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## The Impact of the Sarbanes-Oxley Act on Clients' Audit Opinion Shopping Behavior\*

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**ABSTRACT:** This study investigates whether the tendency for audit clients to engage in opinion shopping becomes weaker after the enforcement of the Sarbanes-Oxley Act (SOX). While Lennox (2000) provides evidence that U.K. firms successfully engage in opinion shopping, there is limited evidence on the mitigating effect of SOX on opinion shopping. Using observations collected from the period before and after the enforcement of SOX (year 2001, 2004 and 2005), we find that, for our sample period, firms are likely to switch (retain) their incumbent auditors when the likelihood of receiving a going concern opinion is lower (higher) from a successor auditor, suggesting evidence of opinion shopping. More importantly, we find that firms are less likely to engage in opinion shopping after the enforcement of SOX. These findings suggest that more stringent legal and audit environment in the post-SOX period, at least partially, restricts firms' opportunistic behavior of shopping for a better audit opinion and enhances auditor independence. These findings provide valuable implications to regulators as well as academicians and practitioners.

**Keywords:** audit opinion shopping, Sarbanes-Oxley Act, auditor independence, going concern audit opinion.

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## I. Introduction

Regulators have expressed concerns over the "opinion shopping" behavior, a practice in which clients search for alternative auditors who are likely to issue a clean opinion when the clients and their incumbent auditors have disagreements about the appropriate audit opinions. In this study, we examine whether the Sarbanes-Oxley Act (hereafter, SOX) affects a firm's opinion shopping behavior, by adopting Lennox's (2000) innovative methodology that identifies the tendency of clients' audit opinion shopping.<sup>1)</sup>

Clients may switch auditors or threaten their incumbent auditors to switch auditors to avoid receiving unfavorable audit opinions (Carcello and Neal 2000, 2003). When clients dismiss uncooperative auditors and subsequently hire new auditors who are willing to issue a clean audit opinion, it could lead to impaired auditor independence (Krishnan and Stephens 1995; Teoh 1992). Therefore, opinion shopping behavior of clients has long been of concern to regulators worldwide. For example, SOX mandated the Government Accounting Office (GAO) to develop mechanisms to strengthen auditors' resistance to opinion shopping threats in the U.S. In a similar vein, European Commission (2010) and Institute of Chartered Accountants in England and Wales (2002) discuss possible introduction of mandatory auditor rotation to prevent opinion shopping and improve auditor independence. Choi et al. (2015) also note a number of cases from other countries in which regulators express concerns over the negative consequences of opinion shopping.

However, the prevalence of opinion shopping and its effect are not conclusive in prior studies. Although a few studies find that some auditor switches appear to be related to opinion shopping (Archambeault and DeZoort 2001; Smith 1986), other early studies in general fail to find evidence on the successful opinion shopping (i.e., receiving a more favorable audit opinion) (Chow and Rice 1982; Krishnan 1994; Krishnan and Stephens 1995). These studies find that "post-switch audit opinions are not more favorable than pre-switch audit opinions" (Choi et al.

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1) Securities and Exchange Commission (SEC, 1988) formally defines opinion shopping as 'the search for an auditor willing to support a proposed accounting treatment designed to help a company achieve its reporting objectives even though that treatment might frustrate reliable reporting.' Thus, SEC's (1988) view on opinion shopping is broader than the one used in this study. Following Lennox (2000) and Choi et al. (2015), this study focuses on a more narrow definition of opinion shopping which is related to audit opinion.