THE ROLE OF INTERNAL ROTATION OF KEY AUDIT TEAM MEMBERS – EVIDENCE FROM GHANA

РОЛЬ ВНУТРЕННЕЙ РОТАЦИИ ЧЛЕНОВ ОСНОВНЫХ АУДИТОРСКИХ ГРУПП – ПРИМЕР ИЗ ГАНЫ

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Abstract

There are no clear-cut regulations in Ghana requiring firms to rotate engagement team members of a clients' audit. However, firms may be actively engaged in the task of rotating engagement team members to reduce risk. Although major accounting scandals have occurred due to failure in the work of audit firms, very little research on internal audit rotation is available. This paper examines the factors affecting the rotation of audit engagement team members, challenges faced by firms in the process of rotating audit engagement team members, and identifies the benefits of audit team rotation to firms. We find that there is more accountability, less risk, and firms (clients of audit firms) benefit more if the members of the audit team are rotated.

Аннотация

В Гане нет четких правил, требующих от фирм ротации членов группы по взаимодействию с аудиторами клиентов. Однако фирмы могут активно участвовать в выполнении задачи ротации членов группы по взаимодействию для снижения риска. Хотя крупные бухгалтерские скандалы произошли из-за сбоев в работе аудиторских фирм, существует очень мало исследований по вопросам ротации внутреннего аудита. В этой статье рассматриваются факторы, влияющие на ротацию членов группы по привлечению аудиторов, проблемы, с которыми сталкиваются фирмы в процессе ротации членов группы по привлечению аудиторов, и определяются преимущества ротации аудиторских групп для фирм. Мы обнаруживаем, что существует больше подотчетности, меньше рисков, и фирмы (клиенты аудиторских фирм) получают больше пользы, если члены аудиторской группы меняются местами.

Keywords: Internal audit, Ghana, audit team members, internal rotation, audit firms.

Ключевые слова: внутренний аудит, Гана, члены аудиторской группы, внутренняя ротация, аудиторские фирмы.

Background Of The Study

The Sarbanes Oxley Act of 2002 ("SOX"), in an attempt to strengthen auditor independence, required the audit engagement partner to rotate from that position after five years and the reviewing partner also has to rotate from that position on the engagement team (Thomas, 2011). This SOX act has subsequently led to other mandatory firm-based rotations in other countries.

A statement released on 3rd April 2014 by the European Union stated that Public-interest entities will be required to change their statutory auditors after a maximum engagement period of 10 years (Commission, 2014). This mandatory audit firm rotation by companies in Europe was a stride made with the premise from the Sarbanes Oxley Act of the United States of America in 2002.

The regulations on mandatory audit firm rotation (especially in the Netherlands) were borne in the early 2000s motivated by the accounting scandals that hit the accounting industry. Major scandals at the birth of the 21st century included the Waste Management scandal, Enron Scandal, WorldCom scandal, Bernie Madoff Ponzi scheme, Instock trading scandal, Tyco accounting scandal, Health South accounting scandal, and many others. However, many countries including the United States of America's SOX require audit firms to rotate audit engagement partners after several years. Although the idea of mandatory audit firm rotation has come up, a firm like Ernst & Young believes that a mandatory audit firm rotation will affect audit quality (Bostrom, 2015). But why would audit firms want to maintain the mandatory audit partner rotation?

The second challenge to external audit continuity is the consequence of mandatory rotation on audit partner retention and career development (US Department of the Treasury, 2008). Certain regulations and norms seek to improve the work of public accountants (Abdul-Kadir et al, 2020), however, such regulations and norms should be put under the strictest of tests to know whether it is a good one, and/or whether it is done in practice in the best of forms to yield the needed results.

The rotation requirement, while well intended, may place the small market companies at a significant disadvantage in securing for their investors the highest quality external audit services (US Department of the Treasury, 2008). The statement made at the Advisory Committee on the Auditing Profession by the US Treasury on February 4, 2008, sends the signal that there are possible challenges and benefits associated with audit partner rotation by and in the audit firms.

