AUDITOR QUALITY AND STAGE OF MORAL REASONING

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Abstract

Recent audit failures call into question auditors' ethical integrity. Although inconclusive, the accounting literature suggests that moral reasoning may be an important component of auditor quality. The purpose of our study is to empirically test whether moral reasoning is an element of auditor quality.

Assuming Big Five firms hire higher quality auditors than non-Big Five firms, auditors' moral reasoning is assessed and compared across firm type. We found that Big Five auditors' stage of moral reasoning is significantly higher than non-Big Five auditors, suggesting a link between auditor quality and moral reasoning. We also investigate whether there are differences in the ethical socialization processes across firm type. Although no statistically significant differences were found, auditors exhibited an ethical socialization process that was directionally opposite than that reported by Ponemon (1990, 1992b). Possible explanations for these results and implications for future research are discussed.

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INTRODUCTION

Enron, Xerox, WorldCom, and a host of other corporations were mentioned daily in the headlines because of their questionable accounting practices. Investigations into these cases focused on the integrity and competency of their independent auditors and, ultimately, the causes of these audit failures. While the lack of independence and outright greed were offered as potential explanations for these audit failures (Levitt, 2000; Dugan, 2002), a decline in the quality of auditors entering the profession may be an additional and critical factor underlying these explanations. Indeed, Albrecht and Sack (2000) surveyed academics and found evidence of a decline in the quality of students who are choosing accounting as a major.

The American Accounting Association's Financial Accounting Standards Committee (hereafter AAA Committee) states that the quality of auditors and their resulting judgments are a function of their task-specific knowledge and problem-solving ability (AAA, 2001). Previous research has explored numerous variables that may contribute to the quality of auditors' judgments. For example, Ponemon and Gabhart (1993) argued that an individual's moral reasoning is an important determinant of auditors' problem-solving ability. Given the numerous ethical lapses recently reported in the news, the criticality of moral reasoning and ethical judgment by auditors are paramount in today's climate when assessing the quality of the work performed by auditors. While numerous studies have examined auditors' moral reasoning, the link between auditor quality and moral reasoning has not been clearly established. Our study empirically explores this important question and tests whether moral reasoning is an element of auditor quality.

This question takes on greater urgency when one considers the emerging decline in the quality of individuals entering the profession, as demonstrated by fewer students selecting accounting as their major and career.[1] The profession must fully understand the implications of this decline in order to develop plans to counteract such negative effects. The expectation of a continued

decline in quality is not unfounded. Recent legislation which limits non-audit services offered to audit clients (SEC, 2000; Sarbanes-Oxley, 2002) has been cited as a factor that will contribute to a continued decline in the quality of future auditors because these restrictions will further diminish the attractiveness of a career in accounting (AAA, 2001). Indeed, according to the AAA Committee (2001), the "restrictions on CPA firms providing consulting services may impair further firms' ability to obtain high-quality human capital" (p.383).

BACKGROUND

The AAA Committee (2001) states that auditor quality and the quality of audit judgments is a function of the individual's task-specific knowledge as well as their innate problem-solving ability. According to Bonner and Lewis (1990), auditors' innate problem-solving ability has a two-fold affect on the quality of their performance. First, they argue that an auditor's knowledge base is developed by a combination of their task specific experiences and their innate problem-solving ability. Second, their performance is a function of this acquired knowledge base, used in conjunction with their innate problem-solving ability (Bonner and Lewis, 1990).

The ability to interpret data, recognize relationships, and reason analytically are factors underlying an individual's problem-solving ability (Bonner and Lewis, 1990). According to Ponemon and Gabhart (1993), another factor underlying an individual's problem-solving ability is their moral reasoning. Ethical or moral reasoning "focuses on the individual's conception of ethical behavior and how one's belief system dictates conflict resolution and problem solving" (Ponemon and Gabhart, 1993, p. 7). This argument implies that moral reasoning is an important component of an auditor's problem-solving ability and therefore, a critical element of overall auditor quality. Kohlberg's (1981, 1984) theory of moral development provides a useful framework to understand the moral reasoning processes of individuals.

