INFORMAL CONSULTATION IN PUBLIC ACCOUNTING: A STRATEGIC VIEW AND AN EXPERIMENTAL INVESTIGATION

BY

JON DOUGLAS PERKINS

B.S.Acc., University of Missouri at Columbia, 1991
B.S.B.A., University of Missouri at Columbia, 1991
J.D., University of Missouri at Columbia, 1995

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JON DOUGLAS PERKINS

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THE DEGREE OF DOCTOR OF PHILOSOPHY

Mark Peecher
MARK PEECHER — **Director of Thesis Research**

Ira Solomon
IRA SOLOMON — **Head of Department**

Committee on Final Examination†

Ira Solomon
IRA SOLOMON — **Chairperson**

Mark Peecher
MARK PEECHER

Bryan Cloyd
BRYAN CLOYD

Janet Sniezek
JANET SNIEZEK

†Required for doctor's degree but not for master's.

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TABLE OF CONTENTS

CHAPTER 1 INTRODUCTION 1

CHAPTER 2 THEORY AND HYPOTHESIS DEVELOPMENT 5
INFORMAL CONSULTATION IN PUBLIC ACCOUNTING 5
TYPE OF ACCOUNTABILITY 10
KNOWLEDGE OF JUSTIFIEE PREFERENCES 11
CHOICE OF ADVISOR(S) 12
Ignorance of Justifiee Preferences 13
Knowledge Only of the Justifiee's Outcome Preference 16
Knowledge Only of the Justifiee's Process Preference 18
ACCOUNTANTS' INFORMATION DOCUMENTATION 21
SUPERVISORS' EVALUATIONS OF SUBORDINATES' CONSULTATION BEHAVIORS 23

CHAPTER 3 METHOD 26
EXPERIMENT ONE 26
Design, Instrument, Task, and Administration 26
Dependent Variables 27
EXPERIMENT TWO 28

CHAPTER 4 RESULTS 31
EXPERIMENT ONE 31
Subjects, Manipulation Checks, and Descriptive Statistics 31
Tests of Hypotheses 32
Consultation Balance and Extent of Consultation 32
Information Documentation 34
EXPERIMENT TWO 35
Subjects and Descriptive Statistics 35
Tests of Hypotheses 35

CHAPTER 5 CONCLUDING REMARKS 38

REFERENCES 42

APPENDIX A PAPER INSTRUMENT FOR EXPERIMENT ONE 50

APPENDIX B INSTRUMENT FOR EXPERIMENT TWO 76

APPENDIX C FIGURES, EXHIBITS, AND TABLES 87

APPENDIX D COMPUTER INSTRUMENT FOR EXPERIMENT ONE 104

VITA 105

CHAPTER 1

INTRODUCTION

I present a theory of informal consultation in public accounting and report an experiment investigating the joint effect of accountability type and knowledge of a justifiee's preferences on accountants' informal consultation and information documentation behaviors.[1] While informal consultation can help accountants improve the defensibility of and/or better justify their decisions (Gibbins and Emby 1985; Gibbins and Mason 1988; Jamal 1997), strategic informal consultation may impair accountants' efficiency and effectiveness.[2] Efficiency may be impaired (at least in the short term) when accountants employ informal consultation as a strategic vehicle for revealing their knowledge. Ineffectiveness can emerge when accountants informally consult with others expected to agree with a preferred, albeit tenuous, conclusion. Further, a false sense of consensus may obtain and compound the risk of ineffectiveness. For example, others who are unaware of the false consensus may also over-rely on the original accountant's tenuous decision, potentially leading to adverse legal, economic, and/or social consequences for accountants and their firms.

Several psychology studies examine individuals' informal consultation processes (see e.g., Cooper and Sniezek 1999; Harvey and Fischer 1997; Harvey, Harries, and Fischer 2000; Heath and Gonzalez 1995; Sniezek and Buckley 1995). Inconsistent with most accounting contexts, however, these studies use highly structured tasks featuring incentives that motivate participants to focus predominantly or exclusively on the normative accuracy of their decisions.

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[1] "Justifiees" are persons to whom accountants ("justifiers") must justify their judgments or decisions (Peecher 1996).

[2] In this dissertation, I define effectiveness as producing a defensible result and I define efficiency as producing a defensible result with a minimum expense of resources.

Moreover, most of these studies do not manipulate nor measure accountability or justification.[3] I extend the prior accounting and psychology literatures on accountability and consultation by investigating informal consultation mediated by a theory of strategic, adaptive behavior. Key elements of my theory are that the extent to which and how individuals adapt will vary based on factors such as justifiee preferences and institutional constraints. For example, tax accountants and other professionals (e.g., attorneys), who are permitted by professional regulations to advocate client-preferred positions, may be expected to exhibit more strategic consultation behaviors (e.g., select particular advisors to obtain a consensus opinion) than one would expect from external auditors or others whose professional regulations prohibit or discourage such behavior.

Accounting professionals and students participate in an experiment designed to investigate the effects of accountability type (process versus outcome) and knowledge of the justifiee's outcome or process preference in an ambiguous tax context on accountants' informal consultation behaviors (namely consultation balance and extent of consultation[4]) and information documentation.[5] Specifically, I give participants an ambiguous tax problem and ask them to provide an initial tentative estimate of the probability that a taxing authority would uphold the client's preferred tax reporting position.[6] Participants tentatively decide whether to recommend that the client adopt that position and then choose from a menu of advisors with whom they

[3] Harvey and Fischer (1997) note that there may be reasons for consultation other than improving accuracy. However, they studied how individuals use advice given to them, not advice seeking, and they do not manipulate social variables or discuss accountability.

[4] I define consultation balance as selecting an equal set of advisors on both sides of an issue in a non-systematic order. I define extent of consultation as the amount of resources consumed in an individual's consultation process. These resources could include number of advisors consulted, time spent consulting, and/or a monetary cost of consultation.

[5] I focus on accountability to a superior in this dissertation. While my theory generalizes to other types of justifiees, in this dissertation I do not address accountants' informal consultation when faced with accountabilities to multiple justifiees.

[6] I choose a tax setting because I believe it is a setting in which accountants are likely to exhibit the strategic, adaptive behavior I theorize occurs in the presence of differing types of accountability and knowledge of justifiee preferences.

could consult. After consulting with up to six advisors, participants write a brief memorandum in which they state and justify their final judgments. Finally, participants complete a post-experimental questionnaire about their consultation processes, manipulation checks, and basic demographics. Consistent with expectations, participants' accountability type and knowledge of justifiee preferences jointly affect their informal consultation and information documentation behaviors. Specifically, participants generally engage in more balanced consultation, consult more advisors, and engage in less information stylization when held accountable for their decision-making processes, but only when they do not know the justifiee's preferences or when the justifiee's process preference for effectiveness is known. These findings suggest that accountants do strategically adapt their consultation and information documentation processes in response to justification pressures in the accounting environment.

I also investigate the effect of accounting subordinates' informal consultation behavior. In a second experiment, I ask managers and partners to rate the performance of six hypothetical process-accountable subordinates. Three of the subordinates knew their superior's effectiveness preference and three of the subordinates knew their superior's efficiency preference. The only difference between the subordinates in each set is the balance of their informal consultation behavior. As expected, participants' performance ratings are found to be consistent with subordinates' consultation balance; the more balanced the consultation, the higher the performance rating. This finding suggests that knowledge of subordinates' consultation behaviors affects superiors' performance evaluations and that process accountable subordinates are evaluated, at least in part, on the balance of their consultation processes.

I structure the remainder of the dissertation as follows. In Chapter 2, I develop the theory and hypotheses. In Chapter 3, I describe the experimental method, including the design, task,

and independent and dependent variables. I present the results in Chapter 4. In Chapter 5, I provide concluding comments, including an overview of the study and its implications, and I provide suggestions for future research.

CHAPTER 2

THEORY AND HYPOTHESIS DEVELOPMENT

INFORMAL CONSULTATION IN PUBLIC ACCOUNTING

Accountants are regularly accountable to multiple parties with various goals and preferences (Gibbins and Newton 1994, Jensen 2000).[7] These parties include clients, shareholders, regulatory agencies (e.g., Internal Revenue Service, Securities and Exchange Commission, etc.), professional organizations (e.g., American Institute of Certified Public Accountants), and superiors within the firm. The goals and preferences of these various parties, however, may conflict or be unknown (Farmer, Rittenberg, and Trompeter 1987). As a result, accountants may engage in information search strategies such as *external discovery* (gathering additional information to find out the position(s) of other persons) and/or *self-support* (gathering additional information to support their initial judgment or decision) (Gibbins and Newton 1994). Informal consultation with other persons is one way accountants can pursue these two strategies. Further, based on attribution theory (Fischhoff 1976; Kelly and Michela 1980), Brown and Solomon (1987) show that evaluatees are held less responsible for outcomes when they secure inputs from other persons (e.g., an assessment of prior probabilities).

Consultation traditionally involves individuals with responsibility for decisions drawing on others' opinions or judgments as inputs into their decision-making processes. One survey indicates that 78 percent of approximately 500 audit and tax managing partners of then Big-6 accounting firms seek advice on a regular basis before making decisions (Sailors, Sylvestre, and Windal 1993). Another survey reports that 93 percent of accountants frequently consult with

[7] People generally are regarded as accountable if they expect to be asked to justify their actions or beliefs to one or more persons (Tetlock 1983, 1985, 1992). For a review of both the positive and negative effects of accountability on judgment and decision making, see Lerner and Tetlock (1999).

other accountants before making decisions (Gibbins and Emby 1985). In a third survey of 70 accounting professionals, all but two stated that they consulted other accounting professionals before making judgments in ambiguous judgment and decision-making situations (Gibbins and Mason 1988).[8] Finally, one author argues that not consulting in high-risk situations is "tantamount to not exercising due care" (Hackenbrack 1997, 127).

Despite such prevalence, consultation does not take place as often as some would like. In a review of the way accounting firms perform audits, the Public Oversight Board's Panel on Audit Effectiveness noted that 13 percent of the audit engagements they examined involved issues for which they felt consultation with other members of the firm would have been prudent but did not occur (POB Panel on Audit Effectiveness 2000, §2.105).[9] The Panel went on to recommend that audit firms further emphasize to their members the importance of consulting on important issues (POB Panel on Audit Effectiveness 2000, §2.107).

Two principal dimensions distinguish informal from formal consultation – autonomy and observability. The degree to which these variables are present does not determine whether consultation is formal or informal; it merely places consultation on a continuum between the two. Autonomy in consultation refers to an individual's ability to choose when and who to consult. Public accounting firms mandate formal consultation in certain situations. In a formal consultation restrictions typically exist for accountants' choice of consultant and these restrictions usually require accountants to follow the advisor's decision.[10] In contrast, in an informal consultation the consultation process and choice of consultant are not pre-specified. Observability in consultation refers to the public nature of the consultation. Formal consultation

[8] The two accounting professionals who did not regularly engage in consultation were sole practitioners.
[9] The POB Panel did not specify whether they were referring to formal or informal consultation. However, both types of consultation provide opportunities for the types of strategic behaviors investigated in this paper.
[10] An example of formal consultation is discussion with a firm specialist (e.g., a specialist in taxation of oil and gas properties) as required by a supervisor or by firm policy due to the nature of the issue at hand.

is generally more public than informal consultation because it is usually mandated by firm policy and firms generally charge the client for time spent consulting.[11] Informal consultation is less likely to be charged to the client, is not necessarily mandated by firm policy, and therefore is not necessarily observable to other members of the firm (notably superiors and other potential justifiees).

Furthermore, in contrast to informal consultation, formal consultation is less likely to take place in the accountant's local office. In their survey of 86 accountants regarding communication of specialized knowledge within public accounting firms, Danos, Eichenseher, and Holt (1989) found that while consultation with accountants in other offices or the firm's national office is important, consultation with accountants in the decision maker's local office takes place much more frequently. Also, in many instances, accountants considered this process to be more important than consultation with accountants outside the local office (Danos et al. 1989). Therefore, in comparison to formal consultation, informal consultation is probably as important and more common.

Even though informal consultation is evidently perceived as a mechanism for improving accountants' judgments and decisions (Gibbins and Emby 1985; Kennedy, Kleinmuntz, and Peecher 1997; POB Panel on Audit Effectiveness 2000), its lack of structure allows accountants to use it as a method of strategic behavior (Rich, Solomon, and Trotman 1997). For example, accountants may engage in informal consultation to demonstrate their knowledge of a particular subject to other accountants. Accountants may also consult with their supervisors to determine their preferred outcomes so that they can change their decision-making process (or even their

[11] While consulting time may be charged to the client by advisee and/or the advisor, anecdotal evidence suggests that if charged, it is more likely for the advisee to do so.

decision) to agree with the supervisor's preferred outcome or to justify their decision to the supervisor.[12]

This strategic use of informal consultation can have adverse effects, however, on the efficiency and effectiveness of accountants. It can adversely affect efficiency when accountants use informal consultation to "show" their knowledge instead of to improve the accuracy or defensibility of their decisions. It can also impact effectiveness in cases when strategic informal consultation gives accountants a false sense of consensus for their decision. This situation could cause accountants to become overconfident about that decision, and in turn, could lead to adverse legal consequences for the accountant and/or the accountant's firm.[13]

Informal consultation is also a mechanism accountants can use to improve both the accuracy and the justifiability of their decisions and the processes they use to arrive at those decisions. In general, psychology studies have found that consultation increases decision-making accuracy for well-structured, simple tasks that have clear-cut normative answers (see e.g., Harvey and Fischer 1997; Pritchard and Sniezek 1995; Yaniv and Kleinberger 2000).[14] However, many accounting decision-making settings are ill-structured and ambiguous (e.g., application of the complex accounting rules for business transactions and interpretation of dense sections of the Internal Revenue Code). Additionally, a lack of consistent outcome feedback

[12] Accountants may also act strategically in formal consultation situations. However, due to limited advisor choices and because formal consultation generally takes place with someone other than peers or direct supervisors, the opportunities to engage in strategic formal consultation as well as the benefits of such strategic consultation likely are much less than for informal consultation.

[13] I do not examine the relative degrees to which informal and formal consultation are inefficient or ineffective. Informal consultation can be a more efficient and effective use of firm resources in cases where questions are more routine in nature (i.e., a question about a basic tax code section or about a basic analytic procedure). In these instances, requiring the use of formal consultation would require firm specialists spending more time on basic questions instead of more complex issues. Further, even if informal consultation is inefficient in the short term, it may be efficient in the long term as a signal of knowledge to colleagues that may increase the efficiency (and maybe even effectiveness) of future auditing or tax engagements.

[14] Examples of these types of tasks include answering questions such as "What is the national flower of Scotland?" and "How many calories are in a single slice of cheese pizza?" (see e.g., Sniezek and Buckley 1995; Cooper and Sniezek 1999). For a study that does not find a relationship between the use of consultation and judgment/decision accuracy, see Heath and Gonzalez (1995).

results in a lack of clear-cut "best" answers (Ashton, Kleinmuntz, Sullivan, and Tomassini 1988; Shields, Solomon, and Jackson 1995; Solomon and Shields 1995). As a result, contingent decision-making theory and motivated reasoning theory suggest that this ambiguity, lack of outcome feedback, and the multiple accountabilities noted earlier interact to shift an accountant's objective function from a focus on making the most accurate decision (i.e., "searching for truth") to a focus on making an acceptable or defensible decision (Beach and Mitchell 1978; Kunda 1990; Peecher 1996). A decision may not be the most accurate in that it may not fully agree with the generally accepted (consensus) view but is acceptable to a justifiee (e.g., a client who wants to take a certain tax reporting position) and/or defensible to another justifiee (e.g., a regulatory body that may allow a range of possible views).[15]

Accountants may also use consultation to accomplish other goals. For example, consensus is a common surrogate for accuracy.[16] Accountants, therefore, could use informal consultation to determine a consensus opinion of the most accurate answer to the problem and thereby improve the "perceived" accuracy of their judgments or decisions. Accountants may also use consultation as a means of inoculating themselves against the negative consequences of their decisions by "spreading the risk" to those advisors whose opinions coincided/agreed with their own (Heath and Gonzalez 1995). In other words, accountants might consult until they reach a consensus opinion and then use that consensus as a justification for that decision. Finally, accountants likely use the consultation process itself as a justification or defense for a decision arising out of that process.[17]

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[15] Not all accurate decisions are defensible, however, as justifiees may have preferred reporting positions and may not be interested in identifying the most accurate position, but rather knowing whether they can support their preferred reporting position.

[16] The results of several accounting studies suggest that consensus is often a good surrogate for accuracy in accounting judgment and decision making (Ashton 1985; Davis, Kennedy, and Maines 2000; Pincus 1990).

[17] This discussion of the possible uses of informal consultation does not mean that informal consultation comes without a cost. Lee (1997) suggests that possible negative consequences of seeking help include a perception by

The above uses of informal consultation are likely to differ based upon at least two factors (as shown in Figure 1): (1) the method used by justifiees to evaluate accountants (based predominantly on accountants' decision-making processes versus on the outcomes)[18] and (2) knowledge of the justifiee's preferences for ultimate outcomes or for the decision-making processes used to arrive at those outcomes.[19]

TYPE OF ACCOUNTABILITY

Justifiees evaluate accountants who are predominantly process accountable ("PA accountants") based on the quality of the decision-making process used to arrive at an outcome more than on the quality of that outcome (Siegel-Jacobs and Yates 1996). While the quality of the decision-making process and outcome are generally correlated, the definition of decision-making quality (or accuracy) is context-dependent (Kruglanski 1989). Prior psychology research suggests that imposition of process accountability improves decision-making quality as follows: (1) it results in more complex and analytic information processing (Chaiken 1980; Hagafors and Brehmer 1983); and (2) it encourages the use of more information in decision making (Tetlock 1983; Tetlock and Boettger 1989). I, therefore, expect PA accountants to consult and use attributes of their consultation processes as justifications for their decisions.

Accountants who are predominantly outcome accountable ("OA accountants"), on the other hand, are evaluated on the quality of the outcome of their decision-making process more than on process quality (Siegel-Jacobs and Yates 1996). Prior psychology research suggests,

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others of incompetence and dependence on other people. These consequences can result in poor impression management. I do not investigate these possible costs in this dissertation.

[18] These two forms of accountability are not mutually exclusive.

[19] Reasons for informal consultation also likely vary based on other factors including the accountant's position in the firm. For example, a staff person may seek consultation as a training tool, while a partner may use consultation to spread risk to other partners. However, I only investigate the two factors noted above in this proposal. For more discussion of factors influencing accountants' informal consultation behaviors, see Perkins (2000).

however, that imposition of outcome accountability results in a decrease in decision-making quality (see e.g., Adelberg and Batson 1978; Arkes, Dawes, and Christensen 1986). Because of the OA accountant's focus on outcomes, I expect them to consult with other advisors to justify a desired outcome.

