

AUDITOR PROCESS ACCOUNTABILITY AND EPISTEMIC MOTIVATION: PRINCIPLES VERSUS RULES-BASED ACCOUNTING STANDARDS

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ABSTRACT

We examine how the nature of accounting standards—principles- versus rules-based— influences auditors’ perceptions of process accountability and their epistemic motivation. Using a between-subjects experiment with 104 auditors from a Big-4 audit firm, we find that principles-based accounting standards significantly increase auditors’ perceptions of process accountability when they examine both structured and unstructured accounting transactions. We confirm a mediation model in which greater process accountability caused by principles-based standards in turn increases auditors’ epistemic motivation – the desire to develop and maintain a rich and accurate understanding of the problem at hand (Kruglanski 1989). We also find that principles-based standards lead auditors to make judgments consistent with the economic substance of the transaction to a greater extent than rules-based standards. Principles-based standards increase auditors’ overall need for evidence and induce greater demand for both diagnostic and nondiagnostic evidence. Auditors are more confident of their judgments under rules-based standards than principles-based standards, even when they reach incorrect decisions. Finally, principles-based standards lead auditors to consider cues other than the provisions of the standard in reaching their decisions, and result in less consensus for structured transactions.

Keywords: principles-based standards, rules-based standards, process accountability, epistemic motivation, International Financial Reporting Standards (IFRS)

I. INTRODUCTION

There is considerable discussion recently on the relative costs and benefits of principles vs. rules-based accounting standards, particularly given the debate concerning whether to adopt International Financial Reporting Standards (IFRS) in the United States. We define principles- and rules-based accounting standards following the incremental perspective discussed by Nelson (2003). We therefore recognize that all standards aiming to operationalize the FASB's conceptual framework are considered to be based on broad principles. Nonetheless, the focus of the current study is the *incremental* effect on auditor behavior when standards include elaborate rules, bright-lines, implementation guidance and/or numeric thresholds as compared to general guidance based on broad principles (Nelson 2003).

Our research addresses a gap in the literature by examining how the nature of accounting standards influences auditors' cognition. We propose that principles-based standards induce qualitative changes in the auditor's judgment process. Specifically, we examine whether working with principles-based standards leads auditors to perceive themselves as subject to greater process accountability than rules-based standards, i.e., the expectation that a decision maker will be judged based on the quality of the process he or she used to arrive at a decision (Siegel-Jacobs and Yates 1996). We also propose that principles-based accounting standards may lead auditors to engage in more systematic and effortful information processing, to exhibit less overconfidence, and to reach more accurate judgments in evaluating economic substance over form of a transaction.

We address these issues in an experiment involving 104 auditors where we manipulate the accounting standards surrounding a lease transaction (rules-based or principles-based) and the underlying economic substance of the lease (structured or unstructured transaction). The findings indicate that principles-based accounting standards increase auditor perceptions of process accountability relative to rules-based standards. Principles-based accounting standards also increase auditors' epistemic motivation, which prior research (Van Kleef et al. 2004; Dreu and Carnevale 2003) has shown leads to more effortful, thorough and systematic information processing. We also find that process accountability fully mediates the effect of principles-based standards on auditors' epistemic motivation.

Additional results indicate principles-based standards increase auditors' perceived overall need for audit evidence and demand for diagnostic evidence relative to rules-based standards. However, principles-based standards also increase auditors' demand for nondiagnostic evidence. Auditors are, in general, more confident of their decisions when accounting standards are based on specific rules rather than on broad principles. We also look at a transaction that is structured to appear to be an operating lease but is actually a capital lease in economic substance. In this setting, auditors who make the correct accounting decision are equally confident, regardless of whether they work with rules- or principles-based standards; however, auditors who make incorrect decisions are significantly more confident if they work with rules-based accounting standards. Finally, auditors' justification memos indicate principles-based standards are more likely to lead auditors to expand their focus and consider cues other than provisions of the standard in making their decisions than do rules-based standards.

The remainder of this paper is divided into four sections. In the next section we provide a review of relevant research and develop the hypotheses. The following two sections contain a description of the method and presentation of the findings. The final section is devoted to a discussion of the major findings and their implications for practice and future research.

II. BACKGROUND AND HYPOTHESES

Principles- and Rules-Based Accounting Standards

Previous research has studied the effects of principles-based vs. rules-based accounting standards on various aspects of both preparer and auditor behavior. The precision provided by rules-based accounting standards has been examined as a possible constraint of aggressive reporting. Trompeter (1994) reports that when accounting standards provide less specific guidance, auditors tend to make more aggressive recommendations. Hackenbrack and Nelson (1996) provide evidence that vague accounting standards can lead auditors to allow aggressive reporting by their clients. Finally, Ng and Tan (2003) find that the availability of authoritative guidance enhances the auditor's negotiation position, and that this effect is moderated by the availability of an effective audit committee.

Although rules-based accounting standards can increase precision, they can also lead to financial engineering (SEC 2008). Under such standards, preparers can engage in highly structured transactions for purposes of meeting bright-line thresholds and achieve a desired accounting treatment. Rules-based standards have also been alleged to promote a "check-the-box" mentality and decrease the quality of financial reporting by not representing accurately the economic substance of events (Schipper 2003). Because principles-based standards allow room for professional judgment, they may increase the quality of financial reporting (Maines et

al. 2003). Ewert and Wagenhofer (2005) show that rules-based standards can increase rather than decrease both accounting and real earnings management. Further, rules-based standards can strengthen the negotiating position of managers who engage in aggressive reporting through structuring transactions in order to meet bright-line thresholds (Nelson 2003).

Recently regulators have expressed their support for principles-based accounting standards, voicing an opinion that such standards would permit focus on the economic substance of transactions (FASB 2002; SEC 2008). Support for the move toward more principles-based standards has also been expressed by audit firms (DiPiazza et al. January, 2008) and the accounting profession (AICPA 2007). Psaros and Trotman (2004) find that when financial statement preparers use a rules-based standard, incentives affect their judgments and they make more aggressive accounting decisions. Tsakumis et al. (2009) find that financial statement preparers are less likely to report aggressively under less precise, principles-based standards, and that less precise standards act as a substitute for audit committee strength in constraining aggressive reporting.

Concerns remain, however, that principles-based standards may invite auditors to support opportunistic reporting if this is aligned with their incentives, and that a move toward principles-based standards would pose high litigation risks and risks to audit quality (Bratton 2003). Regulators have stated that, although principles-based standards could increase the ability of financial reporting to capture the underlying economics of events, the fact that such standards contain less detailed implementation guidance may lead to less consistency by both preparers and auditors and could therefore make litigation or enforcement outcomes more difficult to predict (SEC 2008).

