

## The Effect of Mandatory Auditor Rotation and Retention on Auditor-Client Negotiations Strategies

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### ABSTRACT

The study aims to investigate how the application of mandatory auditor rotation and retention affect the negotiation strategies used by auditors and client. The results of this study provide empirical evidence that can bridge debate between parties that support the implementation of mandatory auditor rotation and retention with the practitioner that opposed to mandatory regulation. The results of this study indicate that the client (management) adjust the strategies they use in negotiations, as well as what auditors do, suggesting that clients respond to increasing inaction and contending strategies as well as integrating and obliging strategies that are participant used to the conditions of auditors mandatory rotation and retention, compared to the absence of conditions auditors mandatory rotation and retention. In accordance with the results of previous studies showing that behavioral changes caused by the application of auditor rotation and retention change negotiation strategies used by the client, so that the research consistently shows that the purpose of mandatory rotation nor retention is associated with changes in economic incentives faced by auditors and the client is caused not only by the length of auditor-client relationship, so that further research into this field promising.

Keywords: Mandatory Auditor Rotation, Retention Mandatory Auditor, Auditor-Client Negotiation, Negotiation Strategy.

### 1. Introduction

This study departs from warm debate between those who support the existence of mandatory rotation with the practitioners who opposed to this arrangement, so this study intends to provide empirical evidence of whether the rotation is accompanied by mandatory auditor retention, effect on the differences in negotiation strategies used by the auditor and clients. Research in this area is considered important, because in fact the effectiveness of this regulation has not been measured because, first the rule is never based on empirical evidence. Second, these rules are still in transition because some companies just beginning to change auditors in 2004 with a record has been audited for five years. .

Focus of this research is that the auditing literature suggests; (1) the auditor-client negotiation often occurs and is an important part of the audit process, and (2) assessment of the auditor and client negotiation is related to various economic and psychological factors

(Tuttle and Wang, 2009). Auditor-client negotiations affect the audited financial statements and therefore contributes to the quality of audits. Understanding negotiation strategies associated with mandatory rotation of auditors based on the belief that reducing the time of audit will reduce the possibility of auditor negotiation strategies preference influenced to accommodate clients' need, so that audit quality can be maintained.

Previous studies such as conducted Mautz and Sharaf (1961) showed that the relationship can cause the auditor lose its independence. Auditors who have long relationships with clients are believe carried the consequences of high dependency or strong economic ties between auditors and clients. The higher the auditor's economic bond with the client, the higher likelihood the auditor allowed the client to choose extrem accounting menthod. On the other hand, some argue opposite. When auditor do initial audit, the first time they have understand the client's business environment and the risk of audit clients, so the start-up costs for the initial audit to be high so it could raise audit fees. Another argument which opposite the rotation settings revealed that the long relationship between the auditor with the client will make the auditors be expert and aware of the client's business. Thus, the auditor is more aware of the extreme behavior management and understand the accounting choices in the business. That is, they do not agree that the behavior of Arthur Andersen, which lost its independence to the client's behavior generalized to other auditors.

Statements about the need to reinforce auditor rotation, research Dopuch et al. (2001) proved that a compulsory rotation makes the independence of auditors is higher than if there are no rules of auditor rotation and retention. Dopuch et al. (2001) found evidence that when the change of auditors imposed mandatory rules, independence is higher than if there are no rules of rotation. Even the highest independence is if the auditor rotation and retention rules imposed mandatory. They found that when both rules apply to the auditors- subject, the frequency of reporting bias on the lowest level.

Previous research of Antle and Nalebuff (1991) states that financial statements should be viewed as a joint report between the auditor and management. Antle and Nalebuff (1991) argues that the report is a joint venture if the auditor is not willing to give an unqualified opinion on management reports. At this point, auditors and clients start negotiating in which the auditor would then offer the revision report. Clients can threaten to replace the auditor and other auditors seek more willing to accept management's view. Alternatively, they decided to expand the audit to obtain more facts. At the end, compromise will occur, the report was revised, and the auditors issued an unqualified opinion on the revision of the report.