The IIA's CBOK study on - Core Competencies for Today's Internal Auditor provides that the internal audit activity must stay updated with the profession while ensuring staff has the adequate knowledge, skills, and experience to provide business organizations with recommendations for change (Bond, 2011). It is in this light and the lack of scholarly work about the area of audit rotation within accounting firms in Ghana that the research seeks to explore even beyond the role of audit team rotation and bring to bear and examine the influencing factors, challenges, and benefits of audit team rotation in audit firms in Ghana.

The objectives of this research are: To examine the factors considered in the rotation of members of audit engagement teams in Ghana; to examine the challenges faced by audit firms in Ghana in the process of rotating audit engagement team members, and to outline the benefits of rotation of audit engagement team members in Ghana.

The findings of this research will be useful to audit firms by providing information on modes of rotating audit engagement team members and why firms need to normalize the practice by outlining its benefits and challenges. This research will also provide feedback on policies (regulations) driving the rotation of audit engagement team members. Thirdly, the research will provide information on the class of audit firms that engage in this practice and this may influence audit regulators and other researchers to pay attention to the phenomenon.

The article first provides an overview of existing literature on the rotation of an engagement team's members by looking at the problem and what exists in the writing of the practice. Subsequently, the article outlines and examines different modes by which

an engagement team's members are rotated and which class of firms is the practice predominant. Finally, the article discusses the findings of the research and its significance to practice and policy.

Audit Rotation

The quality of audit services is defined to be the market-assessed joint probability that a given auditor will both (a) discover a breach in the client's accounting system, and (b) report the breach (DeAngelo, 1981). The audit quality, therefore, influences all that a firm does and may affect the quality of audit the firm seeks to achieve. It is in this direction that (Schauer, 2002) advises that a higher quality audit increases the probability that the financial statements accurately affect the financial position and results of operations of the entity being audited.

However, the idea of a regulatory limitation on auditor tenure is not new. Over the years, it has been considered by a variety of commentators and organizations (Seymour, 2011). Regulation of audit key member rotation literature focuses mainly on the history of audit rotation in the United States of America since the United States of America saw the turn and took the first major steps to regulate audit rotation in the world with the introduction of the Sarbanes Oxley Act (SOX). In this direction, in 1977, in the wake of the Penn Central, Equity Funding, and other corporate scandals, the staff of the Subcommittee on Reports, Accounting, and Management of the Senate Committee on Government Operations, chaired by Sen. Lee Metcalf, published a wide-ranging study of the American "accounting establishment (Seymour, 2011). The study found that the 'Big Eight' and other large accounting firms would readily accept the special stature associated with their designated role as independent auditors, but they would not fully accept the special responsibilities which accompany that position of the independent auditor (Seymour, 2011). This challenge cited by a report from Senator Lee Metcalf reiterated the issue of practice and evidence of accounting firms not abiding by the principle of 'independence' of the auditor.

The journey of audit rotation since 1977 is a clear indication of the long history of recommendations to the problem of independence. Wolf & Hernnanson (2004), in an article in The Certified Public Accountants (CPA) journal, found that the duration of the audit team has a correlation with the propensity of management to commit fraudulent activities: "*when people perform a certain function repeatedly, such as bank reconciliations or setting up new vendor accounts, their capability to commit fraud increases as their knowledge of the function's processes and controls expands over time"* (Wolf & Hernnanson, 2004). This disclosure is a general disclosure to the effects of keeping a person on a particular task or in a particular position for far too long. Familiarity may deliver other problems such as the capability to commit fraud as stated by the authors of the article.

This revelation reiterates one of the major factors that have caused the problem of the lack of independence and therefore the need for audit rotation of key members of an audit if indeed audit quality is to be achieved on an audit. In support, a long association between a corporation and an accounting firm may lead the audit firm generating interests of the client's management and therefore independent action by the audit firm becomes difficult (Seymour, 2011). Besides a long auditor tenure leads to a reduction in audit quality (Carcello & Nagy, 2004).

