

THE EFFECT OF BIG FOUR OFFICE SIZE ON AUDIT QUALITY

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ABSTRACT

Larger offices of Big Four accounting firms are argued to provide higher quality audits than smaller offices due to greater in-house experience and more expertise in administering the audits of publicly listed clients. In addition, larger offices are less likely to have independence-related problems since an individual client is relatively less important due to larger client bases in bigger offices. My conjecture is tested for a sample of 6,568 firm-year observations for the period 2003 to 2005 that are audited by 285 unique offices of the Big Four accounting firms in the United States. The results are consistent with larger offices providing higher quality audits. Specifically, clients in larger offices evidence less earnings management (smaller abnormal accruals and less earnings benchmark beating behavior). Auditors in larger offices are also more likely to issue going concern audit reports, *ceteris paribus*. These results hold after controlling for industry leadership by individual accounting firms and specific offices, and the effects of both absolute client size and relative client size (i.e., client size relative to office size). Importantly, the results are robust to partitioning the sample into upper and lower halves of client size, which indicates the results are not driven by large clients (who may have inherently higher quality earnings). While accounting firms have incentives to provide uniform quality across all practice offices, particularly in the post-SOX era with PCAOB inspections, my results indicate that there are frictions in the ability of firms to accomplish this through their existing knowledge sharing practices and quality control procedures.