KOHLBERG'S THEORY OF MORAL DEVELOPMENT

Kohlberg's Stages of Moral Development model (1981, 1984) identifies three levels: pre-conventional, conventional, and post-conventional, with two stages within each level. At the pre-conventional level (stages 1 and 2), individuals are motivated by a desire to avoid punishment or to earn rewards. Self-interest is a motivating factor. At the conventional level (stages 3 and 4), the individual is more concerned with a referent group, such as the family, peers or an organization, or societal expectations and how these groups perceive his or her morality. At the post-conventional level (stages 5 and 6), there is a clear effort to define morality apart from the authority of referent groups and to focus on universal ethical principles, such as justice, rights and honesty.

Over time, individuals move upwardly through these levels and stages as they are exposed to environments that stimulate higher-level reasoning (Blatt and Kohlberg, 1975; Nelson and Obremski, 1990). According to Kohlberg's theory, as individuals achieve higher stages of moral reasoning, they are also expected to behave more ethically. While research has found a moderate relationship when investigating this linkage (Blasi, 1980), studies in a business context consistently support the moral reasoning-moral behavior relationship (Brabeck, 1984; Green and Weber, 1997; Weber and Gillespie, 1998).

By the very nature of the profession, auditors regularly face ethical conflicts or dilemmas. Auditors are expected to maintain a position of objectivity and independence with their clients, yet fees also influence client relationships (Ponemon, 1990; Ponemon and Gabhart, 1993). How auditors resolve these conflicts is affected by their stage of moral reasoning (Louwers, Ponemon, and Radtke, 1997; Ponemon and Gabhart, 1993). Indeed, prior research has shown that auditors with higher stages of moral reasoning were not influenced by client pressure (Windsor and Ashkanasy, 1995), behaved more ethically (Ponemon, 1992a; Ponemon and Gabhart, 1990), and were better at identifying ethical dilemmas and detecting fraud (Bernardi, 1994; Ponemon, 1993; Sweeney and

Roberts, 1997). While these studies have examined the relationship between auditors' moral reasoning and moral behavior, the link between auditor quality and moral reasoning has not been established. Our study empirically tests whether moral reasoning is an important element of auditor quality.

HYPOTHESIS DEVELOPMENT

According to DeAngelo (1981), audit incentives are structured such that larger firms supply a higher level of audit quality. Furthermore, DeAngelo argues that auditors' capabilities are a critical determinant of audit quality. Given these arguments, the underlying assumption of our study is that the Big Five[2] firms hire higher quality auditors than non-Big Five firms. Therefore, if moral reasoning is an element of auditor quality, we would expect to find that auditors from Big Five firms will use higher stages of moral reasoning when resolving ethical dilemmas than auditors from non-Big Five firms.

Prior research has examined the relationship between firm size and ethical behavior. Loeb (1971) surveyed managers and partners from small, medium, and large CPA firms and found that CPAs from larger offices have higher ethical values than CPAs from both medium and small offices. Although Loeb's (1971) results are consistent with our predictions, much has occurred in accounting practice and education in the last thirty years. For example, in 1988, the American Institute of Certified Public Accountants (AICPA) established a new Code of Professional Conduct to help guide CPAs in the performance of their duties. The new code also addresses education by suggesting ethics coverage throughout the curriculum for accounting majors (AICPA, 1988). The American Assembly of Collegiate Schools of Business (AACSB) suggested the inclusion of ethics in the general education core, the common body of knowledge, and the major field of study for all business majors (AACSB, 1988).