This study expands the research conducted by Wang and Tuttle (2009) that examined the effect of auditor rotation on the negotiation strategies used by auditors and clients, because principle that "all the technical aspects of auditing are important but can not replace the primary skills in auditing, namely art of negotiation. "(Michael Buxbaum, The CPA Journal, 2002). Wang and Tuttle (2009) provide differences in the process of negotiation between auditor and client under the conditions of the rotation and without compulsory rotation of auditors. Their research was based on previous findings by adding two-way negotiation strategy for auditors and clients and then use the protocol negotiations, and explores the process of negotiating the value of assets audited. Furthermore, this research adds a review process of the negotiations not only on the condition of the presence or absence of mandatory rotation, also on condition of presence or absence of mandatory auditor retention. This is based on a variety of backgrounds that mandatory rotation is not necessarily enhance the independence of the auditor during the period prior to the date of the rotation,

because the client can threaten to change their auditors early. In addition the need for rotation, this study also investigated the effect of mandatory retention, which requires the client to retain the incumbent auditor for certain specified number of years (Dopuch et al. 2001). A series of mandatory retention and mandatory rotation of auditors can protect against the replacement earlier, when the client do so based on disagreements between management and auditors relating to the audited report. Mandatory retention is required, either as an alternative to mandatory rotation or as a complement. Related to this idea, the main problems were identified in this study: first, whether the application of mandatory rotation and retention of auditors will affect the negotiation strategies used by management (clients) in the audit negotiation? Second, whether the application of mandatory rotation and retention of auditors will affect the negotiation strategies used by auditors (partners) in the negotiation audit? Third, whether there are differences in strategies used by auditor and client in the absence of mandatory auditor rotation and retention compared with the existence of mandatory auditor rotation and retention?

This research will contribute to the theory and methodology as well as contributions policy contribution. Theoretical and methodological contributions will be obtained for this study contributes to auditing literature by combining experimental methods with real-time negotiation methods, as well as using verbal protocol analysis that was developed, also contributes to the negotiation literature as it tries to capture the unique aspects of the negotiation activities directly (Davis and Holt, 1993). Contributions to regulatory policy as well as to the perpetrators of regulation. In particular mandatory rotation setting is imposed in Indonesia, various professions at the level of polemic associated with the level of legal certainty and perception of the professional person is at risk when conducting an audit, further that allow the emergence of attention from management that still have flexibility in doing “dismissal” against the auditors raised a new phenomenon, that when the rotation was rumored to be able improve independence of auditor, it should be coupled with guarantees for the auditor to have “defense” with the inclusion of mandatory retention arrangements or the existence of a legal contract that the existence of an auditor during a certain period will still be maintained. Therefore, any perception about the auditor profession, the most important during this scrutiny is not the absence of regulation, but whether that regulation is appropriate and adequate? Is it appropriate that the profession of public accountants (auditors) are regulated as it is today? and Does this arrangement provide a strong contribution to the development of the profession in particular.

## **2. Theoretical and Hypotheses Development**

### **2.1 Background of Mandatory Auditor Rotation and Retention**

The attack on the accounting profession (the auditor) has tapered in recent years. Many of the proposals that emerged with the intention of improving the profession. One of them is asking for public companies to rotate auditors periodically. Mandatory rotation has been widely accepted and received recommendations from many parties are expected to cause significant effect on the practice of auditing. Although the mandatory rotation has been widely discussed for more than 70 years and now a mandatory provision, but the profession has not agreed about this provision. Profession argued that this provision would increase the cost of audits to clients, lowering the quality of audits and provide little benefit.

Since 2003, the Finance Minister has tried to bring RUUAP in which a set of mandatory rotation of auditors and KAP. However RUUAP still continue to be revised. To

fill the void of public accountant's regulation, the Minister of Finance issued several rules, was Minister of Finance Regulation No. 17 in 2008. In the regulations mentioned term limits provision of auditing services for three years and six years for the auditor to KAP (Ministry of Finance, 2008). This regulation reinforces the decision of the Minister of Finance of Republic of. 359 in 2003 (Ministry of Finance, 2003). These rules pose a long polemic among public accounting.

Several recent studies specifically examined the possible influence of mandatory rotation. Using case method of decision, Hatfield, Jackson, and Vanderveldes (2007) found that the proposed audit adjustments are more conservative in good condition rotation of audit partners or audit firm rotation. However, Hatfield et al. just look at the proposed adjustments and not the final adjustments. Daniels and Booker (2006) found that the application of mandatory rotation of loan officers to change perceptions about auditor independence, but not about the quality of audits. Kaplan and Mauldin (2008) found that non-professional investors do not have the same perception of the effect mandatory rotation on auditor independence, consistent with the GAO study (2003). Unfortunately these studies did not examine the effect of mandatory rotation on the client-auditor interaction.