However, others held that the length of an audit's engagement team positively impacts the audit quality (Hapsoro & Santoso, 2018). Myers et al. did not find any evidence that supports the assertion that audit long tenure leads to low-quality audits (Myers, Myers, & Omer, 2003). It is also the case been made that although statistically the long stay of an auditor negatively affects an auditor's independence, such a case has not been proven statistically and therefore the assertion of fraud due to the long stay of the auditor is inconclusive (Junaidi, Hartono, Suwardi, Miharjo, & Hartadi, 2016).

Mode and Benefits of Internal Audit Rotation

The companies Act of 2019, Act 992 provides in Section 139 Subsection 11 of the Act, that "An auditor shall hold office for a term of not more than six (6) years and is eligible for appointment after a cooling-off period of not less than six (6) years" (Act992, 2019).

The research seeks to focus on how the audit engagement team rotation is done in Ghana, what factors influence, what benefits are derived, and the challenges faced in the process of rotating audit team members in audit firms. "I believe that audit partner rotation will have a greater impact on small to mid-sized public accounting firms, and, consequently, small to mid-sized publicly-traded companies, as their markets may not support the scale necessary to ensure seamless rotation" (US Department of the Treasury, 2008).

Firm or key partner rotation has benefits to the audit firms, the client and also influences positively the audit quality (Emua, 2017). Since the tenure of the engagement team would be limited, the auditor's incentive for resisting pressure from management would be increased (Seymour, 2011). Pressure from familiarity is not easy to resist and therefore a rotation of key audit members will benefit the audit quality, and provides protection and control from been easily influenced. The lifting of the incentive from auditors working on an audit so that the independence of the audit members is not affected (Cameran, Prencipe, & Trombetta, 2016) is a major benefit of the rotation.

The new audit team leader would bring a fresh viewpoint (Seymour, 2011) which would take time for the management of the audit client to become familiarized with. The style of leadership and performance of the task by the new audit team leader or member would likewise affect any attempt of management of the client to influence the audit work been performed.

Another benefit is that the longer the tenure of the engagement partner, and any other member of the audit engagement team of the client, the greater the discretion to be exercised by the management of the client (Ameyaw, 2018). The opposite is true because,

in the initial years of tenure of a new audit partner, the client manager's accounting discretion decreases (Fargher, Lee, & Mande, 2008).

An audit firm that rotates audit engagement team members would provide greater challenges to senior personnel through exposure to new assignments (OAGC, 2018) and would also provide a broad learning environment for junior personnel to train and grow on the job which would increase their expertise.

Challenges of Internal Audit Rotation

Beyond the benefits, there are challenges to the practice of rotating key members of an audit. Rotation would considerably increase the costs of audits because of the frequent duplication of the start-up and learning time necessary to gain familiarity with a company and its operations (Seymour, 2011) which are necessary for an effective audit."

Also, the rotation of key members may be costly mostly in terms of time to settle in and understand the new environment of the new client (Juneja, 2021). The point has also been reiterated in the CPA journal when (Nashwa, 2004) held that rotation would increase the number of audit and financial reporting failures. Financial reporting failure may also lead to fraud, accounting failures scandals, and subsequent liquidation of both accounting and client firms as has been evidenced in history such as the Enron scandal. Enron Corporation had more than $49 billion in total assets for 2001 and was listed as the seventh-largest U.S. Corporation (ranked by revenues in 2000) by Fortune magazine, filed for Chapter 11 reorganization protection on December 2, 2001, in the United States of America (Anderson, 2002). Also, the cost component of training and briefing members before rotation may discourage firms from rotating although rotation of the lead partner is mandatory in Ghana.