While an emphasis on ethics in education and practice has been on the rise, there also have been fundamental changes in the business strategies of CPA firms and the services they offer. The

Federal Trade Commission (FTC) issued a consent order requiring the AICPA to lessen its ban on the receipt of commissions, referral fees, and contingent fees (FTC, 1990). Emerging technology and market forces also have been cited as contributing factors of the strategy changes (Melancon, 1998). Revenue for the Big Five firms more than doubled in less than a decade, with most of the increase derived from consulting services (Dugan, 2002). Some have criticized the profession for these changes, including Zeff (1987) who stated: "in recent years, a perverse self-interest has come to dominate the traditional interest in the welfare of the profession" (p. 65).

These significant changes in the accounting profession, since Loeb's 1971 study, may explain the conflicting results reported in subsequent studies. Sweeney (1995) conducted an exploratory analysis and found no relationship between moral expertise and firm size. Eynon, et al. (1997) collected data on the moral reasoning of auditors from small firms. Eynon, et al. then compared their small firm data to similar larger firm data reported in earlier studies and found a positive relationship between firm size and moral reasoning. The inconsistent findings of these studies may also be explained by differences in the research methodologies employed by the authors.

Despite these conflicting results, there is still reason to believe that auditors from Big Five firms use higher stages of moral reasoning when resolving ethical dilemmas than auditors from smaller firms. Palmrose (1988) found that, as a group, Big Eight firms engage in less litigation than non-Big Eight firms. Goetz, et al. (1991) argued that larger accounting firms tend to have a more prominent client list, with correspondingly greater public scrutiny and legal exposure. In their study, Goetz, et al. found a positive relationship between firm size and auditors' level of professionalism. Given these results, we propose the following hypothesis:

Hypothesis 1: Auditors from Big Five firms will use a higher stage of moral reasoning when resolving an ethical dilemma than auditors from non-Big Five firms.

If we find Big Five auditors use a higher stage of moral reasoning than non-Big Five auditors (supporting Hypothesis 1), it would be interesting to see whether there are differences across firm types in auditors' moral development once they progress as a member of the firm. Ponemon (1992b) suggested that auditors' moral reasoning is affected by an ethical socialization process within the firm. He found that while auditors' moral reasoning increases as the auditor progresses from staff level [Level 1] to supervisor [Level 2], moral reasoning then begins to decrease at the manager through partner level [Level 3]. Ponemon (1990, 1992b) argues that the decline in moral reasoning in the manager through partner levels may be the result of auditors with lower levels of moral reasoning being selected for promotion. Other research on the relationship between auditor position and moral reasoning has produced similar results (Shaub, 1994; Sweeney, 1995).

If there is a difference in the auditors' stage of moral reasoning between Big Five and non-Big Five firms, this may be partially attributed to a difference in ethical socialization processes. Relying on Ponemon's research findings, we propose the following hypotheses:

Hypothesis 2A: The stages of moral reasoning used by an auditor when resolving an ethical dilemma will increase from the staff [Level 1] through senior [Level 2] levels in both Big Five and non-Big Five firms.

Hypothesis 2B: The stages of moral reasoning used by an auditor when resolving an ethical dilemma will decrease from the manager through partner [Level 3] levels in both Big Five and non-Big Five firms.

METHODOLOGY

Participants

The participants in our study are auditors from ten CPA firms (5 Big Five and 5 non-Big Five) located in a large eastern city. Descriptive analysis of the Big Five firms' demographic information reveals that 66 percent are male, the mean age is 30 years, and mean experience is 7.6 years. The non-Big Five firms' demographic information reveals that 59 percent are male, the mean age is 31.1 years, and mean experience is 5.9 years. None of these demographic variables are significantly different across firm type ($p > .10$).

Materials

In their review of ethics research in accounting, Louwers, Ponemon and Radtke (1997) indicate that the Moral Judgment Interview (developed by Kohlberg and his colleagues) and the Defining Issues Test (developed by Rest, 1986) are alternative instruments that are commonly used to measure moral reasoning. The Moral Judgment Interview (MJI) identifies the predominant stage of moral reasoning while the Defining Issues Test (DIT) computes a P score which is the percentage of the subject's responses that are of the highest stages of moral reasoning (stages 5 and 6). To elicit auditors' moral reasoning in the current study, we use the Moral Reasoning Inventory (MRI) which is an objective instrument similar to the DIT yet measures the subject's predominant stage of moral reasoning, similar to the MJI.

