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An International Comparison of Audit Time-Budget Pressures: The United States and New Zealand

By Ellen Cook
Timothy Kelly

Competitive bidding for audit services has become a major problem in the United States. Under the competitive bidding system, clients obtain bids from different accounting firms to “shop around” for the most cost-effective combination of price, timeliness, and quality suited to their needs. Due to the extremely competitive nature of this system and the perception of many clients that an audit opinion is a homogeneous commodity, firms are often forced to distinguish themselves by offering their services at lower prices. [Hermanson et al; Simon F. Francis]. This reduction of prices is likely to lead to less time budgeted for audits. The resulting increase in time-budget pressure and stress felt by auditors may affect the quality of audit work being performed.

Over several years, studies have been done in the United States indicating that audit time-budget pressures are increasing and that these pressures lead to reduced audit quality and underreported chargeable time on the part of auditors.

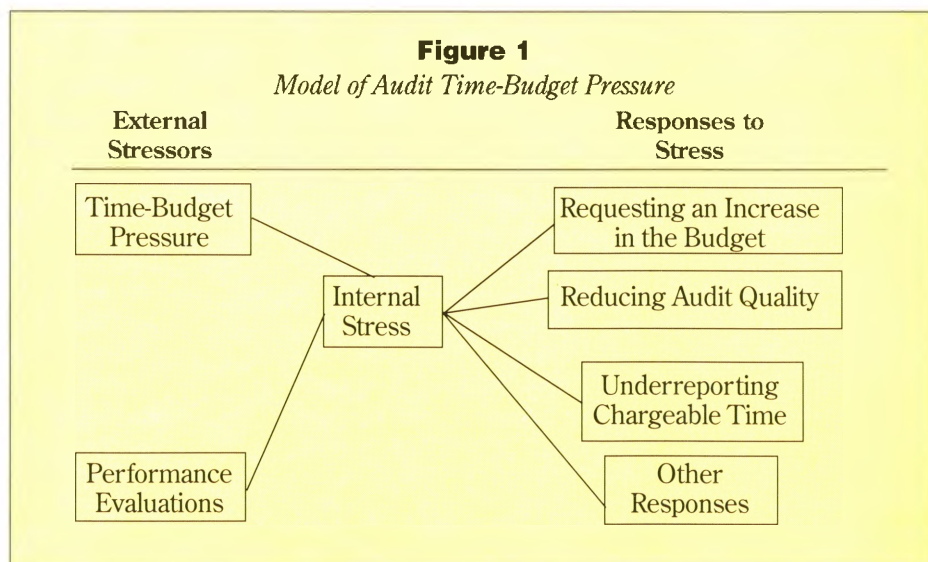
Since no international comparison on this topic has been done, a study of United States and New Zealand auditors was performed in order to compare the extent of time-budget pressures and auditor responses to time-budget pressures. Auditors from both countries were surveyed regarding:

- (1) The causes and extent of time-budget pressures in public accounting,
- (2) The optimal level of time-budget pressure (the desirable level of difficulty),
- (3) The importance of attaining time budgets for performance evaluations,
- (4) The auditors’ behavioral responses to an overly tight time budget (e.g., reducing audit quality), and
- (5) Suggested solutions to the problem of time-budget pressures.

Questionnaires were mailed out to 240 auditors in New Zealand and 120 auditors in the United States (San Diego area). Most auditors receiving questionnaires were from the then “Big Eight” international accounting firms with some questionnaires also being sent to large national and regional firms. The total New Zealand responses were 123 (51% response rate), while 73 United States responses (61% response rate) were obtained. While the U.S. respon-

dents were all from San Diego, the levels of reported underreporting and reductions in audit quality are similar to previous surveys of U.S. auditors. [Lightner et al; Rhode; Kelly & Seiler].