As emphasized by Nelson (2003), behavior can be influenced not only by economic incentives, but by incentives that induce accurate judgment such as requiring auditors to justify their decisions. It is important to study whether principles-based accounting standards provide such incentives by increasing process accountability, and to understand whether principles-based standards induce more systematic, effortful and accurate processing of information by auditors. Jamal and Tan (2008) show that principles-based standards would improve the quality of financial reports only if there is a matching shift in auditors' attitudes towards being more principles-oriented. As such, unanswered questions for empirical research are how, and to what extent, working with principles-based standards affects auditors' cognition, the focus of the current study.

Process Accountability

Process-accountable individuals expect that they will have to justify to evaluators their decision processes, regardless of the outcome of their decisions (Markman and Tetlock 2000; Libby et al. 2004). We focus specifically on auditor process accountability to an audience with unknown views (Lerner and Tetlock 1999), since auditing standards stress independence and auditors are accountable to multiple parties with potentially unknown or conflicting interests such as investors, management, the board, regulators, and the courts. The effects of process accountability on individual and group judgment have been studied extensively in psychology, primarily by Philip Tetlock and colleagues (e.g., Tetlock 1985; Tetlock and Kim 1987; Lerner and Tetlock 1999; Markman and Tetlock 2000).

Process accountability promotes multidimensional and integratively complex thinking (Tetlock et al. 1989). It increases cognitive effort and invokes thorough information processing

(Simonson and Staw 1992; Tetlock et al. 1989); decreases overconfidence (Tetlock and Kim 1987) and improves calibration (Siegel-Jacobs and Yates 1996). Process accountability has been shown to improve the accuracy of decisions and to decrease decision bias (Tetlock and Kim 1987; Mero and Motowidlo 1995; Siegel-Jacobs and Yates 1996). Under process accountability, individuals also show increased self-critical attention (Lerner and Tetlock 1999) and more carefully consider and encode all relevant information provided to them (Tetlock 1992). Process accountability leads negotiators to attend more to the information that is exchanged and to incorporate new information in their understanding of the task at hand (De Dreu et al. 2000).

In accounting, process accountability has been shown to decrease judgment biases (Kennedy 1993), to increase audit effort (Kennedy 1995), and to improve judgment accuracy (Ashton 1992). Tan and Kao (1999) find that task complexity and the auditors' level of knowledge interact with process accountability to affect audit performance. Lastly, Libby et al. (2004) find that under process accountability managers increase their use of unique, domain-specific measures in performance evaluations.

Because principles-based accounting standards provide general guidance, without detailed bright-line rules that determine how an accounting event should be treated and reported, auditors working with such standards are likely less constrained with respect to the process they use to arrive at a decision. We expect that when accounting standards are less specific and prescriptive about the necessary procedures, auditors will feel increased need to justify the process they have used to arrive at a specific audit decision as reflected in our first hypothesis.

H1 Auditors experience greater process accountability under principles-based standards than under rules-based accounting standards.

Epistemic Motivation

Epistemic motivation is defined in psychology as the desire to develop and maintain a rich and accurate understanding of the world (Kruglanski 1989; De Dreu et al. 2006). Dual-process theory in cognitive psychology suggests that the ways in which individuals process information can range from a quick, efficient, and effortless mode to a systematic, deliberate, and effortful manner (Chaiken and Trope 1999). Epistemic motivation causes individuals to engage in systematic, thoughtful, and thorough processing of information (Van Kleef et al. 2004; De Dreu and Carnevale 2003).

Epistemic motivation can be linked to individual dispositional traits such as high need for cognition (Petty and Cacioppo 1986) and low need for cognitive closure (Van Kleef et al. 2004), as well as to situational factors, like process accountability. Research in psychology has established that process accountability induces high levels of epistemic motivation (e.g., Scholten et al. 2007; De Dreu et al. 2006).

Because we expect that principles-based accounting standards will increase process accountability, we hypothesize that process accountability will thereby induce high levels of epistemic motivation in auditors. We propose a mediation model (Baron and Kenny 1986), in which process accountability mediates the effect of principles-based standards on epistemic motivation. The hypothesized mediation model is shown in Figure 1, panel A. Our hypotheses are as follows:

H2 Auditors experience greater epistemic motivation under principles-based standards than under rules-based standards.

H3 Process accountability mediates the effect of principles-based accounting standards on epistemic motivation.

[insert Figure 1, Panel A here.]

Need for Evidence

Previous research has shown that increased process accountability leads decision makers to examine a greater amount of information in their decision making (Tetlock and Boettger 1989). An increase in process accountability causes individuals to thoughtfully consider and encode all diagnostic evidence provided to them (Tetlock 1992; Libby et al. 2004). Further, because process accountability increases the need for self-justification, it is expected to increase the overall need for evidence. Previous research has shown that process accountability leads decision makers to increase the amount of evidence they rely on – whether the evidence is diagnostic (e.g., Libby et al. 2004) or nondiagnostic (e.g., Hackenbrack 1992; Glover 1997). Consistent with this, we expect that principles-based standards will increase auditors' need for audit evidence. It is important to note that examining more diagnostic audit evidence is expected to increase audit quality and the effectiveness of the audit. In contrast, however, if principles-based audit standards lead auditors to examine more nondiagnostic evidence, audit inefficiencies can result even if this nondiagnostic evidence does not in the end affect the auditor's decision. Moreover, if auditors let nondiagnostic evidence influence their judgments, they are likely to fall prey to the dilution effect documented by prior studies (Hackenbrack 1992; Glover 1997), and audit effectiveness could be compromised.

H4a Auditors experience a greater need for diagnostic audit evidence under principles-based standards than under rules-based standards.

H4b Auditors experience a greater need for nondiagnostic audit evidence under principles-based standards than under rules-based standards.

Audit Decision Performance

Process accountability leads decision makers to engage in deep information processing and develop an accurate and multifaceted understanding of decision problems (De Dreu 2007). If principles-based standards increase process accountability, and process accountability increases cognitive effort, we would expect auditors working with principles-based accounting standards to make more normatively correct decisions. Tan and Kao (1999) show that process accountability has no effect on performance for routine, straightforward audit tasks because such tasks do not strain cognition; however, process accountability improves performance for more complex audit tasks, when auditors possess the requisite knowledge and problem-solving abilities. We expect that principles-based accounting standards increase process accountability both when auditors face relatively straightforward, unstructured accounting transactions and when they face more complex or ambiguous situations that involve structured transactions. However, consistent with Tan and Kao (1999) we expect a difference in auditor performance under principles-based standards and rules-based standards only when auditors face a more ambiguous situation. As discussed, of greatest concern is a transaction that is structured under rules-based accounting to meet management's business objectives but in economic substance should be accounted for in a different manner. We posit that auditors using principles-based accounting will be more likely to determine the economic substance of the transaction under such a scenario than those using rules-based standards.

H5 Auditors will be more likely to make decisions consistent with the economic substance of the transaction under principles-based accounting standards than under rules-based accounting standards.