Dopuch et al. (2001) study tested the effect of mandatory auditor rotation and retention (in the period of non-rotating) on the willingness of auditors to issue a report expected by the client. They found that the rotation required to change the interaction between auditor reporting decisions and investment decisions of clients. Specifically, they found that mandatory rotation reduces the willingness of auditors to issue a report according to client preference and willingness of clients to invest (which will reduce the risk of auditor reporting errors). In contrast with Dopuch et al. Wang and Tuttle study (2009) examine the process of direct negotiations on the choice of auditor and client reporting, who extend the generalization Dopuch et al. the major contribution was to examine the process where the auditor and the client reach a decision reporting. It gives a new understanding of auditor-client negotiation strategies under conditions of mandatory rotation.

## **2.2 Auditor-Client Negotiations**

Several previous studies have investigated issues related to auditor-client negotiation (eg, Antle & Nalebuff, 1991; Beattie, Brandt, & Fearnley, 2000; Demski & Frimor, 1999; Farmer, Rittenberg & Trompeter, 1987; Goodwin, 2002; Nelson et al, 2002; Trotman, Wright, & Wright, 2005; Zhang, 1999). These studies generally found that the auditor-client negotiations could materially affect the financial statements at the time identified a number of accounting issues and other contextual issues that affect the auditor-client negotiations. These studies looked specifically at the auditor-client negotiation process with implications relating to how the mandatory rotation can influence this negotiation process (Wang and Tuttle, 2009).

Gibbins et al. (2001) developed a model of auditor-client negotiation process. They used this model to analyze the 93 partners in large audit firms and draw some conclusions that the auditor-client negotiation is a normal part of the auditing and the audit partner to see the negotiations as part of the service for clients where the auditors helped produce the financial statements accordingly. In this provision, both clients and auditors have the desire to reach an agreement. Interestingly, their data showed that the risk retention affects the entire process of the auditor-client negotiations. Continuing this research, Gibbins, McCracken, and Salterio (2005) contributes to the auditor and the client to analyze problem-solving process used by the eight partners of the audit.

Subsequent research conducted by Brown and Johnstone (2005) that examined the influence of engagement risk and auditor negotiation experience. Using computer simulations, they conclude the negotiation strategy of the audit managers and partners based on the opening bid and final bid. This study concluded that uses more dominant contending strategy when the final bid equal with the opening bid. Furthermore, this research suggests that auditors with less experience negotiating client using the concession negotiation strategy when high-risk engagement. However, Brown and Johnstone just doing a simulation of the subject using a constant negotiation strategy. Moreover, they conclude negotiation strategy based on the results negotiations. In a dynamic negotiation, where both parties actively participate, possibly more than one strategy will be used to achieve the expected outcome of negotiations, depending also on the strategy used by the opponent (Pruitt & Carnevale, 1993; Pruitt & Rubin, 1986). Therefore, the negotiation strategy can be ascertained only by directly measuring the negotiation strategies of the negotiation process itself.

Using the case of decision-making, Hatfield, Agoglia, and Sanchez (2005), found that auditors using the tactic of reciprocity when dealing with non-cooperative client. Bame-Aldred and Kida (2007) observed the initial negotiating positions and tactics used by the auditor and client. They found that auditors are less willing to make concessions in negotiations. These studies did not consider the economic conditions at the time when such negotiation tactics used by the subject. The results of this study may not apply when the incentives that encourage the auditor-client negotiations changed (Pruitt & Carnevale, 1993). According to this theory, individuals modify negotiation strategies by taking into account their individual incentives that connects them with others. In accordance with theoretical predictions reveal that attention to self and concern for others affect the negotiation strategy. Savage et al. (1989) expand this theory into the context of the economy by recognizing that the primary motivator in the context of business negotiations is the result of the economy. They characterize two general types of negotiations, one of those types where the negotiators are motivated to establish or maintain a positive relationship and are willing to share the pie through mutually beneficial cooperation. While attention to the substantive results motivate negotiators to break and claim as many pies. From the perspective of the auditor-client agreement in which the dominant economic power, attention to the substantive outcome of negotiations with a focus attribute financially equivalent to the period, while attention to outcomes for parties in line with a focus on how to maintain the relationship between the auditor-client relationship. Because an audit can be characterized as a series of negotiations that repeated from year to year, the attention to the relationship implies that the auditor and the client seeks to ensure the continuation of their involvement in the subsequent period.