In the study of cases of substandard performance by auditors, several of the problem cases were first- or second-year audits (Seymour, 2011). This is indicative of the fact that the firm should have a clear strategy. A strategy that works and which would improve audit quality to the benefit of all stakeholders of the audit should be instituted

and communicated on time for the audit committee to be able to assess and provide additional risks which the audit partner may not have identified (SEC, 2013). Even at the state level, Spain adopted the system of mandatory audit rotation but has since abandoned the policy (Cameran, Di Vincenzo, & Merlotti, 2005).

Due to the possibility of the occurrence of fraud the auditor's attitude of professional scepticism is particularly important when considering the risk of material misstatement due to fraud (CICA, 1995). Identifying and especially declaring material misstatement is crucial to giving an objectively accurate audit opinion on the accounts of a client company. Independence and professional scepticism cannot be separated. Continuous updating of the capability assessment and response is warranted (Wolf & Hernnanson, 2004) and therefore the rotation of key members of an audit should be a continuous and never-ending cycle although the need to be circumspect and have a structure is very crucial to achieving success.

This research focuses on key audit team members and not just the lead partner although literature focused on the "lead partner rotation" has been used due to its significance to the study.

Research Methodology

The purpose of this study is to examine the implications of internal audit rotation of engagement team members on an audit. To achieve this purpose, it became necessary to accomplish some prerequisite objectives. To go ahead with the research, we developed structured interview questions and used them as the basis for obtaining data from respondents. The questions solicited answers from respondents.

Data collected for the research was obtained from audit firms and some individual auditors/audit team members to meet the objectives of the research and obtaining answers to the questions posed under the research. The data was collected from ten (10) firms of which two (2) firms were A+ ranked firms under the 2014 Institute of Chartered

Accountants – Ghana rankings of Audit firms (ICAG, 2014); four (4) were B ranked and the remaining four (4) were lower-ranked firms and individual audit personnel.

This research is qualitative research to examine and explain the internal rotation of audit engagement team members in audit firms in Ghana. With qualitative research, Emphasis is on an in-depth description of an individual, group, situation, or organization (Mouton & Marais, 1990). The research, therefore, focuses on individuals in audit firms.

It is in this view that, the sample for this study was narrowed to firms in the Greater Accra Region (Accra – the capital of Ghana). In 2014, out of the 208 audit firms registered in Ghana, only about 15% were outside Accra including Tema (ICAG, 2014). However, our study cannot cover all those in Accra and therefore 10 firms out of the firms in Accra were targeted as the sample for this study. The 'Big 4' and 6 other firms were targeted for interviews with senior staff. This selection for a sample provided a better conclusion since that gave the sample a much better balance for purposes of generalization.

Table 1: Data Source

Data items	**Interviews**	**Reports, Manuals and laws**	**Articles and Books**
	10	**9**	**16**
Description of Data	Key actors and target group: Representatives from ten (10) audit firms in Accra. Two (2) of the 10 were from the 'Big 4'. These were PricewaterhouseCoopers (PwC)and Deloitte. The six (6) included Baker Tilly Andah & Andah and Ernest Dawlah.	The Companies Act 2019 (Act 992) of Ghana (1); US Treasury Department report (1); Office of the Auditor General of Canada Performance Audit Manual (1); Securities Exchange Commission-US (1); Public Company Accounting Oversight Board (2); Manuals (2); Reports (1)	Journal Articles (11); Web Articles (2); Books (2); Statements (1);

Type of information provided	Reasons, mode, benefits, and challenges of rotating audit engagement team members. The behaviour of organizations to audit rotation and why audit firms to it although they are not obliged to do it.	The laws and modes of best practice presented by regulatory authorities. Also includes reports and meeting, and revelations of the common practice of audit rotation by firms within the jurisdiction of the regulatory authorities	Data on the mode, benefits, and challenges of rotations from limitations from existing literature. Provided a basis for the research.
Limitations of the data	Data collected were limited to firms in Accra since the number of audit firms in Accra makes up about 85% of audit firms in Ghana.	Mainly from other countries, but helped in giving an understanding to common practice in the world.	Direct mention of Ghana was limited

FINDINGS

The responses received from respondents during the interviews make up this section of the article. The responses were based on questions put forth to respondents and are categorized to achieve the objectives of the research.