KNOWLEDGE OF JUSTIFIEE PREFERENCES

The use of informal consultation by accountants likely also differs based on their level of knowledge about the justifiee's preferences (Baumeister and Leary 1995). Knowledge of the justifiee's preferences is continuous. For example, one accountant may have knowledge about a justifiee's preferences because of access to additional information about a justifiee. In this study, "ignorance" of the justifiee's preferences refers to a relatively low level of information regarding those preferences while "knowledge" of the justifiee's preferences refers to a higher level of information regarding those preferences. If the justifiee's preference is known or easily guessed, accountants likely shift their preferences towards the justifiee's preference, a well-established behavior called the *acceptability heuristic* (Tetlock 1983, 1985; see e.g., Buchman, Tetlock, and Reed 1996; Cuccia, Hackenbrack, and Nelson 1995; Hackenbrack and Nelson 1996; Hoffman and Patton 1997; Peecher 1996; Tan, Jubb, and Houghton 1997).[20] When accountants adopt this practice, they are satisficing, i.e., looking for an acceptable decision process or outcome as opposed to the "best" process or outcome (Beach 1990; Ganzach 1993). In such instances, accountants could seek informal consultation to justify using a process or reporting an outcome aligned with the justifiee's to win approval.[21] If ignorant of the justifiee's preference,

[20] Preference shifting may well occur even if the accountant wants to remain objective (Camerer, Loewenstein, and Weber 1989), and even when its use produces relatively poor judgments or decisions (Adelberg and Batson 1978).
[21] Previous psychology research suggests that desire to win someone's approval is a powerful motivation in human judgment and decision-making (see e.g., Baumeister 1982).

accountants may engage in *preemptive self-criticism* (Tetlock 1983; Tetlock, Skitka, and Boettger 1989), a more balanced and complex type of information processing designed to anticipate potential arguments against the processes used or their outcomes (see e.g., Chen, Shechter, and Chaiken 1996; Ashton 1990; Johnson and Kaplan 1991; Koonce, Anderson, and Marchant 1995; Lord 1992; Tan 1995). Accountants who are ignorant of the justifiee's preference sometimes use this type of informal consultation to validate their processes or outcomes if and when justifiees disagree (Jensen 2000).

Further, because of competing economic and professional pressures, justifiees may have differing preferences regarding preferred decision-making processes (Dirsmith and Covaleski 1985; McNair 1991). For example, superiors concerned about litigation may prefer that subordinates focus on an effective process. In contrast, superiors concerned about budgetary constraints may prefer that subordinates focus on efficient processes. Peecher (1996) found that partner preferences for effectiveness and efficiency affect how likely auditors are to believe client explanations for unusual fluctuations. Bierstaker and Wright (1999, 2000) also report that auditors change their time budgeting behavior based on partner preferences for efficiency or effectiveness. Therefore, it is probable that these different partner preferences also affect accountants' informal consultation processes.

CHOICE OF ADVISOR(S)

Once accountants decide to engage in informal consultation, they must select advisor(s). A number of cues likely influence advisor selection including the advisor's actual and perceived level of task-specific expertise (see Harvey and Fischer 1997), the likelihood of agreement with

the accountant's tentative assessment (a "yes man" or "devil's advocate"), or similarity to the accountant in terms of personal characteristics (see Kadous, Kennedy, and Peecher 2000).[22]

Ignorance of Justifiee Preferences

As noted, PA accountants use the consultation process to justify their decision processes. Consequently, they are likely to engage in pre-emptive self-criticism and seek balanced advice (i.e., seek advice from persons who are apt to agree and disagree) to show that they have investigated multiple points of view and thus, have engaged in a more comprehensive overall decision-making process. Because they are secondarily interested in buttressing their decisions and primarily interested in objectively evaluating and documenting possible arguments for and against their decisions, such accountants are likely to consult with a more heterogeneous set of advisors than OA accountants.

Previous psychology research suggests that PA accountants will seek more balanced advice to evaluate and document possible arguments for and against their hypotheses (Chaiken 1980; Hagafors and Brehmer 1983; Siegel-Jacobs and Yates 1996). Psychology research also suggests that OA accountants will consult to justify preferred outcomes. Since these accountants likely will use the acceptability heuristic, they will seek outcome consensus and will be disinclined to obtain advice likely to contradict the justifiee's preferred outcome. Soll (1999) and Kadous et al. (2000) suggest and find that when judges are interested in supporting a particular conclusion, they are motivated to consult advisors who likely support that conclusion. OA accountants may also desire redundant sources of information because they ostensibly want

[22] Another important cue might be the type of work relationship the advisor has with the accountant (i.e., a reviewing superior, peer, subordinate, etc.). One recent study found that auditors were generally unable to predict auditors' choices at a rate any better than chance (Jamal and Tan 2001). However, in that study the authors matched participants with the auditors whose choices they predicted. In informal consultation, accountants are free to choose their advisors. If accountants act strategically, they are more likely to limit their set of possible consultants to persons whose actions/preferences are predictable.

to demonstrate consensus by showing that multiple others agree with them (Festinger 1954; Frey 1986). Therefore, OA accountants will consult to build consensus and seek imbalanced advice in order to support their preferred outcome.

When the justifiee's views are unknown (e.g., when the justifier is on a new assignment), justifiers likely attempt to guess the justifiee's views and employ the acceptability heuristic (Siegel-Jacobs and Yates 1996; Weigold and Schlenker 1991; Zanna and Sande 1987). Siegel-Jacobs and Yates (1996) found that PA subjects used more diagnostic and non-diagnostic cues than did OA subjects. This result likely was due to the absence of clear guidelines to indicate the justifiee's process preference. The absence of clear guidelines likely made PA subjects assume that the justifiee would prefer they consider substantially all diagnostic information in their decision-making processes. Because of this assumption, PA accountants who are ignorant of the justifiee's preferences are more likely (*ceteris paribus*) to have loss functions that favor seeking more diverse opinions, will most likely infer an unbiased justifiee process preference (one that involves seeking information both for and against their hypotheses), and therefore engage in more balanced consultation.

OA accountants, on the other hand, want to guess the justifiee's preferred outcome and justify it. Prior auditing and tax research has shown that unless constrained, accountants tend to act as advocates for their clients (see e.g., Hackenbrack and Nelson 1996; Haynes, Jenkins, and Nutt 1998; Salterio and Koonce 1997). Therefore, OA accountants who are ignorant of the justifiee's preferences are more likely (*ceteris paribus*) to have loss functions that favor adoption of the client's position, will most likely infer a biased outcome preference, and engage in less balanced consultation to justify this position. This difference between PA and OA accountants is

primarily a result of different cost-benefit tradeoffs from the accountant's perspective for a particular outcome.

This analysis leads to the following hypothesis:

H1a: When justifiee preferences are not directly known, PA accountants will engage in more balanced consultation than OA accountants.

PA accountants who are ignorant of the justifiee's preferences also likely consult to a greater extent (i.e., with more advisors) than do OA accountants who are ignorant of the justifiee's preferences because of greater receptiveness to advice conflicting with their tentative decision. As noted, accountants using the acceptability heuristic because they are evaluated based on the outcome of their decision-making processes or are aware of the justifiee's outcome preference are unlikely look to undermine their own tentative decisions or the justifiee's preference. Even though OA accountants do consult from the population non-randomly, the more they consult, the more they run the risk of consulting with an advisor who will give advice contrary to their tentative decisions. So, accountants who use the acceptability heuristic and are thus trying to reach a threshold level of support for their assessments tend to consult with a smaller number of advisors than other accountants. Thus, not only will OA accountants consult a smaller number of advisors, but also this smaller population will be a relatively more biased sample:

H1b: When justifiee preferences are not directly known, PA accountants will consult to a greater extent than OA accountants.

Knowledge Only of the Justifiee's Outcome Preference

As noted, in the absence of direct knowledge of the justifiee's process preference, PA accountants likely try to infer it. PA accountants who know the justifiee's outcome preference, however, are more likely to infer a process preference that would result the justifiee's preferred outcome and feel more certain about it. Because some outcome preferences signal process preferences and vice versa, knowledge of the justifiee's outcome preference may give PA accountants insight into the justifiee's process preference. However, if accountants have knowledge of the justifiee's outcome preference, previous psychology research suggests that they unlikely can ignore such knowledge (Camerer, Loewenstein, and Weber 1989). This tendency will lead PA accountants with knowledge of the justifiee's outcome preference to infer a biased process preference that maximizes reaching the preferred outcome. Therefore, PA accountants who know (or can infer) the justifiee's outcome preference will engage in less balanced consultation than PA accountants who are ignorant of the justifiee's preferences.

OA accountants who know the justifiee's outcome preference possess direct (as opposed to inferred) knowledge about the justifiee's preference regarding the dimension on which they will be evaluated. Since this situation implies little uncertainty as to the justifiee's outcome preference, these accountants likely will engage in less balanced consultation to support the justifiee's preferred outcome. However, these consultations may or may not be less balanced than those of OA accountants who are ignorant of the justifiee's preferences. Depending upon the decision-making context, OA accountants who know the justifiee's outcome preference may place different costs on the possibility that the final outcome is inaccurate or poorly justified. If they judge the cost of an erroneous outcome to be high enough relative to the cost of receiving advice contrary to the justifiee's preferred outcome, OA accountants who know the justifiee's

outcome preference may engage in slightly more balanced consultation in order to minimize the possibility of an inaccurate or poorly justified outcome (Friedrich 1993).

This discussion leads to the following hypothesis relating to changes in consultation balance (also summarized in Panel A of Figure 2):

> *H2a*: The difference in consultation balance between PA accountants who do not know the justifiee's preferences and PA accountants who know the justifiee's outcome preference is greater than the difference in consultation balance between OA accountants who do not know the justifiee's preferences and OA accountants who know the justifiee's outcome preference.

As noted, process accountability encourages usage of greater amounts of information in decision making (Siegel-Jacobs and Yates 1996; Tetlock and Boettger 1989). While knowledge of the justifiee's outcome preference likely will cause PA accountants to infer a biased process preference, such knowledge may or may not affect their extent of consultation. Because PA accountants are evaluated on their decision processes, they are likely to be less concerned than OA accountants are about receiving advice conflicting with the justifiee's preferred outcome even though they may not actively search for it. Thus, the primary effect of this justifiee preference knowledge is likely to be a shift towards imbalanced consultation, not a change in the number of advisors sought. Knowledge of the justifiee's outcome preference also likely will have little effect on OA accountants because they are wary of receiving advice contrary to the justifiee's preferred outcome. Since these accountants already were investing little in the consultation process, elimination of uncertainty regarding the justifiee's outcome preference likely will have little effect on their extent of consultation. However, knowledge of the justifiee's outcome preference may itself be a surrogate for advice from the justifiee, causing

both PA and OA accountants to seek less advice in order to justify their decisions. This reasoning leads to the following hypothesis relating to changes in the extent of consultation (also summarized in Panel B of Figure 2):

> *H2b*: The difference in the extent of consultation between PA accountants who do not know the justifiee's preferences and PA accountants who know the justifiee's outcome preference is equal to the difference in extent of consultation between OA accountants who do not know the justifiee's preferences and OA accountants who know the justifiee's outcome preference.

Knowledge Only of the Justifiee's Process Preference

When they know the justifiee's process preference, PA accountants' consultation behavior likely will depend upon whether the justifiee prefers effectiveness (a relatively "unbiased" preference) or efficiency (a relatively "biased" preference). If the justifiee preference is for effective decision processes, PA accountants will engage in balanced consultation to demonstrate their consideration of multiple views. Further, this consultation likely will be more balanced than that of PA accountants who are ignorant of the justifiee's preferences because knowledge of the justifiee's preferred process preference reduces the uncertainty faced by PA accountants who do not know the justifiee's preferences. Conversely, if the justifiee's preference is for efficient decision processes, PA accountants will primarily focus on accumulating just enough evidence to justify a judgment and will therefore engage in less balanced consultation. This consultation will also be materially different from that of PA accountants who are ignorant of the justifiee's preferences because the uncertainty about the known (efficiency) process preference (less balanced consultation) is much different than the reaction to the inferred (effectiveness) process preference (more balanced consultation).

As noted above, in the absence of direct (as opposed to inferred) knowledge of the justifiee's outcome preference, OA accountants likely will try to infer it, and knowledge of the justifiee's process preference likely will give OA accountants insight into the justifiee's preferred outcome. If OA accountants know the justifiee's process preference, they must believe that it leads to a preferred outcome because they are being held accountable for an outcome, not the process they use to arrive at that outcome. When justifiees demonstrate a process preference for effectiveness versus efficiency (or vice versa), this position changes OA accountants' judged cost-benefit tradeoff for a particular outcome. If the justifiee's process preference is for effectiveness, OA accountants likely reasonably believe that something about the decision-making context causes the justifiee to have concerns about a particular outcome. Most likely, this concern is about the client-preferred outcome, since as previously noted, *ceteris paribus*, when possible, accountants want to adopt client-preferred reporting positions. Therefore, since they believe that the probability that the justifiee prefers a non-client-preferred outcome has increased, OA accountants may assume that the justifiee prefers the non-client-preferred outcome. If the justifiee's process preference is for efficiency, OA accountants likely reasonably believe that the justifiee prefers the client-preferred outcome. In either case, OA accountants will more likely engage in less balanced consultation to support their inferences about the justifiee's preferred outcome. This consultation will not differ materially from that of OA accountants who are ignorant of the justifiee's preferences because those accountants are making similar biased inferences leading to less balanced consultation.

This discussion leads to the following hypotheses relating to changes in consultation balance (also summarized in Panels C and D of Figure 2):

H3a: When the justifiee has a process preference for effectiveness, the difference in balance between PA accountants who do not know the justifiee's preferences and PA accountants who know the justifiee's process preference is greater than the difference in balance between OA accountants who do not know the justifiee's preferences and OA accountants who know the justifiee's process preference.

H3b: When the justifiee has a process preference for efficiency, the difference in balance between PA accountants who do not know the justifiee's preferences and PA accountants who know the justifiee's process preference is greater than the difference in balance between OA accountants who do not know the justifiee's preferences and OA accountants who know the justifiee's process preference.

Knowledge of a justifiee's process preference for effectiveness will result in more consultations by PA accountants to demonstrate to the justifiee that they considered a variety of opinions and thus have sufficient evidence to support their judgments. However, this extent of consultation likely will not differ materially from that of PA accountants who are ignorant of the justifiee's preferences. Those accountants assume an effective process preference and also invest highly in consultation. Knowledge of a justifiee's process preference for efficiency, however, will result in fewer consultations by PA accountants. These accountants are interested in accumulating just enough evidence to justify their preferred position and are less interested in demonstrating to the justifiee that they considered a variety of opinions to reach their conclusions. In addition, PA accountants who know the justifiee's process preference for efficiency likely will consult to a lesser extent than PA accountants who are ignorant of the justifiee's preferences.

Regardless of knowledge of the justifiee's process preference, OA accountants will likely assume a biased outcome preference. Therefore, because OA accountants are interested in reaching only a threshold level of support for their decisions, they will engage in relatively little

consultation. Further, the extent of consultation for these accountants and OA accountants who are ignorant of the justifiee's preferences likely will not differ because they all make similar inferences about the biased nature of the justifiee's outcome preference.

The reasoning outlined above leads to the following hypotheses relating to changes in extent of consultation (also summarized in Panels E and F of Figure 2):

H3c: When the justifiee has a process preference for effectiveness, the difference in the extent of consultation between PA accountants who do not know the justifiee's preferences and PA accountants who know the justifiee's process preference is equal to the difference in the extent of consultation between OA accountants who do not know the justifiee's preferences and OA accountants who know the justifiee's process preference.

H3d: When the justifiee has a process preference for efficiency, the difference in the extent of consultation between PA accountants who do not know the justifiee's preferences and PA accountants who know the justifiee's process preference is greater than the difference in the extent of consultation between OA accountants who do not know the justifiee's preferences and OA accountants who know the justifiee's process preference.

ACCOUNTANTS' INFORMATION DOCUMENTATION

Individuals often stylize information before communicating with evaluative others (see e.g., Caldwell and O'Reilly 1982; O'Reilly 1978, 1983; O'Reilly and Roberts 1974; Rich et al. 1997).[23] Fandt and Ferris (1990) found that, when required to document their decisions to justifiees, individuals who were highly accountable and knew how their justifiees handled similar situations engaged in stylization (i.e., they included more preference-consistent and defensive information into their reports.). Further, O'Reilly (1987, 1983) and Rosen and Tesser (1970) found that some individuals use this type of information management to promote their

[23] Similar to Rich et al. (1997, 482), I define stylization as occurring "when a preparer's persuasion behaviors affect working-paper content and format."

self-interest by portraying a positive self-image to superiors.[24] Similarly, these individuals can use their documentation to justify decisions (see Rich et al. 1997). Therefore, it is likely that when required to justify their decisions, accountants engage in a stylization process and selectively document the information and/or procedures they used to arrive at their decisions. This selective documentation is particularly important in public accounting as documentation regarding accountants' decisions may be reviewed not only by a justifiee, but may also form the basis for the justifiee's subsequent decisions (see Cushing and Loebbecke 1986).

This stylization process is likely to be greater when accountants justify a decision to a justifiee with a known or inferred preference for a particular outcome. As previously observed, this situation arises when accountants are outcome accountable or are process accountable to a justifiee with a known outcome preference or a known process preference for efficiency. In these cases, accountants most likely accumulate just enough evidence to support their decisions and likely will emphasize preference-consistent evidence and exclude contradictory information (if obtained at all) in their documentation. To the contrary, when accountants are process accountable and justify a decision to a justifiee with unknown preferences or a known process preference for effectiveness, they seek more balanced advice so that they can document arguments for and against a particular outcome. In such situations, accountants likely engage in relatively less information stylization.

This discussion leads to the following hypothesis:

[24] Ricchiute (1999) investigated the effect of auditors' decisions on working paper documentation and found that after controlling for justification and persuasion, auditors' prior decisions bias their memory of evidence to document in the working papers. To control for justification and persuasion effects, he assigned participants to *review* and *no review* conditions and found no differences in documentation between the two groups. However, he did not design his study to investigate accountants' justification behavior. Therefore, it is still an open question as to whether accountants selectively document information in response to justification and reputation concerns.

H4: PA accountants who know the justifiee's outcome preference or process preference for efficiency and OA accountants engage in more information stylization than PA accountants who do not know the justifiee's preferences or know the justifiee's process preference for effectiveness.

