

Original Article

The Tax Litigation–auditor change nexus: strategic rotation patterns in Brazil’s hyper-litigious environment

O nexo entre Litigiosidade Tributária e troca de auditor: padrões estratégicos de rotação no ambiente hiper-litigioso brasileiro

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ABSTRACT

Purpose: This study investigates whether tax litigation influences voluntary changes in audit firms among Brazilian publicly listed companies operating within a highly litigious tax environment.

Design/methodology/approach: Using panel data on B3 firms from 2014 to 2023, the study estimates logistic models. Tax litigation is proxied by tax-related provisions plus contingent liabilities scaled by total assets. Control variables include firm size, Big Four engagement, and a COVID-19 crisis dummy (2020–2021).

Findings: The results indicate that greater tax litigation is positively associated with the likelihood of a voluntary audit firm change. Each 1 p.p. rise in tax contingencies relative to assets raises the change probability by about 2.58 p.p. Larger firms change more often. At the same time, Big Four audits and the COVID-19 crisis period are associated with a lower probability of change.

Research limitations/implications: The use of provisions and disclosed contingencies as proxies may not capture all disputes; the sample covers only listed firms. Results highlight the governance role of audit-firm choice under tax risk.

Practical implications: The findings inform audit committees’ retention and rotation policies and guide auditors’ client-risk assessments in litigious contexts.

Social implications: Clearer auditor–client alignment in the context of tax risk can reduce information asymmetry and support investor confidence.

Originality/value: The study identifies a direct link between tax litigation intensity and voluntary audit firm change in Brazil, advancing evidence on how corporate governance adapts in high-litigation settings.

Keywords: Tax Litigation, Voluntary Audit Firm Change, Corporate Governance, Brazil, Contingent Liabilities

RESUMO

Objetivo: Investigar como a litigiosidade tributária influencia decisões de rotação voluntária de auditores em empresas listadas no Brasil, caracterizado por níveis excepcionais de litigância tributária.

Desenho/metodologia/abordagem: Realizou-se regressão logística com dados em painel das companhias abertas listadas na B3 entre 2014 e 2023. A variável independente principal foi mensurada através das provisões e passivos contingentes tributários como proporção do ativo total. As variáveis de controle incluíram tamanho da empresa, presença de auditoria Big Four e períodos de crise econômica (COVID-19).

Resultados: A litigiosidade tributária aumentou significativamente a probabilidade de troca voluntária de auditor. Cada aumento percentual nas provisões tributárias relativas aos ativos totais elevou a probabilidade de mudança de auditor em aproximadamente 2,58 pontos percentuais. Empresas maiores têm maior tendência à troca, enquanto auditoria Big Four e períodos de crise econômica reduziram essa probabilidade.

Limitações/implicações da pesquisa: As limitações incluem o uso das provisões e passivos contingentes como proxies para litígios, podendo não captar completamente os aspectos qualitativos das disputas tributárias. O foco em empresas listadas limita a generalização.

Implicações práticas: Auditores podem melhor compreender estratégias de retenção de clientes em contextos litigiosos. Reguladores podem aprimorar políticas para melhorar a qualidade das auditorias e a conformidade tributária.

Implicações sociais: O estudo promove transparência nas relações auditor-cliente, reduzindo assimetria informacional e aumentando a confiança dos investidores.

Originalidade/valor: O estudo preenche uma lacuna ao analisar especificamente a rotação de auditores como resposta estratégica à litigiosidade tributária no contexto brasileiro, oferecendo insights sobre adaptações da governança corporativa diante de desafios regulatórios extremos.

Palavras-chave: Litigiosidade Tributária, Mudança voluntária de empresa de auditoria, Governança corporativa, Brasil, Passivos contingentes

1 INTRODUCTION

Brazil has an exceptionally elevated level of tax litigation—disputes correspond to 75% of GDP (2019), far above the OECD average of about 0.3% Insper (2021). This environment lengthens dispute resolution, raises compliance costs for firms and the state, and increases uncertainty over future tax outflows. These conditions affect corporate governance choices for listed companies, including relationships with audit firms.

The recognition, measurement, and disclosure of tax contingencies are governed by NBC TG 25 (aligned with IAS 37) Federal Accounting Council (2024); Nascimento et al. (2019). Under this standard, probable losses are accrued, losses are disclosed in notes, and remote losses do not require disclosure Costa et al. (2017); Ribeiro & Oliveira

(2020); Santos et al. (2023). These regulatory provisions shape the presentation of tax disputes appear in financial statements and the information available to users.

