

Does Auditor Specialization Improve Financial Reporting Quality for Not-for-Profit Organizations?



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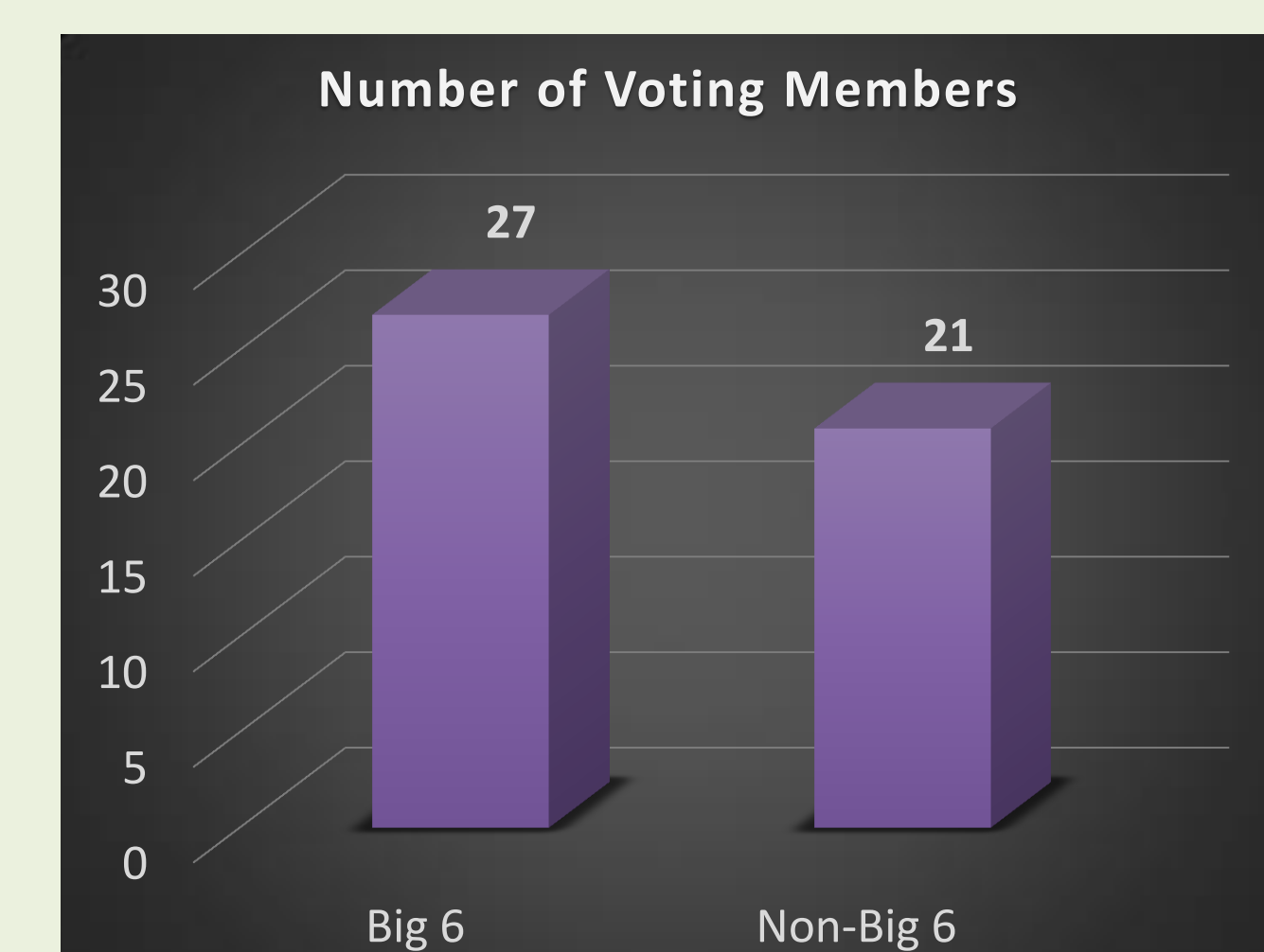
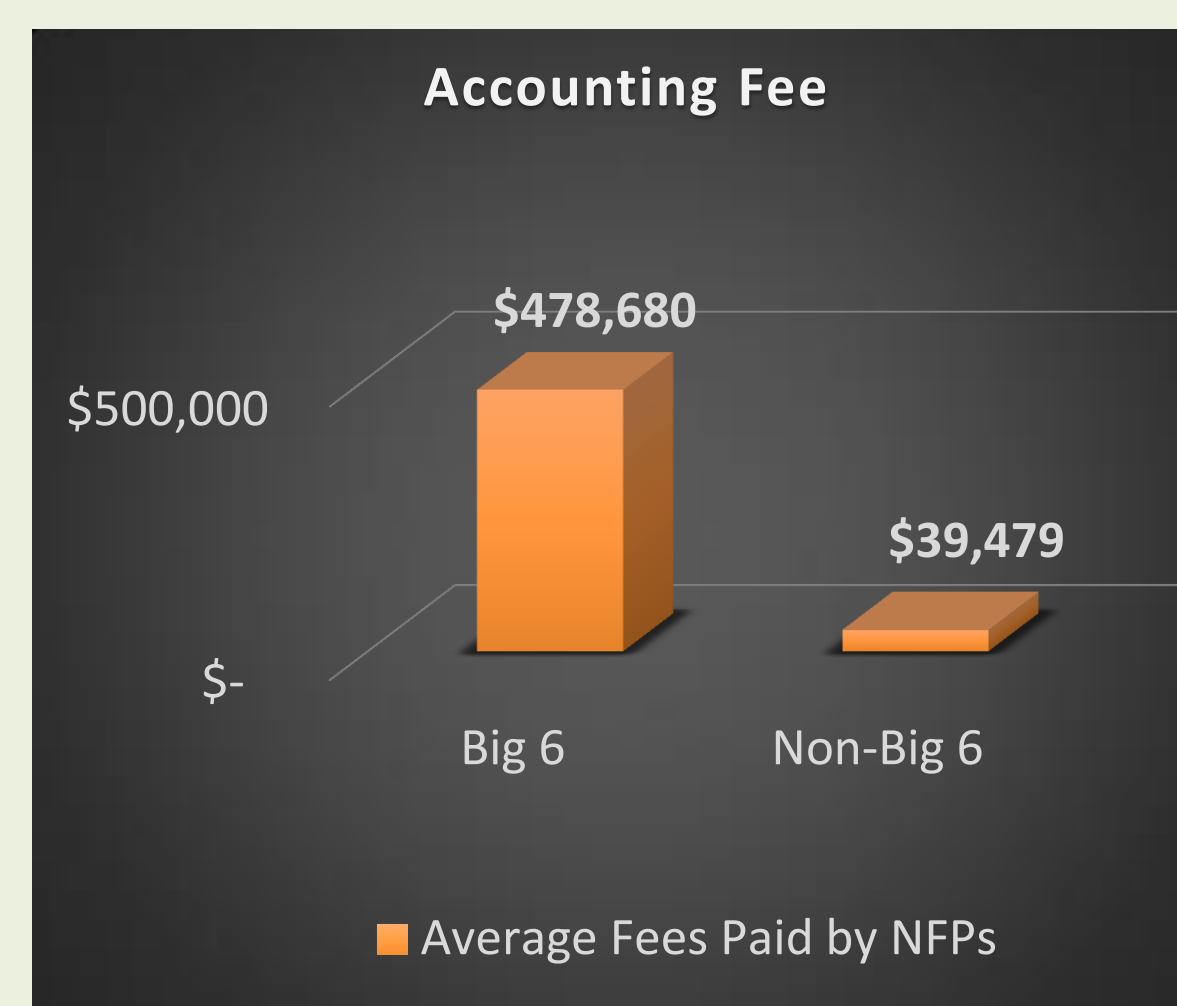
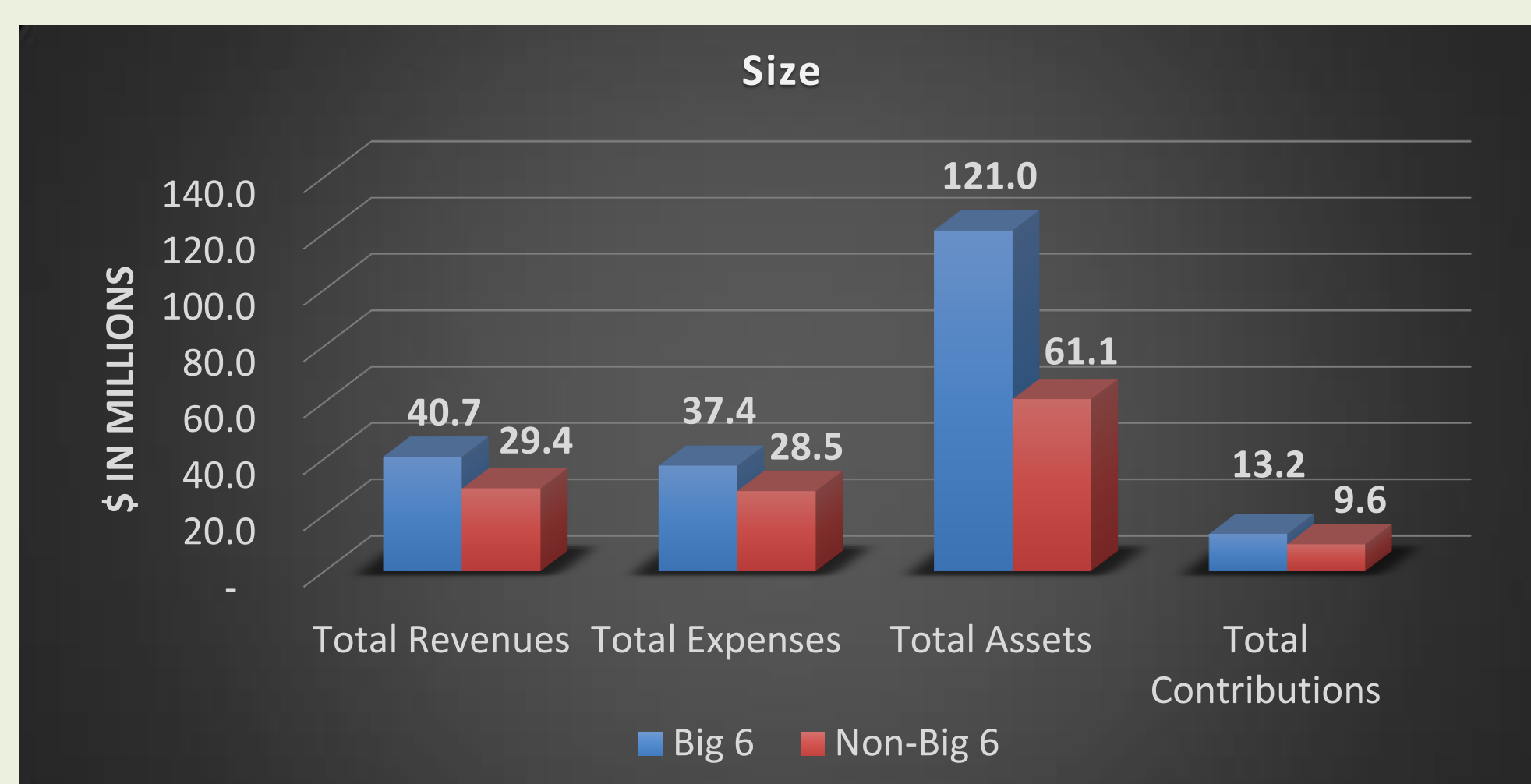
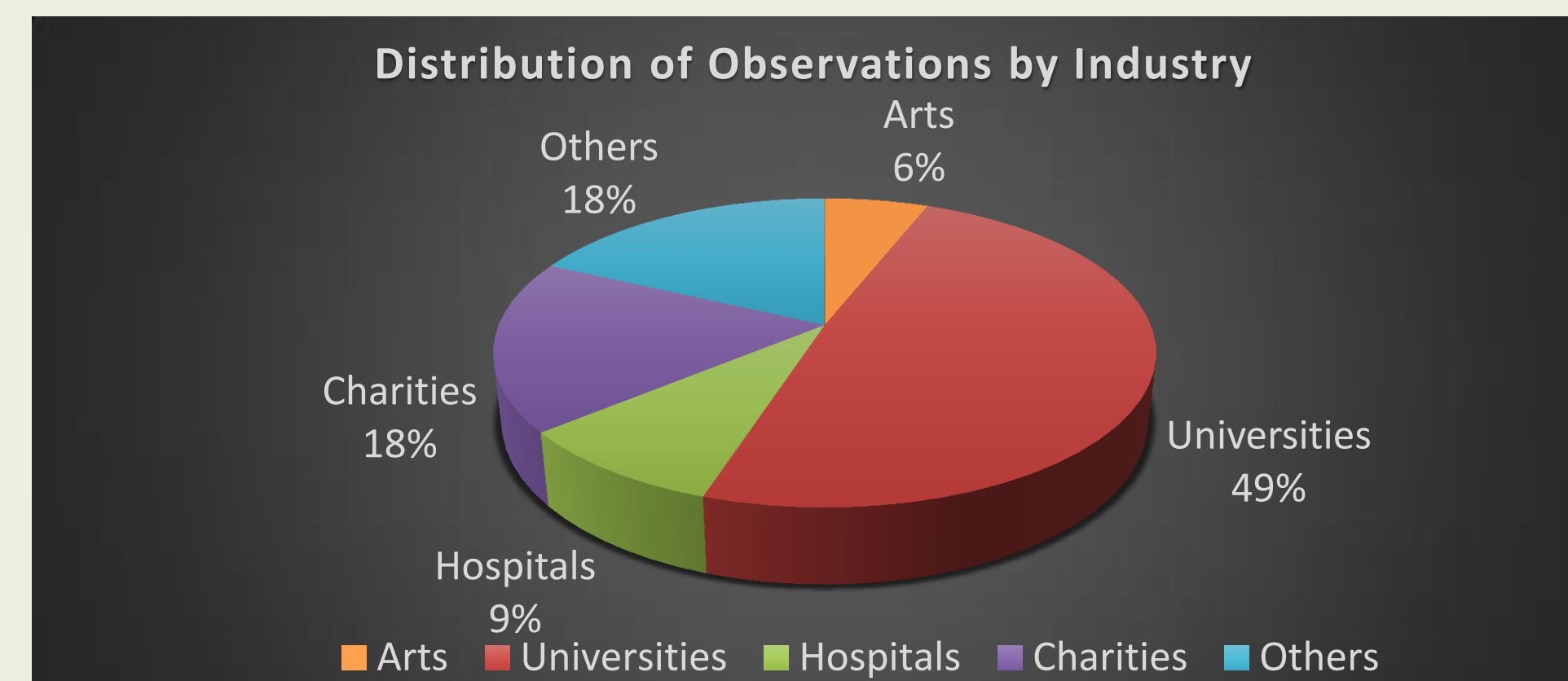
