be more trusting of and committed to one another (Molm, Takahashi, and Peterson 2000; Molm 2003).

Most literature examining SET focuses on organizational employee relationships (Dodgson et al. 2020). However, exchange relationships may also occur between individuals of different organizations (Cropanzano and Mitchell 2005). Specifically, SET has been used to investigate social exchange mechanisms in complex buyer-supplier relationships (BSRs). In complex BSRs, contracts are partly incomplete, and many of the exchanges are non-contractual, occurring over a long period of time and including unspecified obligations (Tanskanen 2015), and value is cocreated in the relationship between the buyer and supplier (e.g., Goffin, Lemke, and Szwejczewski 2006; Kingshott 2006). We posit that the auditor-client relationship also exhibits these characteristics. At its core, this relationship is initiated through a seemingly straightforward negotiated exchange. Namely, clients are contractually obliged to pay a fee, and auditors are tasked with conducting the audit. This suggests a negotiated, economic exchange in which fewer interpersonal bonds are expected (Molm 2003). However, reciprocal exchanges are also at the core of the audit-client relationship.

Clients are typically quite incapable of determining their auditing needs (Causholli and Knechel 2012; Knechel et al. 2020). Moreover, underperforming auditors are often not noticed (Causholli and Knechel 2012), suggesting that not all obligations and expectations in the auditor-client relationship are explicitly specified. Furthermore, some researchers argue that auditors and managers mutually contribute to a smooth audit (e.g., Daoust and Malsch 2020; Guénin-Paracini et al. 2015). In such a complex relationship, characterized by unspecified goals and mutual dependence, SET predicts highly interpersonal interactions (Cropanzano and Mitchell 2005). Such interactions, also called social exchanges, are underpinned by trust and commitment, essential elements due to the partly non-contractual nature and vulnerability inherent in such exchanges (Molm et al. 2000). Trust and commitment are indeed main elements that clients look for in an auditor (e.g., Fiolleau et al. 2013; Free et al. 2021).[46] As they are vital for building trust and commitment (Morgan and Hunt 1994), one can expect reciprocal exchanges to be essential in the auditor selection process. In turn, the resulting

[46] We understand trust and commitment based on Morgan and Hunt (1994), who define trust as existing when one party has confidence in an exchange partner's reliability and integrity and commitment to a relationship as an enduring desire to maintain a valued relationship.

continued working relationships reinforce the trust needed for successful cooperation (e.g., de Brentani and Ragot 1996; Eriksson and Vaghult 2000).

We conclude that SET provides a relevant perspective to study the auditor selection process and its negotiated and reciprocal exchanges, as these exchanges establish the foundation for the longer-term auditor-client relationship. Our setting is particularly interesting for studying the relational dynamics in light of the Regulation, as the SET posits that relationships become stronger over time. In light of this, the ten-year mandatory rotation period can shift what auditors and clients perceive and expect as benefits in the relationship. For example, there is a precise end date to the interactions between individuals, and the audit engagement fee does not represent an annuity for the audit firm. The literature has not adequately explored the initiation and development of auditor-client relationships before auditor selection, including how clients incorporate relational considerations into their decision-making and how auditors position their offerings. Furthermore, the impact of these early interactions on the ongoing auditor-client relationship remains underexamined. Our unit of analysis is the auditor-client relationship, and our research question is:

> **RQ**: How do auditors and clients engage in interpersonal exchanges to build the auditor-client relationship during the auditor selection process?

4. Research Method and Participants

In this study, we examine eight distinct cases concerning their auditor selection process, spanning from 2019 to 2022. Within this sample, seven entities are categorized under the mandatory auditor rotation regime in the Netherlands and identified as PIEs. Among these, six companies rotated their auditor to comply with the legal mandate, while one opted for a change in auditors earlier than mandated. The non-PIE, which is not subject to mandatory auditor rotation, also voluntarily changed its auditor. Seven clients appointed a Big 4 auditor, and one client a non-Big 4 auditor. Six clients changed from one Big 4 auditor to another, one from a Big 4 to a non-Big 4, and another from a non-Big 4 to a Big 4 auditor. The involvement of these companies and their respective auditing firms was facilitated through the efforts of the Foundation for Auditing Research (FAR), which contacted the audit firms for access to their clients that had recently undertaken or were about to undertake an auditor selection process. Five different audit firms provided at least one recent audit firm rotation case. In the final two cases, we observed that the point of saturation had been reached, consistent with the principles articulated by Power and Gendron (2015) and Malsch and Salterio (2016). Specifically, the seventh and eighth cases yielded detailed and consistent information that corroborated the findings from earlier interviews, both through case-by-case analysis and cross-respondent comparisons. The quotes included in this paper are derived from all the cases studied. For our analysis, we draw on the same field study material used in *Chapter 3*.

4.1. Data Collection

Consistent with other qualitative studies on auditor-client interactions (e.g., Cohen et al. 2010; Dodgson et al. 2020; Fiolleau et al. 2013; McCracken et al. 2008), we employed a semi-structured interview approach. For each case, we interviewed the current audit partner, one member of the AC, and at least one member of the client's management involved in the auditor selection process. Table 3.1 shows a more detailed overview of the participants per case.

We conducted semi-structured interviews using pre-defined scripts, which were updated throughout the data collection to better align with our interests. We tailored two distinct interview transcripts to address the specific perspectives of different participant groups: one for audit partners and another for client interviewees (which included ACMs, CFOs, controllers, and internal audit managers). Additionally, we developed specialized subquestions for ACMs and managers, acknowledging the varying roles and responsibilities they hold in the auditor selection process. We drafted these scripts based on best practices and regulations related to auditor selection, drawing on multiple sources (e.g., Deloitte 2016; EC 2014b; KPMG 2018; SOX 2002). Additionally, we reviewed the last 20 years of literature on auditor selection in leading accounting journals, summarizing it to identify potential research avenues for this study (see *Chapter 1*). We then compiled this information into interview scripts, which the researchers on our team reviewed and refined. We identified five key topics for company members and six for audit partners. The interview script included open-ended, neutral general questions and predefined sub-questions for each topic (Power and Gendron 2005). The general questions are available in Appendix 2. Our sub-questions served as conversation guidelines, though we aimed to let respondents freely describe their selection process and explore topics in depth as they saw fit, similar to the approach by other qualitative research on auditor-client interactions (e.g., Dodgson et al. 2020; Fiolleau et al. 2013; Free et al. 2021). We emailed participants a project summary and interview agenda, requesting written consent for their participation and the recording of interviews. Furthermore, we added a support letter from the FAR. The documents are located in Appendices B2, B3, and B4. We also invited the interviewees to provide feedback on additional items or topics for discussion, leading to a minor script update after five interviews. Our field research process was set up and executed following best practice guidelines (e.g., Malsch and Salterio 2016; Power and Gendron 2015; Yin 2014).

We conducted 20 interviews via Microsoft Teams and five in person.[47] Four interviews included two participants each, while the remaining interviews involved a single participant, resulting in a total of 29 participants. Each interview featured two team members: The first author focused on the interview's main content while the other team member (the fourth author for 22 interviews, the third author for three interviews) managed time and posed follow-up questions as needed. Interviews ranged from 23 to 90 minutes, averaging 62 minutes. Three interviews were conducted in English, the remaining 22 interviews were conducted in Dutch. Every session began with an overview of the research and our team and concluded with a review of the confidentiality agreement. We also invited respondents to share their professional backgrounds, including their expertise, experience, and role within the company being studied. To ensure the trustworthiness of our analysis, we performed member-checking (Malsch and Salterio 2016), sending a draft of the manuscript to each interviewee for commentary, and assured participants that any quotes considered for inclusion in our paper would be reviewed with them to verify accurate interpretation. Our member-checking e-mail is presented in Appendix B5. Some participants requested slight modifications to their quotes, and one participant asked for a quote to be removed. We followed our interview scripts but departed from our protocol when responses took us down an important path (Yin 2014).

The first author transcribed the interviews, ensuring the pseudonymization of all mentioned names by assigning random codes to the interviewees.[48] This researcher utilized ten transcripts to inductively generate first-order codes, which were then aggregated into a coding scheme. This scheme encompassed topics predetermined by our review of practitioner, regulatory, and academic literature and identified through extensive discussions among the research team during and after the interviews. Each aggregated code received a concise description, enabling a second coder to analyze the interviews. We employed NVivo software to code and analyze

[47] Due to the COVID-19 pandemic, conducting on-site interviews was largely infeasible.
[48] Throughout the analysis, we assign a unique identifier to each respondent to denote their respective roles. The abbreviations utilized are as follows: AP for Audit Partners, CFO for Chief Financial Officers, ACM for Audit Committee Members, IA for Internal Audit Managers, and C for Controllers. To maintain anonymity and avoid potential identification, the numbering is randomized and does not correspond to any specific case studied. We use the same identifiers as in *Chapter 3*.

the interview data. We regularly reread and reviewed transcripts to keep track of our insights (Kenno, McCracken, and Salterio 2017). Additionally, the first and fourth authors prepared a summary memo of observations from interviewees for each case, which all authors then analyzed. We compared each case memo against every other individual case and the collective set of cases. Throughout the project, we alternated between reviewing our data and examining theoretical concepts to test and validate our findings, as suggested by Yin (2014).

From this process emerged themes that we deemed interesting to analyze through a social exchange theory lens, based on participants' recurrent reports that they highly valued the interpersonal exchanges that occurred during auditor selection. We developed a new coding scheme from the literature on social exchange theory to code our interview data deductively. The codebook is shown in Table 4.2. The first author coded the data based on this scheme. To supplement the interviews, we obtained additional documents on the selection process. These documents include inside correspondence on the selection process (e.g., presentations from the selection committee to the AC, Q&As with the audit firms, audit proposals from both winning and losing bids, outlines of the selection process, scorecards, etc.). We use these evidence sources to clarify and validate findings from the interviews. We have also reviewed publicly available resources, including company websites and annual reports.

TABLE 4.1
Overview Case Studies

Case	Industry	Process duration	Timing Interviews	Respondent Position	Current job experience (in years)	Interview duration
1	Real estate	Seven months	One year after rotation	Audit partner	11-15	70 min
				Internal audit manager	0-5	68 min
				CFO	11-15	68 min
				ACM	0-5	67 min
2	Distribution	Three months	After selection, before rotation	Audit partner	26-30	54 min
				Internal audit manager	6-10	88 min
				Controller	6-10	90 min
				CFO	0-5	55 min
				ACM	16-20	34 min
3	Retail	Six months	After selection, before rotation	Inc. audit partner	11-15	58 min
				Controller	6-10	82 min
				ACM	6-10	70 min
				Audit partner	20-25	61 min
4	Finance	Seven months	Two years after rotation	Audit partner	11-15	64 min
				Audit senior manager	11-15	64 min
				CFO	0-5	56 min
				ACM	6-10	73 min

5	Finance	Six months	One year after rotation	Audit partner	5-10	74 min
				CFO	15-20	78 min
				Internal audit manager	10-15	78 min
				ACM	5-10	52 min
6	Services	Five months	One year after rotation	CFO	10-15	53 min
				Audit partner	5-10	23 min
7	Rental	Three months	One year after rotation	CFO	10-15	68 min
				Audit partner	10-15	51 min
8	Entertainment	Five months	3 months after rotation	CFO	0-5	32 min
				Controller	0-5	72 min
				Controller	5-10	72 min
				ACM	0-5	45 min

Table 4.1 provides an overview of all cases studied and interviews performed. The process duration column shows how long the tender process itself took. In the column 'Timing interviews', the timing of the interviews vis-à-vis the eventual rotation is shown. Abbreviations used in this table are Chief Financial Controller (CFO), Audit committee member (ACM), and Incumbent audit partner (Inc. audit partner). The respondent position is the position with respect to the specific case. We assigned broad job descriptions to the participants to mitigate identification possibilities due to specific job titles. The current job experience pertains to the number of years of experience the respondent has in their current role for the client interviewees. For the auditor interviewees, the current job experience pertains to the number of years of experience in their current role, not fixed to the current audit firm.

TABLE 4.2
Codebook SET

Top-level code	Description	Subcodes
Reciprocal Exchange (Process)	Instances of reciprocal interactions or mutual exchanges emphasizing the give-and-take between auditors, clients, management, and audit committees.	Reciprocal obligations and benefits AC-Management exchange AC-Auditor exchange Management-Auditor exchange
Cost Considerations (Process)	Instances where either party evaluates cost factors. Costs are the elements of relational life that have negative value to a person, such as the effort put into a relationship and the negatives of a partner.	Cost evaluations Punishments
Benefit Considerations (Process)	Perspectives of benefits to the auditor-client relationship. Rewards are the elements of a relationship that have positive value (Rewards can be a sense of acceptance, support, companionship, etc.).	Perceived benefits Incentives and rewards
Power and Interdependency (Process)	Power dynamics and dependencies, particularly between auditors, management, and audit committees.	Power balance Influence of management
Trust and Reliability (Criteria and Process)	Highlights the development of trust and reliability within the auditor-client relationship.	Building trust Trustworthiness Dependability
Social and Cultural Alignment (Criteria and Process)	Elements related to the social and cultural fit between the auditor and the client.	Cultural fit Social understanding Communication styles
Management and Audit Committee Influence (Decision-Making)	Specific focus on how management and the audit committee influence auditor selection and ongoing relationships.	Decision influence Management preferences Audit committee dynamics Individual versus collective decision-making
Role of External Factors (Overarching)	Influence of external factors like regulations and market conditions on auditor, management, and audit committee relationships.	Regulatory compliance Market influences Professional norms
Relationship Longevity and Commitment (Relationship)	Focus on the long-term nature of the relationship and the commitment of all parties.	Effects of mandatory rotation on relationship Long-term engagement Commitment levels Relationship stability
Relationship Outcomes (Relationship)	Outcomes of the auditor-client relationship as influenced by social exchange dynamics.	Awarding/winning the engagement Successful collaboration Conflict resolution Relationship satisfaction

Table 4.2 presents the codebook used for the final coding round of the interviews in Chapter 4.

5. ANALYSIS

5.1. A Foundation of Trust and Commitment

This section discusses what clients and auditors look for in their prospective auditor-client relationship. Client interviewees reported the difficulty of directly quantifying "a good auditor" (e.g., Causholli and Knechel 2012), revealing that the process does not solely involve an assessment of technical qualities but also understanding the qualitative, relational aspects of potential auditors. For example, interviewees mentioned they do not perceive any audit quality differences between the different auditors and look for interpersonal, relationship-building skills:

> [CFO] Look, the auditor's report is some product that all auditors offer in the same manner; this is not what the distinctive aspect is. It sounds crazy, and advice is not exactly the right word, but… [Internal audit manager] Rapport and cooperation and being a conversation partner are the most important. (CFO, CFO3, and Internal audit manager, IA2, interviewed together in the same session)

Almost all client respondents – audit committee members no less than managers – emphasized the importance of cooperation during the audit. ACMs in our study valued a partner that is a business partner, as an ACM (ACM3) stated, "I also don't want auditors who just sit behind their screen doing various things; I want people who have a sense of the business and who can partner with the business." Auditors also recognize the essential role of a good working relationship. An example is stated by an audit partner: "You need to have knowledge and experience, but at a certain point that's a given, and then it's about a person with whom I can work well together" (AP2).

All managers mention that "interpersonal fit" facilitates this relationship. Surprisingly, the ACMs we interviewed also frequently mentioned the importance of an interpersonal fit and the auditor-client relationship. However, their point of view of such an interpersonal fit reflected preferences for auditors' willingness to challenge, an ACM exemplified: "It comes down to the fit, and I find that very personal. You see, what's important to me is that someone does contradict me now and then during one of the interactions" (ACM1). According to this respondent, a good fit includes "Openness, transparency, intellect, reflection, engaging in conversation without judgment, and entering a discussion without preconceptions."

SET posits that trust and commitment are vital components of a relationship. Our study confirms that trust is highly valued by both clients and auditors. ACMs and managers report that clients need to trust their auditors to provide a high-quality audit. As an ACM explained, "There's still a bit of a gut feeling involved, like 'is this it?' You can't put everything into words. When you enter into a partnership, you must have trust that the accountant will do a good job" (ACM6). This quote underscores the reliance on intuition, given the difficulty in measuring and articulating the intangible characteristics of a good auditor. Furthermore, trust at the interpersonal level can also play a role. For instance, as an audit partner mentioned, "As an accountant, you also need a certain level of trust because when there is trust, you hear much more, and then someone also tells you many more things" (AP4). This quote indicates that information-sharing is enhanced when the auditor and client trust each other. Moreover, in all eight cases studied, we noticed that clients highly value the eagerness and commitment shown by the auditor to win the bid. For example, an internal audit manager (IA1) mentioned that they really looked for a "visibly engaged lead partner," indicating that clients value someone who is actively present during the selection process and the audit.

Responses from our interviewees suggest that audit quality perceptions depend on the perspective from which it is viewed (cf. Knechel, Krishnan, Pevzner, Shefchik, and Velury 2013). Our respondents share different views on what constitutes a "good audit". For instance, an audit partner (AP6) specifically described a divergence in expectations between the audit team and the client:

> It is challenging, for instance, regarding whether we deliver, say, 120 percent quality or ultimately meet the deadline. We faced some stark contrasts, and then you saw with the [Client 7] team, it was all about meeting the deadline, while for the auditors, quality was most important. (Audit partner, AP6)

This quote highlights differences in outcome priorities, as auditors may focus more on delivering high-quality audits, while clients might prefer an efficient, smooth audit process to meet all deadlines.