The results of this study indicate that time-budget pressures are as much a problem in New Zealand as in the United States. Many auditors in both countries “at



least occasionally” respond to unattainable budgets by underreporting chargeable time or by reducing audit quality. In addition, the results suggest that audit time budgets tend to be more realistically set in New Zealand than the United States and that auditors in New Zealand find that meeting the time budget is a more important part of their performance evaluations than auditors in the United States.

Model of Audit Time-Budget Pressure

Figure 1 illustrates the suggested relationship between the external stressors (time-budget pressure and performance evaluations) and the internal stress experienced by the auditor. In situations in which auditors are faced with an overly-tight time budget and when attaining the budget is an important part of the auditor’s performance evaluation, we would expect the auditor to experience considerable stress. This stress influences auditors to respond in ways that increase the auditor’s chances of completing his or her work within the specified time budget and that are expected to lead to a favorable performance review. Auditors may take positive approaches in dealing with this stress (e.g. requesting an increase in the budget) or they may take unprofessional approaches such as reducing audit quality or underreporting chargeable time.

Stress influences auditors to respond in ways that increase the auditor’s chances of completing his or her work within the specified time budget and that are expected to lead to a favorable performance review.

In the sections that follow, the causes and extent of time-budget pressures are examined along with the problems associated with over-emphasis on time-budget attainment in performance evaluations. In addition, auditor responses to time-

Table 1
Perceived Extent of Time-Budget Pressures

Percent of Time Budgets Which were	New Zealand		United States	
	Partners and Managers	Seniors and Staff	Partners and Managers	Seniors and Staff
Very tight, practically unattainable	11%	15%	22%	36%
Attainable with considerable effort	44	34	38	34
Attainable with reasonable effort	37	41	35	25
Very easy to attain	8	10	5	5
	100%	100%	100%	100%
Number of respondents	(n=68)	(n=55)	(n=18)	(n=50)

budget pressures (e.g. by underreporting chargeable time and by reducing audit quality) are examined. Finally, potential solutions to the problems associated with time budget pressures suggested by U.S. and New Zealand auditors are presented.

Causes of Time-Budget Pressures

Respondents were asked, in an open-ended question, to specify the causes of time-budget pressures. The causes most frequently cited by both New Zealand and United States auditors include:

- (1) Fee pressures (competition) — New Zealand 50.4%, U.S. 42.5% (includes responses citing the onset of competitive bidding in New Zealand).
- (2) Unrealistic budget due to poor planning — New Zealand 26.8%, U.S. 38.4%.
- (3) Unexpected problems encountered on the audit (e.g., poor records, poor client cooperation) — New Zealand 14.6%, U.S. 8.2%.

In addition to the above causes, about 10% of the responding New Zealand auditors (especially partners

and managers) cited overseas or “headquarters/branch” problems as a cause of time-budget pressures. Fee pressures, though often mentioned by respondents, do not directly cause time-budget pressures. Rather, accounting firms are translating lower fees, brought on by increasing competition, into smaller time-budgets without sufficiently reducing the extent of audit field work performed.

Extent of Time-Budget Pressure

To measure the extent of time-budget pressure in New Zealand and the United States, auditors were asked to classify the audits worked on in their present job positions by degree of difficulty in meeting the time budget. The responses to this question are shown in Table 1.

The New Zealand respondents reported fewer budgets being “very tight, practically unattainable” when compared with the United States respondents. In fact, United States auditors were over twice as likely as New Zealand auditors to say that budgets were practically unattainable.

While some pressure may be necessary to motivate auditors to work in an efficient manner, the results in Table 1 are troubling, especially in the United States. Over half of the respondents described their audit budgets as being either "very tight, practically unattainable" or "attainable with considerable effort."

Optimal Time-Budget Pressure

In another question, auditors were asked to characterize the "optimal" time budget using the same four categories as in Table 1. It is interesting to note that 83% of the New Zealand respondents and 65% of the United States respondents reported that the *optimal* time budget should be "attainable with reasonable effort." This is a stark contrast to the reported difficulty of meeting *actual* time budgets where over half required "considerable effort" or were "practically attainable."