According to Savage et al. (1989), when negotiators lack of attention to the continuation of a relationship, they prefer to adopt non-cooperative strategies. In accordance with findings that the negotiators who have a low attention to substantive results and relationships tend to adopt a strategy of inaction. Strategy of inaction is usually associated with the purpose to avoid losses. The strategy can behave wait-and-see which resulted in an agreement if the profit opportunities offered. Similarly, negotiators who do not pay attention to the relationship but who cares about the substantive outcome is more likely to adopt a strategy of contending. Negotiators who adopt contending strategy actively accentuate their position without considering other parties. For example, client can suppress the auditor to accept the use of aggressive accounting, due to threats of dismissal against the auditor. Conversely, when the negotiators are more concerned about the relationship, they will adopt more cooperative strategies.

To implement the dual-concern model in the regulation of auditor-client negotiations, to identify the economic incentives associated with the actions of each party associated with financial reporting on the condition of the rotation and the retention of compulsory or without rotation and retention compulsory. That is, how to change an auditor and client negotiation process as a function of varying economic conditions when the rotation and retention must be worn. The negotiation strategies are commonly used and a reference in this study were (Lewicki, 2010):

- **Inaction Strategy**

This strategy is analogous to the action to do anything and do not respond to messages other hand, give more comments that are evasive and talk about issues that are irrelevant. This strategy shows the option to not agree in the negotiations, or do not choose to negotiate. There are many factors that can come up with a situation like this: (1) If a person is able to meet the needs of other parties without negotiations, this suggests the use of avoidance strategies. (2) reluctance to give time and effort to negotiate, and (3) The decision to bernegosiasikan highly related to the desire of the results can be achieved if negotiations did not go well.

- **Contending Strategy**

Analogous as a competitive strategy or distributive strategies aimed at creating a pattern of "us-them" or "superiority – inferiority" and will lead to distortions in the decisions of other parties. This strategy demands concessions from other parties and attempting to persuade another party to admit a problem unilaterally. The core of this strategy is to reject the proposals of other parties and making threats not to cooperate.

- **Integrating Strategy**

This strategy states a joint concession, proposing a middle way or filed for each issue, solicit or encourage others to consider common interests, as well as provide information that can justify the existence of a compromise, as well as provide information that can justify the existence of a compromise and most importantly, expressed willingness to negotiate.

- **Obliging Strategy**

This strategy is more priority to other parties and expressed satisfaction that "harmony" of a good relationship is more important, thus providing less benefit to themselves. Recognizing the demand the other party and are at a "lost".

### **2.3 Management's Negotiation Strategy**

When negotiating with the auditor, management (clients) have good reason to pay attention to substantive results. Unlike the auditors accept collateral audit fees, for the current period financial statements management may directly affect their compensation. Therefore, client has a strong incentive to influence the outcome of current negotiations (DeFond & Jiambalvo, 1993). So it can be affirmed that the client's attention to the substance is relatively high in the results of negotiations on the conditions in the absence of mandatory rotation and retention. The focus of attention is associated with the client how to maintain a good relationship, it is generally beneficial to avoid switching costs related to the process of getting a new auditor. Switching cost is considered substantial (GAO, 1996) that lead to high

attention to its relations in a long time. In addition, clients who switched auditors may be subject to political costs associated with market perceptions about opinion shopping. Some research suggests that market perceptions about opinion shopping by the client tends to occur in the early years of auditor-client relationships are more likely to do the replacement auditor. On the other hand, in recent years on the condition of mandatory rotation and retention, with a high focus of attention for substantive results but low attention to the relationship, clients are more likely to adopt a strategy of contending. This prediction is summarized in the following hypothesis:

**H1: Mandatory auditor rotation and retention affects the negotiation strategies used by client-subject.**

**H1a: Client-subject will use a contending strategy most frequently on the condition of absence of mandatory rotation and retention compared to the condition of mandatory rotation and retention.**

**H1b: Client-subject will use obliging strategy most frequently on the condition of mandatory rotation and retention compared to the conditions in the absence of mandatory rotation and retention.**

#### **2.4 Auditor's Negotiation Strategy**

It is assumed in both rotation and retention mandatory conditions or absence of mandatory auditor rotation dan retention, auditors ensure the audit fee for the current year and that the number of the current cost is not affected by the negotiations on the asset values in financial statements preparation. This assumption is used to reduce the concern that auditors place more emphasis substantive results directly. On the other hand, the current audit environment to provide incentives for auditors to consider their long-term relationships with clients. The Government Accounting Office (GAO, 2003) showed that the average tenure of an auditor for Fortune 1000 companies is 22 years. Likewise, a study published by Fulcrum Financial Group (2003) who reported that 10% of firms in their sample had the same auditor for 50 years or more. In conditions of economic incentive, auditors may be willing to admit some of the items in the short term in financial statements to maintain long term relationships with clients, as expressed by some proponents of mandatory rotation (Benson, 2002; Imhoff, 2003; Wolf, Tackett, & Claypool, 1999). Therefore, the auditor's attention to the substantive results are relatively lower compared with their attention to maintaining an ongoing relationship.