Overall, these findings highlight the importance of a good working relationship involving trust and commitment. It is hard to articulate the expectations, and this difficulty makes a good working relationship even more crucial, according to SET. The following section discusses how clients and auditors balance the costs and benefits of engaging in such a relationship during the auditor selection stage.

5.2. Social Exchanges of Value in the Audit

Social Exchange Theory (SET) posits that individuals will continue mutual exchanges as long as the benefits outweigh the costs, eventually developing these exchanges into relationships over time. During the auditor selection process, one key exchange identified in academic literature involves the audit fee. Notably, the clients in our study did not perceive low audit fees as the most important factor for building the auditor-client relationship. Instead, clients anticipate a competitive yet reasonable fee. As a CFO articulated, the fee "should be market-conforming. But we did not go for the cheapest option" (CFO6). When selecting an auditor, the negotiated exchange, specifically the provision of audit services in return for a specified fee, seems to represent a lower-priority aspect of social exchange. Reflecting on SET, it becomes evident that reciprocal exchanges play a more crucial role in the development and maintenance of relationships. This emphasis on reciprocity is supported by our findings.

Switching auditors entails a significant time investment, with the tendering phase stretching between three and nine months. Moreover, establishing a productive auditor-client relationship in the initial year demands considerable time and effort. An ACM noted, "You must realize that the process of choosing such an auditor is very labor-intensive from the audit firms' perspective, but also from the company's side. So, the more people you ask, the more time it will cost you, you need to find a balance in that" (ACM3). This example indicates that clients decide how many audit firms to invite by weighing the cost of the time investment. For auditors, the stakes are high when participating in the selection process. The uncertainty of securing the engagement, coupled with the substantial investment required for the first-year audit, poses a considerable risk, as one of our audit partners interviewed elucidated:

> It's a very large investment. It's actually just an investment decision that you, as a company, including Firm 3, also make. Do we want to invest in the relationship? Because it's both the tender, which costs a lot of time and money and isn't paid and the first-year audit, which is also very expensive. You have to put in much more time and energy than when you were an auditor for a few years. Those are investments in hours, just to put it that way. Half a million is nothing for such a large company as Client 3. Because you spend so much time on it, you also have to do site visits for which you have to fly, which brings out-of-pocket costs. These are all unpaid hours. You have back-office people helping you with creating documents and writing. It's quite an operation. (Audit partner, AP7)

This scenario epitomizes the concept of reciprocal exchange, wherein the benefits of engaging in the relationship are not immediately apparent. Auditors explicitly regard contributions during the tender process and the first-year audit as investments in fostering the relationship. For example, as an audit partner explained, "If you try to bill the startup costs all at once, then you have an issue, then you're actually damaging the relationship. You might be bringing in the money at this moment, but in a later phase, you'll be presented with the bill" (AP2). This quote suggests that low-balling still exists in a mandatory audit firm rotation environment, and the motivation for this low-balling may be to foster the auditor-client relationship. This perspective underscores the intricate balance between short-term financial recovery and nurturing long-term relational ties.

While the costs associated with engaging in an auditor-client relationship are relatively straightforward, particularly regarding time and financial expenditures, the benefits of such engagement for both parties involved are manifold. The negotiated benefit for the auditor is the recurrent audit fees received by the auditor, and the client gets a signed audit report in return. However, the additional advantages gained from investing in the auditor-client relationship are significant. The quote below indicates how an audit partner experiences the benefits of investing in a good auditor-client relationship:

> We have agreed on how we view things and how you view them. If we can't fully reconcile that, we would like to ask you to also communicate with the CFO and reach out to the audit committee to explain the situation, thereby involving everyone in the process. Then things run smoothly. That's the art of it. It has nothing to do with auditing but more with how you interact with each other. And that ultimately increases client satisfaction and acceptance of additional work invoices. On the other hand, you might have a very good audit file and have done well for yourself, but if you haven't maintained the relationship correctly and with respect, eventually, the assignment will end. (Audit partner, AP2)

Effective auditor-client communication is paramount, necessitating the involvement of all relevant parties, the audit partner, management (in this example, the CFO), and the audit committee. For audit firms, investing in a solid auditor-client relationship can yield commercial benefits, including additional fees, as highlighted by several audit partners in our study. More drastically, an unmaintained auditor-client relationship could lead to the client deciding to change audit firms. Furthermore, auditors invest in the auditor-client relationship as a more robust relationship facilitates easier sharing of information by the client. An audit partner (AP4) described how, should tensions arise within the client company, such as between management and the supervisory board, a trustful relationship enables auditors to become privy to these issues during discussions. When discussing examples of poor auditor-client relationships, this audit partner mentioned that "Investment decisions or disposals, so to speak, or significant issues within a company, yes, you just pick up on those less easily," showing how not investing in the auditor-client relationship could result in missing out on essential information during the audit.

Clients seek added value from their auditors in various ways, necessitating investment in the auditor-client relationship. For instance, ACMs and managers want auditors to provide insights beyond formal assessments, such as potential risks in data privacy or other sector-specific issues, based on informal interactions and sector knowledge. An example is shown by the quote below:

> I want an auditor to be able to feel and assess and say, "(…), if I were in [Country X] with all the projects there, the CFO sitting there, watch out, because they're on the verge of being overwhelmed," those are the kinds of things I want to hear from an auditor too. (…) I also want to hear from an auditor, "On data privacy, I think you're at risk," so you want to receive input based on their sector knowledge. It doesn't always have to be completely substantiated, you know, in the management letter, they mention things they're sure about. But I also want to have a chat with an auditor with our feet up on the table and hear what they see and feel and where they say, "Gosh, I'd pay attention to this," or "Hey, in [Country Y], I get the feeling that the management and the property developer are way too close with each other." Well, you won't put that on paper because they can't prove it, but I still want to know. (ACM, ACM3)

In addition to conducting a thorough audit, fostering a solid working relationship offers the client deeper insights, both inside the company and in the broader business environment. Clients expect their auditors to act as business advisors, providing feedback on the company's financial health, performance metrics, and strategic market positioning. They value auditors who can contribute significantly by acting as critical partners, offering sound advice, and pushing the company towards higher achievements.

Our findings suggest clients and auditors implicitly and explicitly weigh the costs and benefits of entering and investing in an auditor-client relationship, as indicated by the quote of an internal audit manager:

> Audit firm X wanted to perform the audit due to their social responsibility, but they are essential advisory suppliers to us. And then you have to think, their fee in the advisory is a factor two to three times larger than the audit fee. Plus, they are intertwined with our digitization and automation agenda. (Internal audit manager, IA1)

The clients, for example, weigh the cost of inviting multiple firms for tendering against having more options. In addition, clients cannot appoint an audit firm performing certain advisory services. In such a case, clients contemplate whether or not to stop the advisory services to invite that particular firm in their auditor selection process. Audit firms also balance participating in the tender process with losing potential advisory assignments, which can be significantly higher than the audit fee, as shown in the quote above. We observed a contrasting perspective from one audit partner, who mentioned they always choose for the audit engagement, as they "Never really weigh whether it comes at the expense of the opportunities for advice, or the current advisory assignments" (AP7). Nonetheless, this audit partner also mentioned that if the relationship is going badly because the clients "Did not meet the agreements we had made, and in terms of norms and values, things were happening that we could not support," they also consciously let these clients go and end the auditor-client relationship.

Our findings illuminate the interdependent nature of the auditor-client relationship and the ambiguity of what "delivering a high-quality audit" entails. Thus, the auditor selection process aims to establish a good relationship underpinned by trust and commitment that will prove vital during the audit (e.g., Dodgson et al. 2020; Fiolleau et al. 2013; Free et al. 2021). Reciprocal exchanges are essential for building trust and commitment to establish a working relationship (Morgan and Hunt 1994). Such exchanges encompass the time investment made by the parties involved to develop a thorough understanding of one another. In the following sections, we discuss how clients and auditors engage in reciprocal exchanges to build such a relationship during the auditor selection process.

5.3. Relationship-building via Social Exchanges During the Auditor Selection Process

SET suggests that relationships are built upon mutual exchanges where each party anticipates receiving something of value in return. In the context of auditor-client relationships, these exchanges go beyond simple commercial transactions and include cooperation, trust, and mutual understanding, all of which are essential for a successful audit (e.g., Guénin-Paracini et al. 2015; Knechel et al. 2020). In this section, we outline how the auditor selection process transpires and where interpersonal exchanges happen, and then we focus on which reciprocal exchanges are performed to build trust and commitment essential for a better working relationship (Cropanzano and Mitchel 2005; Morgan and Hunt 1994).

5.3.1. Selection Process Outline

While the appointment of an auditor is mandatory, the degree of effort invested in the selection process is at the client's discretion, as they are free to determine the organization of their selection process (EC 2014b). The auditor selection processes we studied all began with the audit committee and management setting up a selection committee. These selection committees were composed of four to six people, with each selection committee comprising one or two ACMs, the CFO, and additional management team members. This selection committee started preparing the selection criteria and drafting the RFP, which is the solicitation of an offer for the audit service, which generally includes client demands, the selection process plan, and the evaluation criteria (see Fiolleau et al. 2013 for an overview). Afterward, the clients invited audit firms to participate. Management's role is crucial as they handle the operational aspects of the selection process. Once audit firms are invited, they decide on participation and draft the RFP upon deciding to engage. Next, interviews, presentations, and sometimes even workshops are conducted, with mainly management present. The selection committee makes a decision based on the information provided and the interactions during the interviews and presentations. Afterward, the choice of which auditor to appoint is presented to the board and shareholders. In some cases the new auditor has already started shadowing the incumbent auditor between the selection process and the shareholder appointment.

This entire sequence of activities demonstrates a collaborative approach to auditor selection, with all steps being interconnected and providing ample room for social exchanges influencing the auditor selection process. Auditors, clients' management, and ACMs appear to benefit from a good working relationship (e.g., Dodgson et al. 2020; Free et al. 2021; Guénin-Paracini et al. 2015; Knechel et al. 2020). In addition, the relationship between the audit committee and management is essential in auditor selection decisions (e.g., Free et al. 2021; Gendron and Bédard, 2006). Consequently, we study how all three parties engage in reciprocal exchanges to enhance the auditor-client relationship.

5.3.2. What Auditors and Clients Seek as the Outcome of a Successful Selection Process

Our earlier discussion illustrates the primary goal of a collaborative relationship and smooth audit process. Auditors and clients focus on these attributes from the very beginning, including during initial discussions between potential auditors and clients during the auditor selection process. As observed by a CFO, "I think we take the collaboration with the auditor very seriously and listen carefully to what they say, trying to accommodate them as much as possible, or at least so they can have a smooth audit" (CFO3). While one would expect that the audit committee, from their oversight role, is less involved with the relationship, an ACM mentioned, "The audit firms are large enough, they have enough expertise and knowledge, etc. The most important thing for me is the relationship with the team leader" (ACM5) . Next to the good working relationship to provide a "smooth" audit, most tender participants mentioned that auditors and clients have to be able to communicate productively even in case of disagreement. An example is shown in the following quote:

> Yes, I think that fit is important because you're entering into a multi-year trajectory together, where you're essentially opposite each other as auditor and auditee. Still, as I mentioned before, you must do that while maintaining the relationship because you expect something from each other. You have to remain in a good conversation even if we disagree. You have to come to a solution somehow. Then I think that fit is important to accept how the client is in the game, how the accountant is in the game, I think then you have an understanding of each other's situation and then just come to a better consensus in the end. (Audit partner, AP6)

This audit partner argued that, while coming from different roles, you have to be able to have discussions and disagreements, and having a good fit helps in understanding each other. Furthermore, this quote exemplifies the reciprocal exchanges during the auditor selection process, as both parties "expect something from each other", even though this is not explicitly specified. On the client side, these open discussions are also perceived as highly important by ACMs and managers. For example, an ACM noticed, "You have to report more [due to new regulations]. So, having that trust with your accountant, exchanging ideas from the start, becomes increasingly important" (ACM1). This quote indicates that clients notice the more stringent regulatory setting and suggests that, as a result, the relationship becomes even more important. Overall, these quotes indicate that when selecting an auditor, the parties involved consider a good working relationship essential. In the following sections, we analyze the specific interactions during the auditor selection process that contribute to relationship-building.

5.3.3. Developing and Assessing Trust and Commitment

While we mainly focused on auditor-selection committee interactions, reciprocal exchanges occur between the management and the auditor and the audit committee and the auditor, engaging in a series of exchanges to develop and maintain a positive working relationship. Moreover, interactions between management and the audit committee in the client's organization further reflect these reciprocal dynamics. In the following sections, we will discuss which reciprocal exchanges auditors and clients engage in to gain trust and build commitment in the relationship.

During the auditor selection phase, this principle of reciprocal exchange is further evidenced as auditors invest time and effort to try to familiarize themselves with the client, even informally, aiming to identify key decision-makers. This approach facilitates a deeper understanding of the formal RFP process. It also enables auditors to probe beyond surface-level inquiries, thereby gaining insights into the client's underlying needs. This strategic engagement is crucial for auditors aiming to win the bid.

Reciprocal exchanges include getting to know each other during interviews, presentations, and sometimes workshops. We notice audit partners engage in relationship-building even before the tender process starts. Past interactions with auditing firms influence current selection decisions, underscoring the long-lasting nature of social exchanges. For instance, an audit partner (AP2), mentioned that "You've already been spending at least five years building a relationship" before the process started due to, e.g., providing non-audit services or participating in a previous selection process. The investment in this auditor-client relationship, this reciprocal exchange, can help in better answering the client's demands:

> It's always the art, at least from our side, to build a relationship with the people during the bidding process. To have already been there for coffee a few times before that, so you know the faces, and they know you. That often gives you easier access to ask questions behind the questions. (…) What happens is, when you have a personal bond, you have an advantage in the proposal process because you know more topics that they find important, and you make those topics reappear in your proposal. The client recognizes his topics and says, look, you see, that plays into my feelings. That is the relationship that actually needs to be built in the pre-proposal phase to introduce that bias. (Audit partner, AP2)

These quotes underscore the advantage auditors can gain by investing in the auditor-client relationship early on, as this engagement allows them to gather insights that enable the creation of proposals more precisely tailored to the client's needs. Clients respond to these reciprocal changes by facilitating the auditor selection process and creating a "level playing field" for all tender participants. Clients share detailed company information, often using an information platform shared with all tender participants. Clients usually share that extra information with the other tender participants if one party receives more information. For instance, an internal audit manager noted:

> We tried to organize the process in such a way that if we felt we had given Firm 3 more information in a conversation than Firm 4, then we would provide Firm 4 a heads-up after the conversation. We would be a sort of process guardian. We notice that we have given more information to one party than another, so you will also get that information. (…) The controller and I tried to create a level playing field for both parties. (Internal audit manager, IA1)

This quote particularly shows how clients display their commitment to a fair process and their potential future auditor-client relationship.

The auditor selection process, as previously noted, entails significant costs for auditors and clients, with the outcomes often being uncertain. In instances where firms do not win the bid, audit partners sought a follow-up conversation to glean insights into the reasons behind their unsuccessful bid in several of our cases. This gesture is generally well-received by clients, as highlighted by a CFO, “I actually enjoyed seeing that. Everyone had really put a lot of time and energy into it, so I don’t mind giving some feedback afterward” (CFO2). Even when the immediate benefits for both parties seem uncertain, preserving and comprehending the relationship, and showing commitment to each other, remain important. This illustrates a dedication to a partnership that extends beyond the immediate transactional situation. Given that building trust and commitment helps towards a better working relationship (Morgan and Hunt 1994), and a continued working relationship helps reinforce the trust needed for successful cooperation (Knechel et al. 2020), clients and auditors seek ways to trust each other, which we discuss in the following sections.

5.3.3.1. The Role of Expertise in Establishing Trust

Even though clients generally cannot assess the audit’s quality (Causholli and Knechel 2012), clients and auditors use the auditor selection process to evaluate the other parties’ reliability and integrity. As an audit partner (AP7) emphasized, “You also seek out people you trust, people you can rely on. People you can count on to conduct a high-quality audit.” The first selection in all our cases was deciding to hire a Big 4 or a non-Big 4 auditor. Within Big 4 firms, the differences in capability to perform the audit are seen as minimal. For instance, an ACM noted, “Ultimately, those three Big 4 companies, they can all do the audit well, right” (ACM3). This statement shows that clients trust the audit will succeed, particularly where the Big 4 are involved.

In the RFP, clients outline the criteria they require from their prospective auditor. We analyzed our documentary evidence and investigated the request for proposals. Team expertise, IT knowledge, audit approach, team qualifications, and auditor reputation were crucial in all cases. Furthermore, in most cases, we notice that an audit approach that embraces digitization and automation is vital for securing the bid, aiming to optimize the IT benefits for both the client and the audit firm. Moreover, in some cases, auditors with knowledge of ESG are sought after to ensure comprehensive ESG reporting in tandem with technological adeptness.

According to our respondents, the audit fee is crucial, although not to economize on fees but as a signal of whether the other party can be trusted. For example, clients who are overly focused on paying low fees may be unattractive to auditors, as it suggests a lack of emphasis on receiving a high-quality audit (and low potential economic benefit). For example, an audit partner recounted a previous experience with their client: “They were known as a party that didn’t really want to pay well, so that was actually my first reaction, one of not really wanting to participate” (AP6). Thus, an image of being a low-paying client may result in auditors not participating in tender processes.