While most respondents in both countries believed that the optimal audit time budget should be "attainable with reasonable effort," the question of how to define "reasonable

effort" remains to clarify the respondents' beliefs as to the meaning of the term "reasonable effort, respondents were asked to respond to the following question: "Time budgets should be established so that auditors with average ability should be able to attain the budget what percentage of the time?"

Over half of the respondents described their audit budgets as being either "very tight, practically unattainable" or "attainable with considerable effort."

As can be seen in Table 2, most respondents believed that audit time budgets should be set up so that they are attainable more than 75% of the time by the average auditor. A fairly large group of respondents believed that audit time budgets should be set up so that they are attainable between 50% and 75% of the time. Thus, the results in Table 2 clarify that

respondents believed that the term "reasonable effort" meant "able to be completed by the average auditor more often than not." The actual time-budget pressure experienced by auditors, as reported in Table 1, is far greater than the optimal situation described in Table 2.

Time Budgets and Performance Evaluations

Prior U.S.-based research has shown that attaining the audit time budget is an important component of employee performance evaluations. [same as old 3] In the current study, auditors were asked, "How much do you think the attainment of time budgets actually enters into the performance evaluation of your work?" Table 3 summarizes the results.

In New Zealand, 85% of partners and managers reported that attaining time budgets is "very important" or is of "considerable importance" in the performance evaluations of their work. On the other hand, only 68% of the United States partners and managers held this same opinion. At the senior and staff levels, 68% in New Zealand and 50% in the United States agreed that attaining audit time budgets was of major importance as part of their performance evaluations.

Thus, while United States auditors face *more demanding* time-budgets than New Zealand auditors, attaining audit time-budgets is perceived as a less important part of U.S. auditor's performance evaluations (especially by seniors and staff). Since over one-third of the time-budgets faced by United States seniors and staff were reported to be "practically attainable", it would be logical to see a reduction of the importance of time-budget attainment as a component of performance evaluations. Perhaps it is because New Zealand auditors are less frequently faced with *unreasonable* budgets, that attaining the budget can be a more important part of their performance evaluations.

Responses to Time-Budget and Performance Evaluation Pressures

Prior research has indicated that auditors sometimes respond to time-budget pressures by underreporting chargeable time or by reducing the

Table 2
Optimal Level of Difficulty of Audit Time Budgets

Percent of Auditors who Believe that Time Budgets Should Be Attainable:	New Zealand		United States	
	Partners and Managers	Seniors and Staff	Partners and Managers	Seniors and Staff
Less than 25% of the time	3%	0%	10%	2%
25-50% of the time	9	7	16	15
50-75% of the time	29	47	37	28
More than 75% of the time	59	46	37	55
	100%	100%	100%	100%
Number of respondents	(n=68)	(n=54)	(n=19)	(n=53)

Table 3
*Perceived Importance of Attaining Time-Budgets
 for Performance Evaluations*

	New Zealand		United States	
	Partners and Managers	Seniors and Staff	Partners and Managers	Seniors and Staff
Very important consideration	13%	9%	5%	7%
Considerable importance	71	59	63	43
Somewhat important	16	26	27	46
Not very important	0	6	5	4
	100%	100%	100%	100%
Number of respondents	(n=68)	(n=54)	(n=19)	(n=53)

quality of their work (e.g. by making overly-quick reviews of invoices). In this study, auditors were asked about their past responses to a budget that was so tight that it was unattainable. The responses to this question are summarized in Table 4.

Though time-budget pressures are very prevalent in public accounting, the results of the survey indicate that in both countries many auditors respond to these pressures in a highly professional manner. Over 90% of all respondents indicated that they "at least occasionally" respond to an overly tight budget by "working harder and charging all time properly." In addition, over 75% of the partners and managers and over 40% of the seniors and staff from both countries "at least occasionally" respond to an overly tight budget by "requesting and obtaining an increase in the budget."