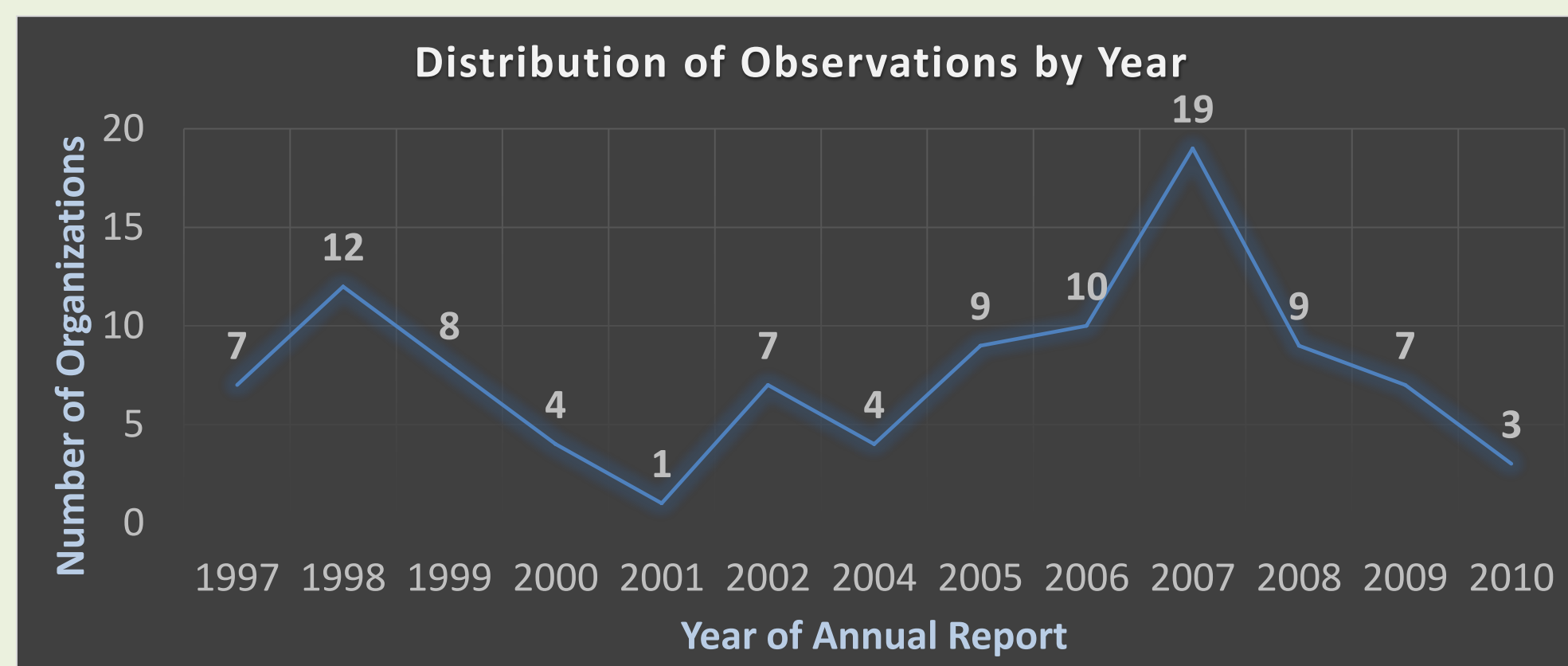
Abstract

This paper examines the relation between the auditor specialization and the financial reporting quality of not-for-profit organizations (NFPs). Although prior studies have documented that NFPs audited by accounting firms specialized in NFPs tend to have higher financial reporting quality, this study complements this literature by hand collecting the data. For fifty NFPs audited by Big 6 accounting firms and the other fifty audited by non-Big 6 that I randomly selected from an intersection of SOI files (Statistics of Income) from National Center for Charitable Statistics (NCCS) and Federal Audit Clearinghouse (FAC) files, I hand collected annual reports, number of pages, number of financial statements, and number of accounts in an annual report. The results suggest that NFPs audited by Big 6 firms are larger in size and are more likely to have an annual report. However, contrary to my expectation, there was no significant difference between NFPs audited by Big 6 and those audited by non-Big 6 in terms of number of pages, financial statements, and accounts in an annual report. Although the statistical analysis based on one hundred randomly selected observations results in no difference, I find that NFPs audited by Big 6 publish a qualitatively better annual report than those audited by non-Big 6.