Decision Confidence

Research in psychology has found that process accountability leads decision makers to engage in preemptive self-criticism wherein they anticipate potential objections and counterarguments and, as an adaptive strategy, attempt to demonstrate awareness of potential flaws in their reasoning (Tetlock 1983). Because process accountability induces preemptive self-criticism, it may reduce decision makers' confidence in their decisions. Arkes et al. document reduced levels of confidence in participants exposed to process accountability than in a control group (Arkes et al. 1987). Tetlock and Kim (1987) and Siegel-Jacobs and Yates (1996) show that process accountability decreases overall confidence levels, and also leads to decreased overconfidence and improved calibration of individuals' judgment.¹ Consistent with psychology research on process accountability, we expect that principles-based standards would decrease auditors' overall confidence level in their decisions, and will decrease overconfidence in normatively incorrect decisions. Our hypotheses are as follows:

H6a Auditors are less confident in their decisions under principles-based standards than under rules-based standards.

H6b Auditors exhibit greater overconfidence under rules-based standards than under principles-based standards.

¹ Perfect calibration means that, in the long run, for all answers assigned a given probability, the proportion correct equals the probability assigned (e.g., if a perfectly calibrated person is 80% confident in predicting that it will rain every day, over the long run it will rain on 80% of all days).

III. METHOD

Overview and Design

In our experiment auditors from a Big 4 audit firm made a decision about the proper classification of a lease and the amount and type of further evidence needed. Further, they completed scales measuring process accountability and epistemic motivation. The experiment is a 2x2 design, with type of accounting standard (principles-based or rules-based) and economic substance of the transaction (structured or unstructured) manipulated between subjects.

Participants and Administration

A total of 104 participants (38 females and 66 males) from the US offices of a Big 4 audit firm participated in the experiment. Participants had a mean (median) level of experience of seven (four) years. We asked auditors to report whether they have worked with IFRS on audit engagements as a proxy for their exposure to principles-based standards. Forty-seven participants (45 percent) reported that they had worked with IFRS. Participants encountered the issue of accounting for leases an average of seven times during their careers, suggesting they possessed the requisite level of task specific experience. There were no significant demographic differences across experimental conditions (all $p > 0.27$). Demographic variables were also insignificant as covariates in all analyses.

The experiment was administered on the audit firm's premises during three training sessions conducted in the spring of 2009. There were no significant effects of the experimental session in any of the analyses. The study was introduced by an audit partner who expressed the firm's support for this research and requested diligent participation. Participants were asked to

use their professional judgment as they would on an actual audit engagement. Participants provided informed consent to participate in the study and then proceeded to work on the experimental task.

The task consisted of analyzing an audit situation in which the classification of a lease was in question (operating lease or capital lease). The experimental materials were pilot-tested with four audit partners who had expertise in lease accounting, and whose suggestions were incorporated in the final instruments. Participants read background information about a company located in country "X", which had entered into a significant lease transaction. To mitigate the possibility that participants would automatically revert to familiar rules-based U.S. accounting standards regarding leases, instructions emphasized that participants should determine the proper treatment of the company's accounting transactions in accordance with the accounting standards promulgated in the country in which the client operates, and that participants should ignore SFAS 13 and any previous accounting guidance they may have received in that area. The background narrative noted that due to a restrictive debt covenant that specifies a debt/equity ratio below a certain threshold, the company's management has incentives to record the lease as an operating lease and not a capital one.

After reading the applicable lease accounting standard (either rules-based or principles-based), participants were provided with information on the lease contract as well as background information on the company's historical treatment of leases. Participants arrived at a decision regarding the proper classification of the lease and determined the amount and type of further evidence they would like to receive. They also provided justification memos supporting their decisions and completed the process accountability and epistemic motivation

scales. Participants then filled out a post-experimental questionnaire and provided demographic information.

Independent Variables

Type of Accounting Standard

The type of accounting standard was manipulated at two levels: principles-based or rules-based. The precise wording of this manipulation is shown in Panel A of Exhibit 1. Participants in the principles-based condition read that the classification of leases adopted in the accounting standard was based on the extent to which risks and rewards incidental to ownership of a leased asset lie with the lessor or the lessee. The standard stipulated that a lease should be classified as a capital lease if it transferred substantially all the risks and rewards incidental to ownership and as an operating lease if it did not transfer substantially all the risks and rewards incidental to ownership.²

Participants in the rules-based condition read that if a lease meets one of three criteria, it should be recorded as a capital lease; otherwise it should be recorded as an operating lease. The criteria were: (1) the term of the lease is equal to or greater than 80% of the leased asset's useful life, (2) the present value of the lease payments is equal to or greater than 80% of the fair market value of the leased asset, and (3) at the end of the lease term, asset ownership is transferred to the lessee. The numeric thresholds for the rules-based condition were purposefully different from the numeric thresholds in SFAS 13 in order to discourage participants from automatically reverting to a US-GAAP mode of thinking. However, the use of

² We used wording from IAS 17 (Leases) as a basis for this manipulation.

numeric thresholds is consistent with the form of U.S. rules-based standards regarding leases.

Economic Substance of the Lease

The economic substance of the lease was manipulated at two levels – structured and unstructured nature of the lease transaction. The structured lease condition presented a lease that was highly engineered to appear as an operating lease but that had the economic substance and characteristics of a capital lease (see Panel B of Exhibit 1). The lease in the unstructured condition was designed to reflect the underlying economic substance of an operating lease and lacked any indicators of a capital lease transaction (Panel B of Exhibit 1). The manipulations were designed through pilot tests and consultations with four audit partners with expertise on leases.

Participants in the structured lease condition read that the net present value of the minimum lease payments, discounted using the incremental borrowing rate of the lessee, was \$836,000 while the current market value of the asset was \$1,050,000. The narrative also specified that the lease term was 37 years and the useful life of the asset was 50 years, indicating that in fact the lease was held for essentially the economic life of the asset. Thus, the lease term was for 74 percent of the asset's life and the net present value of the lease payments represented 79.6 percent of the fair market value of the asset – just below the 80 percent threshold specified by the rules-based accounting standard. Further, the narrative emphasized that the company would have the option to renew the lease at the end of the lease term, and that historically the company had been renewing all previous leases from this lessor at the end of their contracted terms.

Participants in the unstructured lease condition read that the net present value of the minimum lease payments, discounted using the incremental borrowing rate of the lessee, was \$630,900 while the current market value of the asset was \$1,050,000. The lease term was specified as 25 years and the useful life of the asset was 50 years. Finally, the narrative emphasized that historically the company has not been renewing any of the previous leases from this lessor at the end of their contracted terms. Collectively, these terms portrayed a transaction where the lessor used the asset for a period that is substantially less than its economic life and the value of the transaction was significantly less than the market value of the asset.

Pilot tests conducted with audit partners (n=4) revealed unanimous agreement that, given the economic substance of the transactions, the structured lease should be normatively categorized as a capital lease and the unstructured lease should be classified as an operating lease. Suggestions from the panel of partners were also incorporated in the case scenarios.