SUPERVISORS' EVALUATIONS OF SUBORDINATES' CONSULTATION BEHAVIORS

Previous research suggests that accountants may adapt their decision processes to persuade supervisors of the appropriateness of their decisions and the processes they used to arrive at those decisions (e.g., Rich et al. 1997). While supervisors normally may not have information about subordinates' informal consultation behaviors, one way accountants could attempt to persuade supervisors in this manner is by revealing such information to them. However, supervisors' knowledge of these persuasion attempts may allow them to anticipate the strategic informal consultation behaviors exhibited in the first experiment.

Previous research suggests that supervisors anticipate that their views may impact subordinates' decisions, but they generally do not fully anticipate the effects of their views on those decisions (Wilks 2002). To the extent that this is the case, I expect supervisors to focus on surface features of the subordinates' decision-making processes, such as consultation balance, rather than on subordinates' strategic motives resulting from their knowledge of justifiee preferences. Accordingly, I predict that supervisors discount the extent to which subordinates' knowledge of justifiees' preferences affects the subordinates' informal consultation behaviors and therefore, *ceteris paribus*, their evaluations will be a function of the balance of the subordinates' informal consultation behaviors.

To investigate this prediction, I compare two process accountable cells of my previous 2 x 4 design: (1) knowledge of the justifiee's process preference for effectiveness and (2)

knowledge of the justifiee's process preference for efficiency.[25] Because I expect consultation behavior of subordinates in the process accountable / knowledge of the justifiee's process preference for effectiveness condition in the first experiment to be extremely balanced (or asymptotically so), I predict no significant difference between supervisors' evaluations of those individuals and their evaluations of subordinates who exhibit perfectly balanced consultation behavior in that situation. However, I do expect supervisors' evaluations of those individuals to be significantly higher than their evaluations of subordinates who exhibit perfectly unbalanced consultation behavior due to the difference in consultation balance.[26]

Because I expect the consultation behavior of participants in the process accountable / knowledge of the justifiee's process preference for efficiency condition to be unbalanced, I predict no significant difference between supervisors' evaluations of those subordinates and their evaluations of subordinates who exhibit perfectly unbalanced consultation behavior in that situation. However, I predict supervisors' evaluations of those subordinates to be significantly lower than their evaluation of subordinates who exhibit perfectly balanced consultation behavior due to the difference in consultation balance.

Finally, due to the predicted difference in the balance of their consultation behaviors, I expect that supervisors' evaluations of subordinates who are process accountable and have knowledge of the justifiee's process preference for effectiveness to be significantly higher than their evaluations of subordinates who are process accountable and have knowledge of the justifiee's process preference for efficiency.

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[25] I choose only these cells for two reasons: (1) Managers and partners are to serve as participants and they are an expensive and scarce resource and (2) these cells occur often in practice.

[26] I expect supervisors who are evaluating process accountable subordinates to prefer more balanced consultation behaviors because those subordinates focus on justifiable processes, not necessarily justifiable outcomes. If the subordinates to be evaluated were outcome accountable, supervisors may prefer less balanced consultation possibly leading to a consensus for a particular outcome.

This analysis leads to the following hypotheses (also summarized in Figure 4):

H5a: When subordinates are process accountable and a justifiee has a preference for effectiveness, supervisors' performance evaluations of subordinates who exhibit the median consultation balance behavior from experiment one are the same as their evaluations of subordinates who exhibit perfectly balanced consultation behavior.

H5b: When subordinates are process accountable and a justifiee has a preference for effectiveness, supervisors' performance evaluations of subordinates who exhibit the median consultation balance behavior from experiment one are higher than their evaluations of subordinates who exhibit perfectly unbalanced consultation behavior.

H6a: When subordinates are process accountable and a justifiee has a preference for efficiency, supervisors' performance evaluations of subordinates who exhibit the median consultation balance behavior from experiment one are lower than their evaluations of subordinates who exhibit perfectly balanced consultation behavior.

H6b: When subordinates are process accountable and a justifiee has a preference for efficiency, supervisors' performance evaluations of subordinates who exhibit the median consultation balance behavior from experiment one are the same as their evaluations of subordinates who exhibit perfectly unbalanced consultation behavior.

H7: When subordinates are process accountable, supervisors' performance evaluations of subordinates who have knowledge of a justifiee's preference for effectiveness and exhibit the median consultation balance behavior from experiment one are higher than their evaluations for subordinates who have knowledge of a justifiee's preference for efficiency and exhibit the median consultation behavior from experiment one.

CHAPTER 3

METHOD

EXPERIMENT ONE

Design, Instrument, Task, and Administration

I investigate accountants' consultation behaviors and information documentation using a 4 (level of knowledge of justifiee preferences) x 2 (accountability type) experimental design with repeated measures on the latter factor. Using two ambiguous tax cases[27], I manipulate two independent variables: (1) the amount of participants' knowledge of the justifiee's preferences regarding the issue (ignorant, knowledge of outcome preference, knowledge of process preference (effectiveness), or knowledge of process preference (efficiency)) and (2) the nature of participants' accountability to the justifiee (process or outcome).[28] I manipulate the nature of participants' accountability within subjects.[29] To mitigate order effects, I counterbalance the order of both the nature of the participants' accountability to the justifiee and the two cases.

For both cases, participants initially recommend a tax reporting position, give an estimate of the probability that the taxing authority would uphold the client's preferred tax reporting

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[27] One of the cases is a modified version of a case from Cloyd and Spilker (1999) while the other is a modified version of a case from Davis and Mason (2003).

[28] My theory is continuous as to accountability type because individuals are not simply process or outcome accountable; one is merely emphasized relative to the other. Similarly, knowledge of the justifiee's preferences is continuous as individuals may have differing levels of knowledge about the justifiee's preferences. To provide a powerful test of my theory, I operationalize these factors using distinct and categorical levels. To the extent my experimental participants interpret my operationalizations of effectiveness and efficiency differently than I define those constructs in Chapter 1, I expect more noise in my results. To reinforce the accountability manipulations, at the beginning of the experiment, I ask participants to print their names on the experimental instrument and inform them that professionals from their firm may review some of their responses and might communicate directly with them regarding their performance.

[29] This within-subjects design allows me to observe individual participants' strategic behaviors as they change their informal consultation behavior in response to changes in accountability type. It also allows me to use participants as their own controls, removing the effect of individual characteristics (e.g., risk propensity, need for cognitive closure, etc.) that might be correlated with participants' informal consultation behavior.

position, and indicate their level of confidence in that estimate.[30] Participants can then choose to consult from up to six of eight advisors listed on a set menu. Participants repeat this process until they no longer desire (or are able) to consult.[31] After participants consult their advisors, I ask them to make a final recommendation, probability estimate, confidence assessment, and write a brief justification memorandum.[32] Finally, after participants complete both tasks, I ask them to answer a post-experimental questionnaire containing questions about their consultation processes, manipulation checks, and basic demographic information. I outline the sequence of experimental procedures in Exhibit 1.

Dependent Variables

I measure two dependent variables. The dependent variable for H1a, H2a, H3a, and H3b is the balance of advisors selected by the participants. To investigate participants' search patterns, I develop a measure to weight each advisor a participant consulted. I give the greatest weight to the first advisor, the next greatest to the next, and so on. I also sign the weight based on the nature of the advisor (aggressive or conservative) and then sum the weights to yield a composite balance score. Values for this measure range from virtually 0 (a perfectly balanced

[30] The use of two different cases raises the issue of whether or not the two cases can or should be made equivalent across a range of task attributes. As a result, I designed the two cases to be as similar as possible along at least two dimensions (complexity and risk) and I measure participants' perceptions of task complexity and risk. I included these variables as covariates in the statistical analyses reported in Section 4 (results untabulated) and they were not statistically significant.

[31] I limited the total number of advisors participants could consult because in practice, accountants will be able to have a limited number of consultations before reaching a final decision and avoid a strategy of consulting with all available advisors (Pritchard and Sniezek 1995). I chose six as a limit because empirical evidence from Gibbins and Mason (1988) suggests that, in the course of making professional judgments, most accountants interact with between three and five advisors.

[32] Participants only wrote a brief justification memorandum for the first case due to time constraints.

consultation process) to 1 (a completely unbalanced consultation process). For a detailed discussion of the measure and an example of its use, see Exhibit 2.[33]

I measure the extent of participant consultation (the dependent variable for H1b, H2b, H3c, and H3d) based on the number of advisors consulted by the participants. Finally, I measure information stylization (the dependent variable for H4) by summing the information documented in a participant's justification memorandum supporting his or her judgment and dividing that sum by the total number of pieces of information documented. I standardize this ratio by subtracting 0.5 and taking the absolute value of the result. This process results in a measure whose values range from 0 to 0.5 where a greater number indicates a larger amount of information stylization.

EXPERIMENT TWO

To investigate supervisors' evaluations of subordinates' informal consultation behaviors, I give participants the assignment memorandum for one of the cases from the initial experiment and tell them that two hypothetical superiors each gave this assignment to six subordinates. The participants evaluate the six subordinates performance in two sets of three. In one of the sets, the supervisor has a process preference for effectiveness; in the other, the supervisor has a process preference for efficiency. For each subordinate, I give participants the supervisor's preference

[33] Because my theory is one of strategic, adaptive behavior, it is appropriate to operationalize consultation balance by taking into account individuals' strategic and systematic (and thus non-random) behavior. One key element of such behavior is the order in which the advisors are consulted. To reflect strategic, adaptive behavior of the participants in their advisor choices, I employ a differential weighting scheme in which the weights assigned to each advisor decrease with each advisor chosen. The results (presented in Chapter 4) are qualitatively similar, however, when calculated using a probability-weighted measure similar to the one used in Turner (2001) and they are robust to alternative differential weighting schemes. Specifically, results obtained using weights with one-quarter the distance between them relative to the weights I use (0.230769, 0.205128, 0.179487, 0.153846, 0.128205, and 0.102564) and results obtained using weights with four times the distance between them relative to the weights I use (0.318182, 0.257575, 0.196970, 0.136363, 0.075758, and 0.015151) are qualitatively similar to the results I report in this dissertation.

regarding the process to be used to investigate the assignment (preference for an effective or an efficient process) as well as a description of each subordinate's informal consultation behavior and the subordinate's final judgment. Participants are told that informal consultation in this context refers to communication with other members of the firm that is not required by firm policy. The three subordinates in each set are identical in every respect except that they exhibit different informal consultation behaviors. One subordinate is perfectly balanced in her consultation behavior, one is perfectly unbalanced in her consultation behaviors, and one exhibits the median consultation behaviors for that condition from the initial experiment.[34] I choose the median consultation behaviors because they are the best proxies for strategic, adaptive behavior in those conditions.

Participants rate each subordinate's overall performance as well as the efficiency of the subordinate's performance. They rate each subordinate's overall performance using a 9-point Likert-type scale with endpoints of 1 (extremely low quality) and 9 (extremely high quality) while they rate efficiency using a 9-point Likert-type scale with endpoints of 1 (extremely inefficient) and 9 (extremely efficient). I instruct participants to assume that all of the subordinates have identical experience with the issue(s) raised in the case, had equivalent access to, and reviewed all of the law relevant to these issue(s). I also instruct participants to assume that all subordinates had the opportunity to informally consult with up to six advisors regarding the case, that each subordinate fully briefed each consulted advisor on the client facts and relevant law, and that the advisors are members of the firm who had identical experience and expertise with the issue(s) raised in the case. After evaluating all six subordinates, I ask participants to answer a post-experimental questionnaire containing basic demographic

[34] To mitigate order effects, I counterbalance the order of the two sets of subordinates as well as the order of the subordinates in each set.

information and questions about the importance of informal consultation in an accountant's decision-making process.

CHAPTER 4

RESULTS

EXPERIMENT ONE

Subjects, Manipulation Checks, and Descriptive Statistics

Sixty-five staff and senior professionals from three Big-5 public accounting firms and 60 undergraduate accountancy students from a large midwestern university participated in the study.[35] The professional participants have a mean (median) of 34.8 (30) months of tax experience with a minimum of 11 months and a maximum of 108 months.[36] All participants completed the experimental instrument in 45 to 60 minutes. Responses to manipulation check questions indicate that while all participants felt some process and outcome accountability for each case, process accountable participants felt significantly more process accountable than outcome accountable ($\mu_{Process} = 7.02$ versus $\mu_{Outcome} = 4.56$, p (one-sided) < 0.01) and outcome accountable participants felt significantly more outcome accountable than process accountable ($\mu_{Outcome} = 7.05$ versus $\mu_{Process} = 4.16$, p (one-sided) < 0.01).[37] Further, responses to manipulation

[35] In addition to staff and senior professional participants, I use accountancy students because I do not expect them to differ materially from staff and senior professional participants in their informal consultation behavior. No theoretical reason suggests that these professionals' behavior should differ from accountancy students' behavior in this context, as informal consultation is a process used by individuals in a variety of contexts. For a discussion of the use of student participants in accounting studies see Ashton and Kramer (1980), Peecher and Solomon (2001), and Walters-York and Curatola (1998).

[36] Eighteen of the professionals are from Deloitte & Touche, LLP, 29 are from Andersen, LLP, and 18 are from Ernst & Young, LLP. To check for possible firm effects, I compared consultation balance, extent of consultation, perceived case complexity, and advocacy scores across all three firms and found no significant differences between them. Further, I control for expertise/experience effects by selecting participants who have relatively small amounts of tax expertise/experience and by choosing two tax issues that are not commonly encountered in tax practice. I also collected information from each participant regarding their accounting experience and experience with the issues in the two cases and used them as covariates in my statistical analyses. As I note in the footnotes to Tables 2-4, these items were not statistically significant and had no impact on the treatment effects.

[37] Participants' response rates did not materially differ across all eight experimental conditions. I gathered these data by asking each participant to respond to the following question after each case using a 9-point Likert-type scale with endpoints of 1 (no pressure) and 9 (maximum pressure): "[H]ow much pressure did you feel to justify the following: (a) The quality of my final judgment/decision and (b) The quality of the decision-making process I used to reach my final judgment/decision."

check questions indicate that all participants attended to the information, or noted that none was given to them about the justifiee's preference.[38]

Table 1 contains descriptive statistics for participants' consultation balance, extent of consultation, and information documentation. Comparison of professional and student participant data reveal no significant differences between the two participant groups for each cell of the experimental design.[39] As a result, I combine professional and student participant responses.[40]

Finally, because power is an important issue for both significant and non-significant results of hypothesis tests, I calculate the statistical power of the tests of each of the nine hypotheses reported below (Burgstahler 1987). Using the formulae provided in Cohen (1988) with $\alpha = 0.05$, the power of each of the tests is greater than 0.90.

Tests of Hypotheses

Consultation Balance and Extent of Consultation

H1a predicts that, in the absence of direct knowledge of justifiee preferences, process accountable ("PA") accountants engage in more balanced consultation than outcome accountable ("OA") accountants. The results support this hypothesis ($\mu_{Process} = 0.17$ versus $\mu_{Outcome} = 0.28$, p (one-sided) < 0.01, Panel C of Table 2). As predicted in H1b, the same relationship holds for

[38] Each participant responded to the following question: "Which of the following best summarizes the manager's stated preferences in the case: (a) He/she would like to support the client's position if possible, (b) He/she would like you to be as effective and thorough as possible in your analysis of this issue, (c) He/she would like you to be as efficient as possible in your analysis of this issue, and (d) The manager revealed no preferences regarding this case."

[39] I compare professional and student data by conducting both t-tests for differences between the various cells of the experimental design for consultation balance, extent of consultation, and information documentation (results untabluated). In addition, I ran ANOVAs for consultation balance, extent of consultation, and information documentation with participant type as a factor (results untabulated).

[40] The results for all tests of the hypotheses are identical for the combined data and only the professional data.

accountants' extent of consultation ($\mu_{Process}$ = 5.53 versus $\mu_{Outcome}$ = 4.28, p (one-sided) < 0.01, Panel C of Table 3).

H2a predicts that knowledge of the justifiee's outcome preference has a greater effect on the consultation balance of PA accountants than on that of OA accountants. The results support this hypothesis (p (one-sided) < 0.01, Panel C of Table 2). H2b, however, predicts that knowledge of the justifiee's outcome preference will not differentially affect the extent of consultation by PA and OA accountants. This hypothesis is not supported (p (two-sided) = 0.02, Panel C of Table 3). In general, PA participants consulted less (p (one-sided) = 0.01) when given knowledge of the justifiee's outcome preference, while OA accountants did not significantly change their consultation rate (p (one-sided) = 0.64) with knowledge of this information. For the PA accountants, knowledge of the justifiee's outcome preference may have served as a source of advice, which decreased their need for consultation. For the OA accountants, this information probably had little or no effect on their extent of consultation as they may have already assumed this knowledge.[41]

H3a predicts that knowledge of the justifiee's process preference for effectiveness has a greater impact on the consultation balances of PA accountants than on those of OA accountants. The results do not support this hypothesis (p (one-sided) = 0.17, Panel C of Table 2). One possible explanation for this result is that PA accountants believed there were asymmetric penalties for being to balanced versus too imbalanced in this condition. Another possible explanation is that PA accountants may already have assumed that the justifiee was concerned about effectiveness as part of their process accountability. Therefore, justifiee process preference knowledge might not have been new information for PA accountants while OA accountants may have already assumed a particular outcome preference when they learned that

[41] For graphical representations of these results, see Panels A and B of Figure 3.

they were outcome accountable. H3c predicts that knowledge of the justifiee's process preference for effectiveness will not differentially affect PA and OA accountants' extent of consultation. The results are consistent with this hypothesis (p (two-sided) = 0.26, Panel C of Table 3).[42]

As predicted in H3b, knowledge of the justifiee's process preference for efficiency affects the consultation balances of PA accountants more than those of OA accountants (p (one-sided) = 0.01, Panel C of Table 2). H3d predicts that the same result will occur with respect to PA and OA accountants' extent of consultation. This hypothesis is supported (p (one-sided) < 0.01, Panel C of Table 3).[43]

Information Documentation

To examine accountants' information documentation, I converted participants' handwritten justification memoranda to typewritten, electronic form so that no information was available to coders about experimental conditions. Two independent persons coded the 125 memoranda. These persons were Ph.D. students familiar with the two cases, but blind to the experimental conditions. In coding the memoranda, the two individuals identified the law, case facts, and other information that participants identified as supportive or contradictory of their judgments. After the two individuals completed their task, they met jointly to resolve coding differences.[44]

H4 predicts that OA accountants and PA accountants who know the justifiee's outcome preferences or process preference for efficiency engage in more information stylization than PA accountants who do not know the justifiee's preferences or know the justifiee's process

[42] For graphical representations of these results, see Panels C and E of Figure 3.
[43] For graphical representations of these results, see Panels D and F of Figure 3.
[44] The intercoder agreement for the two coders' content analysis was 0.85.

preference for effectiveness. The results support this hypothesis (p (one-sided) < 0.01, Panel C of Table 4). This result is particularly important given recent research that reports that supervisors may not be able to anticipate subordinates' evidence distortion (Wilks 2002) and that exposure to selective evidence documentation affects supervisors' judgments (Ricchiute 1999).