Moreover, most clients in our study were not merely looking for the lowest price but instead sought to justify fee differences with the expected quality of the audit. The concern exists that reducing the price too much could detrimentally affect the audit quality. The following quote exemplifies the influence of the fee on the decision-making process:

> The fee should never be the leading factor, but the strange thing was, two that were very close to each other, one had a significantly higher fee than the other, it was really, there was like a 20% difference. Then you know, if you go back to the second one and say, hey, you’re 20% more expensive than the other, they’re going to adjust that. But then we said, well, he didn’t set it that high for no reason, and you can force someone to lower the price, but I believe that ultimately no auditor says I want to lose on the fee. (ACM, ACM3)

This ACM depicts that clients can negotiate the fees with auditors and implies that auditors do not want to lose the tender process on fee considerations. Nonetheless, clients mention that they can become doubtful if there is a large gap between the different proposed fees and consequently distrust the low-bidding auditor to provide a high-quality audit. However, clients mention they can opt for the lower cost if the price difference is substantial. We interpret this as clients balancing the risk of receiving a low-quality audit with significant cost savings. Despite this, both auditors and clients acknowledge that due to the requirement to adhere to the International Standards on Auditing (ISA), a base level of work (and thus fees) is expected. As an audit partner (AP2) explained, “In the end, everyone has to live up to the ISAs standards, so everyone needs approximately the same amount of work and fees to do that.” Furthermore, the previous auditor’s audit fee is public information, which auditors use to baseline their fee.

Interestingly, all our client respondents perceived limited differences among the audit firms regarding the mentioned criteria. The following quote by an ACM highlights the similarity across various audit firms and teams regarding quantifiable criteria and the existing confidence in their ability to conduct a technically sound audit:

> Actually, many selection criteria are objectifiable, and most pass over the bar of having good technical teams, and then you have the fee, which is also comparable. So, in terms of the objective criteria, it doesn't differentiate. Well, I've also experienced a turnover at [Company X]. I must say, the turnovers I've witnessed often don't revolve around objective criteria. So, it comes down to the fit, and I find that very personal. (ACM, ACM1)

More importantly, in one case, a bidding firm lacked in-house expertise on a critical accounting issue, unlike a competitor who possessed this specialized knowledge. Despite this, the firm, without this expertise, pledged to dedicate a senior manager to focus on this area for an entire year to develop the necessary skills. This promise of investment and signal of commitment was a decisive factor for the auditor selection in this case, providing trust that the auditor would be able to perform the audit. Especially in this setting where the perceived differences between audit firms are minor, we find that the emphasis on building trust and commitment and fostering cooperation significantly impacts the auditor selection process and the subsequent auditor-client relationship.

5.3.3.2. A Smooth Audit Arising from Fit and Collaboration

The previous section highlighted the importance of ensuring that both parties possess the technical audit skills required for a successful audit. This section focuses on how all three parties (the auditor, management, and ACM) strengthen their working relationship and establish themselves as reliable partners during the auditor selection process, emphasizing the development of mutual trust and confidence in their collaborative capabilities. Since stringent audit standards lead most clients to see minimal differences in audit quality among bidding firms, subtle interpersonal exchanges make a difference.

Auditors who present well-prepared proposals and align their language with the client's, using terminology familiar from client conversations or their website, are valued. Furthermore, the proposal can be seen as a tool to provide credibility about the quality of the auditor's work, as an ACM highlighted:

> I don't have confidence in people who hold such positions and make not just one but many mistakes in their proposal; then I think, how can I trust them to deliver their work correctly later on? (ACM, ACM6)

Compatibility at the interpersonal level was a key factor in every case of auditor rotation. For example, another ACM (ACM2) highlighted the need for a human approach, being down to earth and not too formal, and they tested this during the selection. Clients view their auditors as essential business allies, expecting them to act as the organization's "eyes and ears" (ACM, ACM3) and establish a strong connection. Our respondents emphasized the significant value a lead partner brings through probing questions and insightful advice.

The cultural fit between audit teams and the client company is a critical consideration for clients. For instance, the controller from one client pointed out their preference for an auditor who could thrive in their decentralized environment, mirroring that company's culture. Similarly, the management team of another client looked for an auditor with a hands-on, business-centric approach that resonated with their operational style. The controller in Case 2 also noted that the right fit could facilitate the resolution of potential disputes.

In another case, one audit firm presented two partners during the tender process and allowed the client to select their preferred partner, which was a decisive factor in winning a bid. The client anticipated both partners to deliver comparable audit quality, yet their distinct styles became apparent. The ultimate choice was influenced more by the compatibility and connection with the audit partner, who aligned more closely with the company's cultural and social ethos. Despite larger clients feeling empowered to request a change in partners, this option seems seldom utilized, as only one client demanded a different audit partner because of reputation issues. Presenting multiple partner options is highly appreciated, as a controller (C1) mentioned that "Firm 3 proposed two lead partners, and we thought that was a very smart move on their part." This controller, later in the interview, mentioned that the proposed partner symbolizes how well the auditor understands the client's needs, as shown in the following quote:

> The audit firm internally decided on whom they would suggest. It is, of course, some type of relationship and human fit. And yes, I don't think that they chose the best… Well, the best, in terms of quality, he was excellent. However, the match in the conversations, understanding us, and knowing what type of client you are talking to may not be the best. (Controller, C1)

This discussion shows that clients gain confidence in the relationship when the audit firm presents a suitable partner. Clients, in order to test the potential for a strong working relationship, expect the audit firm to accurately assess both their audit needs and, more importantly, their interpersonal needs. Additionally, clients view minimizing disruption throughout the audit process as a positive indicator of a good working relationship. As a CFO (CFO4) highlighted, "And do you dare to say something about the stickiness of your teams? For example, do you say that this is the team I start with and that it may look different next year, or are you willing to commit to certain key players in your audit team?" This quote is telling because clients look for auditor commitment through team continuity in building the relationship. Moreover, we notice that all clients value the assurance of the audit partner and team's availability (i.e., commitment) in terms of time and geographical proximity and, to a lesser extent, the partner's autonomy in decision-making. According to the clients, the audit teams must manage their projects and time effectively to avoid disrupting client operations. Moreover, they must collaborate seamlessly, not just among themselves but also with the client, ensuring the audit partner is well-informed about the team's activities. This smooth, constructive team dynamics requirement holds even more weight in international audits involving multiple teams across borders. The clients in our study favor auditors who can provide independent insights and stand firm on their positions without constant back-and-forth with their firm and who remain accessible for addressing any issues or delays that may arise. In addition, clients gain trust in the relationship when getting to know the team and how interactions within the team happen during the auditors' proposals, as shown in the quote below:

> You observe how the team reacts to each other, which is very interesting. There was an entirely different approach in terms of presenting their team. One let the whole team talk and had short videos, so it was very efficient, while the other firm excluded a large part of the team, so you could notice a clear difference in approach and how they interact within the team. (ACM, ACM5)

In our cases, clients prefer audit firms that align with their accounting stance. While audit firms may propose their viewpoints early on and request position papers, clients are wary of any post-selection changes to their accounting practices. As an ACM noted, "You want the new auditor to endorse the positions taken in the past, and if they don't endorse them, you want to know that beforehand" (ACM3). This respondent highlights that they prefer the usual way of working and refrain from changing stances on, for example, depreciation terms or lease constructions. Therefore, to avoid this and to develop trust in the auditor-client relationship, in the lead-up to auditor rotation, multiple clients in our study ask potential auditors about their stance on certain accounting decisions, demonstrating their ability to offer pragmatic solutions without major deviations from the previous auditor's approach. This is particularly relevant given the mandate for auditor rotation, which aims to introduce a fresh perspective and enhance audit quality. However, the effectiveness of this mandate could be impeded by the incumbent auditor's established accounting stances and methodologies, potentially limiting the intended benefits of auditor rotation.

Finally, when searching for the commitment needed in the auditor-client relationship, we notice that most clients value an auditor eager to win the bid. The following quote by an ACM highlights that it is essential for auditors to empathize with the company, to really get to know the company:

> You can really feel how eager people are to get that assignment, even though they haven't been in data rooms and whatnot, but you see one has really empathized with the company and the other much less. Well, that doesn't say everything, but it does give an indication. (ACM, ACM3)

However, as one CFO discussed, this can also pose a risk when talking about overly eager tender participants, as "You shouldn't be too eager either; you still need to remain objective" (CFO2). This respondent indicated that eagerness may reduce client skepticism. Overall, the reciprocal exchanges aimed at relationship-building between the auditor and the client reveal an intricate balancing of the auditor's professionalism and commercialism.

Our findings suggest that, during the auditor selection process, both auditors and clients prioritize indicators that a robust auditor-client relationship can be established through significant investment in interpersonal interactions. We posit that a key motivation for both parties is the desire to conduct an audit with minimal disruption to their routine operations. However, several of these factors are seemingly at odds with auditor independence, and the following section discusses how social exchanges play a role during the deliberation over the auditor selection decision.

5.4. Social Exchanges in Deliberating over the Selection Decision

Despite regulatory efforts limiting management influence in the auditor selection process, we find significant management involvement during the entire process. In all our case studies, management and the audit committee, specifically the audit committee chair, execute the selection process together in a selection committee. In the following sections, we will discuss the exchanges between management and the audit committee, the management-auditor and audit committee-auditor exchanges, and the differences between these.

5.4.1. Management-Audit Committee Exchanges

The audit committee is crucial in the auditor selection process, as they are the liaison between the board's needs and the practical needs of management. The audit committee's role is to organize the selection process formally, yet the selection committee primarily conducts the selection process. Some clients involve the entire audit committee to leverage their expertise in the evaluation process. However, in most cases, the audit committee delegates the preliminary assessment to a selection committee, reserving the audit committee's input for final recommendations, which likely minimizes the costs associated with the audit committee's time and involvement.

We notice an interesting group dynamic during this decision-making process. All selection committee members either fill out a scorecard or provide a ranking of the participating audit firms. In some cases, additional client employees participate in the interviews and share their opinions formally (through scorecards) or informally (by discussing their findings verbally, which the selection committee can then use to inform the decision). Decision-making was straightforward in each case, and all opinions were aligned, except once, where the CFO preferred a different auditor than the rest of the selection committee. The selection committee usually comes together and decides through discussion, with different people combining their perspectives and demands. Given the differences in the goal of an audit for managers compared to the ACMs (e.g., Abbott and Parker 2000), one would expect the ACMs to prefer some auditor attributes that diverge from management's preferences. Yet, in almost all cases, management and audit committee preferences were highly aligned regarding criteria and the preferred prospective auditor. This can be explained by the exchanges between management and the audit committee before the selection process, building trust throughout this process. For example, an ACM mentioned, "It is good that [management] executed the process. It is also important for themselves. They have an interest in working with a good auditor. At the same time, we set the criteria together, which allows for delegation" (ACM2). ACMs appear to trust management executing the process because the criteria are co-determined, and the ACMs perceive their and management's goals as aligned. Building on this, an ACM (ACM6) mentioned serving both management and audit committee roles in the auditor selection process throughout their career and that the decision-making criteria do not differ for these roles. This ACM highlights the collaboration between management and the audit committee in carrying out their responsibilities on the selection committee, as they "reported our findings and discussions, ultimately gathering the positives and negatives together." The following quote by a controller (C3) represents a forward-looking decision-making process and how the roles are assigned in the selection committee:

> So, I deliberately chose a commissioner, a member of the Board of Directors, head of internal audit, and myself, so there were four of us. I agreed with them that the selection committee makes the decision on who is number one, two, and three, and that decision cannot be made by someone else. I also agreed that the head of the selection committee must manage their own group. (…) I was convinced the four of us would not conflict, so we didn't set up a formal procedure in case of a vote tie. My team or I would probably be the decisive vote because we work with the external accountant every week. So I think that would be decisive, but we haven't organized anything formally; we said as a selection committee, we need to agree as one. By the way, the choice of 1, 2, and 3 was unanimous in the selection committee, so there was no discussion about that either. You never know that in advance; it could be the other way around, but we all have a good relationship with each other, so I was also confident that it would go well. (Controller, C3)

This controller indicated that each selection committee member is responsible for their own group's vote. That is, the chairman of the selection committee had to ensure that they made decisions on behalf of the audit committee and the Supervisory Board. As a member of the Board of Directors, the CFO needed to orchestrate the vote coming from the Board of Directors. Next, the internal auditor and financial controller both were responsible for coordinating their respective team's votes. In the final part of the quote above, the controller underscored the importance of good relationships between the decision-makers to facilitate decision-making. This example also exemplifies the decisive vote of management, as the audit committee vote only counts for one of the four final votes. While the audit committee, in most cases, was not perceived as the main decision-making body, management team members acknowledged the limits to management's influence. As a CFO stated, "in the end [management influence] can be zero, [the audit committee] have the final say at the end. But as long as there is trust in the team, which I believe is there, they mainly follow our advice" (CFO3).

The main preference difference we notice between ACMs and management team members is that ACMs tend to focus more on the strategic benefits the auditor can provide. For example, an ACM mentioned, "We are much more interested in whether they have a vision for strategic themes such as ESG and non-financial reporting and have experience with them, knowing that we still have to start with them and with the non-financial reporting requirements coming up" (ACM1). More importantly, the ACMs are the only client respondents mentioning that they test whether the partner is capable of being critical towards the client. Nevertheless, ACMs also recognize the pragmatic need for the auditor and management to align with day-to-day operational realities, arguing that the audit is more likely effective than if the audit committee solely selects the auditor. Here, the emphasis on success through collaboration underlines the social exchange theory's premise that beneficial outcomes arise from successful reciprocal exchanges. Given the ACMs' larger focus on strategy and the auditor's capability of being critical, the question remains how successful they can be at soliciting a critical auditor in the current selection process set-up.

Finally, auditors try to assess the key decision-makers during the selection process. As one audit partner mentioned, "Look, what you do upfront is assess who you know and how you will influence the people. That is what we irreverently do. By the way, all audit firms do that" (AP3). This statement underscores the strategic use of auditor-client interactions to identify and target influential individuals within the client's organization. By concentrating their efforts on these key figures, auditors aim to enhance their chances of securing the audit engagement.

5.4.2. Social Exchanges and the Use of Scorecards

In most cases, the selection committee utilizes a scorecard based on predefined selection criteria to make their decision formally. However, our interviews suggest that choosing an audit partner, team, and firm goes beyond simply adding scores from proposals and interviews. According to our respondents, it involves a comprehensive evaluation of each firm's ability to meet the client's needs, incorporating both the explicit criteria on the scorecards and the implicit, relational factors that emerge during the selection process. This perspective is corroborated by the views of ACMs and management, who underscore the importance of looking beyond quantifiable metrics to fully appreciate the value an auditing firm offers:

> We do not look at the mean of all scores, and that firm wins. We also made interview reports to obtain the subjectivities as well. However, it is challenging because we are too closely involved to complete the entire process objectively. It is human work, actually. (Controller, C1)

The decision-making process is not a linear progression from objective assessment to selection but a dynamic process, where discretion in terms of benefit and cost significantly influences the final decision. The following quote particularly highlights how the decision-making is influenced by subtle, less quantifiable metrics related to the auditor-client relationship:

> Why does someone like someone else more? People try to rationalize the reason for this. From science, you would think people start with a decision tree and then get some feeling with the decision. However, in practice, people begin with a feeling or a preference and then rationalize this decision. (Audit partner, AP2)

The quotes above provide additional evidence that the decision-making may begin with subjective feelings rather than purely objective assessments, indicating that personal rapport could influence the selection. We notice this in how scorecards were used, with their outcomes not being used as conclusive deciders but as aids to validate choices that ultimately were based on gut feelings about which firm was the right fit for the client's needs, as a controller (C1) mentioned that the "audit tender process is not an automatic exercise." This is not restricted to verbal statements; one scorecard mentions explicitly, "While following criteria will be scored on 1-5, the selection of the winning tender participant will not be the party obtaining the largest score on the items below as some of the criteria weigh more in importance than others and other criteria will also be taken into account." This underscores the complex nature of the selection process, emphasizing the interplay between quantifiable metrics and relational dynamics.

5.5. Social Exchanges to Start the Audit

The auditor selection process ends with the start of the new engagement and the auditor's onboarding. To get the working relationship off the right foot, the new auditor already starts shadowing the incumbent audit team before the final shareholder vote (e.g., Gipper et al. 2020). Previous literature has already documented the first year of an audit being very intensive, which all of our respondents noted. However, this shadowing already helps in the first year, as one audit partner (AP7) stated, "[The new audit engagement] doesn't feel new anymore because we were already involved everywhere in [the year before the appointment]. And we've already had Q1 and Q2. So it's actually already an ongoing relationship and an ongoing client." Given that the relational side has been tested extensively during the selection process, including pre-empting potential disagreements on accounting positions and establishing interpersonal fit, our respondents feel they got what they expected from the first year. Our findings suggest that while rotation requirements can impose constraints on relationship-building in certain respects, they can actually spur relationship-building during the selection process, highlighting a complex dynamic within auditor-client engagements.