The MRI is a paper-and-pencil survey instrument developed by the authors to determine the stage of moral reasoning deemed most important to the auditor. The auditors are asked to read a short ethical dilemma, then asked to answer the following question: "When trying to select an action decision for [the ethical

dilemma], what degree of importance [from 'great' to 'none'] did you assign to each of the following statements?" The MRI version used in this project presented the auditors with two ethical dilemmas: Chris – where the main decision-maker was confronted with orders from a superior to shred evidence of an illegally authorized loan, and Heinz – where the decision focused on whether to steal an experimental drug in the hope of saving a dying spouse.

Ethics research using scenarios (or dilemmas) is more compelling and yields better generalizable results if the context of the scenario is familiar to the participant, has been used in previous research, and is grounded in a strong theoretical tradition (Weber, 1992). The use of the Chris dilemma addresses each of these elements for promising research since the dilemma is adapted from a real experience encountered by an MBA student / full-time manager (Hosmer, 1996), was used in previous moral reasoning research (under the title of "Roger," Weber, 1990, 1996; Weber and Wasieleski, 2001), and embodies core elements found in classic moral development theory (Kohlberg, 1981, 1984). Although the Heinz dilemma is not set in a business context, this dilemma was included as a control dilemma since it has been widely used in moral reasoning and moral development research for decades (Colby and Kohlberg, 1987; Rest and Narvaez , 1994).

The eight statements following each ethical dilemma represent two reasoning statements paralleling Kohlberg's moral reasoning stage model: stages 1 and 2, stage 3, stage 4, and stages 5 and 6. Researchers have found that adult subjects tend to reason at one of these four stage groupings, often combining stages 1 and 2 and stages 5 and 6 (see Weber, 1990; Weber and Gillespie, 1998). In an earlier phase of the research project, the MRI was pre-tested (N = 217) and initial instrument validity weaknesses were found since some of the moral reasoning statements were not understood as being representative of the intended stage of moral reasoning, indicated by alpha scores below .80. These problems were corrected and the instrument was re-tested (N = 118), ensuring that the version of the MRI used in this study passed a

statistical internal validity test (all alphas above .80, with a majority at or above .90). The auditors' responses are analyzed to determine their predominant stage of moral reasoning, following the moral reasoning evaluation process developed by Kohlberg (1981, 1984) and adapted by Weber (1991).

Procedure

The MRIs were couriered to a contact person within each firm who then distributed the MRIs to individual auditors. Individual auditor and firm anonymity were guaranteed. The instructions to the contact person asked that they distribute the MRIs to auditors with various levels of experience. Enclosed with each MRI was a Background Questionnaire and a stamped envelope addressed to the authors. The instructions to the individual auditors asked them to complete the MRI first, followed by the Background Questionnaire. Once completed, the MRI and Background Questionnaire were to be placed in the envelope and mailed directly to the authors. These procedures resulted in a response rate for Big Five and non-Big Five firms of 79 percent and 70 percent, respectively and were not significantly different ($p > .10$).

Results

In order to test our hypotheses, a repeated measures ANOVA was performed. The dependent variable, Moral Reasoning, is a measure of the stage of moral reasoning used by our auditor subjects while resolving the ethical dilemmas. Moral Reasoning is a within-subject variable because it is assessed twice for each auditor: first while considering the social dilemma (Heinz) and then while considering the business dilemma (Chris).

There are two between-subject independent variables: Firm Type and Level. Firm Type indicates whether an auditor is from a Big Five firm or a non-Big Five firm. Level is an indication of the auditor's hierarchical level within his/her firm. Based on their responses to our Background Questionnaire, auditors were categorized into three levels, as illustrated in Table 1. These three levels were established based on Ponemon's (1990,

1992b) finding that auditors' moral reasoning increases as they progress from staff to supervisor, then begins to decrease at the manager level.