The attention to the relationship is higher in conditions with no rotation and mandatory retention and lower in the presence of mandatory rotation and retention, it was found that the obliging strategy as a strategy to dominate for auditors in the absence of mandatory rotation and retention and strategies that dominate the inaction as a strategy for the auditor to the rotation and retention compulsory.

Further disclosed that without mandatory rotation and retention, the auditor has a relatively low concern for the substantive and relatively high attention to the relationship compared with the auditors on the condition of mandatory rotation and retention. This in turn leads to greater adoption in obliging and integrating strategy during negotiations. Furthermore, the presence of mandatory rotation and retention, the auditor has a relatively

low concern for the relationship, leading to the strategic use of inaction, so the argument is formulated in the following hypothesis:

**H2: Mandatory auditor rotation and retention will affect the negotiation strategies used by auditors-subject.**

**H2a: Auditor-subject will use most frequently obliging strategy on condition the absence of mandatory rotation and retention compared to the condition of mandatory rotation and retention.**

**H2b: Auditor-subject will use most frequently contending strategy on the condition of mandatory rotation and retention compared with conditions in the absence of mandatory rotation and retention.**

In recent years the existence and retention of mandatory rotation, auditors seem to power on the client. Economic predictions is that the negotiation will not occur and that the auditor would only assign them to the client's position. However, the literature suggests that people do not really follow the predictions of the economy but often follow social norms relating to fair play even when given full powers to others (Davis & Holt, 1993; Kagel & Roth, 1995). Therefore, this study makes predictions comparison, recognizing the relative economic strength rather than absolute economic power of the predictions of equilibrium without considering the impact of social factors. To the extent that the level of cooperation led to the successful negotiation, the following hypothesis was proposed:

**H3a: The condition of mandatory rotation and retention leads to a lack of cooperation by auditor-subject in negotiation.**

**H3b: The condition of mandatory rotation and retention leads to a more of cooperation by client-subject in negotiation.**

**H4: The negotiations most often end up with the deadlock in the condition of mandatory rotation and retention compared to conditions in the absence of mandatory rotation and retention.**

Under conditions when agreement is reached or not deadlocked, obliging those who use the strategy more likely to accept a lower payoff and the contending parties using a strategy more likely to receive higher yields than those using other strategies (Pruitt & Carnevale, 1993), so proposed the following hypothesis:

**H5: The results of the negotiations will be closer to the auditors-subject preferences on the conditions in the presence of mandatory rotation and retention, and closer to the client subject-preferences in absence of mandatory rotation and retention.**

### 3. Methods

#### 3.1 Experiment Design

This research uses experimental methods 2x2 full factorial design between subject as summarized below:

	No Retention	Retention for tree period
No Rotation	No Retention/No Rotation	Retention
Rotation after four periods	Rotation	Retention/Rotation

Adapted from Dopuch *et al.* (2000)

In this experiment, the task of negotiations conducted over four sessions for each condition of negotiations (without rotation and without retention (TRO and TRE); rotation (Ro); Retention (Re) and the rotation and retention (Ro and Re)) with 11 (eleven) participants in each session. The sequence of steps detailing the interactions between the auditor subjects and the client-subject is summarized below:

- Step 1: In each session, 5 (five) participants were randomly acting as manager (client) and 6 (six) participants assigned as an auditor. Managers and auditors then paired, one client and one auditor who negotiated the asset value that will be reported in the audited financial statements. Therefore, each session consists of five auditor-client pairs of negotiators
- Step 2: In the negotiating text, the pair negotiator read the same set of information related to the actual asset value. The actual value of the asset inventory for each negotiation period is predetermined.
- Step 3: The participants then perform two exercise periods. This training period does not affect the value of assets exempt from the preparation and testing hypotheses.
- Step 4: Pair negotiators carry four negotiation period for each session. To start each negotiation period, the client filed the value of the asset stocks on the dialog sheet negotiations, after receiving the preparation of client assets, the auditor may choose to directly receive the value of assets delivered dosage or negotiate with clients through negotiation dialog sheet. Negotiations take place by gluing a particular sentence of a few sentences that have been provided in the book of experiments into the dialog sheet negotiations for the respective periods. The auditor may accept the value delivered by the client at any time before the negotiation period expires. If the auditor does not receive the value delivered by the client before the negotiation period ends, the possibility of negotiations will end in stalemate, and the client may choose to maintain or replace the auditor (for the conditions in the absence of mandatory retention).
- Step 5: The client then randomly paired with a new auditor and an auditor in the next period is randomly moved again to another client, if other clients are available. Auditors will not be transferred to the same manager.
- Step 6: Payment of the participants performed each end of the period of negotiations based on the results of negotiations conducted by a pair negotiator based payment schemes that have been determined.

