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The Relationship Between Audit Fees and Audit Quality: Recent Evidence and an Updated Literature Review

SUMMARY:

The relationship between audit fees and audit quality is one of the most extensively researched topics in the field of auditing. This study reviews the findings of the past decade with the aim of uncovering and presenting the patterns observed regarding the impact of audit fees. The review synthesizes evidence from research conducted in various contexts. The research highlights that due to the complexity of the topic, we cannot establish universally clear relationships that apply to all settings. However, several key factors have been identified that significantly influence the effects of audit fees, such as specialized expertise, the level of uncertainty, and corporate and institutional structures. Additionally, the findings of the past decade have further reinforced the assumption that abnormal audit fees can ultimately impair the quality of financial reporting.

Keywords: audit fees, audit quality, auditor independence, literature review

JEL-codes: M41, M42

INTRODUCTION

Audit quality has always been a cornerstone of reliable financial reporting and, consequently, of trust in capital markets. The assurance provided by independent auditors reduces information asymmetry between corporate managers and external stakeholders, thereby supporting effective decision-making and strengthening investor confidence. One of the most debated determinants of audit quality is audit fees. On the one hand, higher fees may signal that auditors allocate more time, resources, and expertise to the engagement, which in turn may enhance audit quality. On the other hand, excessive reliance on clients as a major source of income may threaten auditor independence and reduce professional skepticism. This tension has fueled an extensive body of research over the past decades, yet empirical results remain mixed and context-dependent.

In light of recent economic challenges—including heightened market volatility, corporate failures, and increasing regulatory scrutiny—the question of how audit fees relate to audit quality has regained particular relevance. The COVID-19 pandemic, global inflationary pressures, and the rise of complex business models have significantly reshaped the auditing environment. Audit firms face greater risks and higher expect-

tations, while companies are under pressure to control costs. These circumstances make it timely to revisit the fee–quality debate, as both practitioners and policymakers seek to balance economic sustainability with the need for reliable assurance.

Moreover, the academic literature has seen a wave of new contributions in recent years, ranging from large-scale meta-analyses to context-specific studies conducted in both developed and emerging economies. These studies have provided fresh evidence on the role of abnormal audit fees, the impact of regulatory reforms, and the importance of auditor expertise and technological change. At the same time, methodological advances in measuring audit quality—such as refined accrual-based proxies, restatement analyses, and going-concern opinions—have enriched the debate but also revealed new complexities.

METHODOLOGY

The purpose of this paper is to provide an updated literature review that synthesizes these latest findings and offers a comprehensive overview of the current state of knowledge. By systematically examining both the theoretical perspectives and empirical evidence, the study aims to clarify where consensus has emerged, where results remain contradictory, and what research gaps persist. This updated review also highlights the implications for regulators, audit practitioners, and corporate governance systems. Ultimately, by revisiting the audit fee–audit quality nexus in today's economic environment, the paper seeks to contribute to a more nuanced understanding of a topic that remains central to the integrity of financial reporting.

RESULTS

Before examining the relationship between audit fees and audit quality, it is essential to clarify what is meant by accounting quality itself. Accounting quality is not a directly observable characteristic; rather, it is an abstract construct that requires estimation and interpretation. Consequently, multiple approaches have emerged in both theory and practice to capture this concept. Even when researchers do not explicitly define accounting quality, their methodological choices implicitly reveal the perspective they adopt.

Some studies approach the issue from the user's perspective, emphasizing the value relevance of reported information (e.g., Liu et al., 2011; Elbakry et al., 2017; Uwuigbe et al., 2017). Others focus on compliance with accounting regulations, frequently using discretionary accruals as a proxy (e.g., Bouchareb et al., 2014; Fields et al., 2018; Chowdhury et al., 2018). A third group of studies applies models that address both perspectives

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simultaneously, such as bankruptcy prediction models that assess reporting quality from the standpoint of both users and regulators (e.g., Bodle et al., 2016). Ideally, these approaches would converge, yet in practice, regulatory compliance and user expectations often diverge. This divergence arises not only from imperfections in accounting standards but also from the inherently heterogeneous information needs of users, which cannot be satisfied simultaneously.