Table I
Sample by Level in Organization and Type of Firm

		Big Five		Non-Big Five	
Position in Organization	**Level**	**n**	**Yrs. Exp.**	**n**	**Yrs. Exp.**
Manager, Sr. Manager, Director, Partner	3	48	11.6	15	12
Senior Auditor	2	22	4.1	16	6.5
Staff I, Staff II, In-Charge	1	20	2.2	25	1.8
Total/Average		90	7.6	56	5.9

Hypothesis 1 investigates whether Big Five auditors will use a higher stage of moral reasoning when resolving an ethical dilemma than non-Big Five auditors. In order to test Hypothesis 1, we examine whether Firm Type had a significant effect on Moral Reasoning. The results indicate that Moral Reasoning was significantly affected by Firm Type ($F = 4.38$, $p = .038$). Further analysis reveals that the differences in Moral Reasoning by Firm Type are consistent with our prediction. When resolving the business-oriented Chris dilemma, auditors from the Big Five firms have an average stage of moral reasoning of 4.56 compared to 4.36 for auditors from non-Big Five firms. When resolving the Heinz dilemma, auditors from the Big Five firms have an average stage of moral reasoning of 3.83 compared to 3.67 for auditors from non-Big Five firms. As shown in Table II, the differences in the stages of moral reasoning used to resolve the Chris ethical dilemma is statistically significant across firm type (Chris: $t = 1.64$, $p = 0.05$). The difference in the stage of moral reasoning between the auditors from the Big Five versus non-Big Five firms for the Heinz dilemma is marginally significant (Heinz, $t = 1.35$, $p = 0.09$). Therefore, Hypothesis 1 is supported.

Table II
Comparison of Auditors from Big Five versus Non-Big Five Firms

	Big Five	*Non-Big Five*	*t Stat*	*p (1-tail)*
Chris - *Mean*	4.56	4.36	1.64	0.05
Heinz - *Mean*	3.83	3.67	1.28	0.09
n	90	56		

Although the relative differences across the average stage scores may appear small, it is important to note that adults tend to reason at stages 2, 3 or 4, thus condensing the realistic range of stage scores to a three-point scale. Other research using similar moral reasoning measures also found statistically significant differences with relatively subtle changes in the moral reasoning stage scores (Weber and Wasieleski, 2001). As argued by Weber and Gillespie (1998), "even relatively small change in the average stage score (e.g., of less than half a stage) may be a noteworthy difference in moral reasoning" (p. 458).

Hypotheses 2A and 2B investigate whether auditors' stage of moral reasoning varies based on their hierarchical level within their firm. In order to test Hypotheses 2A and 2B, we examine whether Level had a significant effect on Moral Reasoning. The results indicate that Level did not significantly affect Moral Reasoning ($F = 0.53$, $p = .589$). Therefore, Hypotheses 2A and 2B are not supported.

While the results of our test of Hypotheses 2A and 2B were not significant, further analysis reveals that the responses to both the Chris and the Heinz dilemmas were directionally opposite of past research and our predictions. Table III compares the stage of moral reasoning used by Level 1 and Level 2 auditors (Hypothesis 2A). As illustrated in Panel A of Table III, Level 1 auditors, on average, have a 4.51 stage of moral reasoning for the Chris dilemma, compared to Level 2 auditors' average stage score of 4.38. Similarly, when resolving the Heinz dilemma, Level 1 auditors have an average stage of moral reasoning that is higher

than the average for the Level 2 auditors, 3.73 versus 3.71, respectively.