EXPERIMENT TWO

Subjects and Descriptive Statistics

Twenty-five professionals (seven partners and 18 managers) from two Big 5 public accounting firms participated in the study.[45] The participants have a mean (median) of 12.98 (11.88) years of tax experience with a minimum of 4.5 years and a maximum of 28.5 years. All participants completed the experimental instrument in 10 to 20 minutes.

In the post-experimental questionnaire, participants rated the importance of informal consultation in accountants' decision-making processes using a 9-point Likert-type scale with endpoints of 1 (extremely unimportant) and 9 (extremely important). The mean response is 7.06, indicating that participants feel that informal consultation is an important part of accountants' decision-making processes.

Tests of Hypotheses

The results support my expectations. As predicted in H5a, for the justifiee with a process preference for effectiveness, participants overall evaluations for the subordinates exhibiting the completely balanced and median balanced behaviors are not significantly different ($\mu_{Balanced}$ = 6.05 versus μ_{Median} = 5.75, p (two-sided) = 0.57). However, participants' overall evaluations for

[45] Eleven of the professionals (two partners and nine managers) are from Deloitte & Touche, LLP and 14 (five partners and nine managers) are from PricewaterhouseCoopers, LLP. To check for possible firm effects, I compare responses between the firms and find no significant differences.

the subordinates exhibiting the median balanced and completely unbalanced behaviors are significantly different in the expected direction(μ_{Median} = 5.75 versus $\mu_{Unbalanced}$ = 4.46, p (one-sided) = 0.01). This supports H5b. As predicted in H6a, for the justifiee with a process preference for efficiency, participants' overall evaluations for the subordinate exhibiting the completely balanced behavior are significantly higher than their overall evaluations for the subordinate exhibiting the median balanced behavior ($\mu_{Balanced}$ = 6.05 versus μ_{Median} = 4.95, p (one-sided) < 0.01). However, participants' overall evaluations for the subordinates exhibiting the median balanced and completely unbalanced behaviors are not significantly different (μ_{Median} = 4.95 versus $\mu_{Unbalanced}$ = 4.28, p (two-sided) = 0.18). This supports H6b. Finally, participants' overall evaluations for the subordinate exhibiting the median balanced behavior in the effectiveness condition were greater than their overall evaluations for the subordinate exhibiting the median balanced behavior in the efficiency condition ($\mu_{Effectiveness}$ = 5.75 versus $\mu_{Efficiency}$ = 4.95, p (one-sided) = 0.05) as predicted in H7.[46]

Overall, these results suggest that superiors consider informal consultation to be an important part of subordinates' decision-making processes and that subordinates' consultation behaviors affect supervisors' evaluations of the subordinates' performance.[47] They also suggest

[46] The statistical power of each of these t-tests ranges from approximately 0.60 and 0.75. Consequently, while the tests are not as powerful as would be ideal, they allow for a reasonable level of confidence in any inferences drawn from them.

[47] The results for t-test comparisons of participants' efficiency evaluations are substantially similar except there is no significant difference between participants' efficiency evaluations of the two median behaviors (p (two-sided) = 0.63). Follow-up discussions with several participants suggests that, while in theory efficiency and effectiveness are two different constructs (one deals with the time/effort taken to reach a decision while the other deals with the defensibility of the decision), professional standards cause some accounting professionals to correlate the two and that anecdotally the perceived correlation between the two appears to increase with greater amounts of experience. In particular, with experience, accountants evaluate efficiency assuming a certain level of effectiveness (i.e., an accountant must be at least minimally effective in order to be efficient). Statistically, there is a high correlation between participants' overall performance and efficiency evaluations for each of the six subordinates. Additional analysis revealed no significant interactions between the ratings. As a result, I conducted t-tests in which I combined the two ratings for each of the six subordinates. The results for each of the comparisons are qualitatively

that subordinates may not be particularly adept at anticipating supervisors' performance evaluation criteria.

similar (i.e., the statistically significant results are still statistically significant while the statistically non-significant results are still non-significant).

CHAPTER 5

CONCLUDING REMARKS

Based on my theory of informal consultation, I investigate how accountability type (process versus outcome) and knowledge of a justifiee's outcome or process preference affect two dimensions of accountants' informal consultation processes (the types and number of advisors chosen) as well as accountants' information documentation behaviors, and supervisors' performance evaluations. The experimental results suggest that accountants engage in strategic informal consultation and information documentation. In addition, the results suggest that supervisors do not take justifiee preferences sufficiently into account when evaluating subordinates' informal consultation behaviors.

Specifically, process accountable accountants engage in more balanced consultation and consult to a greater extent than outcome accountable accountants. Further, knowledge of the justifiee's outcome preference causes both process accountable and outcome accountable accountants to engage in less balanced consultation. However, contrary to expectations, process accountable accountants consulted less when given knowledge of the justifiee's outcome preference, while outcome accountable accountants did not significantly change their consultation rate. Knowledge of the justifiee's outcome preference may have served as a source of advice for process accountable accountants, thereby decreasing their need for advice. For outcome accountable accountants, this knowledge may not have had an impact on their extent of consultation as they may already have assumed the preference. Consistent with expectations, only when the justifiee has a preference for effectiveness (as opposed to efficiency) does knowledge of the justifiee's process preference cause process accountable accountants to engage

in more balanced consultation and consult to a greater extent than outcome accountable accountants.

Finally, accountability type and knowledge of justifiee preferences also affect accountants' information documentation. Specifically, process accountable accountants who know the justifiee's outcome preference or process preference for efficiency and outcome accountable accountants engage in more information stylization than process accountable accountants who do not know the justifiee's process preference or know the justifiee's process preference for effectiveness.

With regard to supervisors' evaluations of subordinates' informal consultation behaviors, participants disregarded the justifee's preferences when evaluating subordinates' and instead evaluated the subordinates based on the balance of their informal consultation behaviors. The more balanced the behaviors, the higher the evaluations.

This study contributes to the accounting and psychology literatures by providing a theory and experimental evidence that shows the extent to which and how people engage in informal consultation in ill-structured decision-making settings. In particular, I provide evidence on the extent to which and how tax professionals act strategically to manage their reputations in response to accountability and justifiee preferences. I also provide evidence that supervisors are not fully cognizant of this strategic behavior.

This strategic behavior should, and most likely does, have implications for accountants' efficiency and effectiveness. The strategic use of informal consultation may impair effectiveness when it produces false consensus, potentially resulting in overconfidence on the part of accountants and those who rely on accountants' judgments and decisions. This overconfidence can potentially result in adverse consequences for accountants and their firms. An extreme

example of the consequences of strategic consultation apparently arose in Andersen's audit of Enron. Several individuals allegedly refused to consult with other members of the firm who were known to not support the use of various aggressive accounting practices in favor of others who supported Enron's use of such practices (Chicago Tribune 2002, A1).

Although this study provides evidence of strategic informal consultation behavior, it is subject to several limitations that provide opportunities for future research. I chose to investigate informal consultation in a tax setting, a setting whose institutional features make it more likely to see this strategic behavior. Future research could investigate individuals' strategic, adaptive informal consultation behavior in other settings such as auditing and medicine. Also, I used professional participants who were only accountable to one justifiee. Accountants face competing accountabilities within their ambiguous decision-making environments stemming from clients, superiors, or regulators, such as the Securities and Exchange Commission and the Internal Revenue Service (Gibbins and Newton 1994). Future research could extend this study by investigating the effect of multiple accountabilities on accountants' informal consultation processes.

Further, I chose to focus only on accountants' strategic informal consultation in response to accountability and justifiee preferences. Other aspects of accountants' informal consultation processes may provide areas for fruitful research, including other environmental and personal factors that affect accountants' use of informal consultation, the processes accountants follow when asking for advice, and various judgment and decision-making consequences of informal consultation behavior for both subordinates and their superiors. For example, recent research suggests that affective reactions can influence risky decision making in accounting contexts (Moreno, Kida, and Smith 2002). Such affective reactions also may have consequences for

accountants' informal consultation processes. Also, Vera-Munoz and Kinney (1999) report that problem information content affects accountants' problem recognition, information analysis, and perceptions of information relevance. Accountants could manipulate their informal consultation processes by selectively communicating information to advisors as well as by framing the information in various ways in order to elicit desired recommendations.

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APPENDIX A

PAPER INSTRUMENT FOR EXPERIMENT ONE

General Instructions

1. Thank you for agreeing to participate in this study, which is being conducted to learn more about how accounting professionals make judgments and decisions in practice. On the following pages, you will be asked to complete two short cases that are simplified versions of "real world" tasks in tax practice. Participation should require no more than one hour of your time. Please plan your time appropriately to ensure that you are able to complete the study within that time frame.

2. Various instructions and reminders appear throughout the two cases. Please carefully read and follow the instructions.

3. This is not a "test," and there are no definitely correct answers to the questions you will be asked. No special technical tax knowledge is required, as all relevant tax law will be explained during the cases. However, your careful completion of the cases is critical to the success of the study. Please answer the questions as honestly and conscientiously as you can, just as you would do in a real-life situation. Since the study is focused on individual judgment and decision making, please do not discuss the study with others prior to, during, or after you are finished unless contacted by a professional from your firm for the purpose of providing feedback on your responses. Likewise, do not use any materials not provided to you (e.g., the Internal Revenue Code or a textbook).

4. Participation in this study is important but voluntary. You are free to withdraw from the study at any time for any reason.

5. If you would like, you may receive a copy of the results of this study by selecting the appropriate option at the end of the study.

Thank you.

Jon D. Perkins, J.D., CPA
Ph.D. Candidate
University of Illinois at Urbana-Champaign

Professor Ira Solomon
R. C. Evans Endowed Chair in Commerce
University of Illinois at Urbana-Champaign

Feedback Procedures

Please read carefully

Participant responses will be reviewed by professionals from your firm [*by your instructor, if a student*]. After reviewing your responses, you may be given feedback on your responses. Please print your full name, e-mail address, current job title (if applicable), and the address and phone number of your home office (if applicable) in the space below to facilitate any subsequent communications.

Please Print Legibly

Name (first and last): _____

E-mail Address: _____

Current Job Title: _____

Office Phone: (_____)_____

Office Address: _____

_____

_____

_____

Informed Consent

Please read the following statements and sign below.

I have read a description of the study and understand that it will last for about one hour. My participation in this study is voluntary and I may discontinue my participation at any time. Participant responses will be reviewed by professionals from my firm [*by my instructor, if a student*]. After reviewing my responses, I may be contacted to review my responses.

I also understand that should I have any question about the study after today, I might directly contact Professor Ira Solomon (isolomon@uiuc.edu) or Jon Perkins (jdperkin@uiuc.edu or 217-351-8275). If I so desire for my future reference, I can obtain a copy of the consent form from the researchers upon completion of this study.

Signature Date

Assignment Memorandum

TO: Tax staff person
FROM: Tax manager
SUBJECT: Jim Hunt; character of loss on sale of land

Jim Hunt is the CEO of Delta Electronics, Inc., an important client for whom we have done audit and tax work for many years. We are in the process of preparing Jim's 2000 federal income tax return and need to decide whether a loss he realized during 2000 on sales of real estate should be treated as ordinary or capital. To make this decision, we need to determine whether Jim is a dealer or investor in that real estate.

[*Insert knowledge of justifiee preference here; no preference information given in ignorance condition*]

[Outcome preference] **It is important, if possible, to be able to support the client's preferred position.**

[Process preference for effectiveness] **To best defend our treatment of this item on the return, we would like you to be as effective and thorough as possible in your analysis of this issue.**

[Process preference for efficiency] **We are concerned about the amount of time we have already invested in this client's return. As a result, we would like you to be as efficient as possible in your analysis of this issue.**

[*Insert accountability type here*]

[Process accountability] **Your performance on this task will be evaluated based SOLELY on the quality of the decision-making process you use to make your final judgment/decision, NOT on the final judgment/decision you make.**

[Outcome accountability] **Your performance on this task will be evaluated based SOLELY on the quality of your final judgment/decision, NOT on the process by which you make that final judgment/decision.**

Case Facts

On June 1, 1996, Jim Hunt purchased 40 acres of undeveloped land. Other than his personal residences, this was Jim's first and only real estate purchase. At the time, Jim was confident that the land would appreciate in value due to the planned construction of a regional shopping mall nearby. The land was already zoned for "retail/commercial" use and he hoped to sell the land in a single transaction after construction on the shopping mall began. Unfortunately, plans for the shopping mall fell through in early 1997 and Jim was unable to find a buyer for the property. He began placing advertisements in the local paper once a month and he put a "for sale" sign on the property that was visible from the highway. Despite Jim's sales efforts, he was unable to locate a buyer.

In June 1999, Jim decided that the property would be much more marketable if he subdivided the land into individual lots for residential development. Jim hired an engineer to plat the property into 110 individual lots and to determine the location of streets, etc. Jim submitted the engineer's drawings to the City Planning Board along with his application to have the property's zoning changed to "single family residential." The zoning change was approved in September 1999. Jim incurred engineering and legal costs in this process.

In October 1999, Jim hired a contractor to build the necessary streets, curbs, and drainage systems, and to connect the property to the city's utility systems (e.g., water, sewer, and electricity). Development was completed by June 2000.

In August 2000, Jim sold six developed lots. In October, a residential builder offered to purchase the remaining 104 lots. Jim accepted the offer and ceased other sales activities. The sale was completed on November 1, 2000. Jim realized a net loss on the transaction.

We estimate that if Jim is treated as a dealer in real estate with regard to this transaction, it will reduce his 2000 federal income tax liability by $200,000 because the entire loss would be deductible in 2000. In contrast, if Jim is treated as an investor, he could only deduct a $3,000 capital loss in 2000 and the remainder of the loss would be a capital loss carry-forward to 2001 and later years. With the possible exception of this completed transaction, Jim had no other capital gain or loss transactions this year.

Relevant Law and Analysis

I.R.C. §1221 defines a "capital asset" by exception. The relevant exception in this case is provided in §1221(1), which provides that "property held by a taxpayer primarily for sale to customers in the ordinary course of his trade or business" is NOT a capital asset.

If Jim's real estate is considered a §1221(1) asset (i.e., if Jim is viewed as a "dealer"), then the loss will be treated as ordinary. In contrast, if the property is not considered a §1221(1) asset (i.e., if Jim is viewed as an "investor"), then the loss will be treated as a capital loss.

Under §1211(b), capital losses can only be deducted first against capital gains (without limit) and then against ordinary income (but only up to $3,000 per year). As a result, it could take Jim many years to realize the tax benefit of a large capital loss. Obviously, therefore, Jim would prefer to be treated as a dealer with respect to this property so that he can deduct ALL of his loss against other ordinary income on his 2000 income tax return.

Several factors considered by the courts as indicative of dealer versus investor status are summarized below. Courts have stressed that no one factor is determinative and that each case must be considered on its own facts. Moreover, these factors have not always been applied on a consistent basis.

Number and Frequency of Sales. Generally, the greater the number of sales, the more frequent the sales, and the more continuity in sales activities, the greater the likelihood that the taxpayer will be considered a dealer.

Development Activities. Generally, the greater the development activities, the more likely the taxpayer will be considered a dealer.

Sales Activities. Generally, the more the taxpayer advertises, solicits customers, lists the property, and otherwise promotes the sale of the property, the more likely the taxpayer will be considered a dealer.

Purpose of Acquisition. Generally, the purpose for which the property was originally acquired AND the purpose for which the property was held at the time of its disposition are important in deciding whether the taxpayer is a dealer.

Questions

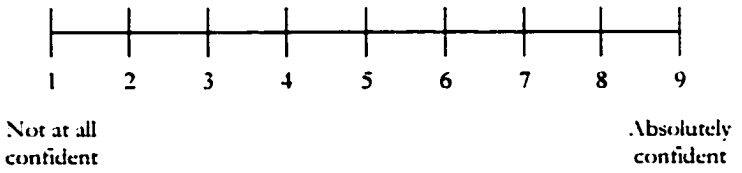
1. How do you recommend we treat the sale of this property on Jim Hunt's 2000 income tax return? *Circle one.*

   Dealer Investor

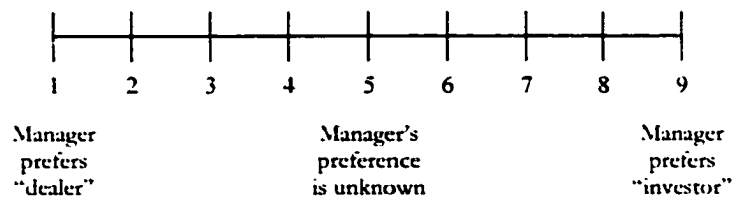
2. How confident are you that the treatment you indicated would be upheld by a court if litigated? *Enter a number from 0 to 100, where 0 indicates no chance that this position will be supported and 100 indicates that you are absolutely certain that this position will be supported.*

   _____ %

3. How confident are you that the tax manager in this case would find your choice and judgment in #1 acceptable? *Indicate your response on the scale below.*



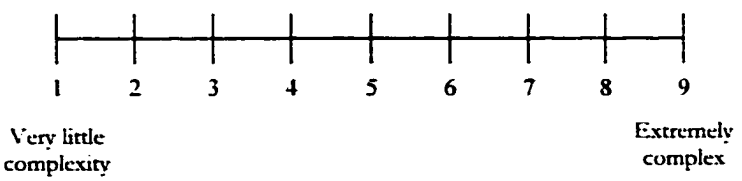
4. Do you think you know whether the tax manager in this case prefers dealer or investor treatment? *Indicate your response on the scale below.*



5. Do you expect that the tax manager in this case would agree with your assessments in #1 and #2 above? *Circle one.*

   Yes No

6. Please rate the level of complexity of this case:



Advice Selection – Jim Hunt Case

To aid you in making your judgments, you may consult with up to six (6) of the following persons. Budget and time constraints limit you to a total of six consultations. You are not required to engage in any consultation nor must you consult with all six advisors. You may assume that each person has been briefed on the facts and relevant law in this case. Recall [*insert knowledge of justifiee preferences and accountability type here*].

You have information about each of the advisors regarding their aggressiveness in their decision making (where 1 is "tending to be very conservative" and 9 is "tending to be very aggressive") and their preference for emphasizing effectiveness or efficiency in their decision-making process.