Before linking audit fees to outcomes, we first clarify how accounting quality is commonly measured. Because quality is not directly observable, researchers rely on proxies, of which discretionary accruals have become the most prevalent. The idea has roots in early 20th-century balance-sheet theories (dynamic and organic approaches) where accruals played a central role (Stion, 2012). In empirical work, accruals serve as a lens on reporting quality: Healy (1985) defined total accruals as the difference between reported earnings and operating cash flows, while Dechow et al. (1995) decomposed earnings into cash flow and accrual components, yielding an equivalent computation. Jones (1991) operationalized total accruals from working-capital changes adjusted for cash and depreciation, and DeAngelo (1986) formalized their period-to-period change, distinguishing non-discretionary (NDACC) from discretionary (DACC) components. The core identification strategy estimates expected (non-discretionary) accruals—via the Jones (1991) cross-sectional regression—and infers discretionary accruals as the residual ($DACC = TACC - NDACC$).

Methodological refinements followed. The Modified Jones model adjusts for receivables to better address revenue manipulation (Dechow et al., 1995). Performance effects prompted Kothari et al. (2005) to recommend performance-matching; subsequent work corroborated the importance of performance controls (Keung & Shih, 2014). Extensions have added further regressors to improve explanatory power (Islam et al., 2011), though variables must reflect institutional context rather than merely restate components of total accruals.

Despite criticisms, discretionary accruals remain the workhorse proxy. Perotti & Wagenhofer (2014) conclude they are among the most suitable measures for examining reporting quality, and recent surveys confirm their continued dominance (McNichols & Stubben, 2018). Still, researchers warn about noise and potential bias—particularly for firm-level inference and non-random samples (Christodoulou et al., 2018; McNichols & Stubben, 2018). Best practice therefore requires explicit theorizing about manipulation mechanisms, careful sample design, thoughtful model choice, appropriate controls, and a critical interpretation of results.

A fundamental difficulty in assessing accounting quality lies in the fact that financial statements are not directly comparable across individual firms. Each report is shaped by firm-specific circumstances, industry characteristics, and national institutional settings, which makes it problematic to draw conclusions at the level of single entities. For this reason, most empirical studies examine reporting quality through comparisons across groups of firms, sectors, or countries. Such an approach, however, inevitably requires a wide range of control variables to isolate the effect of any single determinant.

International research has therefore incorporated numerous controls—such as firm size, leverage, industry membership, governance characteristics, and country-level insti-

tutional factors—in order to address the simultaneity and interdependence of influences on reporting quality. This reflects the broader reality that accounting outcomes result not only from the standards applied but also from the incentive structures and institutional environments in which firms operate (Soderstrom & Sun, 2007; ICAEW, 2016).

Given this complexity, identifying the specific role of audit fees in shaping accounting quality requires narrowing the analytical focus. Only by controlling for the wide set of confounding variables can we meaningfully assess whether, and to what extent, audit fees contribute to differences in audit and reporting quality. This highlights both the methodological challenges and the importance of carefully designed research frameworks in disentangling the audit fee–audit quality relationship.

Audit fees influence both the independence and the capabilities of auditors, and thereby indirectly affect the quality of financial statements. The literature generally identifies two competing hypotheses. First, when audit fees are lower than expected given the risks and scope of the engagement, auditors may lack the resources to detect material misstatements, resulting in lower-quality financial reporting (Martinez & Moraes, 2017). Second, when audit fees are higher than expected, auditors may become economically dependent on their clients, potentially impairing independence and reducing professional skepticism (Choi et al., 2010b). Both perspectives suggest that deviations from “normal” audit fees—whether abnormally low or high—can threaten reporting quality.