Table III
Comparison of Level 2 versus Level 1 Auditors

Panel A: All Firms				
	Level 2	**Level 1**	**t Stat**	**p(1-tail)**
Chris - Mean	4.38	4.51	-0.80	0.21
Heinz - Mean	3.71	3.73	-0.13	0.45
n	38	45		
Panel B: Big Five Firms				
	Level 2	**Level 1**	**t Stat**	**p(1-tail)**
Chris - Mean	4.48	4.63	-0.58	0.28
Heinz - Mean	3.73	3.85	-0.48	0.32
n	22	20		
Panel C: Non-Big Five Firms				
	Level 2	**Level 1**	**t Stat**	**p(1-tail)**
Chris - Mean	4.25	4.42	-0.83	0.21
Heinz - Mean	3.69	3.64	0.20	0.42
n	16	25		

Embedded in Hypothesis 2A is the assumption that there are differences in the stage of moral reasoning used by Level 2 auditors versus Level 1 auditors for both types of firms used in our study – Big Five and non-Big Five. We failed to discover any significant differences between Level 2 and Level 1 auditors for either type of firm. However, as illustrated in Panel B and Panel C of Table III, Level 1 auditors' mean stage of moral reasoning is higher than Level 2 auditors for the Chris dilemma for both Big Five and non-Big Five firms. For the Heinz dilemma, Level 1 auditors' mean stage of moral reasoning was higher than Level 2 auditors for the Big Five firms only. Therefore, the general pattern of results comparing Level 1 and Level 2 auditors of both Big Five and non-Big Five firms is the opposite of our prediction and prior research.

Table IV compares the stage of moral reasoning of Level 2 auditors and Level 3 auditors (Hypothesis 2B). Consistent with our analysis of Hypothesis 2A, the responses to both the Chris and the Heinz dilemmas were directionally opposite of past research and our prediction. As illustrated in Panel A of Table IV, Level 3 auditors, on average, have a 4.52 stage of moral reasoning for the Chris dilemma, compared to the Level 2 auditors' average stage score of 4.38. Similarly, when resolving the Heinz dilemma, Level 3 auditors have an average stage of moral reasoning that is higher than the average for the Level 2 auditors, 3.83 versus 3.71, respectively.

Table IV
Comparison of Level 3 versus Level 2 Auditors

Panel A: All Firms				
	Level 3	**Level 2**	**t Stat**	**p(1-tail)**
Chris –Mean	4.52	4.38	0.98	0.17
Heinz - Mean	3.83	3.71	0.86	0.20
n	63	38		
Panel B: Big Five Firms				
	Level 3	**Level 2**	**t Stat**	**p(1-tail)**
Chris - Mean	4.57	4.48	0.52	0.30
Heinz - Mean	3.88	3.73	0.79	0.22
n	48	22		
Panel C: Non-Big Five Firms				
	Level 3	**Level 2**	**t Stat**	**p(1-tail)**
Chris - Mean	4.37	4.25	0.47	0.32
Heinz - Mean	3.70	3.69	0.05	0.48
n	15	16		

Embedded in Hypothesis 2B is the assumption that there are differences in the stage of moral reasoning used by Level 3 auditors versus Level 2 auditors for both types of firms used in our

study. Although we failed to discover any significant differences between Level 3 and Level 2 auditors for either type of firm, Panels B and C of Table IV illustrates that our results are directionally opposite of our predictions and prior research. While analyzing both dilemmas, Level 2 auditors' mean stage of moral reasoning was lower than Level 3 auditors for both Big Five and non-Big Five firms.

CONCLUSIONS AND IMPLICATIONS

The purpose of our study is to determine whether moral reasoning is an important element of auditor quality. Based on the assumption that the Big Five firms attract higher quality personnel than non-Big Five firms, our results indicate that moral reasoning may be an element of auditor quality. Supporting Hypothesis 1, auditors from the Big Five firms use higher stages of moral reasoning than auditors from non-Big Five firms when resolving ethical dilemmas.

This is an important finding, particularly in light of the decline in the quality of individuals entering the profession that was documented by Albrecht and Sack (2000). This decline in quality may accelerate in the future given recent changes in legislation which limit the non-audit services offered to audit clients (SEC, 2000; Sarbanes-Oxley, 2002). These new independence rules are expected to have an adverse effect on the quality of accounting majors because the imposed limits on non-audit services will further diminish the attractiveness of a career in accounting (AAA, 2001).