Unfortunately, the results in Table 4 also confirm prior research studies which indicated that auditors often act in unprofessional manners in response to time-budget and performance evaluation pressures. Only the first two responses shown in Table 4 can be considered desirable behaviors. The other responses can result in reducing morale, jeopardiz-

ing the integrity of the audit, and obscuring the actual time required to accomplish the audit, resulting in inaccurate information and poor planning of future audits.

In general, compared with partners and managers, more auditors at the senior and staff levels in both countries "at least occasionally" reduce audit quality or underreport chargeable time, perhaps because they less frequently request budget increases. Further, New Zealand auditors are more likely than United States auditors to "at least occasionally" engage in desirable behaviors. Underreporting is especially a problem with New Zealand staff auditors, as over 50% of these auditors "at least occasionally" underreport chargeable time. More alarmingly, over 30% of all New Zealand respondents and over 20% of all United States respondents indicated that they "at least occasionally" reduced the quality of their work in order to meet an overly-tight time budget. Public accounting firms will need to take actions to maintain audit quality in order to avoid increased litigation and loss of prestige for the profession.

While the audit quality problem is obviously more important than

underreporting, the amount of underreporting is far from trivial. Auditors in the study were asked how many hours they personally underreport in a normal month. In addition, they were asked to estimate the percentage of partners, managers, seniors, and staff auditors who underreport at least three chargeable hours in a normal month. The results generally indicate that auditors underestimate the extent of underreporting in the profession. For example, 58% of the responding New Zealand staff auditors replied that they underreport three hours or more in a normal month. However, New Zealand partners and managers estimated that only 21% of staff auditors underreport three or more hours in a normal month.

The extent of underreporting was somewhat lower at all levels in the United States. For example, 50% of the responding United States staff auditors replied that they underreport three hours or more in a normal month. United States partners and managers underestimated the extent of staff auditor underreporting and believed that only 30% of staff auditors underreport three hours or more in a normal month.

In both the United States and New Zealand, senior and staff auditors more correctly estimated the extent of underreporting (by all job levels) than did the partners and managers. Clearly, partners and managers need to be made aware of the actual extent of underreporting in the profession.

Underreported hours (perhaps as much as 5% of all hours worked) represent hours that cannot be billed to the client, and will therefore not be considered in planning future audits, thus resulting in unrealistic future bids. More importantly, if inadequate time budgets are perpetuated, the temptation to reduce audit quality remains, with potentially disastrous consequences for the public accounting firm involved and for the profession as a whole.

Suggested Solutions

The first step in finding the solution to a problem is recognizing that a problem exists. This study confirms that problems with time-budget pressures exist in both the United States and New Zealand.

When respondents were asked the

extent of underreporting among their peers, they vastly underestimated the time actually underreported. Approximately 50% of the respondents in both countries and at all levels underreport three or more hours in a normal month. However, the auditors in this study perceived that underreporting is much less extensive. In particular, many partners and managers did not recognize that a problem exists.

Clearly, public accounting firms will need to take action to reduce time-budget pressures.

Although respondents were not asked about their perception of the extent of auditors reducing audit quality to meet difficult time budgets, it is quite possible that partners and managers would also underestimate the extent to which audit quality is being reduced by staff auditors to meet time budgets. Despite a firm's best efforts, such quality reduction acts often cannot be detected by a review process.

Once it is recognized that time-budget pressures pose significant problems, one step toward a solution would be encouraging staff to ask for budget increases when it becomes evident that the audit cannot be carried out effectively under the existing budget. Less than 50% of responding senior and staff "at least occasionally" used this option. This suggests that many senior and staff auditors perceive asking for a time-budget increase as a personally risky strategy.