[insert Exhibit 1 here]

Dependent Variables

Process Accountability

Process accountability was measured on a 5-item scale developed for this study based on descriptions of process accountability manipulations used in previous research in psychology (Tetlock and Boettger 1989; Tetlock and Kim 1987; Markman and Tetlock 2000; Siegel-Jacobs and Yates 1996; Brtek and Motowidlo 2002). Participants were asked to assess the following with respect to the accounting standard: (a) to what extent are you free to determine the types

of information relevant to your decision (1=very little, 7=very much), (b) how difficult will it be to determine whether a piece of information is relevant to the lease decision (1=very difficult, 7=very easy), (c) every auditor will be examining the same types of information in making a decision regarding the lease (1=strongly disagree, 7=strongly agree), (d) I have discretion in deciding how much I want to weight various facts in reaching a decision (1=strongly disagree, 7=strongly agree), (e) to what extent will an auditor have to defend to others his application of this accounting standard (1=very little, 7=very much).

Items (b) and (c) were reverse-scored so that high scores in all five measures would reflect an increase in process accountability. Responses were averaged into one scale exhibiting high level reliability (Cronbach's alpha = 0.82).

Epistemic Motivation

Epistemic motivation was measured with a 3-item scale used in De Dreu et al. (1999). Participants rated the following items on 7-point Likert scales (1=strongly disagree, 7=strongly agree): To apply this accounting standard, (a) I had to think deeply before making a decision, (b) I was required to consider a large number of possible perspectives, (c) I had to make judgments and decisions as thoroughly as possible. Responses were averaged into one scale again with strong reliability as measured by Cronbach's alpha (0.87).

Audit Evidence

The need for audit evidence was measured with the question: To what extent do you feel you need additional evidence to help you in your decision about the lease classification (1=no need for additional evidence, 7=imperative need for additional evidence).

Participants were also presented with 32 evidence items (shown in Table 1) and were asked to mark any evidence items that they would need to examine in deciding how to record the lease. The evidence items were initially identified by the authors to include items diagnostic to the lease classification decision based on the accounting standards as well as nondiagnostic items. The respective diagnosticity or nondiagnosticity of the evidence items was then confirmed by four audit partners whose feedback was incorporated in the list of items.

The evidence contained eight items diagnostic to the lease classification decision (items 7, 10, 11, 14, 16, 24, 25, and 29) and twenty-four nondiagnostic items. The amount of evidence requested by participants was measured by the total number of items requested. We also measured the number of diagnostic and nondiagnostic items requested by participants.

[insert Table 1 here]

Audit Decision Performance

Audit decision performance was measured with participants' classification of the lease on a binary scale: either an operating or a capital lease. Participants were also instructed to provide a justification memo supporting their decision. Justification memos are common in audit practice, and asking participants to provide one increases the mundane realism of our experiment. We expected the justification memos to provide evidence on the breadth of cues considered by auditors and the focus of auditors' reasoning process when confronted with accounting standards that focus on broad principles or on specific rules, as well as the effort expended on the task.

Our exploratory analyses of the justification memos examined how the type of accounting standard affects auditors' focus on the standard itself versus additional evidence cues. Rules-

based standards may narrow the auditors' focus on the implementation guidance provided in the standard, perhaps to the exclusion of other diagnostic evidence cues that provide insight into the economic substance of the transaction. We expected to find that principles-based standards expand the auditor's focus to consider a greater breadth of evidence cues than rules-based standards.

Two independent coders, blind to the study's design and hypotheses, coded the number of times the justification memos discussed the accounting standard or cues other than the standard. The intraclass correlation coefficients (Shrout and Fleiss 1979) were 0.84 and 0.81, respectively, indicating good inter-rater reliability. The mean of the two coders' ratings was used in the analyses.³

We also measured the length of the justification memo (by the number of words contained in the memo) as a proxy for expended effort. In an additional exploratory analysis we expected that auditors in the principles-based condition would expend greater effort in justifying their conclusion and therefore their justification memos would be longer.

Decision Confidence

Participants' confidence in their lease classification decision was assessed on a 7-point Likert scale: How confident are you in your decision about how the lease should be classified (1=not at all confident, 7=very confident).

³ Results are qualitatively the same if either of the two coders' ratings is used in the analyses.

IV. RESULTS

Manipulation Checks

We tested the effectiveness of the accounting standard manipulation by comparing participants' ratings of two items on 7-point Likert scales: (a) the accounting standard was based on (1=detailed rules, 7=broad principles), (b) the accounting standard provided (1=specific guidance, 7=general guidance). Participants in the principles-based condition agreed more that the standard was based on broad principles (mean of 6.16) and that it provided general guidance (mean of 6.10) than participants in the rules-based condition (means of 2.60 and 2.60, respectively). T-tests revealed that the manipulation was successful (both p-values < 0.000, two-tailed). Five participants gave end-of-scale responses in the direction opposite of expectations; our results are unchanged if we exclude those participants from the analyses. We did not have a manipulation check for the economic substance of the lease, since it reflects specific differences in the nature of each transaction (e.g., length of the lease) and one of our dependent variables was participants' classification of the lease.⁴

Process Accountability

H1 proposed that auditors experience greater process accountability under principles-based standards than under rules-based standards. The means for each experimental condition are shown in Panel A of Table 2.

[insert Table 2 here].

An ANOVA (Table 2, Panel B) shows auditors perceive greater process accountability when they work with principles-based accounting standards (mean = 4.91) than when they work with

⁴ Other studies in which experimental manipulations were not checked under similar conditions and for analogous reasons include Gaynor et al. (2009) and Nelson (1993).

rules-based accounting standards (mean = 3.16, one-tailed p-value = 0.000) and therefore H1 is supported. This effect does not depend on the economic substance of the transaction (two-tailed p-value = 0.592). Process accountability is greater both for the more structured transaction possessing the characteristics of a capital lease and for the unstructured, more straightforward case with characteristics of an operating lease.

Epistemic Motivation

H2 proposed that epistemic motivation is greater under principles-based standards than under rules-based standards. Panel A of Table 3 shows descriptive statistics for epistemic motivation, and ANOVA results are displayed in Panel B. Auditors working with principles-based standards experience significantly higher epistemic motivation (mean = 4.88) than auditors working with rules-based standards (mean = 3.41, one-tailed p = 0.000), therefore H2 is supported.

[insert Table 3 here].

H3 proposed that process accountability mediates the effect of principles-based accounting standards on epistemic motivation; that is, principles-based standards increase process accountability and the increase in process accountability induces epistemic motivation in auditors. We test the mediation model by performing several regression analyses as discussed by Baron and Kenny (1986). Results from our analyses (not tabulated) indicate that: (1) principles-based accounting standards increase process accountability; (2) principles-based accounting standards increase epistemic motivation; (3) when both principles-based standards and process accountability are included as predictors of epistemic motivation, the effect of

process accountability is significant, but principles-based standards are no longer significant. Results from a Sobel test (Sobel 1982) indicate that the effect of principles-based standards on auditors' epistemic motivation is fully mediated by process accountability ($z = 3.23$, one-tailed $p = 0.001$), therefore H3 is supported. The confirmed mediation model is shown in Figure 1, panel B.