The new independence rules come on the heels of some highly publicized audit failures. A goal of the new independence rules is to reduce the pressure on the client-auditor relationship (SEC, 2000; Sarbanes-Oxley, 2002). Critics argue that non-audit services have compromised the ability of auditors to remain independent while auditing financial statements. Indeed, accounting research has found evidence that auditors' decisions are influenced by client economic pressure (Farmer, et al., 1987; Trompeter, 1994; Shaub and Lawrence, 1996).

Despite the changes in the independence rules, however, significant client pressure is expected to continue. Beck, et al. (1988) found that the effect of consulting services on auditor retention is small in comparison with retention based on audit services. Melancon (2000) argues that the reduction in alternative revenue sources will place greater pressure on firms to maintain positive relationships with their clients. Based on their review of the literature, the AAA Committee concluded that consulting services have little effect on client relations beyond those that already exist as a result of the auditing relationship (AAA, 2001).

If significant client pressure is expected to continue even in the wake of the new independence rules, then employing auditors with higher moral reasoning seems to be a prudent way to combat such pressures. Indeed, Windsor and Ashkanasy (1995) found that auditors with higher moral reasoning are not affected by client economic pressure. Ironically, the expectation of continued client pressure and a decline in the quality of future auditors, coupled with our results that moral reasoning is a critical element of auditor quality, suggests that future auditors may be even more susceptible to client pressure. Thus, the problem of audit failures may be exacerbated in the future.

To combat these problems, the accounting profession needs to develop plans to ensure that the moral reasoning of future auditors develops to its fullest potential. Ponemon and Gabhart (1993) argue that by upholding high ethical standards, individual firms can create environments in which moral reasoning and behavior thrive. According to Shaub (1994), educators can influence the moral reasoning of the profession by developing ethics education that goes beyond simply following rules when facing ethical dilemmas. Indeed, developing pedagogy that goes beyond the rote memorization of rules is consistent with Albrecht and Sack's (2000) message on how accounting education needs to be structured. Our results further demonstrate the importance of upholding high ethical standards in both practice and education for the purpose of enhancing the moral reasoning of future accountants.

Prior research has documented an ethical socialization process in which auditors' moral reasoning increases as they progress from staff level to supervisor, then begins to decrease at the manager through partner level (Ponemon, 1990, 1992b; Shaub, 1994; Sweeney, 1995). Hypotheses 2A and 2B investigate the pattern of auditors' ethical socialization in our sample and whether differences exist between Big Five and non-Big Five firms. Our analysis failed to find support for these hypotheses.

While the results of our analysis testing Hypotheses 2A and 2B are not statistically significant, it is interesting to note that they are directionally opposite of past research. In our study, staff level auditors exhibit a higher stage of moral reasoning than senior auditors when resolving both the Chris and Heinz dilemmas. In addition, managers through partners exhibit a higher stage of moral reasoning than senior auditors when resolving both ethical dilemmas. Further analysis reveals that both Big Five and non-Big Five auditors have similar ethical socialization patterns.

Although our study increases the understanding of the elements of auditor quality, the conclusions drawn may be somewhat limited due to the sample population used in our study. Auditors who participated in this study are from a large eastern city. Prior research has documented that the ethical development of auditors may vary based on firm affiliation, as well as the firm's geographic location (Jeffrey and Weatherholt, 1996). Future research could investigate whether moral reasoning is an element of auditor quality in other geographic locations.

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Footnotes

1. One of the reasons cited by Albrecht and Sack (2000) as a cause in the decline of the quality of accounting students is that they do not envision accounting as an attractive career opportunity.
2. Although the largest accounting firms are now referred to as "the Big Four", our data was collected just before the news of Enron surfaced. Thus, because our subject pool includes Andersen auditors, we refer to the largest accounting firms as "the Big Five".