Some additional solutions suggested by New Zealand and United States auditors are shown in Table 5. Suggestions such as improving communication with clients, involving more job levels in the budgeting process, and decoupling time budgets from fees were made by auditors from both countries. New Zealand respondents suggested peer review which has already been instituted in the United States, though it is yet too early to assess its effect on audit quality. The suggestion of price collusion, offered by a few, would

Table 4
Auditors Behavioral Responses to Overly Tight Budgets

Method of response to an overly tight budget	Percent of auditors who at least "occasionally" respond in the indicated manners			
	New Zealand		United States	
	Partners and Managers	Seniors and Staff	Partners and Managers	Seniors and Staff
Worked harder but charged all time properly	91%	90%	95%	91%
Requested and obtained an increase in the budget	78	43	89	42
Underreported chargeable time by performing work on personal time	38	52	22	38
Reduced the quality of work to meet the budget	30	33	21	22
Shifted chargeable time to nonchargeable categories on time report	15	31	16	29
Charged time to other jobs	9	10	0	6
Charged time to other audit areas on the same audit	24	28	43	43
Number of respondents	(n=68)	(n=54)	(n=19)	(n=52)

violate laws in both countries, however efforts can be made through the AICPA to educate the public on the true costs of effective auditing. Equally to the point would be for firms to completely avoid predatory pricing and the fierce price competition it breeds. Firms can work to differentiate themselves based on value, quality, and service, rather than price. However, if lower fees become the norm, firms may need to accept lower billing rates rather than creating unrealistic budgets based on existing billing rates.

It is interesting to note that partners and managers proposed a restructuring of the industry and a segregation of non-audit services. It was at the senior and staff level that solutions involving better planning were proposed. However, the need for better communication with the client and the need to set realistic budgets was articulated at every level. Of course, efforts to reduce costs through use of computer technology and other efficiencies continue to be of great importance.

Conclusion

It is notable that in a profession already known for its pressure, the increased use of competitive bidding in the United States and New Zealand has increased that pressure with respect to time budgets for audits. Clearly, public accounting firms will need to take action to reduce time-budget pressures if attaining the time budget continues to be an important part of performance evaluations. This study links time-budget pressures to reduced audit quality, which if left unchecked, will damage the professional reputation of CPAs. In addition, the study links time-budget pressures to underreporting of chargeable time.

Many of the respondents' suggestions for resolving time-budget pressures can and should be implemented, such as involving auditors from various levels in the budgeting process, communicating more effectively with the client as to audit procedures and requirements, and decoupling audit budget hours from audit fees.

It is important that the accounting profession study problems associated with time-budget pressures and begin to implement solutions. Underreporting has been shown in prior research to lead to auditor job dissatisfaction and turnover, as well as to potentially inadequate billings. In addition, time-budget pressure has been shown to be associated with reduced audit quality in both this and prior studies. Reduced audit quality is a major problem being faced in both the United States and New Zealand which must continue to be addressed by both practicing auditors and researchers.

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Table 5
Suggested Solutions to Time-Budget Pressures

Proposed Solution	Percentage Mentioning This Item	Sample Quotations
Better planning & procedures	19%	"Involve staff at lower level in setting of budget."
Set realistic budgets (fees)	19%	"Budgets must be realistically set and fee recoveries determined before the job commences. No way can the job suffer and standards be allowed to fall."
Better communication with client cost to do the job."	11%	"It's important that the client know what it actually
Change relationship between fee and time budget	9%	"Fees billed should be a reflection of hours taken (efficiently) rather than hours worked being a reflection of fees recoverable." "Decouple the time budget from fees."
Structural changes be instituted	8%	"Institute peer review process on 3 year basis" (New Zealand comment). "Make it more difficult for clients to change auditors' (United States comment)
Profession unite for higher fees and better quality.	6%	"Good service for more money."
Segregate non-audit services	2%	"Negotiate separate fees for special work."

(n = 193)