### 3.2 Research Sample

This study uses student of accounting profession as surrogate of the auditors as much as forty four and use master student of management science as surrogate of the company manager (client) as many as forty at the University of Gadjah Mada. Each participant then paired in the audit assignment negotiations relating to determining the value of company stock assets in the consolidated audited.

### **3.3 Experimental Manipulation**

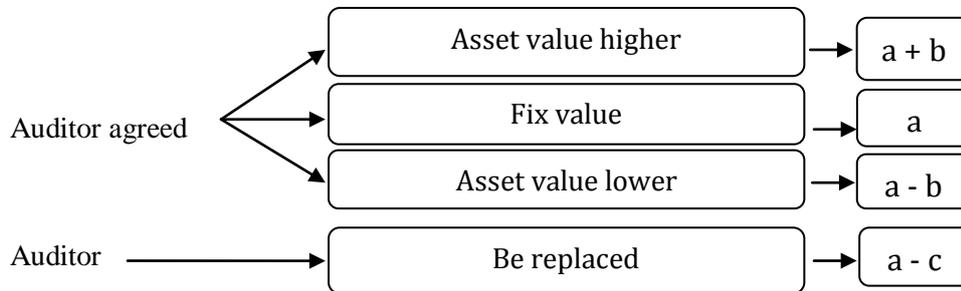
Because the predictions in this study are based on changes in the client and auditor incentives are influenced by the presence of conditions and retention of mandatory rotation, then the experiment was manipulated with two levels of mandatory rotation (rotation mandatory versus without rotation), and manipulated with two levels of mandatory retention (retention of mandatory versus without retention). Participants on the condition of mandatory rotation (Ro) was told that each pair of client-auditor will continue negotiations to four periods, and after four period is completed, the client must replace the old auditor. While the participants on the conditions in the absence of rotation mandatory (TRo) was told that every client and the auditor continues to negotiate for an unlimited period. While on the condition of mandatory retention (Re), participants were told that the client-auditor will retain their position as a negotiating partner for at least 3 (three) consecutive periods. While the condition without the mandatory retention (TRe) participants are not obliged to maintain its position as a negotiating partner and manager in this condition is allowed to perform the replacement of the auditor at any time diinginkan.

### **3.5 Participants' Payoff**

Experimental instructions also indicate the payment scheme for each client and the auditors in accordance with their respective conditions. Payments to clients subject in each period is determined by whether the auditor receives the asset value of stock delivered by client or reject the asset value of such preparations. While, payments to auditors in each period is determined by whether the auditor receives the value of assets delivered by the manager and whether the value received is greater than the actual value of asset. But in case of negotiations deadlock, then the auditor does not receive anything for the next period when the auditors did not find new clients. Therefore, auditors have an incentive to negotiate a lower asset value to avoid fines, but not too low, causing a deadlock and the risk of no longer being used by the client in the next period on the conditions in the absence of mandatory rotation and retention. Payment scheme is described as follows:

**Figure 1**  
**Payoff Scheme**

**For Manager:**



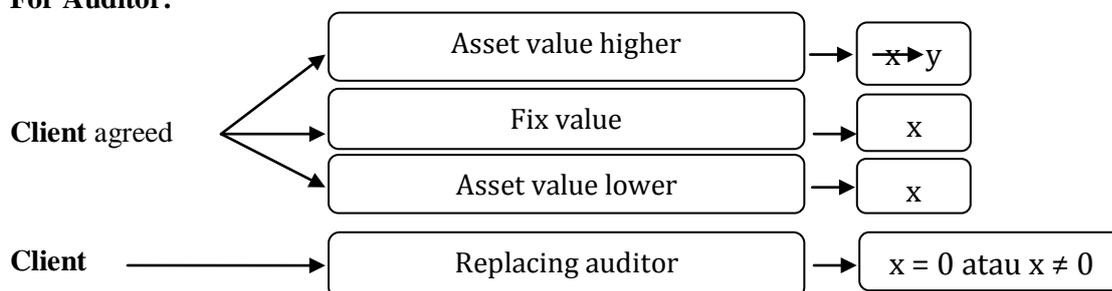
**Note:**

$a$  = Manager fixed compensation (Rp1.000.000.000).