6. DISCUSSION

All client respondents, managers, and ACMs emphasized the importance of cooperation during the audit. Clients highlighted the importance of interpersonal fit, trust, and commitment between all parties in the audit, in line with findings by Fiolleau et al. (2013) and Free et al. (2021), albeit now in our mandatory audit firm rotation setting. Because of the audit's credence good nature, and consequently, the difficulty of assessing audit quality (Causholli and Knechel 2012), clients use attributes of experience goods to judge audit quality based on service quality, as argued by Christensen et al.'s (2024) working paper. The importance of relational factors starkly contrasts with the Regulation's transparency and non-discrimination intentions.

Engaging in a good auditor-client working relationship may improve audit quality, as improved auditor-client communication can have financial reporting implications. The SET literature suggests that these exchanges foster trust and commitment (e.g., Cropanzano and Mitchell 2005), and this trust and commitment could be beneficial for the audit, as this may improve collaboration between auditors and their clients to achieve accurate and reliable audits (Carlisle et al. 2023; Daoust and Malsch 2020; Guénin-Paracini et al. 2015; Knechel et al. 2020). Furthermore, limited or poor communication can adversely affect evidence gathering and audit quality (e.g., Hatfield et al. 2022; Saiewitz and Kida 2018). However, if this increased trust and commitment results in auditors feeling the need to uphold these positive reciprocal exchanges, this could lead to auditors being more concessionary in negotiations with the client over subjective financial reporting issues (Dodgson et al. 2020; Koch and Salterio 2017). Our interviewees shared the perspective that a better auditor-client relationship can lead to a more efficient working environment and, consequently, higher audit quality (Dodgson et al. 2020; Guénin-Paracini et al. 2015; Knechel et al. 2020; Malsch and Daoust 2020). Moreover, interviewees cautioned that a bad auditor-client relationship could result in an ending assignment, in line with Fiolleau et al. (2013) and McCracken et al. (2008). Our findings show that auditors care about the auditor-client relationship, not only from a commercial perspective. We find that auditors also invest in the auditor-client relationship to achieve operational independence, adding to the findings of Guénin-Paracini et al. (2015). We also show evidence that low-balling still exists (e.g., Cameran, Francis, Marra, and Pettinicchio 2015; Goddard and Schmidt 202), although we provide further details on why auditors and clients engage in low-balling: our respondents explain that low-balling is a reciprocal exchange in the auditor-client relationship because billing the start-up costs all at once may damage the relationship. We also find that managers and ACMs seek added value from their auditors beyond formal assessments, such as insights into sector-specific and risk management issues. While this finding aligns with those of Free et al. (2021) in the Australian setting, it diverges from those of Christensen et al. (2024) in the US. This interesting contrast may be due to the more stringent PCAOB independence regulations over non-audit services.

Our findings add to the auditor-client relationship literature by investigating the exchanges taking place before and during the auditor selection process to build the trust and commitment needed to engage in a successful long-term relationship (Cropanzano and Mitchell 2005). Specifically, we provide evidence of what clients and auditors look for as part of a "successful" audit and which exchanges help demonstrate auditor-client compatibility. We find that auditors and clients engage in reciprocal exchanges, i.e., exchanges without knowing whether or when the counter-party will reciprocate (Molm 2003). For example, auditors spend much time getting to know the client to build a personal bond. Auditors then use this personal bond to gain additional knowledge about the client's needs, which may help win the bid because clients appreciate this effort. Auditors even try to assess who the key decision-makers are during the selection process, as they use auditor-client interactions to determine who to focus on during the selection process. This finding contrasts with the Regulation's demand for 'transparent and non-discriminatory' criteria when selecting an auditor. While the audit proposals serve as a tool for gaining trust in the technical expertise relevant to the audit, both positive and negative audit fee differences compared to competitors can lead clients to distrust the auditor to provide a high-quality audit. Adopting the perspective that auditing is a credence good and the level of audit effort needed from the auditor is unknown (Causholli and Knechel 2012), the client relies on signals of credibility, such as whether the audit proposal looks professional. Even the team presentation can be a signaling factor of how the auditor-client relationship will develop. More importantly, the client wants the audit firm to assign a fitting audit partner. Specifically, we argue that similarity in culture and style are highly important criteria, akin to hiring decisions by elite professional service firms (Daoust 2020; Rivera 2012). Moreover, clients prefer auditors who align with their accounting stances and those who are eager to win the bid. While too much eagerness may also induce client doubt, the finding that eagerness and similarity in accounting stances influence the selection process contrasts with the goal of the Regulation.

Finally, we notice that management strongly influences the decision in the selection, consistent with prior research (e.g., Fiolleau et al. 2013; Taminiau and Heusinkveld 2017). In our study, we investigate how the management and the audit committee interact and notice that the ACMs understand the need for auditors and management to work closely with everyday business operations. They believe audits are more likely to be successful if the audit committee and management choose the auditor together rather than the audit committee doing it alone. The audit committee's reliance on management's preparatory work and the collaborative establishment of selection criteria exemplify the mutual effort to build a trusting and successful relationship. This dynamic is also reflected in how clients utilize scorecards. Clients do not use the outcomes of such scorecards as conclusive deciders but as aids to validate choices ultimately based on a gut feeling about which firm is the right fit for their, mainly relational, needs.

The Regulation's goal of imposing a ten-year limit on auditor-client engagements was to mitigate concerns about auditor independence arising from prolonged engagements leading to auditor-client relationships. This rotation mandate is rooted in the desire to preserve the objectivity and fresh perspective of the auditor (Allam et al. 2017). The respondents view the mandatory rotation policy as generally beneficial, arguing that it introduces fresh perspectives and insights into the audit process. Regarding relationship-building, respondents mention that the mandatory rotation requirement introduces a balancing act between staying independent and needing a certain level of trust. Various respondents explained that trust facilitates more open communication, leading to a richer exchange of information. In turn, this openness enhances the quality of the audit, as a higher degree of transparency allows auditors to gain deeper insights into the client's operations:

> On the one hand, rotation is good because it brings a fresh perspective and ensures that people don't become too familiar with the clients and remain objective. At the same time, as an accountant, you also need a certain level of trust because if there is trust, you also hear much more, and then someone tells you many more things. So, it's quite an interesting balance that you need to find between the two. (Audit partner, AP4)

The quote suggests that mandatory audit firm rotation may impair operational independence, potentially reducing audit quality (Guénin-Paracini et al. 2015). Moreover, considering the results outlined in this paper, the introduction of mandatory audit firm rotation does not inherently constrain the depth of relationship-building, as ten years appears to provide sufficient time for auditors and clients to invest in relationship-building. We argue that the introduction of mandatory audit firm rotation may have resulted in auditors and clients focusing more on the value of the social exchange relationship while viewing the audit itself as a commodity barely distinguishable between the different firms. Furthermore, the respondents expressed some frustration about the rotation requirements. Some of our respondents recommend more flexibility in the timing of mandatory rotations to mitigate risks associated with auditor changes during significant organizational transformations. In addition, rotating earlier than the maximum rotation period is perceived as sensitive, as a CFO (CFO 4) questioned, "Why should I have to wait for a mandatory rotation moment to justify that after a relationship of 4 or 5 years, the collaboration requires something new? I am more surprised that it is sensitive for me to switch beforehand."

Finally, auditors may find having to change auditors "Such a pity; I know the company extremely well, I regret it, it's such a nice client, we have a good relationship, and we conduct a good audit.", as an audit partner (AP7) mentioned. Audit partners perceive auditor changes as unfavorable because they lose client-specific knowledge, and "it takes time to truly understand a company, to build a relationship, and to get into the audit; you don't do that within a year, of course." These quotes indicate that the introduction of mandatory audit firm rotation is costly not only because of the expensive tender process but also because of the – largely ignored – relational costs.

7. CONCLUSION

This study uncovers how clients and auditors engage in interpersonal auditor-client interactions during the auditor selection process in the context of newly introduced mandatory audit firm rotation requirements. We identify how decision-makers in the auditor selection process pinpoint, articulate, and assess their needs and how auditors respond to these expectations. We applied SET to explore the nature of the exchanges that indicate a compatible auditor-client match and reinforce mutual trust and commitment. Finally, we considered how these interactions influence the subsequent working relationship. We investigated these issues by studying the interpersonal interactions among managers, ACMs, and auditors who submitted proposals for eight distinct auditor selections in large Dutch companies by combining semi-structured interviews with documentary evidence about the process.

Mandatory rotation policies aim to improve auditor independence and objectivity. The rigidity of these policies might create obstacles in developing trust-based, committed relationships. However, we find substantial evidence for relationship-building in this setting, with clients and auditors engaging in reciprocal exchanges to build trust and commitment in the auditor-client relationship, starting already in the early stages of the selection process. The influence of these findings on audit quality requires additional investigation, as the quality of audits can be affected positively or negatively by the strength of the working relationship. Regulators can use our findings to evaluate whether current rotation policies meet their intended objectives and to consider how to address the identified relationship-building within the regulatory framework. Our results also have interesting implications for audit firms, as the results show how audit firms anticipate clients' requirements and what clients value from their auditor. For example, clients seek auditors who offer more than just formal assessments and demonstrate a genuine eagerness to understand and meet their specific needs. Auditors could use the insights from this study to tailor their team and partner proposals better, recognizing the importance of relationship-building and knowing what can help win the bid. Finally, clients could learn from our results how to organize the selection process and which crucial factors to consider.

As outlined at the end of *Chapter 3* (p.110), several limitations apply to this empirical study. These relate to a limited number of cases, some lack of access to desired interviewees, and differences in interview timing relative to the rotation moment. Despite these practical issues, we followed best practice guidelines for field study design and analysis, such as those suggested by Yin (2014), Malsch and Salterio (2016), and Gendron and Power (2015), and by comparing and contrasting different perspectives and sources from multiple cases.

Specifically for this chapter, ideally, interviews would have been undertaken immediately after the selection process, with a follow-up interview after the first year to discuss the impact of relationship-building.[49] We only investigated relationship-building after the selection process in some cases. In most cases, the relationship was not fully developed yet, as it was the first year of the audit. Follow-up research could study further relationship building. Furthermore, we report findings coming from interviews with the tender-winning auditor. Future research could dive deeper into the exchanges with the losing auditors to determine the differences between winning and losing tender participants. Finally, we notice a divergence between decision-making on paper versus in practice. Future research could add to the decision-making literature by investigating the client's evaluation process. For example, the selection process exhibits characteristics of actuarial and clinical decision-making. Clients are guided by actuarial decision-making in their scorecards, using objective and transparent criteria. This approach aligns with the regulatory focus on objective measures, as discussed in the literature (Westen and Weinberger 2005). Conversely, the selection process gravitates towards clinical decision-making, wherein clients use their expertise to collect, combine, and interpret data nuanced and intuitively (Falzer 2013; Westen and Weinberger 2005).

We look forward to future research on the auditor selection process that will continue to explore and enrich our understanding of how auditor-client relationships are formed and how this influences auditor appointment decisions.

[49] While probably not easily feasible, a real-time study to investigate all interactions could be highly interesting.

GENERAL DISCUSSION AND CONCLUSION

Every audit engagement once started with a client selecting an auditor. Yet, even though the auditor selection process is a crucial mechanism for ensuring auditor independence and enhancing audit quality, an understanding of *how* companies select an auditor was lacking before this dissertation. In this dissertation, I uncover this process in three methodological ways. First, I systematically synthesized the academic literature on the auditor selection process. Then, I investigated archival data to determine whether there is a strategic pairing between clients and auditors. Finally, I conducted qualitative research on eight auditor selection processes at large Dutch companies. In the following sections, I will discuss the main findings using the identified research questions in the literature review, after which I will discuss the practical implications of my dissertation and finalize with some ideas for future research.

1. WHY STUDYING THE AUDITOR SELECTION PROCESS MATTERS

In *Chapter 1*, I find that the research on auditor selection is fragmented, with archival studies focusing on observable characteristics and field studies providing richer insights into intangible criteria and dynamics. For example, the auditor selection hiring authority debate involves audit committees, shareholders, and governments, whose involvement tends to result in higher-quality auditor appointments despite clients perceiving little difference among the Big 4 firms. Field studies contrast with archival research by emphasizing intangible, unmeasurable criteria and the individual audit partner over the firm in the selection process, an aspect often omitted in guidelines and discussions. The lack of public disclosure on auditor selection complicates research, relying on indirect information or proprietary data.

Although literature from the last decades provides evidence that audit partners impact audit quality (e.g., Gul et al. 2013; Hardies et al. 2016; Zerni 2011; Knechel et al. 2015), one of the notable findings from *Chapter 1* is the limited research on the partner level and partner-client matching in the auditor selection process, as also noted by Lennox and Wu (2018). The archival study in *Chapter 2*, therefore, focuses on the partner-client matching process. I explore whether and how audit partners' *prior* experiences with other clients are associated with *current* matching to new clients. First, I find that this alignment matters, as the audit partner-client alignment is associated with lower income-decreasing accruals. Furthermore, the results provide evidence that such alignment is beneficial for the auditor-client relationship, as higher auditor-client alignment is associated with longer tenure and a lower likelihood of an auditor change. Returning to the auditor selection process discussion and whether auditor rotations should be mandatory to enhance independence and, therefore, audit quality, my results indicate that within-firm partner rotations are associated with lower alignment. In contrast, audit firm-induced audit partner rotations are not associated with a difference in partner-client alignment. I assume that this is because to win a bid, audit firms assign their most suited partners to participate in the tender process (in line with Fiolleau, Hoang, Jamal, and Sunder 2013), audit firms scrutinize new clients more carefully than continuing clients (Johnstone and Bedard 2004), and because clients have more options to choose from in firm rotations compared to within-firm partner rotations. These interesting dynamics further spurred my interest in the auditor selection process. Specifically, since I do not find a difference in audit partner-client alignment for audit firm rotations, other factors should be at play.

2. About Compliance, Creativity, Independence, and Interpersonal Fit

First of all, I notice that the reason for switching auditors can influence the auditor selection process, as clients partly use their previous audit partners' perceived strengths and weaknesses to develop their selection criteria (see *Chapter 4)*. Overall, the auditor selection process is organized in a highly comparable way, as the auditor selection processes I study all began when the audit committee and management formed a selection committee, typically including one or two audit committee members, the CFO, and other management team members. This committee develops selection criteria and drafts a request for proposal (RFP), inviting audit firms to participate. The operational aspects of this process are predominantly managed by the company's management. Upon deciding to participate, audit firms respond to the RFP, leading to a series of interviews, presentations, and sometimes workshops, primarily attended by management. The selection committee uses the insights gained from these interactions to make their decision, which is then presented to the board and shareholders. Concurrently, the chosen auditor begins shadowing the incumbent auditor to ensure a smooth transition. In *Chapter 3*, I report evidence of isomorphic, standardization tendencies in the auditor selection process, regarding procedural steps, but also in terms of formal decision-making criteria. This standardization occurs despite the idiosyncratic nature of an audit (Causholli and Knechel 2012). The question arises as to why such homogenization persists in a context that requires tailored approaches. I argue that this isomorphism results from regulatory uncertainty and ambiguity and because of external pressures from, among others, regulatory bodies, investors, and the media. Consequently, I find that clients put great value in best practice guidelines issued by audit firms and other accounting regulations. I argue that the process on the "frontstage" is organized in this structured, "objective" way to create legitimacy for the financial statement users, the media, and the regulators, indicating some impression management by the client.

The results from the case study reveal that in the "backstage" of the auditor selection process, the most interesting dynamics take place. I find that clients decouple their decision-making criteria, decision-making, and decision-makers from the standardized auditor selection processes. Although the standardized criteria outlined in the RFP serve as a checklist and a means to eliminate unsuitable candidates, the key factors influencing clients' decisions, as revealed in interviews, are the interpersonal fit and the auditor's ability to enhance a productive working relationship. Furthermore, the audit committee members highlight the importance of management's daily involvement with auditors, which explains why management team members often emerge as significant influencers in the selection process. However, in a notable instance, the audit committee superseded management's choice due to the auditor's reputation, reflecting the client's consideration of their higher status and the need for increased legitimacy. This study also notes that audit committee members show different levels of involvement in the auditor selection processes I investigated, yet their fundamental decision criteria align closely with those of management. Moreover, while many clients employ scorecards to evaluate audit firms, these tools are viewed more as a means to formalize the process rather than as binding decision-making instruments. These results provided a clear necessity to study the underlying auditor-client interactions at the interpersonal level that accompany this decoupling and to understand why certain characteristics matter to the client, how decision-makers like CFOs and audit committee members identify and express their needs in the selection process, how auditors meet these expectations, and how such interactions signal a good match, which I discuss in *Chapter 4*.

Overall, all respondents highlighted the importance of interpersonal fit, trust, and commitment between all parties in the audit, corroborating the findings by Fiolleau et al. (2013) and Free et al. (2021). There are a variety of reasons for this. Firstly, the perceived quality differences among the tender participants are negligible. In addition, "It is not analytically clear what 'good auditing' really is" (Power 2003, p. 389), and the level of audit effort needed from the auditor is unknown (Causholli and Knechel 2012), which results in the client relying on signals of credibility. Finally, a strong auditor-client relationship can enhance audit quality through better communication, impacting financial reporting and evidence collection (e.g., Hatfield et al. 2022; Saiewitz and Kida 2018). The respondents in the field study confirm that positive relationships are expected to lead to a more efficient working environment (see also Daoust and Malsch 2020; Dodgson et al. 2020; Guénin-Paracini et al. 2015; Knechel et al.