A table of the advisors and their characteristics is shown below:

Advisor	*Level of Aggressiveness*	*Advisor Prefers To Be...*
#1	1	Effective and thorough
#2	1	Efficient
#3	3	Effective and thorough
#4	3	Efficient
#5	7	Effective and thorough
#6	7	Efficient
#7	9	Effective and thorough
#8	9	Efficient

You may select advice from one or more of the advisors (up to a maximum of six advisors) using the computer in front of you. When you are finished obtaining advice, please turn to the next page of the packet.

Questions

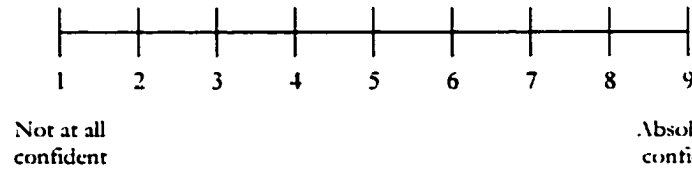
1. How do you recommend we treat the sale of this property on Jim Hunt's 2000 income tax return? *Circle one.*

   Dealer Investor

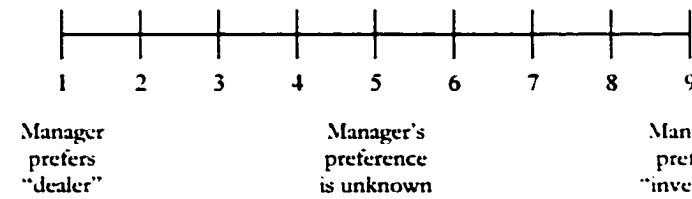
2. How confident are you that the treatment you indicated would be upheld by a court if litigated? *Enter a number from 0 to 100, where 0 indicates no chance that this position will be supported and 100 indicates that you are absolutely certain that this position will be supported.*

   _____ %

3. How confident are you that the tax manager in this case would find your choice and judgment in #1 acceptable? *Indicate your response on the scale below.*



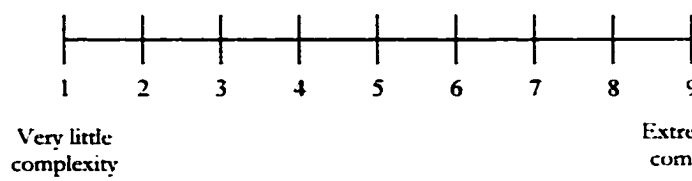
4. Do you think you know whether the tax manager in this case prefers dealer or investor treatment? *Indicate your response on the scale below.*



5. Do you expect that the tax manager in this case would agree with your assessments in #1 and #2 above? *Circle one.*

   Yes No

6. Please rate the level of complexity of this case:



In writing the following memorandum, you may refer back to the previous pages in this case as well as the advice you have received on the computer screen in front of you.

Please write a brief memorandum to the tax manager stating your decision in this case and noting any relevant case facts and law and analysis. Recall [*insert knowledge of justifiee preferences and accountability type here*]. If you need additional paper, please let the experimenter know and additional paper will be provided.

Memorandum

TO: Tax manager
FROM: Tax staff person
SUBJECT: Jim Hunt; character of loss on sale of land

Questions

1. How long have you been working in the tax area?

   _____ Years _____ Months

2. What is your current job title (e.g., staff accountant, revenue agent, senior, manager, associate, etc.)?

   _____

3. Prior to this experiment, had you previously conducted research on the issue of dealer versus investor status? *Circle one.*

   Yes No

   If yes, please indicate the number of times you have addressed this issue and the approximate date of your most recent experience (e.g. 1, 2, ... , 10 times, January 2001)?

   _____

4. Circle the number on the scale below that best indicates your level of expertise with respect to the issue of dealer versus investor status:

novice						*expert*
1	2	3	4	5	6	7

5. Which of the following best summarizes how your performance on the Jim Hunt case will be evaluated? *Circle one.*

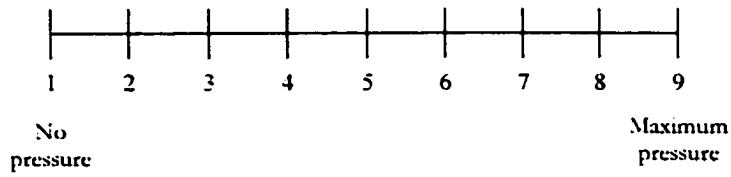
   a. Based SOLELY on the quality of my final judgment/decision, NOT on the decision-making process I used to make my final judgment/decision.

   b. Based SOLELY on the quality of the decision-making process I used to make my final judgment/decision, NOT on the quality of my final judgment/decision.

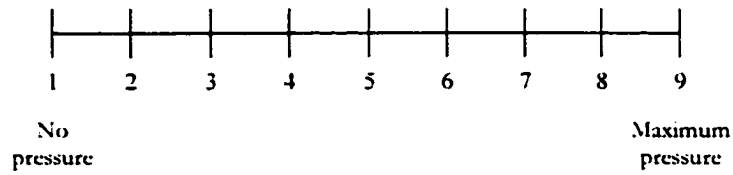
   c. My performance on this case will not be evaluated.

6. For the Jim Hunt case, how much pressure did you feel to justify the following:

   a. The quality of my final judgment/decision:



   b. The quality of the decision-making process I used to reach my final judgment/decision:



7. Which of the following best summarizes the manager's stated preferences in the Jim Hunt case? *Circle one.*

   a. He/she would like to support the client's preferred position if possible.

   b. He/she would like you to be as effective and thorough as possible in your analysis of this issue.

   c. He/she would like you to be as efficient as possible in your analysis of this issue.

   d. The manager revealed no preferences regarding this case.

You have finished the first case.

Please do the following things (in order):

1. **Put all of the pages (including the Feedback Procedures, General Instructions, and Informed Consent pages) in the first envelope and close it.**

2. **Open the second envelope, take out the contents, and proceed to the second case.**

3. **Click on the "Continue" button at the bottom of the computer screen in front of you.**

Assignment Memorandum

TO: Tax staff person
FROM: New tax manager
SUBJECT: Kiehl Corporation; classification of payments on bonds

Kiehl Corporation is an important new client for our firm. As part of our preparation of Kiehl Corporation's 2000 federal income tax return, we need to determine the appropriate tax treatment of payments on certain bonds.

Your task is to render a judgment concerning the treatment of the bonds as debt or equity. There are currently no statutory or administrative guidelines to assist you in making a determination regarding classification of the Kiehl Corporation bonds. However, to assist you in making a judgment, you will be presented with an overview of judicial guidelines related to this issue.

[*Insert knowledge of justifiee preferences and accountability type here; the knowledge is the same as in the first case and the accountability type is the one not used in the first case*]

Case Facts

Kiehl Corporation ("Kiehl") is a manufacturer of fine Pennsylvania Dutch furniture. In 1981, the three original shareholders of Kiehl sold all of their stock to nine persons who presently own 100% of the stock, so that Kiehl remained closely-held. When the original shareholders sold their stock, non-assignable bonds held by them were included in the sale. According to the shareholder agreement, the stock could not be sold without the bonds. In order to determine the gain/loss for the old shareholders and the basis for the new shareholders, the total purchase price paid by each of the nine new shareholders/bondholders was allocated proportionally to both the stock and the bonds.

The bonds have a stated interest rate of 5% and mature in 20 years. The bond interest is non-cumulative and can only be paid if the board of directors determines there is adequate net income. Since the bondholder and shareholder groups are identical, they are fully responsible for the appointment of the board of directors. Bond interest has been paid every year since 1981. The bonds currently represent the only liability of Kiehl other than trade accounts payable.

The nine shareholders of Kiehl are active participants in the management of the corporation and have been active since 1981. Dividends have been paid regularly to the shareholders.

Kiehl has been realizing substantial tax savings by treating the payments made on the non-assignable bonds as interest. We estimate that the present value of the tax savings resulting from past, present, and future treatment of these payments as interest totals approximately $200,000.

Relevant Law and Analysis

The tax law treats corporate debt and corporate stock differently. Payments on debt are deductible by the corporation as interest while payments on corporate stock are treated as dividends not deductible by the corporation. Therefore, it is often desirable for a corporation to treat financial instruments as debt. "Pure" debt can be defined as an unqualified obligation to pay a certain sum at a reasonably close fixed maturity date along with a fixed percentage in interest payable regardless of the debtor's income or lack thereof. Equity can be defined as an investment that allows an investor to share in the risks of a corporation in the hopes of obtaining profit when the corporation is profitable. Often, it is not clear whether a security is properly treated as debt or equity, because it may possess attributes of both. Such an instrument is referred to as a hybrid security. Neither the Internal Revenue Code nor the Regulations provide guidance regarding the proper classification of hybrid securities. However, the issue has been heavily litigated, so that a significant body of case law has developed. The courts consider a number of factors when making a determination. None of these factors taken alone is necessarily determinative. Several factors relevant to this case are discussed below.

Debt-Equity Ratio and Pro-Rata Ownership. The courts may question the classification of an instrument as debt if the purported debt is held pro-rata by shareholders or if the debt to equity ratio is so large that purported creditors are not protected by an adequate equity cushion.

Fixed Maturity Date. The presence of a fixed maturity date suggests that the instrument is debt and the absence of a fixed maturity date suggests equity treatment. Furthermore, if an instrument has a fixed maturity date, it is also important that the maturity date be reasonable. A maturity date that is unreasonably far into the future makes the risk seem greater and thus the instrument appears to resemble stock over debt.

Certainty of Return. If interest can only be paid on purported debt after certain income requirements are met or if the board of directors must approve the interest payments, classification of equity status is favored.

Label Applied By Parties. If an instrument has an ambiguous or hybrid name or label such as debenture stock or guaranteed stock, the courts do not tend to view this as a controlling factor; however, the courts have been reluctant to allow the repudiation of an unambiguous name or label.

Questions

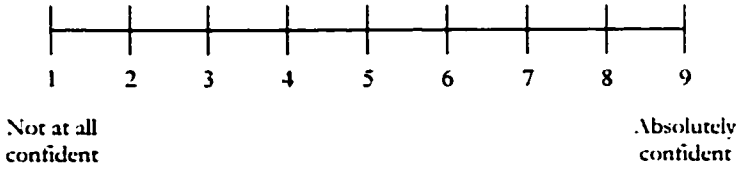
1. How do you recommend we treat the payments made on the non-assignable bonds? *Circle one.*

   Dividends Interest

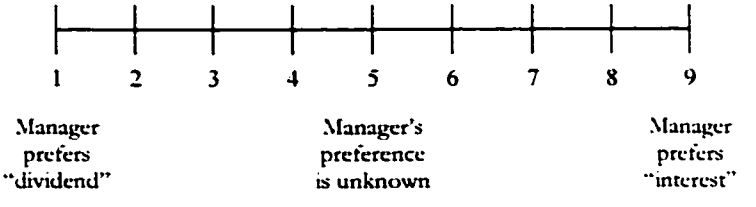
2. How confident are you that the treatment you indicated would be upheld by a court if litigated? *Enter a number from 0 to 100, where 0 indicates no chance that this position will be supported and 100 indicates that you are absolutely certain that this position will be supported.*

   _____ %

3. How confident are you that the tax manager in this case would find your choice and judgment in #1 acceptable? *Indicate your response on the scale below.*



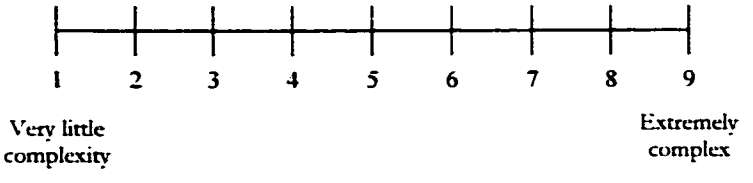
4. Do you think you know whether the tax manager in this case prefers dividend or interest treatment? *Indicate your response on the scale below.*



5. Do you expect that the tax manager in this case would agree with your assessments in #1 and #2 above? *Circle one.*

   Yes No

6. Please rate the level of complexity of this case:



Advice Selection – Kiehl Corp. Case

To aid you in making your judgments, you may consult with up to six (6) of the following persons. Budget and time constraints limit you to a total of six consultations. You are not required to engage in any consultation nor must you consult with all six advisors. You may assume that each person has been briefed on the facts and relevant law in this case. Recall [*insert knowledge of justifiee preferences and accountability type here*].

You have information about each of the advisors regarding their aggressiveness in their decision making (where 1 is "tending to be very conservative" and 9 is "tending to be very aggressive") and their preference for emphasizing effectiveness or efficiency in their decision-making process.

A table of the advisors and their characteristics is shown below:

Advisor	*Level of Aggressiveness*	*Advisor Prefers To Be...*
#9	9	Effective and thorough
#10	7	Effective and thorough
#11	3	Effective and thorough
#12	1	Effective and thorough
#13	9	Efficient
#14	7	Efficient
#15	3	Efficient
#16	1	Efficient

You may select advice from one or more of the advisors (up to a maximum of six advisors) using the computer in front of you. When you are finished obtaining advice, please turn to the next page of the packet.

Questions

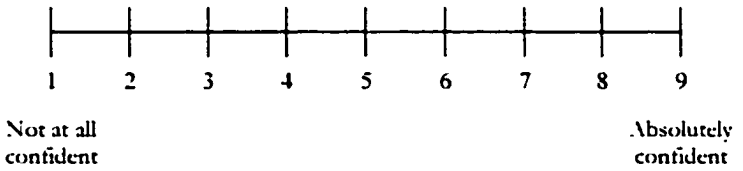
1. How do you recommend we treat the payments made on the non-assignable bonds? *Circle one.*

   Dividends Interest

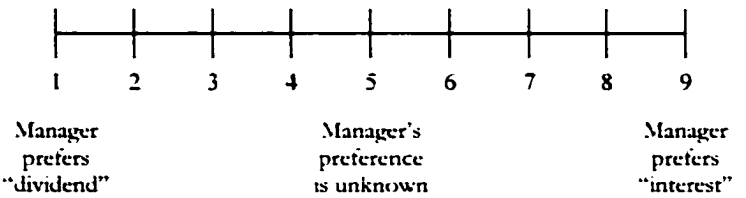
2. How confident are you that the treatment you indicated would be upheld by a court if litigated? *Enter a number from 0 to 100, where 0 indicates no chance that this position will be supported and 100 indicates that you are absolutely certain that this position will be supported.*

   _____ %

3. How confident are you that the tax manager in this case would find your choice and judgment in #1 acceptable? *Indicate your response on the scale below.*



4. Do you think you know whether the tax manager in this case prefers dividend or interest treatment? *Indicate your response on the scale below.*



5. Do you expect that the tax manager in this case would agree with your assessments in #1 and #2 above? *Circle one.*

   Yes No

6. Please rate the level of complexity of this case:

Questions

1. Prior to this experiment, had you previously conducted research on the issue of debt versus equity classification? *Circle one.*

   Yes No

   If yes, please indicate the number of times you have addressed this issue and the approximate date of your most recent experience (e.g. 1, 2, ... , 10 times, January 2001)?

   _____

2. Circle the number on the scale below that best indicates your level of expertise with respect to the issue of debt versus equity classification:

novice						*expert*
1	2	3	4	5	6	7

3. Which of the following best summarizes how your performance on the Kiehl Corporation case will be evaluated? *Circle one.*

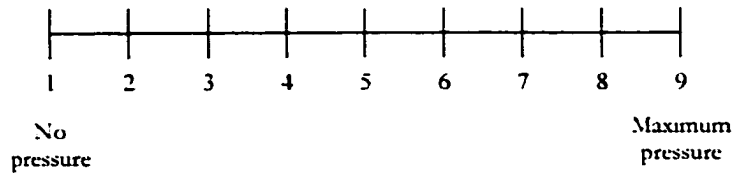
   a. Based SOLELY on the quality of my final judgment/decision, NOT on the decision-making process I used to make my final judgment/decision.

   b. Based SOLELY on the quality of the decision-making process I used to make my final judgment/decision, NOT on the quality of my final judgment/decision.

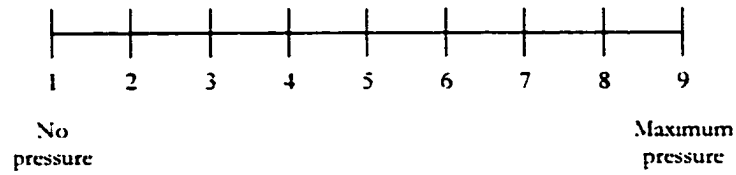
   c. My performance on this case will not be evaluated.

4. For the Kiehl Corporation case, how much pressure did you feel to justify the following:

   a. The quality of my final judgment/decision:



   b. The quality of the decision-making process I used to reach my final judgment/decision:



5. Which of the following best summarizes the manager's stated preferences in the Kiehl Corporation case? *Circle one.*

   a. He/she would like to support the client's preferred position if possible.

   b. He/she would like you to be as effective and thorough as possible in your analysis of this issue.

   c. He/she would like you to be as efficient as possible in your analysis of this issue.

   d. The manager revealed no preferences regarding this case.

Questions

1. Did you have any prior knowledge of this study? (i.e., prior to today, did you discuss this study with any previous participants?) *Circle one.*

   Yes No

   If yes, please explain:

   _____

   _____

   _____

2. Approximately how many people in the following positions in your office do you feel you could informally consult with regarding a particularly ambiguous tax issue?

   Partner: _____
   Manager: _____
   Senior: _____
   Staff: _____

Please indicate your level of agreement with each of the following statements by circling a number on the corresponding scale.

For example if you strongly agree with the statement circle the "7" on the scale. If you strongly disagree with the statement, circle the "1". If the extent to which you agree/disagree with the statement lies somewhere between these two extremes, circle a number that best represents that level of agreement with the statement.

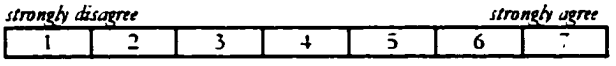
1. In an instance where no judicial authority exists with respect to an issue **and** where the Code and Regulations are ambiguous, I feel that the taxpayer is entitled to take the most favorable tax treatment.

strongly disagree						*strongly agree*
1	2	3	4	5	6	7

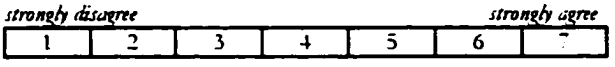
2. Generally speaking, my loyalties are first to the tax system, then to the taxpayer.

strongly disagree						*strongly agree*
1	2	3	4	5	6	7

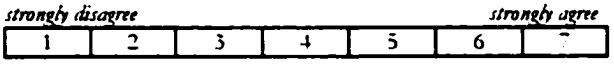
3. I feel I should apply ambiguous tax law to the taxpayer's benefit.