To operationalize this concept, researchers have distinguished between normal and abnormal audit fees. Choi et al. (2010b) proposed an econometric model estimating expected fees based on firm characteristics (e.g., size, leverage, industry, risk factors), with deviations classified as abnormal. This approach highlights the complexity of determining fee adequacy at scale, as opposed to individual contracts where the expected level of compensation is easier to benchmark. Regulators have also recognized the risks: in Hungary, for example, audit fees must be independent of report outcomes, proportionate to engagement requirements, and transparent (Act LXXV of 2007). International standards such as the IESBA Code similarly warn of self-interest threats where auditors are excessively reliant on fees from a single client, or where fee pressures undermine audit scope.

Empirical findings provide nuanced evidence regarding the audit fee–audit quality nexus. Some studies confirm the negative consequences of abnormal fees. Choi et al. (2010b) report that abnormally high fees are associated with reduced audit quality, while Martinez and Moraes (2017) find that firms paying abnormally low fees engage in more aggressive earnings management. Hossain et al. (2016) highlight the risk of cross-client fee dependence within audit networks, which may compromise independence.

Other research presents more mixed or even opposite results. Rahmina and Agoes (2014), using survey data from audit professionals, document a positive perceived association between audit fees and audit quality, reflecting practitioners’ belief that greater resources enhance service quality. Similarly, studies controlling for audit firm characteristics often find that higher fees charged by Big 4 auditors correspond with higher-quality reporting, but these outcomes are attributable to auditor expertise rather than fee levels per se (Cahan & Sun, 2015; Bills

et al., 2015). Conversely, Chen et al. (2018) show no significant relationship between fee reductions during the global financial crisis and reporting quality, suggesting that fee variation alone does not always drive audit outcomes.

Zhang et al. (2018) demonstrate that political uncertainty and geographic client dispersion increase audit fees, while also influencing quality outcomes through higher perceived risk. Bronson et al. (2017) and Asthana et al. (2015) document that foreign listings and cross-market exposures elevate fees due to both workload and litigation risk, often coupled with improved reporting. Finally, evidence also suggests that partner-level characteristics matter: more experienced signing partners command higher fees, consistent with higher expected audit quality (Cahan & Sun, 2015).

Recent contributions continue to complicate but also enrich the debate on how audit fees interact with audit quality. One notable strand of recent research focuses on perceptions of stakeholders regarding the role of new reporting requirements. Bepari, Nahar, and Mollik (2024) conducted fieldwork in Bangladesh on the introduction of key audit matters (KAMs) reporting. They found that while auditors perceived improvements in quality control, particularly in the planning and execution of audits, these changes were largely driven by coercive regulatory pressures and did not translate into higher audit fees. Furthermore, the transparency of audit reports did not improve, since auditors often disclosed generic items while masking more critical issues. Matters that might otherwise lead to a modified opinion were instead reframed as KAMs, leading to a paradox where performative audit quality improved, but transparency arguably declined. These findings suggest that regulatory interventions may increase the effort component of audit quality without necessarily enhancing the informational value of audit reports.

Evidence from emerging markets has further diversified the picture. In Indonesia, Hidayati and Djamil (2024) analyzed manufacturing firms between 2020 and 2022 and concluded that audit fees, tenure, and rotation significantly influenced audit quality, while auditor reputation did not. Their results showed high explanatory power, with the independent variables accounting for over 75% of the variation in audit quality, emphasizing the economic drivers of audit performance. However, Fernandez, Chan, Salim, Sitepu, and Simanjuntak (2024), using a broader sample of 201 observations from 67 firms between 2019 and 2021, reported that neither audit fees, tenure, nor reputation had a significant effect on quality. This stark contrast illustrates the difficulty of generalizing results across time frames, industries, and methodological approaches, and it underscores the need for caution when interpreting fee–quality dynamics in heterogeneous markets such as Indonesia.