In the area of qualification to lead an audit engagement team, all firms had set the minimum of a professionally qualified chartered accountant with requisite knowledge and experience in the field of accounting.

Mode of Internally Rotating Audit Team Members

Top four firms like Pricewaterhouse Coopers listed its Risk Management Department as the department in charge of the rotation of engagement team members. However smaller firms like Ernest Dawlah, and Baker Tilly Andah and Andah listed the Managing Partner as in charge of such rotations. This is the case in smaller firms because of the problem of team members not wanting to be rotated although it is a policy of the company.

Concerning the question posed on the mode of rotation - “In which manner does the firm rotate key members of an audit team?” Respondents said that rotation depended on two (2) factors. These were:

- The number of years for which a person has served in a role.
- The rank, experience, understanding, and knowledge in the client’s field of work.

No clear-cut pattern of rotation was evident except that the number of years was used with no other requirement fixed. The number of years an engagement team member may be rotated from a particular engagement included 2 years, 3years, and 4 years. However, for large firms, it was dependent on the type of industry. PricewaterhouseCoopers and Deloitte listed a maximum of seven (7) years for Public interest entities and high-profile clients; maximum of ten (10) years for Non-Public interest entities; and for other teams’ rotation is accomplished through promotion of staff over the years.

Factors Considered In Internal Audit Rotation

Respondents gave similar responses to why the need for audit rotation. The responses were usually positive factors that necessitated the need for such rotation. Interestingly none of the responses cited regulation or law as a factor. The responses included:

- To address the familiarity threat to objectivity from long association with clients
- To have a fresh, objective, and critical approach to the recurring assurance engagement
- To provide an opportunity to take a new look at our clients’ enterprise, issues, and problems and bring onboard new ways of contributing to their success
- Rotation is done for training purposes
- Rotation is done to mitigate ethical standard threats

Benefits of Internal Audit Rotation

The advantages of rotation of audit team members to the firm received from respondents, included:

- to have a workforce with diverse knowledge across industries'
- to have a fresh, objective, and critical approach to the recurring assurance engagement
- to provide an opportunity to take a new look at the entity's enterprise (clients' enterprise)
- by undertaking audit assignments in various industries, staff gain more training and expertise
- to reduce the threat to familiarity.

These advantages along with the factors above motivate firms to rotate team members. It is also important to note that respondents cited no disadvantages or negative effects to rotating audit engagement team members to the firm. With this in mind, it is no surprise that all respondents said yes to the rotation of audit engagement team members even though no law exists to oblige audit firms to rotate engagement team members.

Challenges of Internal Audit Rotation

Although there were no negative effects to the audit firm doing the rotation, challenges were however cited by respondents. These challenges were however linked to the enforcement of the rotation but were viewed by firms as challenges and not significant enough to be seen as negative effects. These included:

- Resistance to change by client staff due to the need to build a new relationship with the audit team members
- Development of a learning curve
- The potential loss of client
- No challenges since all are rotated
- Learning of client's system all over again

- New members of the engagement team have to learn the entity and its environment all over again whereas outgoing team members are well vest in the systems of the client

The potential loss of a client brings to bear a major challenge. It means that clients are not welcoming to the issue of rotation of engagement team members and this is very worrying. The challenge of new engagement team members having to learn about the client and its environment including the industry and then apply that to the work been done dominated discussions on the challenges. This is however unavoidable. And it is worse for inexperienced personnel or first-timers to the particular industry they are been transferred to.