Limitation of the Study

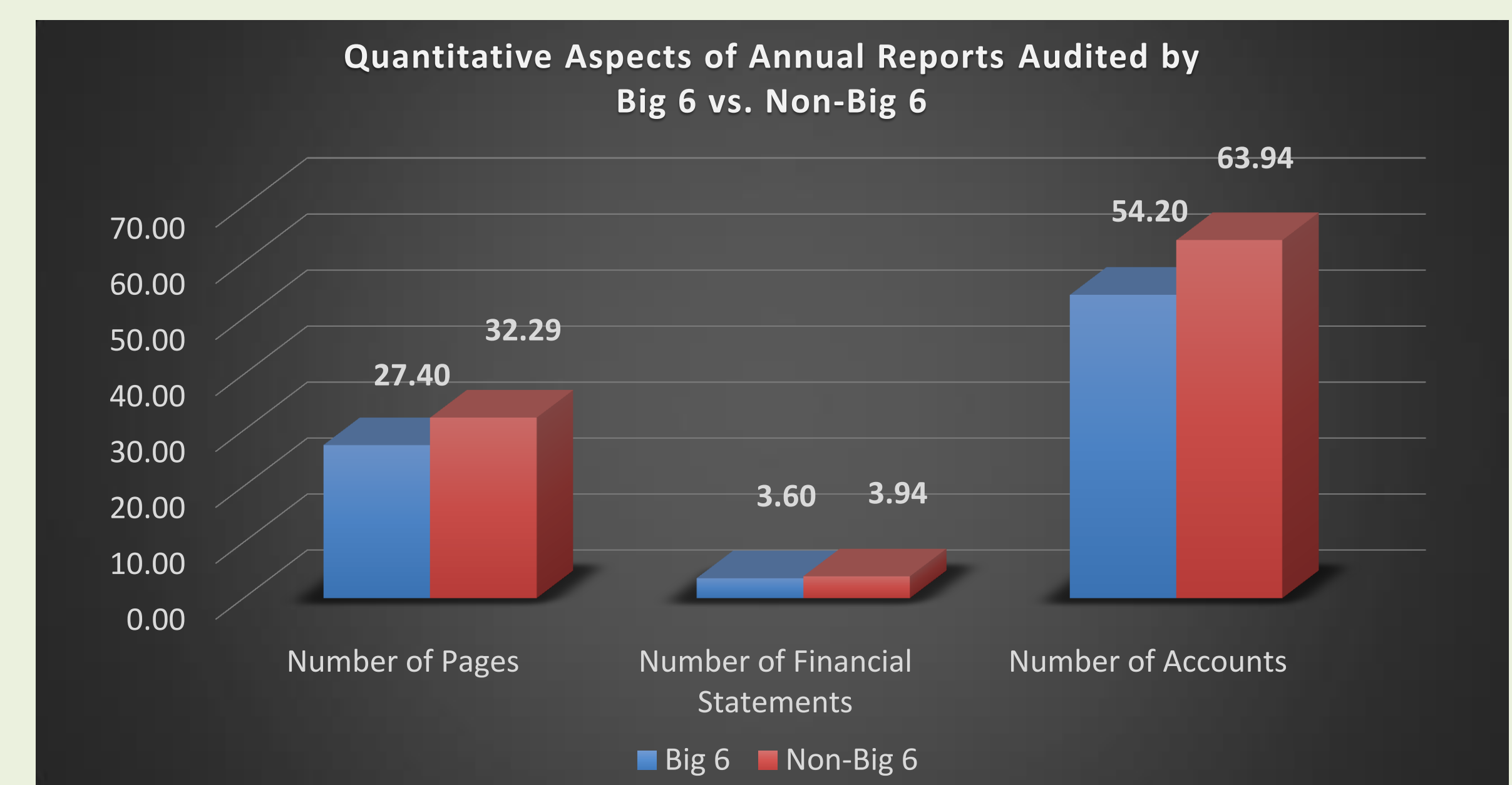
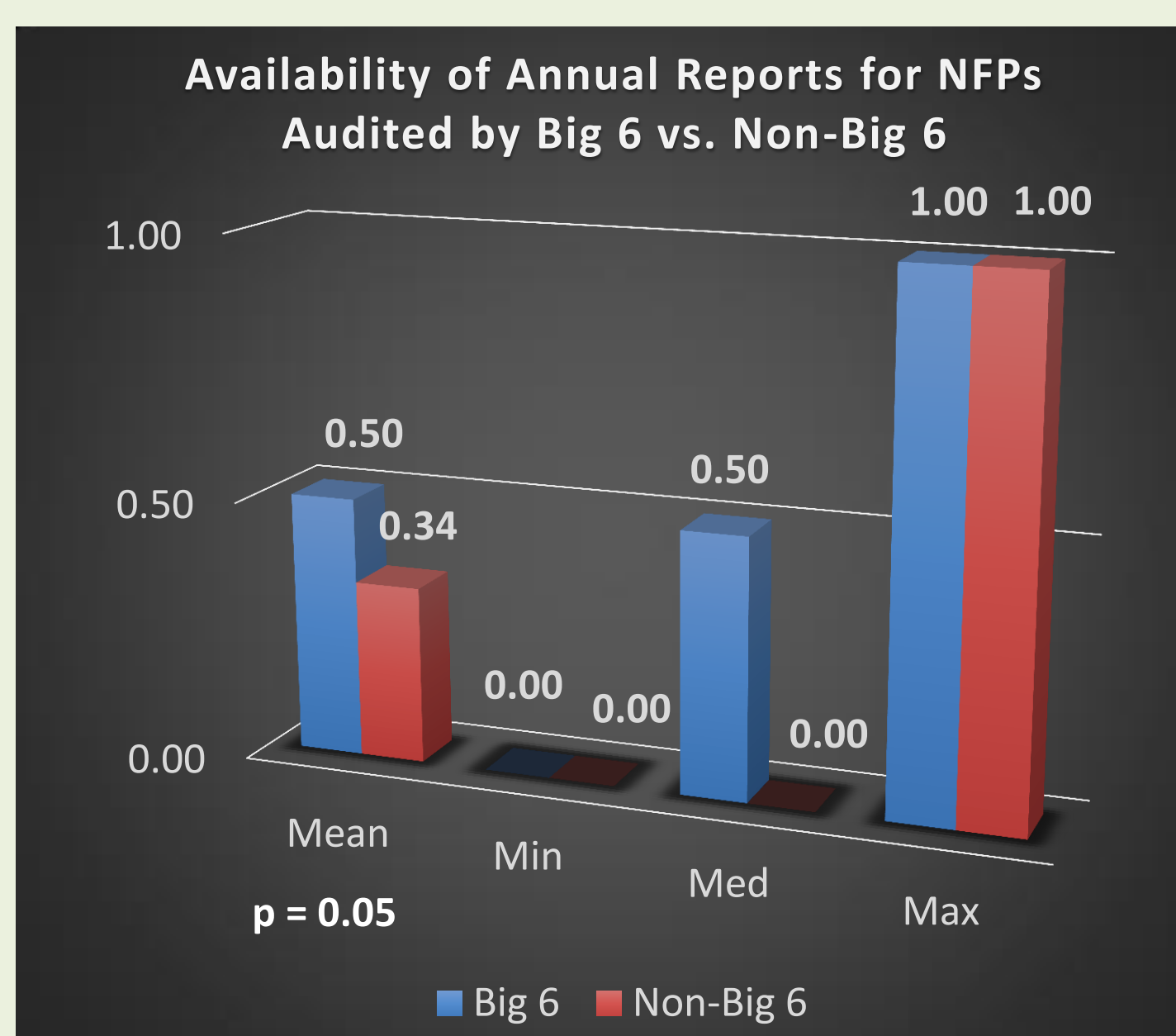
Even though the differences in terms of number of pages, number of financial statements, and number of accounts between the annual reports audited by Big 6 auditors compared to Non-Big 6 auditors are statistically insignificant, I observe that those financial statements audited by Big 6 auditors are indeed more succinctly presented, and hence, are easier for users to read. Therefore, I will increase the sample size to 500 observations in order to obtain more consistent results before reaching the conclusion regarding the relationship between the auditor size and the quantitative characteristics of NFPs' annual reports.