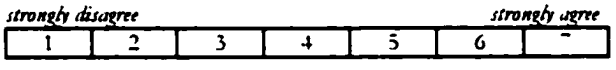
4. When examining a tax return, I tend to point out to taxpayers reasonable positions they could have taken which would have contributed to minimizing their tax liability.



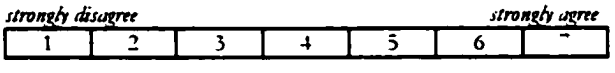
5. I do not believe it is important that I encourage taxpayers to pay the least amount of taxes possible.



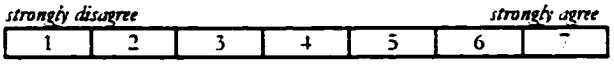
6. I never interpret unclear/ambiguous laws in favor of the taxpayers.



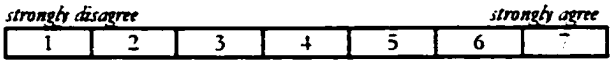
7. It is important to use trends in the law by trying to establish a pattern of more favorable treatment for the taxpayer and then extending this pattern to the taxpayer's position.



8. Where **no** judicial authority exists with respect to an issue, I feel that the taxpayer is entitled to take the most favorable tax treatment.



9. The taxpayer has the right to structure transactions in ways that yield the best tax result, even if the law is unclear in an area.



You have finished the second case.

Please do the following things:

1. **Put all of the pages back in the second envelope and close it.**

2. **Please DO NOT touch the computer screen in front of you. The experimenter will close the computer program.**

Thank you for your time and effort!

If you would like to receive a copy of the results of this study, please check the box below.

☐

APPENDIX B

INSTRUMENT FOR EXPERIMENT TWO

Department of Accountancy

UNIVERSITY OF ILLINOIS AT URBANA-CHAMPAIGN

General Instructions

1. We are conducting this study to learn about how accounting professionals make judgments and decisions. On the following pages, you will be asked to evaluate several individuals' decision-making processes. Your participation should consume no more than 15 – 20 minutes of your time. Your name will not be associated with your responses as you will only be identified by a unique participant identification number and that identification number will not be included in any data analysis or presentation.

2. Please carefully follow various instructions and reminders that appear throughout.

3. This is not a "test," and there are no single correct answers to the questions you will be asked. Please answer the questions conscientiously, just as you would do in a real-life situation. Also, please do not discuss the study with others prior to, during, or after completion.

4. Participation in this study is important but voluntary. You are free to withdraw from the study at any time for any reason.

5. If you would like, you may receive a copy of the results of this study by selecting the appropriate option at the end of the study.

Thank you.

Jon D. Perkins, J.D., CPA
Ph.D. Candidate
University of Illinois at Urbana-Champaign

Professor Ira Solomon
R. C. Evans Endowed Chair in Commerce
University of Illinois at Urbana-Champaign

Department of Accountancy

UNIVERSITY OF ILLINOIS AT URBANA-CHAMPAIGN

Informed Consent

Please read the following statements and sign below.

I have read a description of the study and understand that it should take no more than approximately 15 – 20 minutes to complete. I also understand that the purpose of this study is to learn about how accounting professionals make judgments and decisions. My participation in this study is voluntary and I may discontinue my participation at any time. I will not be exposed to any form of risk greater than that faced in ordinary life as a result of my participation in this study. If I choose not to participate in this study, I will not be penalized by my firm for non-participation. My name will not be associated with my responses as I will only be identified by a unique participant identification number and that identification number will not be included in any data analysis or presentation.

I also understand that should I have any questions about the study after today, I may directly contact Professor Ira Solomon (isolomon@uiuc.edu) or Jon Perkins (jdperkin@uiuc.edu or 217-351-8275). If I have any questions about my rights as a research participant, I may contact the University of Illinois at Urbana-Champaign Institutional Review Board at (217) 333-2670. Finally, if I so desire for my future reference, I can obtain a copy of this consent form from the researchers upon completion of this study.

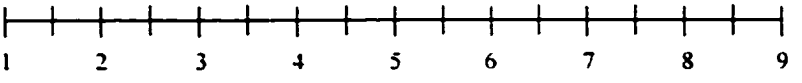
Signature Date

Instructions

On the next page you will see an assignment memorandum relating to a task that two hypothetical supervisors have given several subordinates to complete. On the pages that follow, you will be asked to evaluate six subordinates in two sets of three (see below). For each set, you will be given additional information from the subordinates' supervisor regarding the criteria they will use to evaluate the subordinates' performance as well as a description of each subordinate's informal consultation behavior and the subordinate's final judgment. In this study, informal consultation refers to communication with other members of the firm that is not required by firm policy.

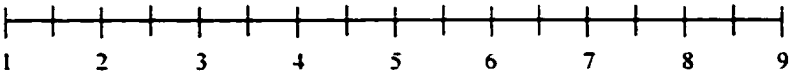
You then will be asked to answer the following two questions for each subordinate. When marking your answers, please make an X on the scale between 1 and 9 at the point that best reflects your judgment:

1. Please rate **Subordinate X's** overall performance considering all potential evaluators (superiors, courts, IRS, etc.). Consider the same performance dimensions that you would use in practice:



Extremely low quality — Extremely high quality

2. Please rate the efficiency of **Subordinate X's** performance. Consider the same performance dimensions that you would use in practice:



Extremely inefficient — Extremely efficient

When making your assessments, please assume that all of the subordinates have identical experience with the issue(s) raised in the case, had equivalent access to, and reviewed all of the law relevant to these issue(s). Please also assume that all subordinates had the opportunity to informally consult with up to six advisors regarding the case and that each subordinate fully briefed each consulted advisor on the client facts and relevant law. Assume further that the advisors were members of the firm who had identical experience and expertise with the issue(s) raised in the case. Each advisor has a reputation for being either: (1) aggressive (tending to support aggressive/riskier tax positions) or (2) conservative (tending to support conservative/less risky tax positions).

Please turn to the next page.

Please review the assignment memorandum below and then turn to the next page and begin.

Tax Issue

TO: Subordinates
FROM: Supervisors A and B
SUBJECT: Jim Hunt; character of loss on sale of land

Jim Hunt is the CEO of Delta Electronics, Inc., an important client for whom we have done audit and tax work for many years. We are in the process of preparing Jim's 2000 federal income tax return and need to decide whether a loss he realized during 2000 on sales of real estate should be treated as ordinary or capital. To make this decision, we need to determine whether Jim is a dealer or investor in that real estate for income tax purposes.

We estimate that if Jim were treated as a dealer in real estate with regard to this transaction, said treatment would reduce his 2000 federal income tax liability by $200,000 because the entire loss would be deductible in 2000. In contrast, if Jim were treated as an investor, he only could deduct a $3,000 capital loss in 2000 and the remainder of the loss would be a capital loss carry-forward to 2001 and later years. With the possible exception of this completed transaction, Jim had no other capital gain or loss transactions this year.

Subordinates 1 – 3 report to **Supervisor A**. Along with the assignment memorandum you saw earlier, each of these subordinates was given the following additional instructions:

> "To best defend our treatment of this item on the return, we would like you to be as EFFECTIVE AND THOROUGH as possible in your analysis of this issue. Also, your performance on this task will be evaluated based SOLELY on the quality of the decision-making process you use to make your final judgment/decision, NOT on the final judgment/decision you make."

These subordinates' informal consultation behaviors and final judgments were as follows:

SUBORDINATE #1

Consulted with four advisors *in the following order*:

First advisor:	Conservative (Judgment: Investor)
Second advisor:	Aggressive (Judgment: Dealer)
Third advisor:	Aggressive (Judgment: Dealer)
Fourth advisor:	Aggressive (Judgment: Dealer)
Final judgment:	Jim Hunt should be considered a dealer and, therefore, the loss on the sale of real estate should be treated as ordinary.

SUBORDINATE #2

Consulted with four advisors *in the following order*:

First advisor:	Aggressive (Judgment: Dealer)
Second advisor:	Conservative (Judgment: Investor)
Third advisor:	Conservative (Judgment: Investor)
Fourth advisor:	Aggressive (Judgment: Dealer)
Final judgment:	Jim Hunt should be considered a dealer and, therefore, the loss on the sale of real estate should be treated as ordinary.

SUBORDINATE #3

Consulted with four advisors *in the following order*:

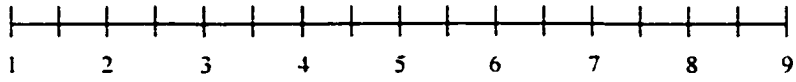
First advisor:	Aggressive (Judgment: Dealer)
Second advisor:	Aggressive (Judgment: Dealer)
Third advisor:	Aggressive (Judgment: Dealer)
Fourth advisor:	Aggressive (Judgment: Dealer)
Final judgment:	Jim Hunt should be considered a dealer and, therefore, the loss on the sale of real estate should be treated as ordinary.

Please turn to the next page.

Based on this information, please answer the following questions. When marking your answers, please make an X on the scale between 1 and 9 at the point that best reflects your judgment.

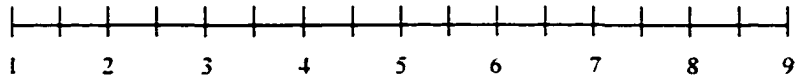
---

1. Please rate **Subordinate #1's** overall performance considering all potential evaluators (superiors, courts, IRS, etc.). Consider the same performance dimensions that you would use in practice:



Extremely low quality — Extremely high quality

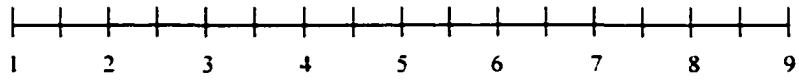
2. Please rate the efficiency of **Subordinate #1's** performance. Consider the same performance dimensions that you would use in practice:



Extremely inefficient — Extremely efficient

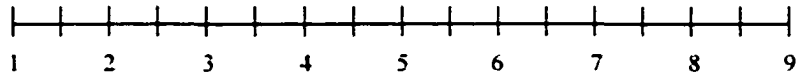
---

3. Please rate **Subordinate #2's** overall performance considering all potential evaluators (superiors, courts, IRS, etc.). Consider the same performance dimensions that you would use in practice:



Extremely low quality — Extremely high quality

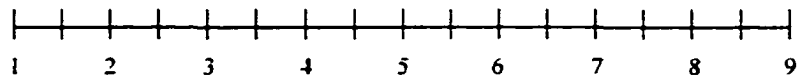
4. Please rate the efficiency of **Subordinate #2's** performance. Consider the same performance dimensions that you would use in practice:



Extremely inefficient — Extremely efficient

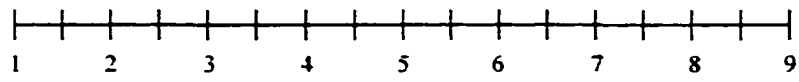
---

5. Please rate **Subordinate #3's** overall performance considering all potential evaluators (superiors, courts, IRS, etc.). Consider the same performance dimensions that you would use in practice:



Extremely low quality — Extremely high quality

6. Please rate the efficiency of **Subordinate #3's** performance. Consider the same performance dimensions that you would use in practice:



Extremely inefficient — Extremely efficient

Please turn to the next page.

Subordinates 4 – 6 report to **Supervisor B**. Along with the assignment memorandum you saw earlier, each of these subordinates was given the following additional instructions:

"We are concerned about the amount of time we have already invested in this client's return. As a result, we would like you to be as EFFICIENT as possible in your analysis of this issue. Also, your performance on this task will be evaluated based SOLELY on the quality of the decision-making process you use to make your final judgment/decision, NOT on the final judgment/decision you make."

These subordinates' informal consultation behaviors and final judgments were as follows:

SUBORDINATE #4

Consulted with four advisors *in the following order*:

First advisor:	Aggressive (Judgment: Dealer)
Second advisor:	Aggressive (Judgment: Dealer)
Third advisor:	Aggressive (Judgment: Dealer)
Fourth advisor:	Aggressive (Judgment: Dealer)
Final judgment:	Jim Hunt should be considered a dealer and, therefore, the loss on the sale of real estate should be treated as ordinary.

SUBORDINATE #5

Consulted with four advisors *in the following order*:

First advisor:	Conservative (Judgment: Investor)
Second advisor:	Aggressive (Judgment: Dealer)
Third advisor:	Aggressive (Judgment: Dealer)
Fourth advisor:	Aggressive (Judgment: Dealer)
Final judgment:	Jim Hunt should be considered a dealer and, therefore, the loss on the sale of real estate should be treated as ordinary.

SUBORDINATE #6

Consulted with four advisors (and received their judgments) *in the following order*:

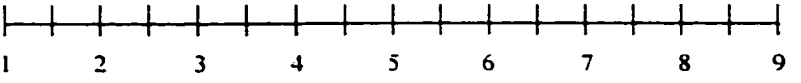
First advisor:	Aggressive (Judgment: Dealer)
Second advisor:	Conservative (Judgment: Investor)
Third advisor:	Conservative (Judgment: Investor)
Fourth advisor:	Aggressive (Judgment: Dealer)
Final judgment:	Jim Hunt should be considered a dealer and, therefore, the loss on the sale of real estate should be treated as ordinary.

Please turn to the next page.

Based on this information, please answer the following questions. When marking your answers, please make an X on the scale between 1 and 9 at the point that best reflects your judgment.

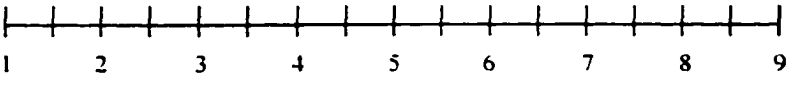
---

1. Please rate **Subordinate #4's** overall performance considering all potential evaluators (superiors, courts, IRS, etc.). Consider the same performance dimensions that you would use in practice:



Extremely low quality — Extremely high quality

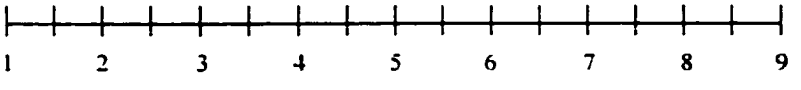
2. Please rate the efficiency of **Subordinate #4's** performance. Consider the same performance dimensions that you would use in practice:



Extremely inefficient — Extremely efficient

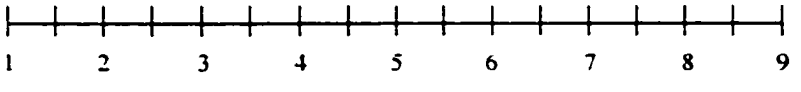
---

3. Please rate **Subordinate #5's** overall performance considering all potential evaluators (superiors, courts, IRS, etc.). Consider the same performance dimensions that you would use in practice:



Extremely low quality — Extremely high quality

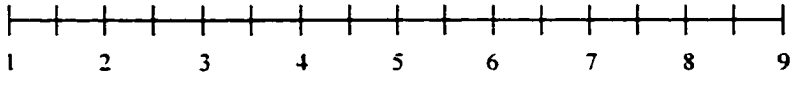
4. Please rate the efficiency of **Subordinate #5's** performance. Consider the same performance dimensions that you would use in practice:



Extremely inefficient — Extremely efficient

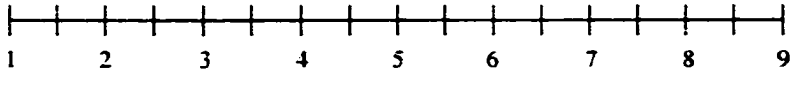
---

5. Please rate **Subordinate #6's** overall performance considering all potential evaluators (superiors, courts, IRS, etc.). Consider the same performance dimensions that you would use in practice:



Extremely low quality — Extremely high quality

6. Please rate the efficiency of **Subordinate #6's** performance. Consider the same performance dimensions that you would use in practice:



Extremely inefficient — Extremely efficient

Please turn to the next page.

Follow-Up Questions

1. Did you have any prior knowledge of this study? (i.e., prior to today, did you discuss this study with any other participants?) *Circle one.*

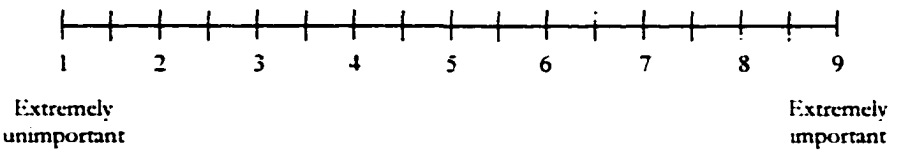
   Yes No

2. Please rank order the following parts of an accountant's decision-making process in order of importance (use 1, 2, 3, etc. with 1 being the most important, 2 being the next most important, etc.):

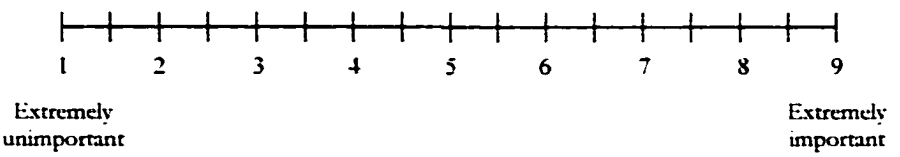
Issue identification	_____
Finding relevant precedent	_____
Staying within budgeted hours	_____
Consultation with knowledgeable advisors	_____
Advising the client regarding any risks they are taking	_____
_____	_____
_____	_____

   You may use the blank lines to indicate (and rate) any other factors that you consider to be important but are not listed.

3. How important is informal consultation with others in an accountant's decision-making process?

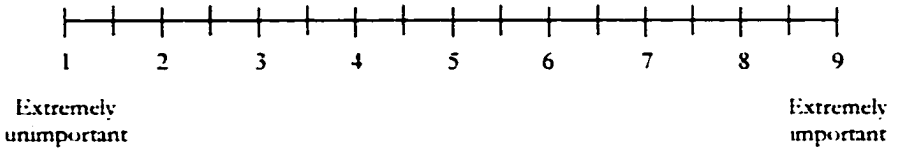


4. In evaluating a subordinate's overall performance, to what extent does the **balance** (i.e., aggressiveness and conservativeness) of advisors consulted matter?

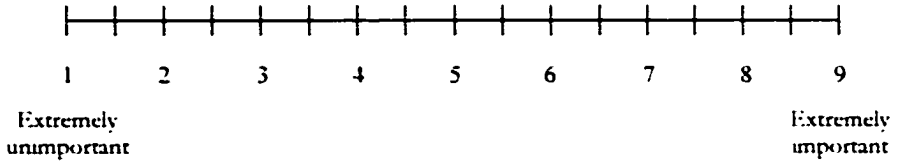


Please turn to the next page.