Discussion

The findings provided in this paper sought to meet the objectives of analyzing the practice of rotation of audit engagement team members in Ghana by identify the challenges and benefits and associated with the mode of rotation of engagement team members. As was identified in the responses obtained, there are no clear-cut regulations in Ghana requiring firms to rotate engagement team members of a clients' audit. However, to mitigate the threat of familiarity and balancing with the need for the performance of audit, firms are actively engaged - as indicated by the respondents of this research study, in the task of rotating engagement team members with departments such as the Risk Department handling that task in big firms, and the Managing Partner or Engagement Team Leader performing that task in smaller firms. This shows the seriousness to which firms consider the task of rotation of engagement team members on each audit.

Mitigating the threat of familiarity was a reason stated by all respondents as to why the firm rotates audit team members. This is not surprising because the threat of familiarity was also cited in the events leading to the enactment of the Sarbanes Oxley Act (SOX). Professional accounting institutions consider the threat of familiarity in

making rules, and regulations as well as setting standards for accountants and the accounting profession (IESBA, Strengthening Safeguards Against Familiarity Threats, 2012)

Rotating engagement team members serves as a training ground for members of the engagement team and provides firms with an increased pool of individuals who are knowledgeable and have experience in the audit of multiple industries (IESBA, 2013). Also, as indicated by Ernest Dawlah Chartered Accountants and Management Consultants, new ideas and fresh strength are brought into the engagement team to improve its work.

There are however challenges to the rotation of audit engagement team members. As indicated from the respondents to this research, the time needed by new members to learn about the client and its environment; less expertise on the part of new members; disagreements with the client and/or audit member rotated and a potential loss of the client.

Also, all respondent firms indicated that they appoint only chartered accountants with the requisite knowledge to lead engagement teams. The Companies Act, 2019 - Act 992 stipulates that all companies registered under the law, regardless of size or public interest level, must be audited by auditors registered with the Institute of Chartered Accountants Ghana (ICAG) (ifac, 2021). Rotation is also done depending on the industry with a maximum of ten (10) years for some industries if audited by big firms. Smaller firms set between 2 to 5 years with no consideration based on the industry or the type of firm.

Managerial Implications

Rotation of audit engagement team members is relevant and a necessary task been undertaken by audit firms in Ghana. Also, a cap on the maximum number of years an individual can stay on a particular engagement team is necessary to mitigate extensively the threat of familiarity.

Also, firms should consider the industry in which their clients operate, the quality and experience of the new member to be introduced to their team, the size and complexity of the client, and use that as a guide in rotating members. These should be added to the major factor of the number of years a person stays on the engagement team. This would provide better results compared to the current practice of smaller firms where only the number of years is considered. Furthermore, firms should analyze the results of their rotations among the various engagement teams. If this is done, each firm will be able to improve on its factors considered and the pattern of rotation.

Again, clients should be made to understand the need for rotation. If rotation is governed by legislation, challenges and disagreements may not arise between the audit firm and the client. The firm will also not be faced with the challenge of losing a client and/or keeping members who may pose familiarity threats due to disagreements with the client.

Limitations and Avenues for Future Research

Concerning the sample chosen for the study, the research met several challenges which prevented the achievement of the targeted sample for responses. Out of the four big four (4) firms, responses were obtained from only two – PricewaterhouseCoopers (PwC) and Deloitte. The other eight responses were obtained from other firms including Baker Tilly Andah & Andah and Ernest Dawlah Chartered Accountants and Management Consultants. The mode of data collection was also restricted to structured interview questions. Responses were received via answering the interview questions on paper and through phone interviews. This challenge was caused primarily due to time constraints and the preference of firms for these methods over the face to face interviews.

We believe that future research can collect significant data and apply a quantitative research technique to identify the influence of internal rotation on firm performance. This will expand the study even further and may have a wider theoretical contribution.

Conclusion

It is understood from the study that firms are actively engaged in the practice of rotating engagement team members to achieve audit quality. This has provided benefits far exceeding the limited challenges faced in the practice. Firms have also chosen departments and individuals with the requisite knowledge in handling such rotation. This shows the importance of the practice. The recommendations above if enforced will lead to success to the benefit of the firm, client, and the accounting profession in Ghana.

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