Descriptive Statistics



Main Results

| Results | | | | |
|-----------|---------------|-----------------|--------------------------------|--------------------|
| | Annual Report | Number of Pages | Number of Financial Statements | Number of Accounts |
| Big 6 | Mean | 0.50 | 27.4 | 3.6 |
| | Min | 0.00 | 13.0 | 2.0 |
| | Med | 0.50 | 26.0 | 3.0 |
| | Max | 1.00 | 80.0 | 7.0 |
| Non-Big 6 | Mean | 0.34 | 32.3 | 3.9 |
| | Min | 0.00 | 13.0 | 2.0 |
| | Med | 0.00 | 28.0 | 4.0 |
| | Max | 1.00 | 104.0 | 9.0 |
| t-test | 0.05 | not significant | not significant | not significant |
| Total | 0.42 | 29.4 | 3.7 | 58.1 |
| | 0.00 | 27.0 | 3.5 | 57.0 |
| | 0.00 | 13.0 | 2.0 | 27.0 |
| | 1.00 | 104.0 | 9.0 | 95.0 |



Qualitative Comparison

CALIFORNIA ASSOCIATION FOR RESEARCH IN ASTRONOMY
Audited by KPMG LLP
Statement of Activities Year Ended September 30, 2010 and 2009

| | | |
|--|---------------|---------------|
| Expenses (notes 10 and 14): | | |
| Program services: | | |
| Observatory operations | 15,147,270 | 15,554,667 |
| Research | 125,351 | 262,210 |
| Administrative and general | 2,818,712 | 2,386,498 |
| Fund-raising | 445,504 | 499,311 |
| Total expenses | 18,536,837 | 18,702,686 |
| Change in unrestricted net assets | 1,665,594 | 3,728,373 |
| Change in temporarily restricted net assets (note 13): | | |
| Contributions, net | 305,865 | 189,551 |
| Interest earned | 21,033 | 39,683 |
| Net assets released from restriction | (1,146,444) | (1,223,562) |
| Change in temporarily restricted net assets | (819,546) | (994,328) |
| Change in net assets | 846,048 | 2,734,045 |
| Net assets at beginning of year | 89,227,561 | 86,493,516 |
| Net assets at end of year | \$ 90,073,609 | \$ 89,227,561 |

COLLEGE OF ST. SCHOLASTICA, INC.
Audited by Larson Allen LLP
Statement of Activities Year Ended June 30, 2010 and 2009

| EXPENSES AND LOSSES | 2010 | 2009 |
|--|---------------|--------------|
| Program Expenses: | | |
| Instruction | 26,841,367 | 26,841,367 |
| Public Services | 2,696,798 | 2,696,798 |
| Academic Support | 5,915,739 | 5,915,739 |
| Student Services | 12,645,052 | 12,645,052 |
| Auxiliary Enterprises | 6,257,537 | 6,257,537 |
| Support Expenses: | | |
| Institutional Support | 8,435,487 | 8,435,487 |
| Allocable Expenses: | | |
| Operation and Maintenance of Plant | 3,160,092 | 3,160,092 |
| Interest Expense | 1,431,191 | 1,431,191 |
| Depreciation, Amortization and Accretion Expense | 2,814,648 | 2,814,648 |
| Less: Allocated Expenses | (7,405,931) | (7,405,931) |
| Loss on Write-Off of Contribution Receivables | - | 40,862 |
| (Gain) Loss on Disposal of Plant Facilities | 7,202 | 7,202 |
| Total Expenses and Losses | 62,795,152 | 62,840,104 |
| CHANGE IN NET ASSETS | | |
| Net Assets - Beginning of Year | 39,998,371 | 6,545,358 |
| Net Assets - End of Year | \$ 44,795,397 | \$ 7,816,448 |