2020), and they actively seek signals indicating the potential for such relationships. To test and build this relationship during the auditor selection process, my findings reveal that auditors and clients engage in social exchanges aimed at building trust and commitment towards each other. Auditors invest time in understanding the client to form a personal bond, thereby enhancing their chances of winning the bid. This effort to build a personal connection and understand the client's needs, including identifying key decision-makers, is crucial despite regulations advocating for transparent and unbiased selection criteria. Trust-building extends throughout the entire selection process. The audit proposals are used to show the technical expertise. At the same time, the interviews, presentations, and perceived effort during the process can signal the auditor's credibility and potential for a productive auditor-client relationship. Furthermore, the selection is influenced by the perceived fit of the audit partner in terms of culture and style, as well as the prospective partner's alignment with the client's accounting approaches. Even the audit fee can prove to be a tool for gaining trust in the auditor, as both positive and negative audit fee differences compared to competitors can lead clients to distrust the auditor to provide a high-quality audit. In my studies, I find that management plays a significant role in the auditor selection process, aligning with previous research. However, I add to the literature by investigating the interplay between management and audit committee members, who acknowledge the importance of collaboration between auditors and management for effective audits. They favor a joint selection approach by the audit committee and management over the audit committee acting independently. This collaborative effort is evident in how management's preparatory work influences the audit committee and in the joint development of selection criteria, highlighting the necessity of mutual trust for successful cooperation. Finally, as also highlighted in *Chapter 3*, scorecards are not used as definitive decision-making tools but as aids to validate choices that are at least partly based on a gut feeling about which firm is the right fit for their (mainly) relational needs, emphasizing the importance of relational compatibility with the audit firm.

In conclusion, these studies contribute to the literature by providing a comprehensive overview of the auditor selection process in large companies. The sample of eight cases enables the identification of key similarities and differences among various cases and types of participants, including managers, audit partners, and audit committee members. Furthermore, this research offers evidence on the criteria that are most significant to clients and how auditors address client expectations. While previous literature has predominantly focused on expectations from a single role, this dissertation also examines the interactions among different parties involved in the process. Additionally, this work enriches the understanding of the auditor-client relationship literature by demonstrating that this relationship is established during the auditor selection process and significantly influences auditor choice. Finally, this dissertation investigates the auditor independence literature by exploring the impact of policies such as enhanced audit committee requirements and the introduction of mandatory audit firm rotation on the auditor selection process resulting from the introduction of the European Union (EU) Audit Reform in 2014.

3. Implications of the Dissertation

3.1. About Independence and Relationships

A significant motivation for this dissertation was the introduction of the 2014 EU Audit Reform, which implemented stricter rules on auditor independence (e.g., Cameran, Prencipe, and Trombetta 2016; de Jong, Hijink, and in 't Veld; European Commission 2010; European Commission 2014a; European Commission 2014b; PCAOB 2011). The underlying premise was to enhance audit quality by weakening the economic and relational bonds between auditors and their clients (Fiolleau et al. 2013). Regulations have focused on the auditor selection process, as this process emerges as an important mechanism for ensuring auditor independence and the overall quality of the audit (Adelopo 2012; ICAS 2017; Regulation (EU) No 537/2014). An overview of the auditor selection requirements is explained in *Chapter 3*. The main points of impact on the auditor selection process are (1) the introduction of mandatory audit firm rotation for public interest entities (PIEs) to limit relationship-building and bring new audit insights, (2) the increased audit committee responsibilities and the shareholder voting on the auditor, and (3), the new auditor should be selected on transparent and non-discriminatory criteria.

Yet, while (1) indeed is seen as beneficial for bringing new insights, the rotation policy also requires a balance between independence and trust for effective communication and audit quality. Some of my interviewees suggest more flexibility in rotation timing, especially during significant organizational changes, to avoid the drawbacks of losing client-specific knowledge and the relational costs associated with auditor changes. Despite concerns about operational independence, ten-year rotations do not significantly hinder relationship building, allowing for social exchanges throughout the auditor selection process. The social exchange theory (SET) literature suggests that these exchanges foster trust and commitment (e.g., Cropanzano and Mitchell 2005), and this trust and commitment could be beneficial for the audit, as this may improve collaboration between auditors and their clients to achieve accurate and reliable audits

(Carlisle, Gimbar, and Jenkins 2023; Daoust and Malsch 2020; Guénin-Paracini et al. 2015; Knechel at al. 2020). However, if this increased trust and commitment results in auditors feeling the need to uphold these positive reciprocal exchanges, this could lead to auditors being more concessionary in negotiations with the client over subjective financial reporting issues (Dodgson et al. 2020; Koch and Salterio 2017). Furthermore, this relationship-building occurs between management, audit committee members, and auditors. Management's day-to-day interactions with auditors position them as key influencers, a perspective supported by audit committee members. This dynamic reflects the nuanced interplay between management's operational role and the AC's strategic oversight for legitimacy. Additionally, while Regulation (EU) No 537/2014 formally grants shareholders appointment authority at the annual general meeting, their involvement tends to be ceremonial, with few actively questioning the selection process. However, shareholder influence may increase the importance of a well-organized selection process. I did not study the change in audit committee influence. However, regarding (2), the audit committee is not as involved in the auditor selection process as Regulation (EU) No 537/2014 stipulates. Nonetheless, shareholder voting may actually help in organizing a formal auditor selection process to reinforce the trust of investors (Maijoor and Vanstraelen 2012). Finally, regarding (3), clients highly value the personal bond with the auditor, someone who is similar in terms of culture and style, eagerness, and someone they can trust. Especially in light of the difference between what clients put in their audit proposals compared to interview findings, I argue that these criteria are not as transparent and non-discriminatory as EU Regulation 537/2014 highlights. Further evidence of this is that scorecards, a tool for making decisions transparent and non-discriminatory, are used during the process, but mainly to validate the feeling gathered during the auditor selection process.

Overall, regulatory changes surrounding the auditor selection process have only partly succeeded in their goal. I argue that this is because the legislator did not take the auditor-client relationship sufficiently into account, as the focus on auditor independence ignores the operational efficiency that such a relationship may bring to the audit due to the interactive nature of the audit process. This corroborates the studies of Dodgson et al. (2020), Knechel et al. (2020), and Guénin-Paracini et al. (2015). While the regulation does not suggest a standardized selection process, I find that the pressures still result in a uniform approach. One should be careful that each audit's idiosyncratic nature is still sufficiently considered (Causholli and Knechel 2012). In particular, standardization may not necessarily enhance audit quality as client-specific needs and expectations could be insufficiently considered in the search for uniformity in process organization (Knechel et al. 2020). Additionally, an important argument against mandatory audit firm rotation is that a change in audit firm results in the loss of client-specific knowledge and the lack of an effective working relationship with the client (Arruñada 2000; Gold, Klynsmit, Wallage, and Wright 2018), two factors which clients and auditors highly value throughout the selection process. Furthermore, my results indicate that the introduction of mandatory audit firm rotation is costly not only because of the expensive tender process, for which auditors and clients spend many hours but also because of the – largely ignored – relational costs.

Finally, there are additional consequences resulting from the new regulations. Due to the stringent regulations, the quality of all PIE-licensed audit firms is sufficiently high, at least according to my interviewees. Yet, my findings show that clients perceive a lack of choice in the Dutch audit market, as only six PIE-licensed audit firms are allowed to audit PIEs. Additionally, clients are not allowed to hire firms that provide certain consulting services as their prospective auditors. Furthermore, in the case of a mandatory audit firm rotation, clients are not allowed to reappoint their current auditor, and most clients had at least two non-eligible firms due to cooling-in and cooling-off issues. Given that most PIEs in this study refrain from hiring a non-Big 4 audit firm, clients typically faced limited choices, often restricted to two firms, with one client reporting only a single eligible firm. Furthermore, most clients studied change within the Big 4. Consequently, I argue that the goal of increasing competition outside of the Big 4 in the audit market (EC 2010) may not have been achieved, especially given the limited engagement with non-Big 4 firms by PIEs. More detrimentally, because of this lack of choice, clients may not be allowed to hire the best-suited auditor. Finally, I find that auditors may still engage in low-balling (Cameran, Francis, Marra, and Pettinicchio 2015; Goddard and Schmidt 2021), as I find that auditors invest in the auditor-client relationship during the selection process, and therefore do not bill additional fees that result from a more demanding first-year audit.

3.2. The Auditor Selection Process: A Guide for Organizing the Process and Winning the Bid

This study informs clients on best practices about the auditor selection process and how large clients organize their selection process. This dissertation can, therefore, be used when setting up the next auditor selection process. For example, I find that auditor selection timing is important and may influence audit quality, so I suggest starting the process at least a year before the tender process begins. Next, this dissertation highlights that shifting the hiring power away from managers (e.g., Fatemi 2012; Mayhew and Pike 2004; van Brenk, Renes, and

Trompeter 2020) and increasing audit committee involvement (e.g., Chen and Zhou 2007; Beasley, Carcello, Hermanson, and Neal 2009) may increase the quality of the auditor selected. Additionally, I suggest clients be wary of the auditor's relationship-building activities to ensure that the criteria are set up as measurable as possible before the selection process is carried out and evaluate these criteria transparently.

This dissertation offers evidence of how audit firms anticipate clients' requirements and deliver greater satisfaction while simultaneously improving their own quality (Daugherty and Tervo 2008). Auditors may use my results to determine what to focus on in their subsequent selection process participation, as clients value a strong auditor-client relationship characterized by interpersonal fit, trust, and commitment, resulting in improved communication and efficient working environments, as good working relationships facilitate auditor-client interactions (e.g., Guénin-Paracini et al. 2015; Hatfield, Hoang, Ricci, and Thomas 2022) and auditor objectivity (Herda and Lavelle 2015, 2022). Clients also seek auditors who offer more than just formal assessments, appreciating insights into sector-specific and risk management issues. This emphasis on relational factors over mere technical expertise highlights clients' preference for auditors who not only align with their accounting stances but also demonstrate a genuine eagerness to understand and meet their specific needs (Fiolleau et al. 2013). Such a relationship, built on mutual understanding and cooperation, is crucial for clients, particularly in mandatory audit firm rotation settings, where the ability to develop and maintain trust can significantly impact the perceived quality and value of the audit services provided. Clients rely on signals of credibility because of the difficulty of assessing a 'good auditor' (Causholli and Knechel 2012). Signals of credibility include ensuring the proposal looks good and presenting a partner and team that 'fits' with the client's needs.

4. Limitations and Areas for Future Research

While I investigate the auditor selection process from three different methodological perspectives, this study has inherent methodological and data limitations. In addition, given the widely dispersed literature on the auditor selection process, the different actors involved, different types of companies, and so on, it is impossible to outline everything in one dissertation.

First, I will discuss some of the *methodological* shortcomings of each chapter. In *Chapter 1*, I followed literature review best practices (e.g., Hardies et al. 2024). Nonetheless, there is inherently some judgment necessary to determine the search criteria, paper inclusion, and evidence quality, and certain papers could have been excluded because they were published in other journals or not returned by my search terms. In *Chapter 2*, I used a new measure to investigate audit partner-client alignment. While this is a good starting point, and plenty of robustness analyses have been performed, different weights could be given to the different matching variables. In addition, especially when including my case-study findings, partner-client alignment may encompass many other, unmeasurable, variables. Furthermore, I use proxies to measure audit quality, which, as with all audit quality proxies, are a proxy and inherently limited in encompassing audit quality. *Chapters 3* and *4* include case study-based research. As with all interview research, my results may be subject to participant and researcher bias. I tried to overcome this by following best practice guidelines in auditing field research, such as those suggested by Yin (2014), Malsch and Salterio (2016), and Gendron and Power (2015).

This dissertation encompasses some *data (and content)* limitations, or as I would like to call this, opened some areas for further research. Regarding *Chapter 2*, my data arise from a single country, so future research will have to establish the generalizability of my results. While the Belgian audit market is similar to many other small European audit markets, it differs in important respects from others, such as the US audit market. Because of stronger liability concerns, audit partner-client alignment could be even more important in the US audit market. Such concerns make alignment more critical from a defensive auditing perspective. Future research might also attempt to draw distinctions in alignment under mandatory audit firm rotation regimes compared to voluntary audit firm rotation. Additional questions raised were at least partly solved in *Chapters 3* and *4*. Although I report on eight distinct auditor selection cases in these chapters, which facilitates comparing and contrasting findings, it is insufficient to generalize to all audit firm rotation cases. Since my sample consists of smaller and larger, private and public, and voluntary and mandatory rotation firms, variation exists between my cases that might not be explained through my theoretical framework. Due to availability issues, I did not interview the same management positions at every firm. Some interviews were also conducted sometime after the rotation, so some details may have already faded from participants' memories. In these cases, I report data from Dutch PIEs, and different country and regulatory settings may result in different findings.[50]

In *Chapter 1*, I already extensively outlined suggestions for future research, which I will not repeat here. Nonetheless, given the interesting findings from *Chapters 2*, *3*, and *4*, I pinpoint

[50] I conducted one PIE case study in the Belgian setting, with an interview with the CFO, the audit committee chair, and the audit partner. The results of this study are unreported but highly similar to those found in the Dutch case studies.

some suggestions and how to address them. The results indicate that best practice guidelines highly impact the auditor selection process. It would be interesting to investigate how audit firms and professional bodies shape their best practices. Additionally, I find that audit proposals can serve as a tool to create credibility toward the client. If given access to such audit proposals, their content, language, and layout could be investigated to determine what helps best convey the auditor's qualities. In the case studies, I only interviewed the winning audit partner. While the interviews provided a rather clear overview of which characteristics matter for winning the bid, future research could focus on partners that lost a bid and further explicate which factors are deal-breakers. Finally, experimental research could build on my findings by investigating whether specific features of the auditor selection process affect auditors' subsequent behavior and audit outcomes and how management involvement in the selection process affects the power dynamics in audit-client interactions after the appointment.

Overall, the findings in this dissertation have significant implications for academics studying auditor selection behavior. The contributions extend beyond this area, influencing various streams of auditing literature, including auditor switching, auditor hiring, and, more broadly, audit quality and auditor independence studies. While this dissertation addresses certain questions, it simultaneously opens numerous avenues for further research. I encourage academics to further explore the fascinating auditor selection world.

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APPENDIX A: OVERVIEW INCLUDED STUDIES CHAPTER 1

APPENDIX A: Overview Included Studies

Title	Author(s)	Year	Journal[1]	Setting[2]	Design	Sample Size	Main DV	Main IV	Key Results Related to the Auditor Selection Process	Section[3]
A Matter of Appearances: How Does Auditing Expertise Benefit Audit Committees When Selecting Auditors	Baugh, Hallman, Kachelmeier	2022	CAR	US, 2007-2010, public	Archival	1605 firm-years	Partner attractiveness	AC characteristics	- Audit committees without Big 4 working experience are more likely to engage attractive audit partners.	3.1.2.1.
Adverse Section 404 Opinions and Shareholder Dissatisfaction toward Auditors	Hermanson, Krishnan, Ye	2009	AH	US, 2006, public	Archival	480 firms	Auditor ratification	Material weakness	- Shareholders are less likely to vote for auditor ratification if the company received an adverse opinion because of only noncompany-level material weaknesses. - Shareholders may blame the auditor for being partly responsible for material weaknesses.	3.3.2.
An Analysis of Forced Auditor Change: The Case of Former Arthur Andersen Clients	Blouin, Grein, Rountree	2007	TAR	US, 2002, public	Archival	407 former Arthur Andersen clients	Follow Arthur Andersen auditor	AC financial expertise	- The presence of a financial expert on the audit committee had a marginal influence on the committee's choice of auditor. Other board characteristics were unassociated with a company's auditor selection. - Client companies may follow their audit engagement partner when that partner changes to another audit firm, trading off switching costs and agency concerns.	3.1.1.; 3.1.2.1.
An Examination of Partner Perceptions of Partner Rotation: Direct and Indirect Consequences to Audit Quality	Daugherty, Dickins, Hatfield, Higgs,	2012	AJPT	US	Semi-structured interviews and survey	Survey: 370 partners, 7 semi-structured interviews	Audit quality	Partner perceptions	- Audit partners sometimes need to relocate to maintain industry expertise and continue serving clients in the same industry. - Partners report a two- to three-year new-client familiarization period before they are fully effective on new engagements, increasing the amount of time audit engagements suffer from ''start-up'' efficacy concerns.	3.1.1.; 3.3.1.1.
An Experimental Investigation of the Influence of Audit Fee Structure and Auditor Selection Rights on Auditor Independence and Client Investment Decisions	Fatemi	2012	AJPT	US	Experiment	150 undergraduate majors	Objectivity violations	Selection responsibility	- Auditors' interpretation of information they acquire from investigations is affected by the placement of hiring responsibility. - Under manager selection, when low-balling exists, auditors initially attribute a higher accuracy to favorable test results (those indicating a high asset value) than to unfavorable test results (those indicating a low asset value). The difference in accuracy assessments dissipates with time. - Under investor selection, accuracy assessments of favorable and unfavorable test results do not differ. Management is heavily involved in auditor selection decisions. - Transferring the power to hire and fire the auditor from managers to investors reduces objectivity violations	3.1.2.2.; 3.3.2.