[insert Figure 1, Panel B here].

Audit Evidence

H4 proposed that auditors experience a greater need for evidence under principles-based standards than under rules-based standards. Descriptive statistics for the variable need for audit evidence are shown in Panel A of Table 4. Panel B indicates that auditors report a significantly greater need for audit evidence when they work with principles-based standards (mean = 5.16) than with rules-based standards (mean = 3.92, one-tailed $p = 0.000$).

[insert Table 4 here].

We also examine the amount and type of evidence that auditors indicate they need to examine in deciding how to classify the lease. Descriptive statistics for the total amount of additional evidence cues requested, as well as the number of diagnostic and nondiagnostic items, are shown in Table 5, Panel A. Panel B shows that auditors request a significantly greater amount of evidence under principles-based standards (mean = 6.63) than under rules-based standards (mean = 3.37, one-tailed $p = 0.000$).

Auditors working with principles-based standards request a greater amount of diagnostic evidence (mean = 4.31) than auditors working with rules-based standards (mean = 2.33, one-

tailed $p = 0.000$), therefore H4a is supported. However, principles-based standards also lead auditors to examine a greater amount of evidence that is nondiagnostic to the lease classification decision (mean = 2.35) than do rules-based standards (mean = 1.10, one-tailed $p = 0.016$), thereby supporting H4b.

[insert Table 5 here].

Audit Decision Performance

We examine classification decisions made by participants in the two conditions that are designed to reflect leases of different economic substance: a highly structured lease and an unstructured lease. Our a priori expectations and pilot tests indicated that, according to the economic substance of the transaction, the unstructured lease should normatively be classified as an operating lease and the structured lease as a capital lease.

Unstructured Lease Condition

Results for the unstructured lease condition are shown in Table 6, Panel A. When analyzing this relatively straightforward lease transaction, auditors in both the principles-based condition (24 out of 26) and the rules-based condition (25 out of 26) predominantly classified the lease as an operating one. Noteworthy, auditors working with principles-based standards do not appear more likely to make type I errors (i.e., incorrectly classify the transaction as a capital lease) than auditors working with rules-based standards (Fisher's Exact Test $p = 1.000$, two-tailed). This finding is contrary to the view expressed by some (cf. Bratton 2003) that IFRS may lead to improper conclusions since detailed guidance is not provided.

[insert Table 6 here].

Structured Lease Condition

Results for the structured lease transaction, where the economic substance of the transaction is a capital lease, are shown in Panel B of Table 6. Four auditors in this condition stated as their sole reason for classifying the lease as a capital lease that the net present value of lease payments calculation (79.6) percent rounds up to 80 percent, and therefore the net present value of lease payments criterion has been met because of rounding. Since these four participants classify the lease as capital *only* because they perceive that the 80 percent threshold has been met due to rounding, we exclude them from this analysis.⁵

Results shown in Table 6, Panel B reveal that auditors in the principles-based condition are significantly more likely to recognize the economic substance of the transaction and accordingly classify the structured lease as a capital lease than are auditors in the rules-based condition (Fisher's exact test $p = 0.049$, one-tailed). Auditors working with rules-based standards appear more likely to make a type II error because they ignore the economic substance of the transaction and focus on numeric thresholds instead.

We should note that our findings may understate the value of a principles-based standard with respect to decision performance superiority, since participants in both the rules- and the principles-based condition examined the same amount of evidence provided in the experimental case and had an opportunity to request, but not to examine, additional evidence. Given our finding that principles-based standards increase auditors' demand for audit evidence, it would be interesting to explore whether the additional evidence examined would lead to further improvements in auditors' decision performance.

⁵ Including these participants in the analysis does not change the direction of our results, but decreases their significance.

Finally, we observe that the variance in the classification decisions of auditors is greater under principles-based standards (0.26) than under rules-based standards (0.18, $F = 10.55$, $p=0.002$). Auditors therefore exhibit lower consensus using principles-based standards in this more ambiguous situation involving a structured accounting transaction.

Decision Confidence

Table 7 presents results for participants' level of confidence in lease classification decisions. Overall, auditors working with principles-based standards display a significantly lower level of confidence (mean = 5.13) than do those using rules-based standards (mean = 5.90, one-tailed $p = 0.000$), supporting H6a.

[insert Table 7 here].

The fact that auditors' overall level of confidence is higher under rules-based based standards than under principles-based standards is informative in itself with respect to an auditor justifying his or her decision in front of regulators, judges, or other reviewers. It is even more meaningful, however, to distinguish between auditors who reach correct decisions and those who reach incorrect decisions. We examine separately the level of confidence of participants who reach a correct decision about the lease classification and participants who reach an incorrect decision. Since auditors in both the principles-based and rules-based standards conditions exhibited a very high level of decision performance for the unstructured lease transaction, there are an insufficient number of incorrect conclusions to address this issue. However, results from untabulated analyses indicate that in the more ambiguous structured lease condition, participants who make a correct decision exhibit similar levels of confidence under principles-based standards (mean = 5.23) and rules-based standards (mean =

5.50, two-tailed p -value = 0.616). However, participants who make an *incorrect* decision are much more confident if they work with rules-based standards (mean = 5.94) than if they work with principles-based standard (mean = 4.69, one-tailed p -value = 0.005). This suggests that rules-based standards lead auditors to be overconfident in their decisions regarding more ambiguous situations that also involve higher misstatement risk. H6b is therefore supported in the structured lease subsample.

Justification Memo Analysis

We performed exploratory analyses on auditors' justification memos in order to evaluate the breadth of cues considered by participants as well as the effort expended on the task.

Results from untabulated analyses comparing the number of times auditors' justification memo discusses the accounting standard versus other cues reveal that participants in the rules-based condition appear to have a much more pervasive focus on the accounting standard, as measured by the number of times they discussed the standard (mean = 2.17) than participants in the principles-based condition (mean = 0.90, two-tailed p = 0.000). These results suggest that principles-based standards lead auditors to expand their focus to cues other than the standard and to consider evidence cues other than the ones specified in the standard (mean = 2.12) in contrast to rules-based standards (mean = 0.67, two-tailed p = 0.000). Taken together, these results are consistent with principles increasing the breadth of evidence considered in making an accounting decision.