Further nuance comes from studies of tenure and switching. Zaafarani, Wati, Angga, and Rosnidah (2024) examined financial firms in Indonesia, focusing on the insurance sub-sector, and found that audit fees significantly affected audit quality, but neither tenure nor auditor turnover had measurable effects. Their findings support the argument that audit fees represent a direct economic input into audit processes, while the presumed independence gains from rotation or switching may not always materialize in practice. Taken together, the Indonesian evidence indicates that in certain industries, par-

ticularly those with higher regulatory or reputational risks, fees play a more decisive role than structural engagement factors.

Beyond Southeast Asia, Ayoola (2024) investigated the Nigerian banking sector between 2008 and 2020 and introduced an innovative mediation model to examine how audit seasonality moderates the relationship between audit fees and audit quality. Using structural equation modeling, the study demonstrated that seasonality fully mediates the link, implying that fees affect quality indirectly by shaping workload patterns across peak audit seasons. This result carries important policy implications: regulatory requirements that concentrate reporting deadlines, such as uniform fiscal year-ends, can inadvertently undermine audit quality even when audit fees appear sufficient. It also highlights the importance of considering temporal and organizational constraints when assessing the impact of fees on audit outcomes.

While economic determinants dominate much of the empirical debate, literature reviews stress the importance of complementary non-financial factors. Krisnia, Rochayatun, and Hafandi (2024) emphasize that audit fees alone cannot guarantee high-quality audits without strong auditor ethics, competence, and independence. Their review argues that professional behavior and ethical standards remain indispensable, suggesting that even well-funded audits may fail to achieve quality if these dimensions are neglected. This perspective aligns with findings from developing economies where higher fees sometimes coexist with weak enforcement and limited auditor capacity, leading to only partial improvements in quality.

Another strand of recent work has shifted focus to the determinants of audit fees themselves and their indirect effect on quality. Wahyuni, Sueny, Wahyu, and Fadewa (2024), conducting a systematic literature review, concluded that audit fees are strongly shaped by firm-specific attributes such as size, complexity, and financial performance, as well as by market conditions and regulatory environments. Larger and more complex firms pay higher fees, which typically allow auditors to allocate greater effort and skepticism. Yet, excessive fee pressure from clients can reduce independence and compromise quality. This dual role reflects the fee paradox: while higher fees often improve the technical dimension of quality, bargaining dynamics may simultaneously create economic dependence.

The European context offers further insights through studies of regulatory reform. Graszchitz and Steller (2025) revisited the Austrian audit market in light of the 2016 EU Audit Reform, replicating and extending prior work on European audit markets. They found that, contrary to wider European trends, audit fees declined after the reform in Austria, likely due to intensified competition among audit firms. Market concentration decreased slightly, but the number of auditors serving public interest entities also fell. Measures of quality such as discretionary accruals and restatements yielded mixed results, while fee caps on non-audit services did reduce those fees, potentially enhancing independence. These findings underscore how the same regulatory package can yield divergent outcomes depending on national market characteristics and competitive dynamics.

Taken together, these recent studies reveal several converging insights. First, audit fees remain a key determinant of audit quality, but their effects are highly context-dependent. In markets such as Bangladesh or Nigeria, regulatory frameworks and

institutional structures moderate the relationship, sometimes producing paradoxical outcomes. In Indonesia, divergent findings across studies show that results are sensitive to sample composition and measurement strategies, suggesting that fee effects cannot be assumed uniform even within the same national setting. Second, non-financial factors such as ethics, competence, and independence interact with fee structures, meaning that quality outcomes hinge on both economic and professional determinants. Third, regulatory reforms such as the EU Audit Reform may alter the fee–quality dynamic in unexpected ways, reducing fees in some markets while delivering only partial improvements in quality.