Title	Author(s)	Year	Journal[1]	Setting[2]	Design	Sample Size	Main DV	Main IV	Key Results Related to the Auditor Selection Process	Section[3]
Are There Adverse Consequences of Mandatory Auditor Rotation? Evidence from the Italian Experience	Cameran Francis, Marra, Pettinicchio	2015	AJPT	Italy, 2006-2009, public	Archival	667 firm-years	Audit fees and audit hours	Mandatory/voluntary rotation	- For the outgoing auditor, there is no evidence of lower-quality audits due to shirking in the final-year engagement. - There is some evidence of abnormally higher fees, as the final-year fees are 7 percent higher than normal. - For the incoming auditor, audit effort (hours) is abnormally higher by 17 percent in the initial engagement, but initial fees are discounted by 16 percent relative to ongoing engagements.	3.1.1.; 3.2.2.
Audit Committee Composition and Shareholder Actions: Evidence from Voting on Auditor Ratification	Raghunandan, Rama	2003	AJPT	US, 2001, public	Archival	199 firms	Auditor ratification	AC quality	- In companies with a high non-audit fee ratio, shareholders are less likely to vote against auditor ratification if the audit committee has solely independent directors. - The results suggest that good audit committees can affect shareholder perceptions related to the auditor, particularly in those situations where shareholders might perceive an increased threat to auditor independence. - The proportion of shareholders not voting for ratification of the auditor in the presence of high non-audit fee ratios (relative to companies with low non-audit fee ratios) will be lower at companies that have (1) solely independent members on the audit committee and (2) have at least one member with accounting or finance expertise on the audit committee.	3.1.2.1.; 3.3.2.
Audit committee diligence around initial audit engagement	Kalelkar	2016	AA	US, 2006-2012, public	Archival	368 firm-years	AC meetings	First-year audit	- Audit committees meet more frequently in the first year of the audit engagement.	3.1.2.1.
Audit committee gender diversity and financial reporting: evidence from restatements	Oradi, Izadi	2019	MAJ	Iran, 2013-2017, public	Archival	683 firm-years	Restatements	AC female director	- There is a significant positive relationship between audit committee gender diversity measures and hiring industry specialist auditors.	3.1.2.1.
Audit committee quality indices, reporting quality and firm value	Almaqoushi, Powell	2021	JBFA	US, 2002-2012, public	Archival	12,301 firm-years	Auditor switch, audit quality	AC quality	- Low AC quality firms are more likely to switch from a Big 4 auditor to a non-Big 4 auditor, indicating a preference for lower quality auditing.	3.1.2.1.
Audit Committee, Board Characteristics, and Auditor Switch Decisions by Andersen's Clients	Chen, Zhou	2007	CAR	US, 2001, public	Archival	821 firms	Timing of AA dismissal	AC and board indices	- Clients with more independent boards dismissed Andersen sooner and were more likely to choose a Big 4 successor auditor. Firms with more effective audit committees and boards of directors responded quickly to the Andersen-Enron situation and were more likely to demand higher reputation auditors. - Firms with more independent audit committees, audit committees with greater financial expertise, and audit committees with larger boards dismissed Andersen earlier.	3.1.2.1.
Audit Firm Appointments, Audit Firm Alumni, and Audit Committee Independence	Lennox, Park	2007	CAR	US, 1995-2000, public	Archival	1198 changing clients	Officers' former audit firm selection	Firm alumnus	- An audit firm is more likely to be appointed if the company has an officer who is an alumnus of that firm. - Companies are less likely to appoint officers' former firms if audit committees are more independent.	3.1.2.1.

Title	Author(s)	Year	Journal[1]	Setting[2]	Design	Sample Size	Main DV	Main IV	Key Results Related to the Auditor Selection Process	Section[3]
Audit Procurement: Managing Audit Quality and Audit Fees in Response to Agency Costs	Jensen, Payne	2005	AJPT	US, 1998, governmental	Survey	228 surveys	Audit quality, procurement metrics	Procurement metrics, agency costs	- US municipalities with higher agency costs have better-developed audit procurement practices (i.e., competitive bidding, multi-year contracts, a focus on technical expertise rather than fees, training and rotation of procurement personnel, and the presence of an audit committee). - Better-developed audit procurement practices were associated with hiring auditors with more industry expertise.	3.2.2.; 3.3.1.1.
Audit Tendering in the UK: A Review of Stakeholders' Views	Allam, Ghattas Kotb, Eldaly	2017	IJA	UK	Content analysis	61 comment letters	N/A	N/A	- Mandatory tendering could have potential benefits from greater auditor independence and a fresh pair of eyes performing audit work. - There is clear conflict of interests among some stakeholder groups such as audit firms and companies on one side and institutional investors on the other side. - Mandatory tendering concerns include increased audit costs, reduced expertise, and auditor susceptibility to pressure from management.	4.1.
Auditor choice in private firms: a stakeholders perspective	Corten Steijvers, Lybaert	2018	MAJ	Belgium, 2015, private	Survey	210 surveys	Big 4	Competitor, supplier, customer Big 4 choice	- Companies value auditor knowledge of related companies, showing that companies align with their main supplier's Big 4 auditor choice	3.3.1.1.
Auditor Ratification: Can't Get No (Dis)Satisfaction	Cunningham	2017	AH	US, 2009-2012, public	Archival	9003 firms	Auditor ratification	Recommendation against ratification by proxy advisors	- Proxy advisors have a statistically significant influence over shareholder voting outcomes when they recommend against auditor ratification. - The against recommendation is rare, and the qualitative significance is less clear. Proxy advisor 'against recommendations ' are based on concerns about auditor independence and poor audit quality, but there appears to be variation in the extent to which proxy advisors issue 'against recommendations' for each of these criteria.	3.3.2.
Auditor search periods as signals of engagement risk: Effects on auditor choice and audit pricing	Mande, Son, Song	2017	AA	US, 2002-2012, public	Archival	5524 firm-years	Big N choice	Auditor search period	- Clients associated with long search periods are less likely to be accepted by Big N auditors. - Delays in appointing successor auditors following resignations are associated with higher audit fees and negative stock market responses.	3.1.1.
Auditor Selection and Audit Committee Characteristics	Abbott, Parker	2000	AJPT	US, 1994, public	Archival	500 firms	Specialized auditor choice	AC characteristics	- Active and independent audit committees are more likely to employ an industry-specialist auditor.	3.1.2.1.
Auditor selection following auditor turnover: Do peers' choices matter?	Li, Sun, Ettredge	2017	AOS	US, 2001-2012, public	Archival	4,074 auditor switches	Choice for social norm office	Proportion of local peers audited by social norm office	- More similar peer companies have a greater propensity to select the norm auditor (i.e., the auditor engaged by the greatest proportion of a company's peers).	3.3.1.1.

Title	Author(s)	Year	Journal[1]	Setting[2]	Design	Sample Size	Main DV	Main IV	Key Results Related to the Auditor Selection Process	Section[3]
Auditor Selection Process: An Interplay of Demand Mechanisms – A Multilevel Network Approach	Kacanski, Lusher, Wang	2021	EAR	Denmark, 2010-2014, public	Archival	774 annual statements	Auditor choice	Network characteristics	- Results show that supervisory boards tend to select auditors who are preferably affiliated with the Big Four rather than the non-Big Four. - The results appear to show that interlocking directorships are not only driven by the same principle, but by combining the reputation effect with the auditor popularity effect. They have a strong influence on aligning corporate decisions across multiple boards.	3.1.2.1.
Auditor Tenure and Shareholder Ratification of the Auditor	Dao, Mishra, Raghunandan	2008	AH	US, 2006, public	Archival	635 firms	Auditor ratification	Tenure	- Shareholder votes against or abstaining from auditor ratification are positively correlated with auditor tenure. - The results suggest that shareholders view long auditor tenure as adversely affecting audit quality, and provide an empirical basis for arguments related to the impact of long auditor tenures on shareholders' perceptions of audit quality.	3.3.2.
Auditor Tenure Disclosure and Shareholder Ratification Voting	Tanyi, Rama, Raghunandan	2021	AH	US, 2017-2018, public	Archival	6436 firm-years	Auditor Ratification	Tenure, post PCAOB rule 2017 (tenure disclosure)	- In the case of clients with long (short) auditor tenure, the proportion of shareholder votes not ratifying the auditor increased (decreased) after public disclosure of auditor tenure.	3.3.2.
Auditor–client management relationships and roles in negotiating financial reporting	McCracken, Salterio, Gibbins	2008	AOS	Canada	Field-study, interview-based	16 interviews, 8 with CFO, 8 with AP	N/A	N/A	- Audit firms appear to manage the assignment of partners to engagements based on CFO preferences and remove those partners who are in ''poor'' relationships, irrespective of why the relationship is considered by the CFO to be ''poor''.	3.3.1.2.
Board Gender Diversity, Auditor Fees, and Auditor Choice	Lai, Srinidhi, Gul, Tsui	2017	CAR	US 2001-2011, public	Archival	2576 firm-years	Audit fees and auditor choice	Board gender diversity	- Firms with gender-diverse boards (audit committees) pay 6 percent (8 percent) higher audit fees and are 6 percent (7 percent) more likely to choose specialist auditors compared to all-male boards (audit committees).	3.1.2.1.
Board Independence and Audit-Firm Type	Beasley, Petroni	2001	AJPT	US, 1993, public and private	Archival	681 insurers	Auditor choice	Outside board directors	- The likelihood of an insurer employing a brand name auditor that specializes in the insurance industry is increasing in the percentage of the members of the board of directors that are considered outsiders. - However, there is no significant association between board composition and the choice of using a non-specialist brand name (Big 6) auditor and a nonbrand name auditor, suggesting specialization is considered to be important, but not brand name in this setting.	3.1.2.1.
Challenging Global Group Audits: The Perspective of US Group Audit Leads*	Downey, Westermann	2021	CAR	US, 2019, public	Survey, Interview	Survey: 148 managers, 16 semi-structured interviews	N/A	N/A	- GGA leads overtly impose their dominance on the CA firms during partner selection. Specifically, rather than permit the local firm to choose a CA partner, the group audit lead actively manages selection of the CA partner(s) identifying a local partner they deem qualified, likely as a way to manage regulatory risk.	3.1.2.2.; 4.2.

Title	Author(s)	Year	Journal[1]	Setting[2]	Design	Sample Size	Main DV	Main IV	Key Results Related to the Auditor Selection Process	Section[3]
Changing the Institutional Framework of Statutory Audit: Internal Stakeholders' Perceptions of the Associated Benefit and Costs	Ruhnke, Schmidt	2016	EAR	Germany	Survey	Surveys: 273 (121 management representatives, 152 supervisory board members)	Audit quality perceptions	Mandatory external rotation, selection by independent regulator	- German management representatives and supervisory board members do not expect auditor appointments by an independent regulator to increase the benefits of audits, such as client-specific expertise and knowledge, professional competence and expertise, independence, professional skepticism, and reputation.	3.3.3.
Compulsory Audit Tendering and Audit Fees: Evidence from Australian Local Government	Boon, Crowe, McKinnon, Ross	2005	IJA	Australia, 1993-2007, governmental	Archival	988 observations	Audit fees	Post-tender year	- Audit tendering introduced significant competition into the local government audit services market and an associated large fee decrease.	3.2.1.
Corporate Governance in the Post-Sarbanes-Oxley Era: Auditors' Experiences*	Cohen, Krishnamoorty, Wright	2010	CAR	US	Semi-structured Interviews	Interviews: 30, 10 audit managers and 18 audit partners	N/A	N/A	- The actual selection influence assigned to the management was 53 percent while that assigned to the audit committee was 41 percent.	3.1.2.2.; 4.1.
Demand for and Assessment of Audit Quality in Private Companies	Esplin, Jamal, Sunder	2018	Abacus	Canada, private	Semi-structured interviews	27 interviews with CFOs, auditors and 'other users'	N/A	N/A	- In all 11 Canadian private companies that had recently hired an auditor, top management (usually the CEO) selected the auditor. - 4 out of 11 companies studied by used an RFP. - High importance of work relationships and specific audit partners' organizational "fit"	3.1.2.2.; 3.2.1.; 3.3.1.; 3.3.1.2.; 4.1.
Do Investors' Perceptions Vary with Types of Nonaudit Fees? Evidence from Auditor Ratification Voting	Mishra, Raghunandan, Rama	2005	AJPT	US, 2003, public	Archival	248 firms	Auditor ratification	Non-audit fees	- The proportion of shareholders voting against auditor ratification in 2003 is (1) positively associated with both the tax fee ratio and the ''other'' fee ratio, but (2) negatively associated with the audit-related fee ratio.	3.3.2.
Do regulations limiting management influence over auditors improve audit quality? Evidence from China	Chi, Lisic, Long, Wang	2013	JAPP	China 2001-2009, public	Archival	5533 firm-years	Abnormal accruals	Limitation of management influence	- Audit quality for CSOEs relative to other companies improves after the enactment of these rules (that limit management influence over auditors).	3.1.2.2.; 3.3.3.
Does Audit Committee Disclosure of Partner-Selection Involvement Signal Greater Audit Quality?	Downes, Draeger, Sadler	2022	AH	US, 2014-2019, public	Archival	3690 firm-years	Audit quality	AP disclosure	- Disclosure of audit committee activity and involvement in the audit partner selection process could lead to selecting a more rigorous partner, resulting in higher audit quality.	3.1.2.1.
Does auditor designation by the regulatory authority improve audit quality? Evidence from Korea	Kim, Yi	2009	JAPP	Korea, 1991-2000, public	Archival,	2750 firm-years	Discretionary accruals	Designated auditor	- The level of discretionary accruals is significantly lower for firms with designated auditors than firms with a free selection of auditors. - Firms with mandatory auditor changes (i.e., auditor designation) report significantly lower discretionary accruals compared to firms with voluntary auditor changes.	3.3.3.

Title	Author(s)	Year	Journal[1]	Setting[2]	Design	Sample Size	Main DV	Main IV	Key Results Related to the Auditor Selection Process	Section[3]
Does Investor Selection of Auditors Enhance Auditor Independence?	Mayhew, Pike	2004	TAR	US	Experiment	40 participants	Auditor effort	Selection responsibility	- Transferring power to hire and fire the auditor from managers to investors decreases the proportion of independence violations, especially combined with eliminating the auditor's moral hazard over effort and this increases the overall economic surplus in the markets examined. Violations reduced from 69-82 to 26-36 percent.	3.3.2.
Does regulator designation of auditors improve independence?	Tang, Ruan, Yang	2017	MAJ	China	Experiment	81 auditors	Auditor recommendation	Selection responsibility	- The regulatory designation of auditors improves their independence.	3.3.3.
Does the Timing of Auditor Changes Affect Audit Quality? Evidence From the Initial Year of the Audit Engagement	Cassell, Hansen, Myers, Seidel	2020	JAAF	US, 2000-2014, public	Archival	7715 auditor changes	Misstatement	Engagement starts during or after fourth fiscal quarter	- The extent to which audit quality suffers in the first year of audit engagements is affected by both the amount of time required to understand the client's business, assess risks, and perform the audit (all of which are driven by client complexity), as well as the amount of time available for auditors to perform these tasks.	3.1.1.
Exploratory insights into audit fee increases: A field study into board member perceptions of auditor pricing practices	Goddard, Schmidt	2021	IJA	Luxembourg, 2018	Semi-structured interviews	12, 10 board members, two audit managers,	N/A	N/A	- Competing auditors commonly engage in low-balling and that, as a result, most board members expect audit fees to decrease when changing auditors.	3.2.2.; 4.1.
Financial Restatements and Shareholder Ratifications of the Auditor	Liu, Raghunandan, Rama	2009	AJPT	US, 2005-2006, public	Archival	194 firms	Auditor ratification	Restatements	- Financial restatements can affect shareholder perceptions related to the auditor and thereby influence their decision of voting on ratifying the auditor.	3.3.2.
Forced Audit Firm Change, Continued Partner-Client Relationship, and Financial Reporting Quality	Chen, Su, Wu	2009	AJPT	China, 2001, public	Archival	174 auditor changes	Client follows the former audit partner to a new audit firm	Accruals	- Clients with greater earnings management activities are more likely to follow their former audit partners to a new audit firm, and aggressive follower clients. - New audit firms are more likely to rotate former partners in the auditing of follower clients in the first post-switch year, a large number of these partners return to their former clients in subsequent years.	3.1.1.
Government and managerial influence on auditor switching under partial privatization	Bagherpour, Monroe, Shailer	2014	JAPP	Iran, 1999-2003, public	Archival	657 firm-years	Auditor switch	Governmental influence	- The likelihood of auditor switches is strongly associated with measures of misalignment between type of auditor and type of controlling shareholder and auditor–managerial misalignment, but these associations are constrained by significant government influence.	3.3.3.
How Audit Committee Chairs Address Information-Processing Barriers	Free, Trotman, Trotman	2021	TAR	Australia, 2017, public	Semi-Structured	24 audit committee chairs	N/A	N/A	- Management and the audit committee perceived no differences among the Big 4 audit firms' expertise. - The engagement partner is extremely important for the audit committee.	3.2.2.; 3.3.1.; 3.3.1.2.