Untabulated analyses also indicate that the length of the justification memo (a proxy for the effort expended in justifying one's decision) did not differ substantially between the principles-based (mean = 45 words) and the rules-based condition (mean = 43 words, two-tailed p =

0.663). Thus, contrary to our expectations, we did not find that principles-based standards lead auditors to offer a lengthier justification of their decisions.⁶

V. DISCUSSION

We examine whether principles-based accounting standards lead to qualitative changes in auditors' judgment and decision processes. In a 2x2 between-subjects experiment, we vary the type of accounting standard (principles- versus rules-based) and the economic substance of an accounting transaction (structured lease versus unstructured lease). Our findings suggest that the nature of the accounting standard strongly influences auditors' sense of process accountability and epistemic motivation. We find that auditors' perception of being accountable for the process employed to reach audit decisions is significantly greater under principles-based standards than under rules-based standards. Establishing a link between principles-based accounting standards and process accountability is important, because previous research has shown that process accountability has substantial positive effects on audit judgment quality, i.e., it can reduce judgment biases (Kennedy 1993; Tetlock and Kim 1987), increase audit effort (Kennedy 1995), and improve judgment accuracy (Ashton 1992; Siegel-Jacobs and Yates 1996). Process accountability can also decrease overconfidence (Tetlock and Kim 1987), increase self-critical attention (Lerner and Tetlock 1999), and improve calibration (Siegel-Jacobs and Yates 1996).

⁶ We also examined the extent to which participants describe their reasoning process in the justification memo. We found that very few auditors focused on describing their reasoning process in the memo, both in the principles-based condition and in the rules-based condition. Instead, auditors appeared to justify their decisions and provide arguments in support of their conclusions, likely because they are more accustomed to doing this than describing their decision process.

We also find that principles-based accounting standards lead auditors to experience greater epistemic motivation, thereby likely resulting in more thorough, effortful, and systematic processing of available information. Previous research in psychology has established process accountability as an important antecedent of epistemic motivation. Our study proposes and confirms a mediation model in which principles-based standards increase process accountability, and the increase in process accountability in turn amplifies epistemic motivation. This finding suggests that a change in implementation guidance from detailed rules to broad principles would induce a significant change in auditors' cognitive processes in making audit decisions.

We find that principles-based standards improve auditors' decision performance when auditors are faced with ambiguous scenarios involving structured accounting transactions. This finding is particularly important because financial engineering and structuring of transactions makes audit judgment more difficult. It also increases audit risk because management has obfuscated the transaction in order to achieve a desired accounting treatment. We find that given the same amount of evidence, principles-based standards lead auditors to make decisions consistent with the economic substance of the transaction more than rules-based standards do. We must recognize, however, that our findings on auditor decision performance are tentative and may understate the advantages of principles-based standards, because in our experiment auditors have the opportunity to request, but not to examine, additional evidence. Because our results indicate that auditors demand more evidence under principles-based standards, more research is needed to examine auditor decision performance given the evaluation of additional evidence.

We observe that auditors who work with principles-based standards experience a higher overall need for evidence – a finding consistent with an increase in epistemic motivation. However, principles-based standards lead auditors to demand a greater amount of both diagnostic and nondiagnostic evidence – evidence irrelevant to the problem at hand. This finding, although consistent with previous research on process accountability in accounting (Hackenbrack 1992; Glover 1997), suggests that principles-based standards may exacerbate the dilution effect in auditing. Future research is needed in this area to understand whether the additional evidence examined would in fact bias audit judgment.

When accounting standards are rules-based auditors tend to focus more on the guidance provided by the standards, and to cite that guidance as justification for their decision. However, when accounting standards are principles-based, auditors tend to expand their focus to consider cues other than the accounting standard – a finding consistent with an increased need for audit evidence, greater breadth of evidence considered, and more thorough, systematic and effortful processing of information.

We find that, in general, auditors display less confidence in their decisions when the standards they work with are based on principles than specific rules. Interestingly, when faced with a relatively complex scenario, auditors who make a correct decision are equally confident, regardless of whether they work with rules-based or principles-based standards. Importantly, however, auditors who make incorrect decisions are significantly more confident in their decisions if they work with rules-based standards. Although principles-based standards could decrease auditors' overall confidence in their decisions – a potentially negative effect when an

auditor needs to justify their judgment in front of regulators and a client, our findings suggest that rules may lead auditors to be overconfident when incorrect decisions are made.

In addition to the general limitations of experimental research, our study is subject to some limitations that may affect the generalizability of our results. Although our experiment presents auditors with an opportunity to request additional evidence items, they do not actually use this additional evidence to form their decision. Future research may study how the examination of greater amount of evidence by auditors who work with principles-based standards influences final judgments. We also examine the judgments of individual auditors, while in practice auditors work in hierarchical teams and may consult with and rely on the judgments of others. A promising avenue for further investigation is the manner in which rules versus principles accounting standards impact such group processes.

Finally, principles-based standards, as feared by many (SEC 2008), led to lower consensus among auditors in the more ambiguous scenario involving a structured lease transaction. A practice concern, thus, is how to improve consensus, given the recent movement towards principles-based standards.

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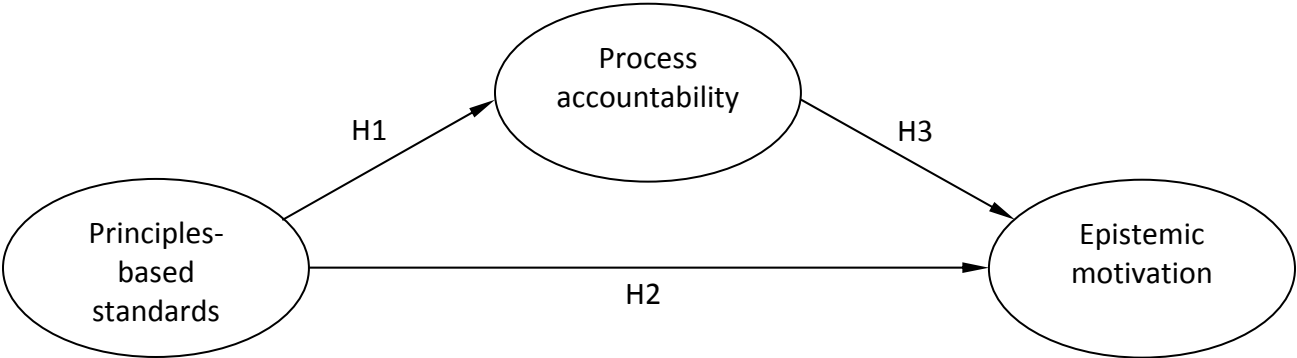
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FIGURE 1. Mediation Model