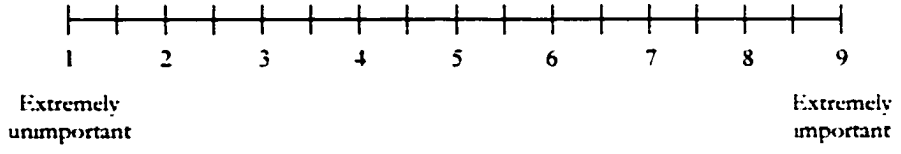
5. In evaluating a subordinate's overall performance, to what extent does the **number** of advisors consulted matter?



6. In evaluating the overall **efficiency** of a subordinate's performance, to what extent does the **balance** (i.e., aggressiveness and conservativeness) of advisors consulted matter?



7. In evaluating the overall **efficiency** of a subordinate's performance, to what extent does the **number** of advisors consulted matter?



8. Please indicate your current job title (e.g., manager, partner, etc.) and your amount of accounting and tax experience:

Current job title	_____	
Accounting experience	_____ Years	_____ Months
Tax experience (if different)	_____ Years	_____ Months

You are finished.

If you would like to receive a copy of the results of this study, please check the box below and provide your e-mail address.

☐ _____

Thank you very much for your participation!

APPENDIX C

FIGURES, EXHIBITS, AND TABLES

FIGURE 1

MODEL OF STRATEGIC INFORMAL CONSULTATION

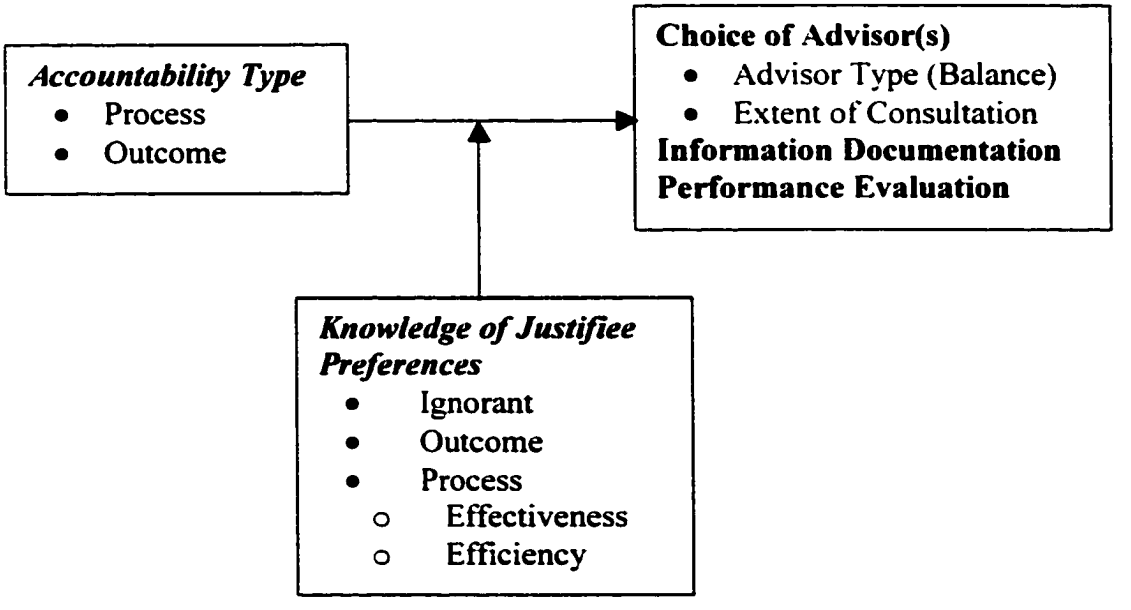
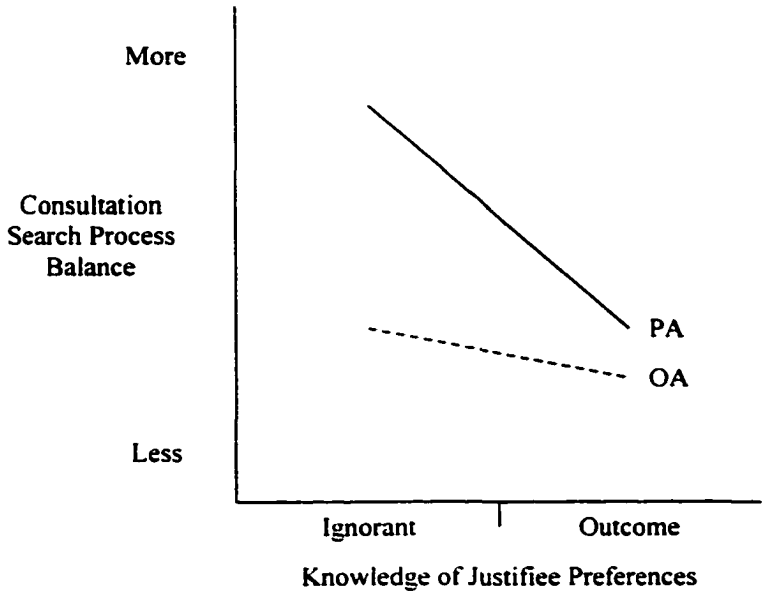


FIGURE 2

GRAPHICAL REPRESENTATION OF HYPOTHESES

Panel A: *Hypothesis #2a*



Panel B: *Hypothesis #2b*

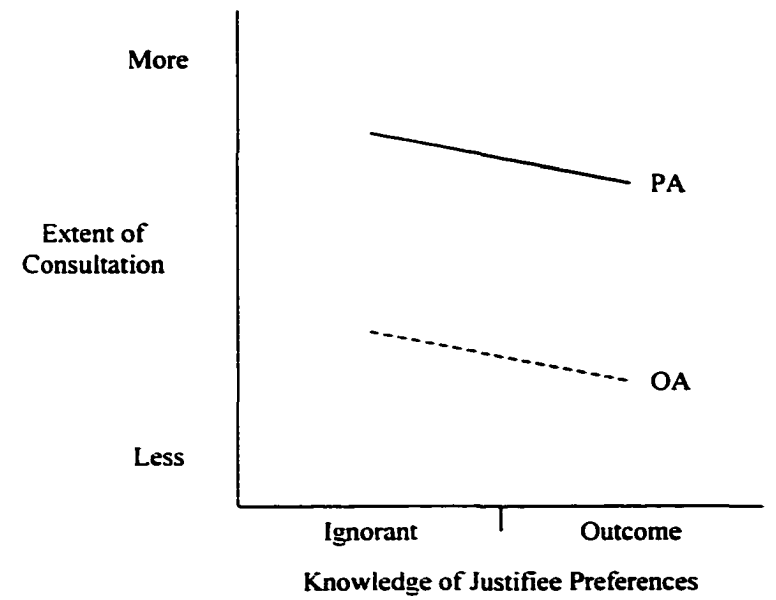
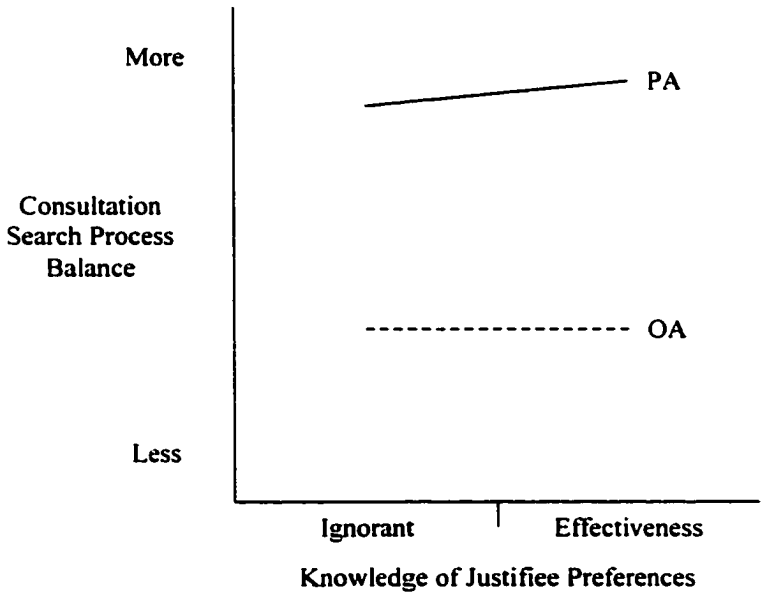


FIGURE 2 (CONTINUED)

GRAPHICAL REPRESENTATION OF HYPOTHESES

Panel C: *Hypothesis #3a*



Panel D: *Hypothesis #3b*

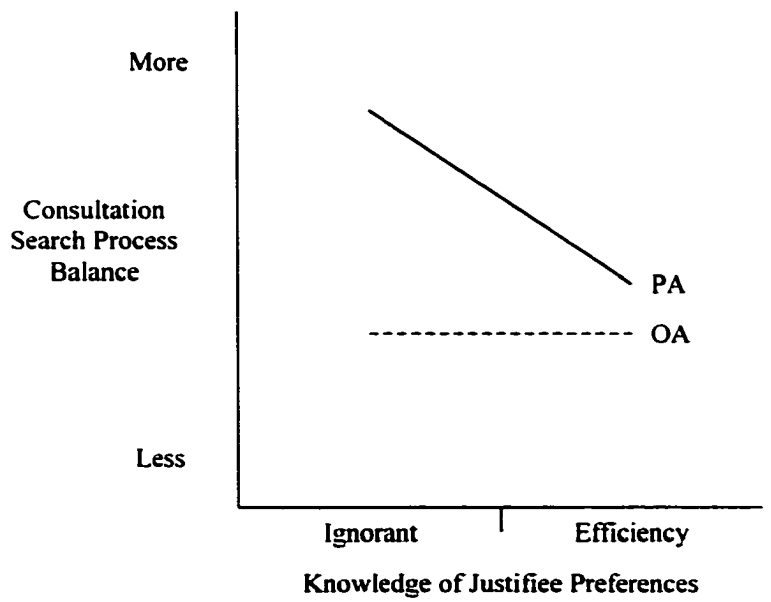
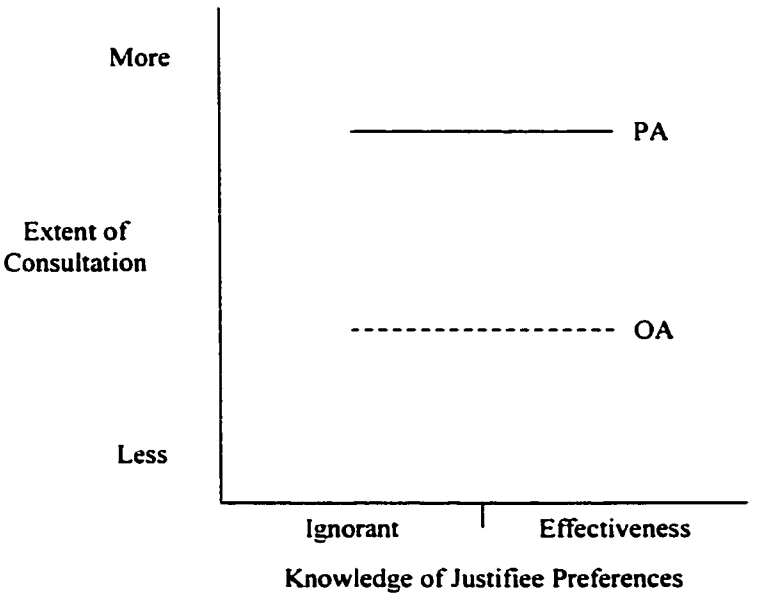


FIGURE 2 (CONTINUED)

GRAPHICAL REPRESENTATION OF HYPOTHESES

Panel E: *Hypothesis #3c*



Panel F: *Hypothesis #3d*

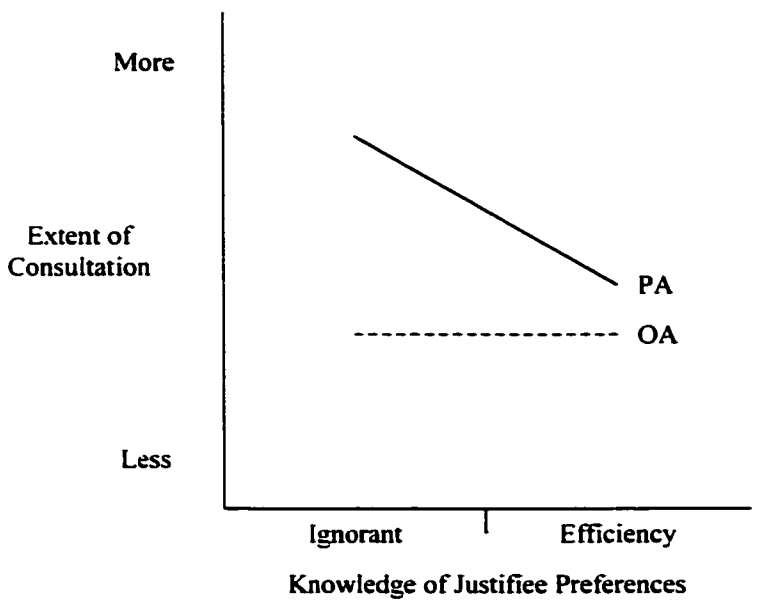
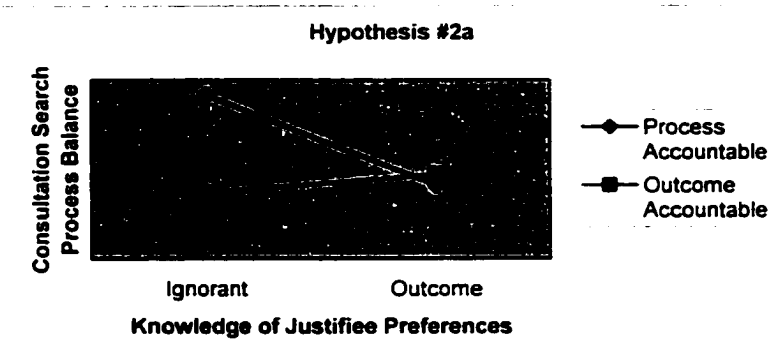


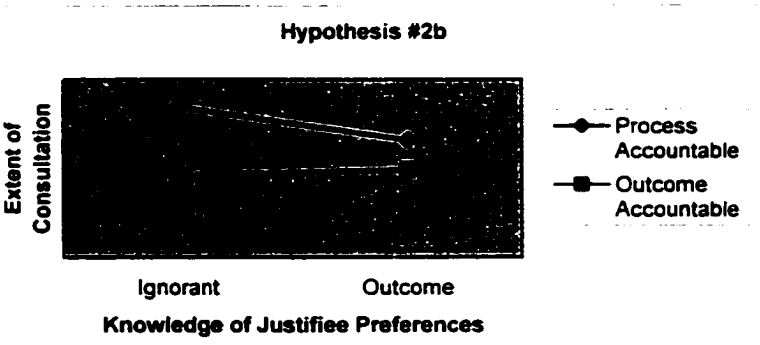
FIGURE 3

GRAPHICAL REPRESENTATION OF RESULTS

Panel A: Hypothesis #2a (p-value (one-sided) < 0.01)



Panel B: Hypothesis #2b (p-value (two-sided) = 0.02)



Panel C: Hypothesis #3a (p-value (one-sided) = 0.17)

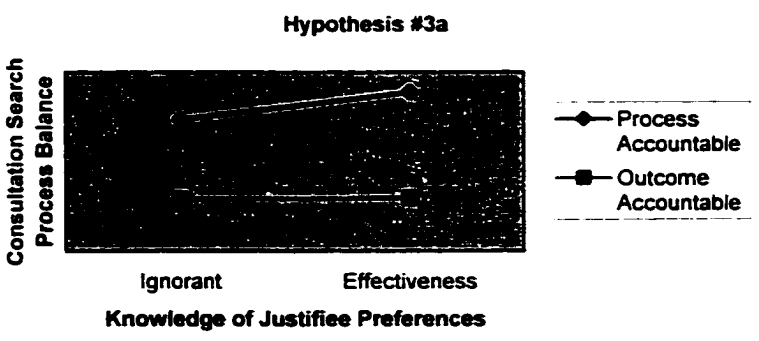
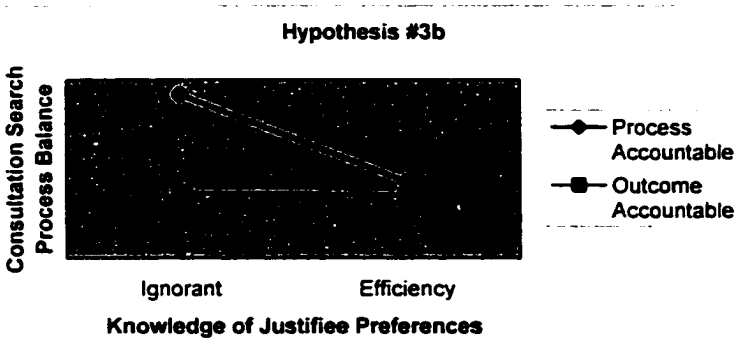


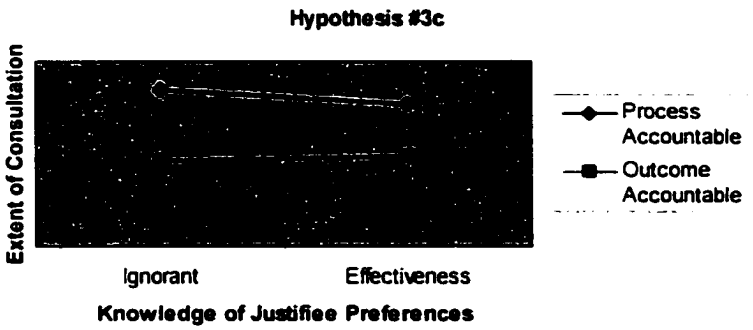
FIGURE 3 (CONTINUED)

GRAPHICAL REPRESENTATION OF RESULTS

Panel D: Hypothesis #3b (p-value (one-sided) = 0.01)



Panel E: Hypothesis #3c (p-value (two-sided) = 0.26)



Panel F: Hypothesis #3d (p-value (one-sided) < 0.01)