Title	Author(s)	Year	Journal[1]	Setting[2]	Design	Sample Size	Main DV	Main IV	Key Results Related to the Auditor Selection Process	Section[3]
How do auditors respond to competition? Evidence from the bidding process	Hallman, Kartapanis, Schmidt	2022	JAE	US, 2005-2016, public	Archival	17,979 firm-years	Audit fees, Audit quality	Competitive bidding	- Incumbents perform higher quality audits and reduce their fees modestly during bidding years. - Big 4 competitive bidding is positively associated with audit quality as measured by a lower likelihood of misstatement. - Big 4 competitive bidding is associated with modest fee reductions in the two years following an auditor change, regardless of whether the incumbent auditor wins reappointment or not.	3.2.2.
How Do Regulatory Reforms to Enhance Auditor Independence Work in Practice	Fiolleau, Hoang, Jamal, Sunder	2013	CAR	Canada, public	Field Study	A firm case study	N/A	N/A	- Tendering in the case was a 90-day process beginning with the company's RFP issuance, 50 days to acquire and prepare information for auditors' written proposals, a subsequent 30-day period until auditors' oral presentations to all members of the auditor selection committee, and a quick deliberation (approximately 10 days) to select and appoint the auditor. - The information exchanged and used for evaluation emphasized cultural fit (e.g., rapport, chemistry, attention to needs) rather than expertise and risk. - The audit committee viewed their role as monitors, rather than drivers, of the process. Management is very involved. - Management and the audit committee perceived no differences among the Big 4 audit firms' expertise. - The bidding firms sought to align engagement team characteristics with the CFO. - Auditors aim to discern the preferences of the company's key decision-makers and customize their proposals accordingly.	3.1.1.; 3.1.2.2.; 3.2.1.; 3.2.2.; 3.2.3.; 3.3.1.; 3.3.1.2.; 4.1.
How Does an Audit Partner's Perceived Technical Expertise and Objectivity Impact the Audit Partner Selection Process? Experimental Evidence on Managers' Recommendations	Bhaskar, Carlisle, Hux	2021	SSRN	US	Experiment	200 accounting and finance executives and managers	Auditor recommendation	Social ties, technical expertise	- Managers appear to be more likely to recommend audit partners with prior Big 4 experience and less likely to recommend audit partners with social ties.	3.2.2.
Insights from an Analysis of Audit Committee Governance Practices at U.S. Registered Investment Companies and Public Operating Companies	Jenkins, Pyhoza, Taylor	2019	SSRN	US, public	Survey and Interviews	Survey: 107 IC ACM, interviews: ten AC, ten management members at ICs, ten OC AC members	N/A	N/A	- Overall, management is heavily involved in auditor selection decisions only in public companies, not investment companies. - This effect is more substantial when the CEO plays a dominant role on the board. - Audit committees of investment companies oversee audit firm retention and hiring decisions substantially. - Conversely, audit committees of public companies perform a more ceremonial role.	3.1.2.1.; 3.1.2.2.

Title	Author(s)	Year	Journal[1]	Setting[2]	Design	Sample Size	Main DV	Main IV	Key Results Related to the Auditor Selection Process	Section[3]
Management Influence on Auditor Selection and Subsequent Impairments of Auditor Independence during the Post-SOX Period	Dhaliwal, Lamoreaux, Lennox, Mauler	2015	CAR	US, 1995-2009, public	Archival	2145 Big 4 appointments	Firm appointment	Management affiliation	- Management affiliation continues to have a significant impact on auditor selection during the post-SOX period. - No consistent evidence is found that management influence over auditor selection leads to impaired auditor independence during the post-SOX period. - The lower propensity of hired affiliate auditors to issue going-concern opinions is partially offset by audit committees that are larger and audit committees with accounting expertise.	3.1.2.1.; 3.1.2.2.
Management Trade-Offs of Internal Control and External Auditor Expertise	Jensen, Payne	2003	AJPT	US, 1992, governmental	Survey	405 cities	Auditor industry expertise	Internal control mechanisms	- Companies that do not hire internal auditors tend to compensate by selecting external auditors with relatively high levels of industry expertise.	3.3.1.1.
Management's Undue Influence over Audit Committee Members: Evidence from Auditor Reporting and Opinion Shopping	Berglund, Draeger, Sterin	2022	AJPT	US, 2004-2017, public	Archival	9868 firm-years	GCO	Management influence	- Higher relative management influence over audit committee members is associated with less conservative auditor reporting and increased opinion shopping behavior..	3.1.2.2.
Managing the Auditor-Client Relationship Through Partner Rotations: The Experiences of Audit Firm Partners	Dodgson, Agoglia, Bennett, Cohen	2020	TAR	US	Semi-structured interviews	20 partners	N/A	N/A	- Partner assignment is typically not random. - Partner rotation is an extended process (rather than a single discrete event). - Interviewees report assigning non-decision-making senior partners as relationship liaisons. When the auditioning of engagement partners is complete and the next partner is selected, interviewees depict the logistical challenges, time commitments, and firm resources invested to ensure that the incoming engagement partner is equipped to hit the ground running when rotation takes place. - Interviewees stress that firms' emphasis on the auditor-client relationship is not limited to the period immediately preceding an engagement partner rotation matching evaluations.	3.1.1.; 3.1.2.1.; 3.3.1.; 3.3.1.2.
Market Reaction to Auditor Ratification Vote Tally	Tanyi, Roland	2017	AH	US, 2010-2015, public	Archival	6621 dismissals	Dismissal	Auditor ratification	- High shareholder disapproval of the auditor's appointment is positively associated with the dismissal of the auditor.	3.3.2.
Military reform, militarily-connected firms and auditor choice	Harymawan	2020	MAJ	Indonesia, 2003-2017, public	Archival	3473 firm-years	Big 4 choice	Military directors	- Firms with a militarily-connected director are less likely to appoint one of the Big 4 auditors.	3.3.3.
Network Analysis of Audit Partner Rotation	Pittman, Wang, Wu,	2022	CAR	China, 2003-2017, public	Archival	3145 rotated-off partners	Partner selection	Connections	- Connections are a major determinant in the selection process. - Engagements are more likely to be rotated to well-connected successors when the audit engagements are more complex, client-specific knowledge is not readily available to the succeeding partners, and the engagements are more valuable to the audit firms.	3.3.1.2.

Title	Author(s)	Year	Journal[1]	Setting[2]	Design	Sample Size	Main DV	Main IV	Key Results Related to the Auditor Selection Process	Section[3]
Non-audit services and shareholder ratification of auditors	Raghunandan	2003	AJPT	US, 2001, public	Archival	172 firms	Auditor ratification	Non-audit fees	- The proportion of votes against the auditor increases with the ratio of non-audit fees.	3.3.2.
On the constitution of audit committee effectiveness	Gendron, Bedard	2006	AOS	Canada, public	Case study	22 interviews at 3 companies	N/A	N/A	- AC opinions on their role in the auditor selection process are mixed, ranging from influential to not having a direct impact but having a monitoring function.	3.1.2.1.; 3.1.2.2.
On the Economics of Mandatory Audit Partner Rotation and Tenure: Evidence from PCAOB Data	Gipper, Hail, Leuz	2021	TAR	US, 2008-2014, public	Archival	17,900 firm-years, 2,385 mandatory engagement-partner rotations (Big 6 clients)	Audit economics	Partner tenure	- There are audit fee pressures around partner rotations, particularly in less concentrated local markets. - There is an increase in total audit hours, engagement partner and review partner hours shortly after rotations. - Audit firms manage transitions differently depending on client size. For larger and more complex clients, evidence of earlier onboarding of incoming partners and shadowing of outgoing partners is found. - For smaller clients, partners spend more time on the assignment in the initial years after rotation. - Audit team rotations are more disruptive than rotating just the lead partner, although not as disruptive as changing the audit firm.	3.1.1.
Perceptions of Audit Service Quality and Auditor Retention	Butcher, Harrison, Ross	2012	IJA	Australia, 2006, governmental	Survey	213 finance professionals and auditors	Auditor retention	Audit service quality	- Competition increased after introduction of mandatory tendering.	3.2.1.
Political Connections, Audit Opinions, and Auditor Choice: Evidence from the Ouster of Government Officers	He, Pan, Tian	2017	AJPT	China, 2004-2014, public	Archival	84 anti-corruption cases,	MAO, auditor choice	Political connections	- Connected state-owned enterprises (SOEs) receive more favorable audit opinions than their non-connected counterparts, whereas connected non-SOEs obtain less favorable opinions. - After the termination of political connections, connected SOEs are more likely, while connected non-SOEs are less likely, to hire local small auditors.	3.3.3.
Pricing Strategies of Big4 and Non-Big4 Auditors in the Light of Audit Tendering	Baumann, Ratzinger-Sakel, Tiedemann	2022	SSRN	Germany, 2016-2019, public	Archival	1028 firm-years	Audit fees	Mandatory tendering	- Auditors (particularly Big 4 auditors) facing a tender charge higher audit fees but do not provide higher quality audits.	3.2.2.
Procurement Practices and the Municipality Auditing Market	Marques, Pinto	2019	JAAF	Portugal, 2007-2011, governmental	Survey	170 surveys of 38 municipalities	Lowest price criterion	Procurement metrics	- The majority of municipalities acquire auditing services through direct selection and choose their auditors based upon the lowest price selection criterion. - However, municipalities where the procurement process is more sophisticated employ the lowest price selection criterion less frequently.	3.3.1.1.
Proposal readability, audit firm size and engagement success	Chang, Stone	2019	MAJ	US, 2008-2012, governmental	Archival/Content analysis	370 audit proposals	Winning bid	Proposal readability	- Increased readability of auditors' proposals improves their likelihood of winning the engagement.	3.2.2.

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Proprietary information spillovers and supplier choice: evidence from auditors	Aobdia	2015	RAS	US, 1985-2011, public	Archival	721 firm-years	Auditor switch	Auditor overlap	- Rival firms become less (more) likely to share the same auditor when the costs of information spillovers increase (decrease).	3.3.1.1.
Realigning Auditors' Accountability: Experimental Evidence	Hurley, Mayhew, Obermire	2019	TAR	US	Experiment	248 undergraduate and graduate students	Audit quality	Hiring responsibility	- Auditors do not simply require increased accountability to investors, but also an elimination of managers' ability to economically punish them through decreased hiring, to increase audit quality.	3.3.2.
Referral as a determining factor for changing auditors in the Belgian auditing market: An empirical study	Branson, Breesch	2004	TIJA	Belgium, 1996, public and private	Archival, Survey	1434 parent companies, 279 surveys	Same auditor choice	Referral	- In group audit scenarios, the management of the parent company influences the auditor selection of the subsidiary company.	3.1.2.2.; 4.2.
Reputation Capital of Directorships and Demand for Audit Quality	Fredriksson, Kiran, Niemi	2020	EAR	Finland, 2007-2016, public	Archival	1249 firm-years	Audit quality	Reputation capital	- Companies that have directors with multiple directorships pay higher fees to their auditors and choose better-known auditors to protect their reputation capital.	3.1.2.1.
Role expectations and agency in the audit tendering process	Taminiau, Heusinkveld	2017	AAAJ	The Netherlands, 2012	Content analysis and Interviews	75 client evaluations of auditors & 8 in-depth interviews with partners and directors	N/A	N/A	- In the context of auditor-client relationships, expectations cannot be considered stable but may vary significantly throughout the tendering process. - Auditors are not only determined by the formal tendering procedures, but are also influenced by their level of agency. - Tendering processes exist of three phases (orientation, intake, and presentation). - The key actors are CFOs, controllers, managers, and the audit committee.	3.1.1.; 3.1.2.2.; 3.2.1.; 3.2.2.; 3.2.3.; 3.3.1.1.
Shareholder Dissatisfaction and Subsequent Audit Outcomes	Tanyi, Rama, Raghunandan, Martin	2020	AH	US, 2004-2015, public	Archival	12085 shareholder ratifications	Auditor effort, reporting quality	Auditor ratification	- Increases in shareholder dissatisfaction, as proxied by shareholder votes against auditor ratification, are associated with higher audit fees and longer audit report lags, which reflect higher auditor effort, in the following fiscal year. - Increases in shareholder dissatisfaction are associated with lower abnormal accruals and a lower likelihood of financial statement misstatements in the following year, indicating higher financial reporting quality.	3.3.2.
Shareholder Votes on Auditor Ratification and Subsequent Auditor Dismissals	Barua, Raghunandan, Rama	2017	AH	US, 2011–2014, public	Archival	12,664 shareholder ratifications, 423 auditor dismissals	Auditor dismissal	Auditor Ratification	- Subsequent auditor dismissals become more likely with increases in the proportion of shareholders not ratifying the auditor.	3.3.2.
Shareholder Voting on Auditor Selection, Audit Fees, and Audit Quality	Dao, Raghunandan, Rama	2012	TAR	US, 2006, public	Archival	1382 firms	Audit fees, audit quality	Auditor ratification	- Firms that started having a shareholder vote pay higher fees than firms that stopped having a shareholder vote. - In firms with shareholder voting on auditor selection (1) subsequent restatements are less likely and (2) abnormal accruals are lower.	3.1.2.2.; 3.3.2.

Title	Author(s)	Year	Journal[1]	Setting[2]	Design	Sample Size	Main DV	Main IV	Key Results Related to the Auditor Selection Process	Section[3]
Shareholder Ratification of Auditors After PCAOB Censures	Tanyi, Rama, Raghunandan	2021	SSRN	US, 2007-2019, public	Archival	3396 firm-years	Auditor ratification	PCAOB censure	- The proportion of votes against the auditor increases with longer auditor tenures, and when there are signs of poor audit quality.	3.3.2.
The Audit Committee Oversight Process	Beasley, Carcello, Hermanson, Neal	2009	CAR	US, 2004-2005, public	Semi-structured interviews	42 ACM	N/A	N/A	- Audit committees generally consider audit firms (especially the Big 4) to be broadly equivalent, shifting much of their focus from the audit firm to the individual partner. - Management is still highly influential in the auditor selection process.	3.1.2.2.; 3.3.1.2.
The audit market effects of disputing a GAAP-deficient PCAOB inspection report	Abbott, Buslepp, Notbohm	2018	AA	US, 2005-2014, public	Archival	113 inspection reports, 805 client companies	Auditor dismissal	Auditor disagreement of PCAOB inspection report, AC financial expertise	- Triennially inspected auditors that dispute the PCAOB findings are far less likely to be dismissed when a client has an audit committee director with accounting-related financial expertise.	3.1.2.1.
The Determinants and Effects of Clients Following Audit Partners Who Switch Audit Firms	Chang, Choy, Lin, Koo	2019	EAR	Taiwan, 1984-2010, public	Archival	1258 company-years	Client moves	Firm tenure, partner tenure, specialization	- Clients are more likely to follow departing partners when the partners have more clients, longer tenure, and when both lead and concurring partners leave simultaneously. - Clients are more likely to stay with their incumbent audit firms when the firms are one of the Big Four or when only the concurring partners leave. client companies may follow their audit engagement partner when that partner changes to another audit firm.	3.1.1.
The effect of a bidding restriction on the audit services market	Hackenbrack, Jensen, Payne	2000	JAR	US, 1995, governm ental	Survey, Archival	675 financial statements	Audit fees	Bidding restriction metrics	- Municipalities covered by the statute paid higher audit fees, engaged larger audit firms and firms with larger municipal audit client bases, and were more likely to be recognized for excellence in financial reporting than municipalities not covered by the statute. - The bidding statute created a market climate in which required nonprice competition impeded the entry of lesser qualified auditors, whereas the anticipated financial rewards induced the entry of more qualified auditors.	3.2.2.
The Effect of Audit Committee and Board of Director Independence on Auditor Resignation	Lee, Mande, Ortman	2004	AJPT	US, 1996-2000, public	Archival	190 auditor resignations	Auditor resignation	Board and AC characteristics	- Audit committee and board independence are both negatively and significantly related to the likelihood of an auditor resignation. - The financial expertise of the audit committee members is inversely related to auditor resignations.	3.1.2.1.