$b$  = 20% from manager compensation.

$c$  = 25% from manager compensation.

**For Auditor:**



**Note:**

$x$  = Auditor fixed compensation (500.000.000).

$y$  = 60% from manager compensation.

$x = 0$  (the auditors did not get clients to the next period after replacement).

$x \neq 0$  (the auditor gets a new client for the next period after replacement).

**3.6 Data Analysis**

Data analysis used in this study is MANOVA (Multivariate Analysis of Variance) to test H1 and H2 and T-Test (Independent Sample Test) to test H1a, H1b, H2a, H2b, H4 and H5 and ANOVA (Analysis of Variance) to test H3a and H3b.

#### 4. Hypothesis Testing

There are 160 negotiations period (4 periods of negotiations in each of four sessions for each of ten negotiating partners). Hypothesis 1 predicts that the rotation mandatory and mandatory retention will affect the negotiation strategies used by auditors subject. In Specifically, H1a suggests that the subject of the auditor will use most often obliging the negotiation strategy when the conditions in the absence of mandatory rotation and retention compared to the condition of mandatory rotation and retention, and H1b indicate that the subject of the auditor will use most often contending negotiation strategy with the conditions of the rotation and mandatory retention than the conditions in the absence of mandatory rotation and retention. H1a and H1b analysis results showed a higher percentage ( $p < 0.000$ ) from the message inaction by the auditors on the condition of mandatory rotation (12.8%) compared to conditions with no mandatory rotation condition (3.6%). This result becomes stronger when it focuses on the period end in a condition of mandatory rotation and retention in which the message subject of integrating the auditors only 1.8% compared to inaction message that is equal to 28.2%. Thus, H1a and H1b is supported. These results suggest that the rotation and the retention of the auditor shall reduce the interest of the subject to maintain relationships with clients. The test subsequently for H1 is to compare the use of the overall strategy by the subject on the condition of the auditor rotation and retention compulsory and in the absence of rotation and conditions retention compulsory. The test results showed Pillai's Trace with  $p < 0.001$ , so that H1 is supported. Hypothesis 2 predicts that the condition of rotation mandatory and retention shall affect the negotiation strategies used by the subject client. The test results show that the conditions in the absence of mandatory rotation and the retention, client-subject will use a contending negotiation strategy ( $p < 0.000$ ; 21.3%) more frequently as predicted by the H2a. Contrary to H2b, indicating that client-subject will use negotiation strategies integrating ( $p < 0.000$ ; 21.7%) more often on the condition of mandatory rotation and retention. The same pattern also emerged for the dominant strategy by the client subject to the final period on the condition of mandatory rotation and retention as well as conditions in the absence of mandatory rotation and retention. The data show that the rotation and retention will affect the negotiation strategies used by the subject client as predicted by H2, so that H2, H2a and H2b is supported. H3a predicts that the condition of mandatory rotation and retention leads to a lack of cooperation by the subject of an auditor in the negotiations, and vice versa H3b suggests that the condition of the rotation and retention must lead to more cooperation by the subject client in the negotiations. The test results showed a significant decrease ( $p < 0.000$ ) in the auditor's level of cooperation by the subject on condition of mandatory rotation and retention (67.4%) than in the absence of conditions and retention of mandatory rotation (80.5%). Therefore, the test results support H3a and H3b. Hypothesis 4 predicted that the negotiations most frequently end up with the deadlock in the conditions and the retention of mandatory rotation than without rotation and the retention of mandatory conditions. Less consistent with this prediction, the test results showed that the level of cooperation on the condition of mandatory rotation and retention was not significantly different from the situation in the absence of mandatory rotation and retention ( $p < 0.070$ ). Likewise for auditors who carried out the replacement level is totally different in both conditions. These findings do not support H4. In Hypothesis 5 predicted that the preference subject to the conditions of auditor rotation and retention of compulsory and closer to the preferences of the client subject to the conditions in the absence of mandatory rotation and retention. Consistent with this prediction, test results showed that the level of cooperation on the condition of the rotation and retention mandatory (80.7%) for subjects auditors ( $p < 0.000$ ) compared to subjects clients (85.7%), in the absence of mandatory rotation and retention, thus H5 is supported.