Panel A: Hypothesized Model



Panel B: Confirmed Model

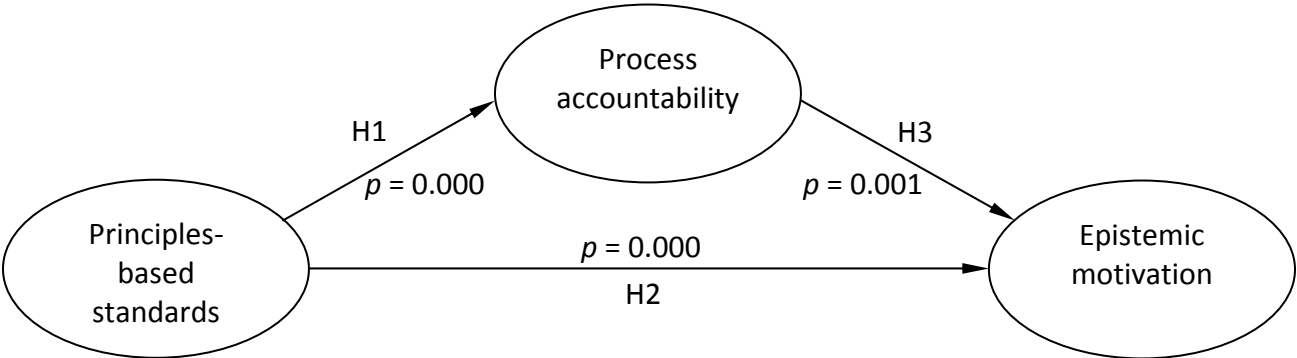


EXHIBIT 1. Manipulations

PANEL A. Type of Accounting Standard

Principles-based:

The classification of leases adopted in this Standard is based on the extent to which risks and rewards incidental to ownership of a leased asset lie with the lessor or the lessee.

A lease is classified as a capital lease if it transfers substantially all the risks and rewards incidental to ownership. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership.

Rules-based:

If a lease meets any of the criteria specified below, it is to be recorded as a capital lease; otherwise it is to be accounted for as an operating lease:

- 1) The term of the lease is equal to or greater than 80% of the leased asset's useful life
- 2) The present value of the lease payments is equal to or greater than 80% of the fair market value of the leased asset or
- 3) At the end of the lease term, asset ownership is transferred to the lessee.

PANEL B. Economic Substance of the Lease

Structured Lease Condition:

ABC Co. is entering into a lease agreement on October 15, 2008. This transaction is significant and material to the current year's audit. The company is leasing a building for 37 years from Landlord Co. Landlord Co. is not a related party to ABC Co. The appraised current market value of the building is \$1,050,000. ABC Co. will make monthly lease payments of \$8,000 on the first day of each calendar month. The estimated useful life of the building is 50 years. The net present value of the minimum lease payments, discounted using the incremental borrowing rate of ABC Co., is \$836,000 at the inception of the lease. Ownership of the building will remain with Landlord Co. at the end of the lease. At the end of the lease term, ABC will have the option to renew the lease on an annual basis.

The lease contract stipulates that ABC Co. will use the building as a production facility. As part of its planned expansion, the company will move equipment to the new facility to manufacture two of its increasingly successful product lines. The facility will also host equipment to manufacture three other new lines of product. ABC Co. has a history of an excellent relationship with Landlord Co., and there have not been any disputes between ABC and Landlord. Historically, ABC has been renewing the leases for all buildings leased from Landlord at the end of their contracted terms. Because of the restrictive debt covenant with the bank, ABC management has a reason to prefer recording the lease as an operating lease and not a capital one.

Unstructured Lease Condition:

ABC Co. is entering into a lease agreement on October 15, 2008. This transaction is significant and material to the current year's audit. The company is leasing a building for 25 years from Landlord Co. Landlord Co. is not a related party to ABC Co. The appraised current market value of the building is \$1,050,000. ABC Co. will make monthly lease payments of \$5,800 on the first day of each calendar month. The estimated useful life of the building is 50 years. The net present value of the minimum lease payments, discounted using the incremental borrowing rate of ABC Co., is \$630,900 at the inception of the lease. Ownership of the building will remain with Landlord Co at the end of the lease. At the end of the lease term, ABC will have the option to renew the lease on an annual basis.

The lease contract stipulates that ABC Co. will use the building as a production facility. As part of its planned expansion, the company will move equipment to the new facility to manufacture two of its increasingly successful product lines. The facility will also host equipment to manufacture three other new lines of product. ABC Co. has a history of an excellent relationship with Landlord Co., and there have not been any disputes between ABC and Landlord. Historically, ABC has not been renewing the leases for any buildings leased from Landlord at the end of their contracted terms. Because of the restrictive debt covenant with the bank, ABC management has a reason to prefer recording the lease as an operating lease and not a capital one.

TABLE 1. Additional Evidence Items

1	Schedule of all fixed assets	17	Restrictions on Retained Earnings
2	Tax return from previous year	18	Number of annual Audit Committee meetings
3	Aging schedule of accounts receivable	19	Dividend payout schedules
4	Depreciation schedules for the last 2 years	20	Loan applications of the company
5	Other obligations of the company	21	ISO quality control report for the company
6	Bad Debt estimation assumptions	22	Repairs and maintenance expense
7	Penalties for failing to continue the lease	23	Directors & Officers' liability insurance coverage
8	R&D related investments	24	Debt covenants for the company
9	Flowchart of internal control	25	Additional incentives related to the lease
10	Schedule of solvency ratios	26	Schedule of disposals of long-term assets
11	Attorney representations related to leases	27	Deeds for fixed assets owned
12	Capital stock repurchase agreements	28	Schedule of annual interest expense incurred
13	Analysis of all revenue accounts	29	Touring and physical examination of building
14	Minutes of the meetings of the Board of Directors	30	Schedule of property pledged to secure loans
15	Revenue projections for next year	31	Planned introductions of new products over the next 5 years
16	Options to cancel the lease	32	Cash lead schedule

TABLE 2. Process Accountability**PANEL A. Descriptive Statistics^a**

Accounting Standard	Economic Substance of Lease	Mean	Std. Deviation	N
Principles	Structured	4.99	0.81	26
	Unstructured	4.84	0.96	26
	Total	4.91	0.89	52
Rules	Structured	3.35	1.12	26
	Unstructured	2.98	1.27	26
	Total	3.16	1.20	52
Total	Structured	4.17	1.27	52
	Unstructured	3.91	1.46	52
	Total	4.04	1.37	104

PANEL B. ANOVA

	df	MS	F	Sig.^b
Standard	1	79.63	71.27	0.000
Economic Substance of Lease	1	1.73	1.55	0.217
Standard X Economic Substance of Lease	1	0.32	0.29	0.592
Error	100	1.12		

^a Process accountability was measured on a 5-item scale. Participants recorded their answers to the following questions on 7-point Likert scales: (a) to what extent are you free to determine the types of information relevant to your decision (1=very little, 7=very much), (b) how difficult will it be to determine whether a piece of information is relevant to the lease decision (1=very difficult, 7=very easy), (c) every auditor will be examining the same types of information in making a decision (1=strongly disagree, 7=strongly agree), (d) I have discretion in deciding how much I want to weight various facts in reaching a decision (1=strongly disagree, 7=strongly agree), (e) to what extent will an auditor have to defend to others his application of this accounting standard (1=very little, 7=very much).

^b We report one-tailed p-values when the results meet directional predictions and two-tailed p-values otherwise.

