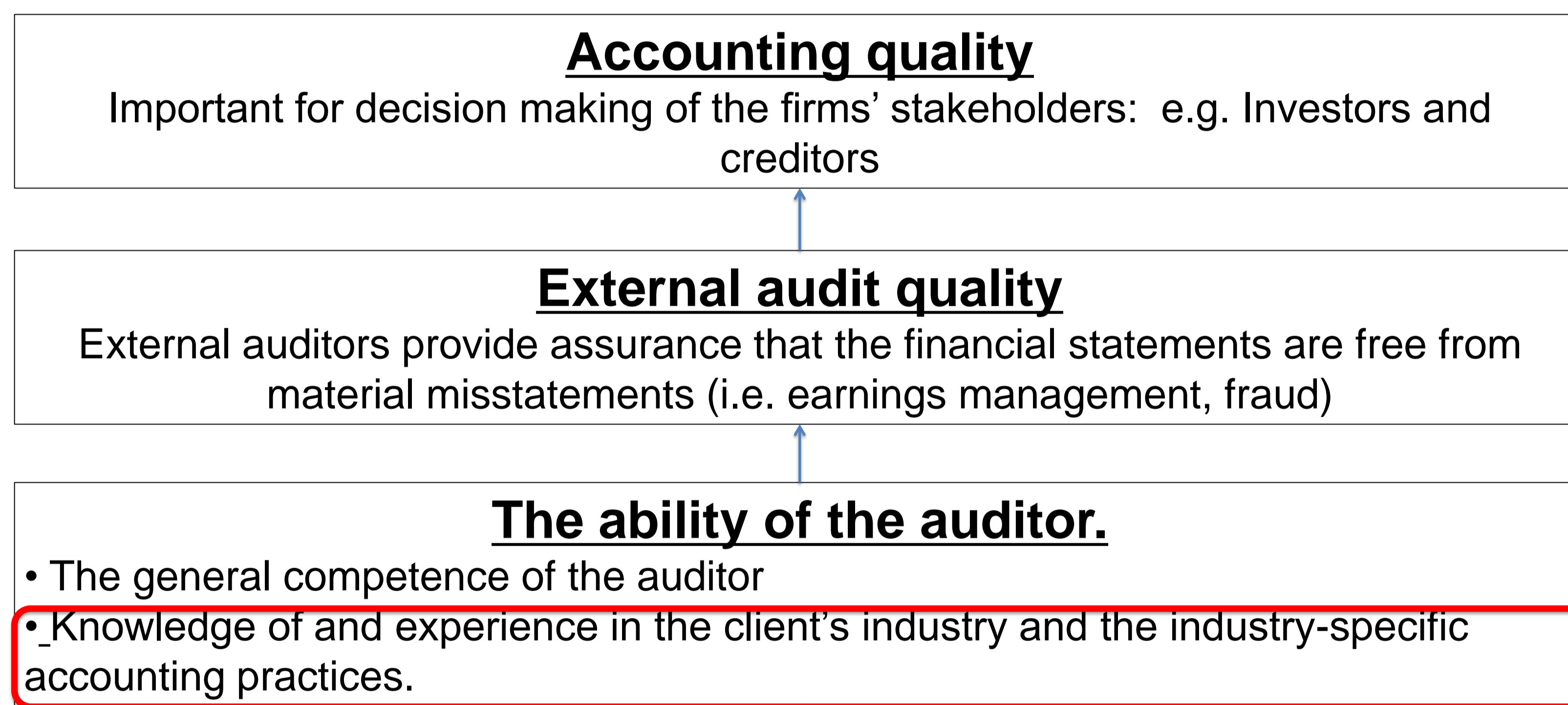




The effect of audit firm client industry experience on audit production and audit fees.

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Production of audit services

Research question: Does increased industry experience lead to more efficient audit engagement.

- Efficiency: spending less audit hours on similar engagements, ceteris paribus.
- More industry experience could lead audit firms to assign **less audit hours** to an engagement.
 - Economies of Scale
 - Industry specialists are better able to judge the risk of audit failure on industry-specific accounts.
 - Non-specialists could reduce their risk of audit failure by assigning excessive more audit hours.
- Industry specialists could change the **mix of audit labor** by assigning more complex tasks to lower level staff.

Audit fees

Research question: Does industry experience lead to a premium for the audit firm or are realized efficiencies entirely passed through

- Prior auditing research: audit markets are highly competitive. Hence, fees should approach marginal cost.
 - Belgian Setting: highly competitive environment (e.g. willekens and Achmadi, 2003)
- Economic theory: experience could be used as a differentiation technique to increase the market power of the supplier, increasing the price above marginal cost.
- Marketing theory: A successful differentiation strategy succeeds in capturing (part of) the additional value it creates for the clients.
 - Experience could lead to **higher audit fees, ceteris paribus.**
- What is the effect of client industry competition on this relationship?

RESULTS

- Increased experience is associated with more efficient engagements
- The entire efficiency gain is passed through to clients
- The efficiency gain is only partially passed through if the audit firm has a strong market position in the client industry and client industry concentration is high.