## 5. Conclusion

The results of this study indicate that the client adjust the strategies they use in the negotiations as well as to what auditors do, its can be observed a change in frequency of use of cooperative strategies by the client when the conditions are the rotation and retention must be worn. A possible reason for the results of this test is that the client respond to an increase in inaction and contending strategies that are used subject to the conditions of auditor rotation and retention will be compared in the absence of conditions of mandatory rotation and retention. If so, the results of this study indicate that behavioral changes caused by the application of auditor rotation and retention of the changes required to move the negotiation strategies used by the subject client. Furthermore, the subject of clients in this study faced the prospect of a subject certain to replace the auditor, it is possible that they give less attention to the impasse of negotiations. Further research is needed to distinguish the possible prospects for the replacement of auditors that there are opportunities in a wider context. Overall, the results of this study provides additional findings from previous studies of auditor-client negotiations by entering how both sides respond to institutional incentives.

Differences strategies, particularly related to differences in incentives on the condition of mandatory rotation and retention, suggests that inconsistent to conclude negotiations for the satisfaction of both parties. The results of this study indicate that the frequency of higher negotiation deadlock occurs not only at the year end audit (in which a change of auditors which is required), but also in the period before the final period and also occur in conditions in the absence of mandatory rotation and retention. The occurrence of many related debate that cost efficiency is assumed to be the focus of attention because of auditor rotation is required, additional research into how the application of mandatory rotation and retention may affect the working relationship between clients and auditors are very beneficial in the future.

The findings in this study are consistent with the goals that mandatory rotation nor retention is attributed that change the incentives faced by auditors and clients are caused not only by the length of audit-client relationship. The research was conducted in the laboratory and thus is limited by factors inherent to the research laboratory, for example, laboratory methods to limit the kinds of tasks and participants that can be used. In addition, the study design only see the auditor incentives to avoid the higher valuation of the asset value of stocks in the audited financial statements. Future research is needed to determine whether these results continue to be consistent in more complex cases. Future research is very possible to see the context of other negotiations on the results of specific audits as well as certain ranges in the audit process. Although manipulation is given in this study can capture the hypothesized theoretical relationship, but it is suspected these results do not necessarily reflect the intensity of the pressures faced by auditors and clients on the actual conditions (the practice). For example, experiments conducted on the condition of the replacement auditor rotation and retention must provide less pressure than punitive sanctions that occurred in the field in the sense that the chances of getting new clients may be lower or higher than what the auditor should be natural subjects in experimental conditions.

Because the focus of this research is on the negotiation process rather than on gathering evidence specifically about the quality of the audit, so this study does not provide enough to predict how much the replacement must occur before the auditor's reputation is affected, whether the replacement of the auditor's reputation affect negatively or positively, so that research should next explore the effects of the reputation of the auditor and the client to get the answers to these questions.

## Appendix A

### Statistical Analysis

#### Hypotheses 1 and 2

##### Multivariate Tests<sup>c</sup>

Effect	Value	F	Sig.
Condition (H1)	.983	5.157	.001
Condition (H2)	1.240	3.760	.001

#### Hypotheses 1a, 1b, 2a ,2b and 4

##### Independent Samples Test

Hypotheses 1a and 1b	t	Sig. (2-tailed)
Period 1	6.957	.000
Period 2	7.071	.000
Period 3	7.071	.000
Period 4	7.071	.000
<b>Hypotheses 2a and 2b</b>		
Period 1	-5.196	.001
Period 2	-5.196	.000
Period 3	-5.774	.000
Period 4	-5.715	.005
<b>Hypotheses 4</b>		
Period 3	-2.449	.070

#### Hypotheses 3a and 3b

##### ANOVA

Preference

	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	5236.950	3	1745.650	38.052	.000
Within Groups	734.000	16	45.875		
Total	5970.950	19			

#### Hypotheses 5

##### Tests of Between-Subjects Effects

Dependent Variable: Preference

Source	Type III Sum of Squares	df	Mean Square	F	Sig.	Partial Eta Squared	
Intercept	Hypothesis	74420.000	1	74420.000	103.361	.062	.990
	Error	720.000	1	720.000 <sup>a</sup>			

Kondisi	Hypothesis	20.000	1	20.000	.002	.973	.002
	Error	11520.000	1	11520.000 <sup>b</sup>			
Profesi	Hypothesis	720.000	1	720.000	.062	.844	.059
	Error	11520.000	1	11520.000 <sup>b</sup>			
Kondisi * Profesi	Hypothesis	11520.000	1	11520.000	256.000	.000	.941
	Error	720.000	16	45.000 <sup>c</sup>			

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