TABLE 3. Epistemic Motivation
PANEL A. Descriptive Statistics^a

Accounting Standard	Economic Substance of Lease	Mean	Std. Deviation	N
Principles	Structured	5.10	1.12	26
	Unstructured	4.65	1.34	26
	Total	4.88	1.24	52
Rules	Structured	3.56	1.44	26
	Unstructured	3.26	1.33	26
	Total	3.41	1.38	52
Total	Structured	4.33	1.50	52
	Unstructured	3.96	1.50	52
	Total	4.15	1.50	104

PANEL B. ANOVA

	Df	MS	F	Sig.^b
Standard	1	55.78	32.37	<i>0.000</i>
Economic Substance of Lease	1	3.66	2.12	<i>0.148</i>
Standard X Economic Substance of Lease	1	0.14	0.08	<i>0.775</i>
Error	100	1.12		

^a Epistemic motivation was measured with a 3-item scale. Participants rated the following items on 7-point Likert scales (1=strongly disagree, 7=strongly agree): To apply this accounting standard, (a) I had to think deeply before making a decision, (b) I was required to consider a large number of possible perspectives, (c) I had to make judgments and decisions as thoroughly as possible.

^b We report one-tailed p-values when the results meet directional predictions and two-tailed p-values otherwise

TABLE 4. Need for Audit Evidence**PANEL A. Descriptive Statistics^a**

Accounting Standard	Economic Substance of Lease	Mean	Std. Deviation	N
Principles	Structured	5.08	1.68	25
	Unstructured	5.25	1.39	24
	Total	5.16	1.53	49
Rules	Structured	4.23	2.03	26
	Unstructured	3.62	1.83	26
	Total	3.92	1.94	52
Total	Structured	4.65	1.90	51
	Unstructured	4.40	1.82	50
	Total	4.52	1.85	101

PANEL B. ANOVA

	df	MS	F	Sig.^b
Standard	1	38.90	12.62	<i>0.000</i>
Economic Substance of Lease	1	1.25	0.41	<i>0.526</i>
Standard X Economic Substance of Lease	1	3.89	1.26	<i>0.264</i>
Error	97	3.08		

^a Participants recorded on 7-point Likert scales their answers to the question: To what extent do you feel you need additional evidence to help you in your decision about the lease classification (1=no need for additional evidence, 7=imperative need for additional evidence).

^b We report one-tailed p-values when the results meet directional predictions and two-tailed p-values otherwise

TABLE 5. Amount of Evidence Requested

PANEL A. Descriptive Statistics

Accounting Standard	Economic Substance of Lease	TOTAL Evidence ^a		DIAGNOSTIC Evidence ^b		NONDIAGNOSTIC Evidence ^c		N
		Mean (St. Dev.)	Mean (St. Dev.)	Mean (St. Dev.)	Mean (St. Dev.)			
Principles	Structured	6.04	(4.00)	3.92	(1.83)	2.15	(3.13)	26
	Unstructured	7.23	(5.27)	4.69	(1.91)	2.54	(4.16)	26
	Total	6.63	(4.67)	4.31	(1.90)	2.35	(3.65)	52
Rules	Structured	3.15	(2.72)	2.27	(1.93)	1.00	(1.47)	26
	Unstructured	3.58	(4.23)	2.38	(2.37)	1.19	(2.21)	26
	Total	3.37	(3.53)	2.33	(2.14)	1.10	(1.86)	52
Total	Structured	4.60	(3.69)	3.10	(2.04)	1.58	(2.49)	52
	Unstructured	5.40	(5.08)	3.54	(2.43)	1.87	(3.37)	52
	Total	5.00	(4.43)	3.32	(2.24)	1.72	(2.95)	104

PANEL B. ANOVA

	df	TOTAL Evidence			DIAGNOSTIC Evidence			NONDIAGNOSTIC Evidence		
		MS	F	Sig. ^d	MS	F	Sig. ^d	MS	F	Sig. ^d
		Standard	1	277.89	16.11	0.000	102.01	24.96	0.000	40.63
Economic Substance of Lease	1	16.96	0.98	0.324	5.09	1.25	0.267	2.16	0.25	0.616
Standard X Economic Substance of Lease	1	3.85	0.22	0.638	2.78	0.68	0.412	0.24	0.03	0.867
Error	100	17.25			4.09			8.54		

^a Participants were presented with 32 evidence items (shown in Table 1) and were asked to mark any evidence items that they would need to examine in deciding how to record the lease. Total evidence was measured by the number of items requested by participants.

^b Diagnostic evidence was measured by the number of items relevant to the lease classification decision that were requested by participants. (Diagnostic items were items 7, 10, 11, 14, 16, 24, 25, and 29 in Table 1.)

^c Nondiagnostic evidence was measured by the number of items not relevant to the lease classification decision that were requested by participants. (Nondiagnostic items were items 1, 2, 3, 4, 5, 6, 8, 9, 12, 13, 15, 17, 18, 19, 20, 21, 22, 23, 26, 27, 28, 30, 31, and 32 in Table 1.)

^d We report one-tailed p-values when the results meet directional predictions and two-tailed p-values otherwise

TABLE 6. Audit Decision Performance

PANEL A. Unstructured Lease Condition

		Participant Classification of Lease^a		
		Capital	Operating	Total
Standard	Principles	2	24	26
	Rules	1	25	26
	Total	3	49	52

		Sig.^b
Fisher's Exact Test		<i>1.000</i>

PANEL B. Structured Lease Condition

		Participant Classification of Lease^a		
		Capital	Operating	Total
Standard	Principles	13	13	26
	Rules	5	17	22
	Total	18	30	48

		Sig.^b
Fisher's Exact Test		<i>0.049</i>

^a Participants recorded their lease classification decisions on a binary scale: an operating lease or a capital lease.

^b We report one-tailed p-values when the results meet directional predictions and two-tailed p-values otherwise

TABLE 7. Decision Confidence**PANEL A. Descriptive Statistics^a**

Accounting Standard	Economic Substance of Lease	Mean	Std. Deviation	N
Principles	Structured	4.96	1.25	26
	Unstructured	5.31	1.19	26
	Total	5.13	1.22	52
Rules	Structured	5.80	1.16	25
	Unstructured	6.00	0.85	26
	Total	5.90	1.01	51
Total	Structured	5.37	1.26	51
	Unstructured	5.65	1.08	52
	Total	5.51	1.18	103

PANEL B. ANOVA

	df	MS	F	Sig.^b
Standard	1	15.08	11.99	<i>0.000</i>
Economic Substance of Lease	1	1.92	1.53	<i>0.220</i>
Standard X Economic Substance of Lease	1	0.14	0.11	<i>0.742</i>
Error	99	1.26		

^a Participants responded to the question: How confident are you in your decision about how the lease should be classified (1=not at all confident, 7=very confident).

^b We report one-tailed p-values when the results meet directional predictions and two-tailed p-values otherwise