For research, these developments highlight the importance of cross-country comparability and methodological rigor. The contrast between the findings of Hidayati and Djamil (2024) and Fernandez et al. (2024) demonstrates how differences in model specification can shape conclusions. Studies like Ayoola (2024) show the value of incorporating mediating variables that capture organizational dynamics, while reviews such as Krisnia et al. (2024) and Wahyuni et al. (2024) emphasize the need to move beyond purely financial proxies. For policymakers, the evidence suggests that interventions focused narrowly on audit fees may not yield consistent improvements. Attention must also be paid to workload distribution, corporate governance, ethical enforcement, and the broader institutional environment.

Overall, the most recent wave of studies reinforces that audit quality is multidimensional, shaped by the interplay of fees, auditor behavior, institutional frameworks, and regulatory contexts. The findings collectively point to a more nuanced and conditional relationship than suggested by earlier debates, one that demands both theoretical refinement and methodological innovation in future research.

CONCLUSIONS

The relationship between audit fees and audit quality has attracted sustained scholarly attention because it strikes at the heart of the credibility of financial information. Audit fees represent the economic link between auditor and client, and thus embody both an incentive mechanism and a potential threat to independence. The literature reviewed reveals a duality: on one hand, fees provide the necessary resources for auditors to invest in expertise, time, and procedures; on the other, unusually high or low fees may compromise independence or effort. The most consistent finding across contexts is that abnormal audit fees—whether too high or too low relative to expectations—are associated with risks to audit quality. Yet, the empirical evidence is nuanced, varying across countries, time periods, firm characteristics, and methodological approaches. This complexity underscores the need for careful contextualization when interpreting results.

Two competing theoretical perspectives dominate the discourse. The “low fee” hypothesis suggests that when fees fall below the expected level, auditors may lack the resources to perform sufficient substantive testing, increasing the risk of undetected misstatements. Conversely, the “high fee” hypothesis posits that unusually elevated fees create economic bonding between the auditor and the client, reducing professional skepticism and impairing independence. Both perspectives assume a decline in quality, albeit through different channels. More

recent studies have complicated this binary by showing that fee levels can sometimes correlate positively with quality when they represent legitimate investments in specialist knowledge, international coordination, or additional audit hours. Thus, the fee-quality link cannot be reduced to a simple monotonic relationship, but rather reflects an equilibrium between incentives, independence, and competence.

Empirical results remain mixed. Several studies (e.g., Choi et al., 2010b; Martinez & Moraes, 2017) document a negative association between abnormal fees and audit quality proxies such as discretionary accruals. Others (Rahmina & Agoes, 2014) suggest that higher fees are perceived by practitioners as enabling higher quality audits, though perception-based measures differ from archival proxies. Some researchers have found no statistically significant relationship at all, especially in contexts where regulation tightly constrains auditor behavior (Chen et al., 2018). These divergences highlight not only methodological differences—choice of proxies, sample selection, econometric techniques—but also institutional variation across markets. For instance, fee–quality dynamics in the U.S. or U.K. may not translate directly to emerging markets, where enforcement intensity, litigation risk, and audit market concentration differ substantially.

In conclusion, the relationship between audit fees and audit quality is complex, context-dependent, and theoretically rich. Abnormal fees remain a red flag for potential quality concerns, but the evidence also highlights legitimate scenarios in which higher fees support better audits. Theoretical and empirical advances continue to refine our understanding, yet methodological and contextual challenges persist. For regulators, the task is to safeguard independence without undermining the economic viability of high-quality audits. For scholars, the challenge is to develop innovative measures, exploit new data sources, and contextualize findings across diverse environments. For practitioners, the message is clear: fee negotiations are not mere commercial transactions but decisions that shape the integrity of financial reporting. Future research will need to integrate traditional audit economics with emerging concerns around sustainability, technology, and global governance. Only through such integration can we fully understand how audit pricing affects the quality and reliability of audits in the 21st century.

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