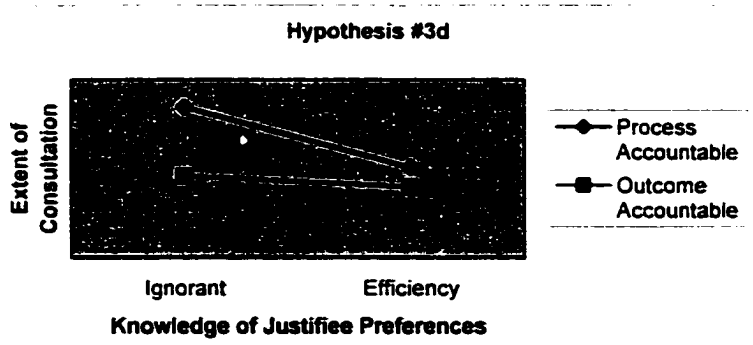
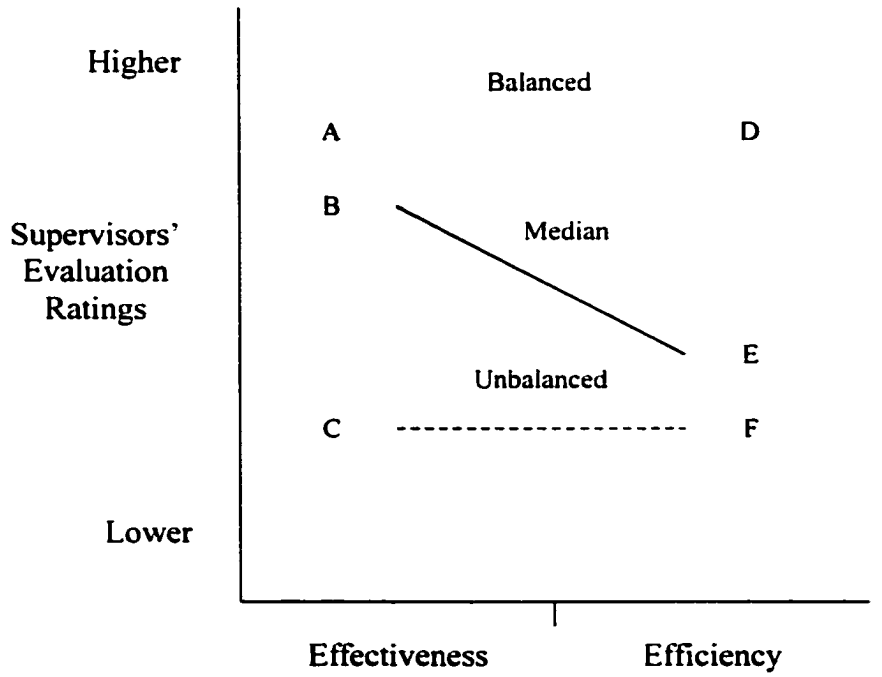


FIGURE 4

SUPERVISORS' PERFORMANCE EVALUATIONS



This graph shows the expected relationships between the supervisors' performance evaluations for each of the six subordinates. The specific relationships corresponding to the hypotheses are as follows:

H5a: B = A
H5b: B > C
H6a: E < D
H6b: E = F
H7: B > E

EXHIBIT 1

SEQUENCE OF EXPERIMENTAL PROCEDURES

TASK ASSIGNMENT PHASE

1. Participants read a description of the justifiee and assignment memorandum. (*Manipulated accountability type and knowledge of justifiee preferences*)*
2. Participants read the case facts and a summary and analysis of the relevant tax law.*
3. Participants asked for the following items:
    a. Recommended tax position for the client
    b. Confidence that their recommendation would be upheld by a court if litigated
    c. Confidence in the acceptability of their recommendation to the superior
    d. An assessment of the tax treatment preferred by the superior
    e. Whether they expect the justifiee to agree with their assessments of (a) and (b)
    f. Rating of the case's level of complexity

ADVICE SOLICITATION PHASE

4. Participants presented with a menu of eight possible advisors from which to choose.
5. Participants choose an advisor.
6. Participants receive advice from advisor chosen.
7. Participants repeat steps 5 through 7 until no more advice is sought (maximum of six advisors).
8. Participants asked to repeat items a-f from Step 3.

POST-CONSULTATION PHASE

9. Subjects write brief justification memorandum.
10. Subjects complete manipulation checks.
11. Subjects complete demographic and other post-experimental questions.

*These items may be reviewed as often as desired up through Step 9.

Participants completed Steps 1 through 8 for each of the two tasks but wrote the brief justification memorandum for the first case only due to time constraints.

EXHIBIT 2

CONSTRUCTION AND EXAMPLE OF BALANCE MEASURE

I base my measure of consultation balance on the idea of a fulcrum or seesaw. I weight each advisor in a participant's consultation process, giving the greatest weight to the first advisor, the next greatest to the next, and so on. I also sign the weight based on the nature of the advisor (aggressive or conservative) in order to distinguish between the two types, sum the weights, and take the absolute value of the result to obtain a composite balance score. I choose the weights to meet the following characteristics:

1. The weights sum to one (before signing the weights based on the nature of the advisor).

   This characteristic facilitates easy interpretation of the measure. A value closer to 0 indicates a more balanced consultation process while a value closer to 1 indicates a more unbalanced consultation process.

2. The weights are evenly spaced apart from one another.

   There is no theoretical reason to expect other than a linear pattern of advisor weights.

3. Each weight is greater than zero (before signing the weights based on the nature of the advisor).

   It is logical to assume that each advisor is selected for a purpose.

Since the participants were able to select up to six advisors and I want to weight the advisors in order of their selection, I weight the six possible advisors as follows:

First advisor chosen = 6W	Fourth advisor chosen = 3W
Second advisor chosen = 5W	Fifth advisor chosen = 2W
Third advisor chosen = 4W	Sixth advisor chosen = W

Since the weights must all sum to one, it follows that 21W = 1 and W = 0.0476904. This results in the following set of weights:

First advisor chosen = 0.285714	Fourth advisor chosen = 0.142857
Second advisor chosen = 0.238095	Fifth advisor chosen = 0.095238
Third advisor chosen = 0.190476	Sixth advisor chosen = 0.047690

To illustrate the use of these weights, suppose an individual consults five advisors in the following order: Aggressive, Aggressive, Conservative, Aggressive, Conservative. Signing the aggressive advisors positively and the conservative advisors negatively results in a balance score of 0.285714 + 0.238095 – 0.190476 + 0.142857 – 0.095238 = 0.380952.

TABLE 1

Descriptive Statistics[a]

Panel A: Participants' Consultation Balance[b]

Accountability Type	*Knowledge of Justifiee Preference*[c]							
	Ignorant		Outcome		Process (Effectiveness)		Process (Efficiency)	
Process	(a1)	0.17 (0.10) 32	(b1)	0.27 (0.14) 32	(c1)	0.13 (0.11) 30	(d1)	0.26 (0.10) 31
Outcome	(a2)	0.28 (0.12) 32	(b2)	0.26 (0.10) 32	(c2)	0.28 (0.11) 30	(d2)	0.28 (0.13) 31

Panel B: Participants' Extent of Consultation[d]

Accountability Type	*Knowledge of Justifiee Preference*							
	Ignorant		Outcome		Process (Effectiveness)		Process (Efficiency)	
Process	(a1)	5.53 (0.76) 32	(b1)	4.97 (0.90) 32	(c1)	5.30 (0.88) 30	(d1)	4.52 (0.89) 31
Outcome	(a2)	4.38 (1.01) 32	(b2)	4.47 (1.02) 32	(c2)	4.47 (1.04) 30	(d2)	4.19 (0.83) 31

Panel C: Participants' Information Documentation[e]

Accountability Type	*Knowledge of Justifiee Preference*							
	Ignorant		Outcome		Process (Effectiveness)		Process (Efficiency)	
Process	(a1)	0.18 (0.18) 16	(b1)	0.44 (0.15) 16	(c1)	0.18 (0.18) 15	(d1)	0.38 (0.19) 15
Outcome	(a2)	0.39 (0.15) 16	(b2)	0.38 (0.18) 16	(c2)	0.40 (0.18) 15	(d2)	0.41 (0.17) 16

[a] This table provides descriptive statistics on participants' consultation balance, extent of consultation, and information documentation. Each cell includes participants' mean score, (standard deviation), and n. I elicited the consultation balance and extent of consultation scores by allowing participants the opportunity to consult with up to six advisors after making a judgment about an ambiguous tax problem. I elicited the information documentation scores by having participants write a justification memorandum for the first of two ambiguous tax problems.

[b] For a discussion of the measure used to calculate participants' balance scores, see Exhibit 2.

[c] Participants completed each case after being given information about the justifiee's preference. I gave no justifiee preference information to participants in the ignorant condition.

[d] I calculated participants' extent of consultation as the number of advisors consulted.

[e] I calculated the information documentation score (i.e., stylization) for each participant by summing the information documented as supportive of his or her judgment and dividing by the total number of pieces of information documented. I then standardized this ratio by subtracting 0.5 and taking the absolute value of the result. Values for this measure may range from 0 to 0.5 where a greater number indicates a greater amount of information stylization.

TABLE 2

The Influence of Accountability Type and Knowledge of Justifiee Preference on Informal Consultation Balance[a]

Panel A: Experimental Design

	Knowledge of Justifiee Preference			
Accountability Type	Ignorant	Outcome	Process (Effectiveness)	Process (Efficiency)
Process	a1	b1	c1	d1
Outcome	a2	b2	c2	d2

Panel B: Repeated Measures ANOVA[b]

Source	*df*	SS	MS	F	Pr > F
Between-Subjects Effect					
Knowledge	3	0.2000	0.0667	4.46	0.01
Error	121	1.8094	0.0150		
Within-Subjects Effects					
Accountability	1	0.2663	0.2663	22.62	< 0.01
Accountability x Knowledge	3	0.2678	0.0893	7.58	< 0.01
Error	121	1.4244	0.0118		

TABLE 2 (CONTINUED)

The Influence of Accountability Type and Knowledge of Justifiee Preference on Informal Consultation Balance[a]

Panel C: Planned Contrasts

	Hypotheses	*Contrasts*	*Test Statistic*	*P – Value*[c]
H1a:	When justifiee preferences are not directly known, PA accountants will engage in more balanced consultation than OA accountants.	a1 < a2	F = 16.48	< 0.01
H2a:	The difference in consultation balance between PA accountants who do not know the justifiee's preferences and PA accountants who know the justifiee's outcome preference is greater than the difference in consultation balance between OA accountants who do not know the justifiee's preferences and OA accountants who know the justifiee's outcome preference.	(b1 – a1) > (b2 – a2)	F = 10.12	< 0.01
H3a:	When the justifiee has a process preference for effectiveness, the difference in balance between PA accountants who do not know the justifiee's preferences and PA accountants who know the justifiee's process preference is greater than the difference in balance between OA accountants who do not know the justifiee's preferences and OA accountants who know the justifiee's process preference.	(c1 – a1) > (c2 – a2)	F = 0.92	0.17
H3b:	When the justifiee has a process preference for efficiency, the difference in balance between PA accountants who do not know the justifiee's preferences and PA accountants who know the justifiee's process preference is greater than the difference in balance between OA accountants who do not know the justifiee's preferences and OA accountants who know the justifiee's process preference.	(d1 – a1) > (d2 – a2)	F = 11.95	0.01

[a] This table provides inferential statistics related to participants' consultation balance. The ANOVA in Panel B is a repeated-measures ANOVA with knowledge of justifiee preferences as a between-subjects factor and accountability type as a within-subjects factor. The planned contrasts in Panel C use the appropriate mean squared error term from the repeated-measures ANOVA in Panel B. As part of my sensitivity analysis, I included participants' advocacy score (measured using a nine-question scale developed in Davis and Mason (2003) and Mason and Levy (2001)), months of tax experience, perceived expertise with the tax issues involved, and perceived case complexity as covariates. Since none of the covariates were statistically significant and had no effect on the treatment effects, I omitted them from the above analysis.

[b] I randomly assigned 16 versions of the experimental instrument to cover the four between-subject treatment conditions and control for order effects associated with the within-subjects accountability manipulation (two levels) and the order in which the cases and advisors were presented to participants (2 cases). Post-experimental analysis indicated that this random assignment was successful as there were no order effects associated with case type ($p = 0.28$ for consultation balance and $p = 0.80$ for extent of consultation) and case order ($p = 0.87$ for consultation balance and $p = 0.45$ for extent of consultation).

[c] All p-values in Panel C are one-tailed.

TABLE 3

The Influence of Accountability Type and Knowledge of Justifiee Preference on Extent of Informal Consultation[a]

Panel A: Experimental Design

	Knowledge of Justifiee Preference			
Accountability Type	Ignorant	Outcome	Process (Effectiveness)	Process (Efficiency)
Process	a1	b1	c1	d1
Outcome	a2	b2	c2	d2

Panel B: Repeated Measures ANOVA[b]

Source	*df*	SS	MS	F	Pr > F
Between-Subjects Effect					
Knowledge	3	13.3302	4.4434	4.19	< 0.01
Error	121	128.1738	1.0593		
Within-Subjects Effects					
Accountability	1	30.8696	30.8696	48.78	< 0.01
Accountability x Knowledge	3	6.4442	2.1481	3.39	0.02
Error	121	76.5798	0.6329		

TABLE 3 (CONTINUED)

The Influence of Accountability Type and Knowledge of Justifiee Preference on Extent of Informal Consultation[a]

Panel C: Planned Contrasts

	Hypotheses	*Contrasts*	*Test Statistic*	*P - Value*
H1b:	When justifiee preferences are not directly known, PA accountants will consult to a greater extent than OA accountants.	a1 > a2	F = 33.80	< 0.01*
H2b:	The difference in the extent of consultation between PA accountants who do not know the justifiee's preferences and PA accountants who know the justifiee's outcome preference is equal to the difference in the extent of consultation between OA accountants who do not know the justifiee's preferences and OA accountants who know the justifiee's outcome preference.	(b1 – a1) = (b2 – a2)	F = 5.44	0.02**
H3c:	When the justifiee has a process preference for effectiveness, the difference in the extent of consultation between PA accountants who do not know the justifiee's preferences and PA accountants who know the justifiee's process preference is equal to the difference in the extent of consultation between OA accountants who do not know the justifiee's preferences and OA accountants who know the justifiee's process preference.	(c1 – a1) = (c2 – a2)	F = 1.28	0.26**
H3d:	When the justifiee has a process preference for efficiency, the difference in the extent of consultation between PA accountants who do not know the justifiee's preferences and PA accountants who know the justifiee's process preference is greater than the difference in the extent of consultation between OA accountants who do not know the justifiee's preferences and OA accountants who know the justifiee's process preference.	(d1 – a1) > (d2 – a2)	F = 8.65	< 0.01*

[a] This table provides inferential statistics related to participants' extent of informal consultation. The ANOVA in Panel B is a repeated-measures ANOVA with knowledge of justifiee preferences as a between-subjects factor and accountability type as a within-subjects factor. The planned contrasts in Panel C use the appropriate mean squared error term from the repeated-measures ANOVA in Panel B. As part of my sensitivity analysis, I included participants' advocacy score (measured using a nine-question scale developed in Davis and Mason (2003) and Mason and Levy (2001)), months of tax experience, perceived expertise with the tax issues involved, and perceived case complexity as covariates. Since none of the covariates were statistically significant and had no effect on the treatment effects, I omitted them from the above analysis.

[b] I randomly assigned 16 versions of the experimental instrument to cover the four between-subject treatment conditions and control for order effects associated with the within-subjects accountability manipulation (two levels) and the order in which the cases and advisors were presented to participants (2 cases). Post-experimental analysis indicated that this random assignment was successful as there were no order effects associated with case type ($p = 0.28$ for consultation balance and $p = 0.80$ for extent of consultation) and case order ($p = 0.87$ for consultation balance and $p = 0.45$ for extent of consultation).

*One-tailed p-value: **Two-tailed p-value.

TABLE 4

The Influence of Accountability Type and Knowledge of Justifiee Preferences on Information Documentation[a]

Panel A: Experimental Design

	Knowledge of Justifiee Preference			
Accountability Type	Ignorant	Outcome	Process (Effectiveness)	Process (Efficiency)
Process	a1	b1	c1	d1
Outcome	a2	b2	c2	d2

Panel B: Two-Way ANOVA

Source	*df*	SS	MS	F	Pr > F
Knowledge	3	0.4159	0.1386	4.72	< 0.01
Accountability	1	0.3108	0.3108	10.59	< 0.01
Knowledge x Accountability	3	0.4495	0.1498	5.10	< 0.01
Error	117	3.4347	0.0294		

Panel C: Planned Contrast

	Hypothesis	*Contrast*	*Test Statistic*	*P - Value*
H4:	PA accountants who know the justifiee's outcome preference or process preference for efficiency and OA accountants engage in more information stylization than PA accountants who do not know the justifiee's preferences or know the justifiee's process preference for effectiveness.	$\frac{(a2 + b1 + b2 + c2 + d1 + d2)}{6} > \frac{(a1 + c1)}{2}$	F = 38.63	< 0.01*

[a] This table provides inferential statistics related to participants' information documentation. The ANOVA in Panel B is a two-way ANOVA with knowledge of justifiee preferences and accountability type as between-subjects factors. The planned contrast in Panel C used the appropriate mean squared error term from the two-way ANOVA in Panel B. As part of my sensitivity analysis, I included participants' advocacy score (measured using a nine-question scale developed in Davis and Mason (2003) and Mason and Levy (2001)), months of tax experience, perceived expertise with the tax issues involved, and perceived case complexity as covariates. Since none of the covariates were statistically significant and had no effect on the treatment effects, I omitted them from the above analysis.

*One-tailed *p*-value.

TABLE 5

Descriptive Statistics for Participants' Overall Performance Evaluations In Experiment Two[a]

Justifiee Process Preference					
Effectiveness			Efficiency		
Completely Balanced Consultation	Median Consultation from Experiment One	Completely Unbalanced Consultation	Completely Balanced Consultation	Median Consultation from Experiment One	Completely Unbalanced Consultation
6.05 (2.00)	5.75 (1.72)	4.46 (2.09)	6.05 (1.77)	4.95 (1.20)	4.28 (2.17)

[a] This table provides descriptive statistics on participants' overall performance evaluations for the six subordinates in the second experiment. Each cell includes participants' mean evaluation (standard deviation). Participants rated each subordinate using a 9-point Likert-type scale with endpoints of 1 (extremely low quality) and 9 (extremely high quality).

APPENDIX D

COMPUTER INSTRUMENT FOR EXPERIMENT ONE

VITA

Jon Douglas Perkins was born in Portsmouth, Virginia on March 31, 1969. He graduated from the University of Missouri at Columbia in 1991 with a Bachelor of Science in Accountancy and a Bachelor of Science in Business Administration with emphases in Finance and Economics. He graduated from the University of Missouri at Columbia School of Law in 1995 with a Juris Doctor degree. For two years he worked as a staff accountant at Moeller & Company, P.C. before relocating to Champaign, Illinois to pursue his Ph.D. in Accountancy. Following the completion of his Ph.D., Jon will begin work at The Florida State University as an Assistant Professor in the Department of Accounting.