Title	Author(s)	Year	Journal[1]	Setting[2]	Design	Sample Size	Main DV	Main IV	Key Results Related to the Auditor Selection Process	Section[3]
The effect of competitive bidding on engagement planning and pricing	Johnstone, Bedard, Ettredge	2004	CAR	US, 1997-1998, public and private	Archival	286 complete proposals	Audit fees, audit hours	Risk metrics	- Competitive bidding is associated with higher planned engagement effort and decreased fees, relative to non-competitive bidding. - Both enhanced service and price discounts are associated with competitive bidding. - An individual partner benefits if an engagement can be gained through service enhancement rather than revenue reduction. - About 50 percent of the clients in the sample chose not to solicit competitive bids.	3.3.1.1.
The Effects of Auditor Designation by the Regulator on Auditor Decisions: Evidence from Korea	Shim, Pae, Choi	2020	BRIA	Korea	Quasi-experiment	375 surveys with auditors	Auditor aggressivenes s	Audit engagement system	- Auditor designation by the Korean regulator leads to less aggressive auditor decisions.	3.3.3.
The Effects of Auditor Rotation, Professional Skepticism, and Interactions with Managers on Audit Quality	Bowlin, Hobson, Piercey	2015	TAR	US	Experiment	226 undergraduate student volunteers,	Effort and aggressivenes s	Rotation	- The effect of auditor rotation on audit quality depends on the auditor's assessment frame. - When auditors assess the honesty of management representations (i.e., a client integrity frame), auditor rotation increases audit effort and decreases the frequency of low-effort audits paired with aggressive financial reporting, decreasing the likelihood of audit failure. - When auditors assess the dishonesty of management representations (i.e., a skepticism frame), auditor rotation decreases audit effort and increases low-effort audits paired with aggressive reporting.	3.1.2.2.
The Effects of Prior Manager-Auditor Affiliation and PCAOB Inspection Reports on Audit Committee Members' Auditor Recommendations	Abbott, Brown, Higgs	2016	BRIA	US	Experiment	118 professionals	Audit firm selection	Inspection, affiliation	- Triennially inspected auditors with unfavorable inspection reports receive less favorable hiring recommendations when management's recommendation is to hire the auditor. - Prior manager-auditor affiliation decreases the participants' hiring recommendations.	3.1.2.1.
The Impact of CEO/CFO Outside Directorships on Auditor Selection and Audit Quality	Yu, Kwak, Park, Zang	2020	EAR	US, 2003-2015, public	Archival	757 firms	Firm selection/hiri ng connected auditor	Connections	- Managers are more likely to appoint auditors with whom they are currently connected, leading to a decrease in audit quality.	3.1.2.2.
The Impact of Mandatory Auditor Tenure Disclosures on Ratification Voting, Auditor Dismissal, and Audit Pricing	Dunn, Lundstrom, Wilkins	2021	CAR	US, 2014-2018, public	Archival	8802 client-years	Auditor ratification, auditor dismissal, audit fees	Tenure and tenure disclosure	- The probability of auditor dismissal increases after disclosure for long-tenured versus short-tenured auditors. shareholder ratification votes against the auditor increase for long-tenured auditors compared to short-tenured auditors in the post-disclosure period.	3.3.2.

Title	Author(s)	Year	Journal[1]	Setting[2]	Design	Sample Size	Main DV	Main IV	Key Results Related to the Auditor Selection Process	Section[3]
The Impact of Risk and the Potential for Loss on Managers' Demand for Audit Quality	Hurley, Mayhew, Obermire, Tegeler	2021	CAR	US	Experiment	166 students	Auditor choice	Risk, potential for loss	- Management choice of the auditor can lead to lower audit quality due to the desire for flexibility in reporting. - Increased risk, the potential for loss, and to a lesser extent their interaction, significantly reduce managers' likelihood of hiring the best available auditor in the market.	3.1.2.2.
The Impact of the Auditor Selection Process and Audit Committee Appointment Power on Investment Recommendations	Gold, Klynsmit, Wallage, Wright	2018	AJPT	The Netherlands	Experiment	118 experienced investment professionals	Recommendation likelihood	AC power	- Audit committees can provide positive signals to investors when given high appointment power. - Audit committee appointment power affects investment recommendations only when a possible auditor change is anticipated (i.e., in the case of rotation and tendering), but not when the auditor selection is voluntary. - Rotation and tendering lead to a higher recommended investment likelihood than voluntary selection, but only when an audit committee has high appointment power.	3.1.2.1.; 4.1.
The Introduction of State Regulation and Auditor Retendering in School Districts: Local Audit Market Structure, Audit Pricing, and Internal Controls Reporting	Elder, Yebba	2020	AJPT	US, 1998-2012, governmental	Archival	6353 firm-years	Auditor choice, auditor switch	State regulation impact	- Retendering policies resulted in greater use of specialist audit firms and increased market concentration. - Audit fees increased substantially after the Acts, with increased fee premiums for specialist auditors. - Audit firms that grew their practices over the sample period and became specialists had higher pricing strategies than established specialists in the market.	3.2.1.; 3.2.2.
The Presence and Effect of the Winner's Curse in the Market for Audit Services: An Experimental Market Examination	Hobson, Marley, Mellon, Stevens	2019	BRIA	US, governmental	Experiment	135 students	Price signal	Audit market type	- Auditors in the simple audit market learn to avoid the winner's curse with pricing experience but this learning effect is hindered in the enriched market. Auditors in the enriched market reduce audit effort when they suffer the winner's curse. - The winner's curse may drive low-balling in the market for audit services.	3.2.2.
The Timing of Auditor Hiring: Determinants and Consequences	Pacheco-Paredes, Rama, Wheatley	2017	AH	US, 2006-2012, public	Archival	1,860 client dismissals	Engagement timing, hiring lag, audit quality	Firm characteristics, engagement timing	- Most auditor changes happen well before the fiscal year-end, in the 300 to 181 days prior. - The appointment of a new CEO or CFO during the fiscal year (but before the auditor change) influences this timing, suggesting that client executives have a significant role in the auditor-hiring process. - Auditor changes closer to the year-end are associated with longer reporting lags and lower audit quality.	3.1.1.
To share or not to share: The importance of peer firm similarity to auditor choice	Bills, Cobabe, Pittman, Stein	2020	AOS	US, 2000-2015, public	Survey and archival	Survey: 40 audit partners, archival: 1,130,588 firm-years	Firms sharing auditor	Similarity	- More similar peer companies have a greater propensity to share the same auditor.	3.3.1.1.

Title	Author(s)	Year	Journal[1]	Setting[2]	Design	Sample Size	Main DV	Main IV	Key Results Related to the Auditor Selection Process	Section[3]
Voluntary audit committees, auditor selection and audit quality: evidence from Taiwan	Kao, Shiue, Tseng	2021	MAJ	Taiwan, 2007-2012, public	Archival	6749 firm-years	Firm has AC, audit partner characteristics, audit quality	Client characteristics, firm has AC	- Voluntary audit committee formation is positively related to an industry specialist lead partner and a lead partner that has a larger number of clients. - Voluntary audit committee formation has a positive impact on audit quality (proxied by discretionary accruals).	3.1.2.1.
Who's Really in Charge? Audit Committee versus CFO Power and Audit Fees	Beck, Mauldin	2014	TAR	US, 2006-2009, public	Archival	9214 firm-years	Audit fees	Relative AC vs CFO tenure	- Larger fee reductions exist in the presence of more powerful CFOs, and smaller fee reductions in the presence of more powerful audit committees. - The CFO or the audit committee primarily influences fees when their counterpart is less powerful.	3.1.2.2.
Why do firms seek shareholders ratification of the independent audit function? The case of foreign cross-listed companies in the United States	Tanyi, Cathey	2020	IJA	US, 2010-2014, public	Archival	1,148 firm-years	Seeking ratification	Company characteristics	- Bank financing, the location of the cross-listed firm's independent auditor (US-based vs. non-US-based audit office), and non-audit fee ratio have the highest marginal effects on the probability of companies requiring their shareholders to ratify the auditor's appointment.	3.3.2.
Why some companies seek shareholder ratification on auditor selection	Krishnan, Ye	2005	AH	US, 2011, public	Archival	383 companies	Seeking ratification	AC characteristics	- Companies are more likely to seek shareholder ratification when they are larger, have more financial expertise on their audit committee, have a Big 4 auditor, purchase more non-audit services, are audited by the same auditor for longer periods, and when shareholder satisfaction with the board is higher.	3.1.2.1.; 3.3.2.

Notes:

1) Accounting Horizons (AH); Accounting, Auditing & Accountability Journal (AAAJ); Accounting, Organizations and Society (AOS); Advances in Accounting (AA); Auditing: A Journal of Practice and Theory (AJPT); Behavioral Research in Accounting (BRIA); Contemporary Accounting Research (CAR); European Accounting Review (EAR); International Journal of Auditing (IJA); Journal of Accounting and Economics (JAE); Journal of Accounting and Public Policy (JAPP); Journal of Accounting Research (JAR); Journal of Accounting, Auditing and Finance (JAAF); Journal of Business, Finance & Accounting (JBFA); Managerial Auditing Journal (MAJ); Review of Accounting Studies (RAS); The Accounting Review (TAR); The International Journal of Accounting (TIJA).

2) The setting refers to the country of origin of the dataset. If specified in the study, this column also refers to whether the sample focuses on public, private, or governmental audits. If not specified in the study, or the study is an experiment, we do not report the detailed setting. This column also indicates the study's time period (if reported).

3) Section refers to the related in-text paragraph to locate studies within the research synthesis.

APPENDIX B: CHAPTERS 3 AND 4

APPENDIX B1

Interview Scripts

Interview script auditors

Main question: *Could you walk us through the process of becoming the auditor of a new client, from the starting point of this process all the way until your appointment? We are interested in key events, key people, and key decisions. What do you consider the starting point of this process? And then guide us from that point through to the appointment until the eventual relationship with the client.*

- **Topic 1:** Could you discuss the key events you engaged in after learning about the RFP?
- **Topic 2:** After the tender process is initiated, clients, of course, eventually have to evaluate the proposal that you sent. In your experience, what are the most important criteria that clients consider when selecting a new auditor (in the context of mandatory rotation)? Was this client typical in this respect, or was this a somewhat "special case"?
- **Topic 3:** Could you elaborate on the preparation of the audit proposal and how you present yourself to the client?
- **Topic 4:** Could you provide a little more detail on who the key people are from the initial selection to eventually the AGM/selection?
- **Topic 5:** Can you describe the transition from your client's incumbent auditor to you and tell us something about your relationship with the client?
- **Topic 6:** How do you feel about mandatory rotation?

Interview script clients

Main question: *Could you walk us through the process of selecting a new auditor from the starting point of this process all the way until the new auditor is appointed? We are interested in key events, key people, and key decisions. What do you consider the starting point of this process? And then guide us from that point through to the auditor appointment until the eventual relationship.*

- **Topic 1:** Could you elaborate on the RFP process?
- **Topic 2:** After the tender process is initiated, you, of course, eventually have to evaluate the proposals that you received. Can you tell us how you evaluate such proposals?
- **Topic 3:** Could you provide a little more detail on who the key people are from the initial selection to eventually the AGM/selection?
- **Topic 4:** Can you describe the transition from your old to your current auditor and tell us something about your relationship with your current auditor?
- **Topic 5:** What do you think about being mandated to rotate audit firms?

APPENDIX B2

Request for Participation and Research Project Summary

The Auditor Selection Process: from Tender to Relationship Management
Dear [*contact*],

We are writing you regarding the scientific project "The Auditor Selection Process: from Tender to Relationship Management".

The aim of the current project is to obtain a better understanding of the complex process of selecting a new auditor, a process that is essential in preserving auditor independence and ensuring audit quality. To this end, this project investigates companies that recently went through a process of mandatory audit firm rotation, or that will have to go through this process in the near future. We will study not only the company's process, but also perspectives from the incumbent auditor, bidding auditors, and the new auditor. **We kindly invite you to participate in our research project.**

Collaboration on this project would entail your company's sharing of specified documents (for example, audit tender requests for proposal) and participating in a limited number of individual interviews with key personnel involved in the auditor selection process (for example, the CFO or audit committee members).

The results of this project will enhance our scientific understanding of the auditor selection process, but will also be of direct interest and benefit to your company because they will provide insights to help you evaluate your approach and enable you to better manage this process. Assessing and improving the auditor selection process is increasingly important as you will be changing auditors more frequently than in the past.

This research project is sponsored by the Foundation for Auditing Research. The Dutch Foundation for Auditing Research (FAR) aims to enhance the knowledge of what makes a good audit today and to continuously improve audit practices. The FAR conducts its research projects through a unique collaboration between science and practice, sustainably strengthening the learning curve of audit professionals and stakeholders in the auditing field. Attached to this invitation letter, you will also find a letter of support for this research project signed by all major Dutch audit firms, including your current and former auditor.

To confirm your collaboration on this project and to discuss practical arrangements, **please contact the lead supervisor of the project, prof. dr. Kris Hardies, at [Phone number] or kris.hardies@uantwerpen.be**. Please also do not hesitate to contact us if you would have any questions regarding the research project. We like to sincerely thank you in advance for your time and cooperation.

Jonas Vandennieuwenhuysen – University of Antwerp
Prof. dr. Kris Hardies – University of Antwerp
Prof. dr. Marcel van Rinsum – RSM Erasmus University
Prof. dr. Kris Hoang – University of Alabama
Prof. dr. Marie-Laure Vandenhaute – Vrije Universiteit Brussel

APPENDIX B3

Consent Form

Part intended for the participant

I, the undersigned (*name and surname*) __________________ hereby confirm that I have been informed about the content of the study and have received a copy of the information sheet for participants and the consent form. I have read and understood the information. The researcher of the study has provided me with sufficient information with regard to the conditions and duration of the study and its possible effects. Moreover, I was given sufficient time to consider the information and to ask questions, to which I have received adequate answers.

- I have fully understood that I can discontinue my participation in this study at any given time after having informed the executing researcher, without this having any disadvantages.
- I am aware of the goal for which the data provided by me will be collected, processed and used within the framework of this study and that they will be treated in a confidential manner.
- I agree to the collection, processing and use of these data, as described in the information sheet for the participant. Furthermore, I agree to the transfer and processing of these data in other countries than Belgium.
- I understand that I have the right at all times to view my personal data free of charge and to have any incorrect and/or incomplete personal data relating to myself corrected at any time free of charge.
- I voluntarily agree to participate in this study.

Date: ____________________

Signature participant:______________________________

I, the undersigned (*name and surname*) __________________ hereby confirm that I have been informed about the recording of this interview.

- I understand that this recording will solely be used within the scope of the current research project, as described in the information sheet for the participant.
- I understand that this recording will not be shared with any third party
- I understand that this recording will be securely stored for a period of 10 years, after which it will be destroyed.
- I understand that I have the right to listen to my interview and to ask for changes to be made.
- I voluntarily agree to the recording of my interview

1.

Date: ____________________

Signature participant:______________________________

Part intended for the researcher performing the study:

I, the undersigned (*name and surname*)__________________ hereby confirm that I have discussed the procedures as described in the information form with ______________________, during which I have explicitly indicated the possible risks or harms linked to the study. I have explicitly asked whether any ambiguities or questions remained and have answered these to the best of my abilities. Furthermore, I confirm that __________________ has given permission to participate in the study.

Date: ____________________

Signature researcher(s): _____________________________
Contact information: ____________________________________

Signature head of research group: ___________________________
Contact information: kris.hardies@uantwerpen.be – [Phone number]

APPENDIX B4

Support Letter Foundation for Auditing Research

FOUNDATION FOR AUDITING RESEARCH

Participation in Research Project
The Auditor Selection Process: from Tender to Relationship Management

Breukelen, 15 October 2021

We are writing to you regarding the scientific project "The Auditor Selection Process: from Tender to Relationship Management", conducted under the supervision of prof. dr. Kris Hardies from the University of Antwerp, and sponsored by the Foundation for Auditing Research (FAR).

We thank you for collaborating with the researchers of this project to allow for the successful execution of the research. With this letter, FAR confirms that we fully support the execution of this research project and that all nine FAR affiliated audit firms (being Deloitte, EY, KPMG, PwC, BDO, Mazars, Grant Thornton, Bakertilly, and Flynth) have agreed and committed to participate in the research project and related data gathering. To this end, FAR agrees that all relevant research information and documents originating from the aforementioned nine FAR affiliated audit firms (including their firms' proposals and related documents that were part of the audit tender process that is the subject of the current research project) is shared by you with the researchers involved (and with the researchers involved only).

All such data can still only be shared with the researchers involved (and only via the "Digital Vault" facility) and will be processed in accordance with the non-disclosure and data processing requirements that are part of the agreement between the researchers and the Foundation for Auditing Research. The FAR affiliated audit firms, this way, will still not gain access to the other firms' tender documents, not know which other firms were involved in the tender process.

Kind regards,
i/o

Prof. dr. H.M. Prast
Chair of the FAR board

APPENDIX B5

Member-Checking Mail

Dear [participant name],

Some time ago, you participated in our research study on the auditor selection process. This project has been a fun and fascinating undertaking – thank you for your participation and your invaluable insights. We hope that the attached manuscript respectfully conveys both the majority and minority views of our collective participants, who are interviewees from eight auditor selection process cases.

We have completed a draft of the manuscript, which we have attached for your review. This manuscript encompasses the third and fourth chapters of my Ph.D. dissertation, hence the naming of the chapters. As indicated in our interview, we are offering interviewees the option of providing:

- General feedback
- Specific comments
- Suggested edits
- Suggested additional important points we may have missed

We also promised you the possibility to check your quotes. Therefore, you can find your quotes indicated with your respondent number, which is [participant code]. Please let us know if we misinterpreted anything.

In addition, should you feel we have any additional inaccuracies, please let us know. It is very important to us that the sentiments in the manuscript are accurate and, therefore, trustworthy. You are welcome to provide written feedback (bullet points in an email, scanned marked-up print-out, PDF with comments, etc.) or schedule a meeting with us to discuss your feedback over Zoom or Teams.

Importantly, if you would like your comments considered for inclusion in this manuscript revision, kindly send your comments back (or schedule a call before) no later than [date]. However, we will accept comments after this date to consider for a subsequent revision. Please note that this manuscript version is not final. Changes will occur based on collective interviewee feedback, the academic review and discussion process, and any additional data obtained after this revision.

We sincerely hope that you enjoy the manuscript. If you'd prefer, you can save time by reading just Chapter 3, Section 5 on pages [xxx] to [xxx], and Chapter 4, Section 5 on pages [xxx] to [xxx], which report our findings and analysis of the interview transcripts. If that's still too long, we'd love for you to pick a few section headings within those sections that interest you most and read/comment on those.

Sincerely,

Jonas Vandennieuwenhuysen

On behalf of our research team: Marie-Laure, Kris, Kris, and Marcel