Prior research typically examines tax litigation and auditing separately. Existing studies associate auditing with tax avoidance, aggressiveness or auditor resignation Goh et al. (2013); Martinez (2017); however, empirical evidence directly connecting tax litigation intensity to voluntary audit firm change is limited. This study addresses that gap for B3-listed companies from 2014 to 2023, measuring tax litigation by tax-related provisions plus contingent liabilities scaled by total assets and identifying voluntary changes in the external audit firm.

The study investigates whether firms with greater tax-related exposures are more likely to change audit firms, and whether firm size, Big Four engagement, and the COVID19 crisis moderate this relationship. By focusing on audit firm change rather than partner rotation, the construct reflects Brazil's regulatory practice and firms' strategic decisions.

This study contributes by incorporating tax litigation into auditor–client dynamics models and providing evidence from a setting with unusually high litigation. The findings provide guidance to boards, auditors, investors, and regulators regarding retention and rotation policies and the interpretation of audit firm changes under tax risk. The remainder presents the literature review, data and methods, results, and conclusions.

2 LITERATURE REVIEW

2.1 Tax litigation in the Brazilian context

The Brazilian tax system is characterized by a multiplicity of taxes and frequently changing rules, many of which are often open to interpretation. This complexity challenges firms' compliance and sustains a litigious environment Lopo Martinez et al. (2024); Almeida (2018). Proliferation of regulatory provisions and persistent interpretive ambiguity leads to many disputes between taxpayers and authorities, burdening the judiciary, slowing case resolution, increasing costs to firms and the state, and amplifying legal uncertainty Guerra & Guerra (2022); Almeida (2018).

Weak compliance practices and internal controls further exacerbate the incidence of tax-related disputes. Firms lacking robust internal controls are more prone to assessments, fines, and lawsuits, fueling further litigation Baldivieso (2022); Guerra & Guerra (2022); Almeida (2018). Multilevel taxation (federal, state, municipal) increases interpretive difficulty; in some municipalities, lawsuits seek credits whose values are lower than the costs of collection, revealing inefficiencies (Almeida, 2018).

In financial reporting, tax disputes are reflected in provisions and contingent liabilities. Proper recognition requires identifying a present obligation, evaluating the probability of loss, and estimating amounts reliably Lopo Martinez et al. (2024). NBC TG 25 (2009), aligned with IFRS, classifies contingencies as probable (recognized), possible (disclosed), and remote (no disclosure). These rules determine whether items are recognized or merely disclosed Oliveira et al. (2021) and shape users' understanding of risk Costa et al. (2017); Ribeiro & Oliveira (2020); Santos et al. (2023). Managing tax contingencies with prudent provisioning and transparent disclosure can mitigate risk Bédard & Paquette (2021). Tax litigation risk denotes the likelihood that tax positions will be challenged or litigated, with financial and reputational consequences Donelson et al. (2021).

2.2 Voluntary Audit Firm Change

Listed firms face increasing demands for transparent and reliable reporting Martins et al. (2014). Independent auditing supports financial reporting quality and investor confidence Bortolon et al. (2013). Auditing entails the systematic examination of statements, transactions, and processes to assess accuracy and compliance Crepaldi (2004); Perez Junior (1998). In Brazil, certain entities—such as listed companies, financial institutions, insurers, and pension funds—are subject to mandatory audits Oliveira & Santos (2007).

Within this context, audit firm rotation occurs by regulation and voluntarily. Brazil instituted mandatory rotation via Central Bank Resolution 3,198 and CVM Instruction 308/1999, primarily to restore market credibility after prior scandals Oliveira & Santos

(2007); Formigoni et al. (2008). An audit firm may not serve a client for more than five consecutive years, with exceptions e.g., where a Statutory Audit Committee is in place; CVM (2021). Beyond mandatory limits, boards may voluntarily initiate voluntary auditor changes for strategic considerations unrelated to tenure.

The effects of rotation remain contested. Rotation may refresh independence and perspective, potentially improving quality Martinez et al. (2015); Parreira et al. (2020). However, evidence is mixed: some studies do not find that rotation reduces earnings management, and frequent changes may incur startup costs and erode client-specific knowledge Azevedo & Costa (2012). Both mandatory and voluntary changes seek to uphold reporting integrity and reinforce stakeholder trust Oliveira & Santos (2007).

2.3 Tax Litigation and Voluntary Audit Firm Rotation

Tax litigation influences governance decisions, including whether a firm voluntarily changes its audit firm. Higher litigation and reputational exposure shape engagement acceptance and continuance judgments and influence how auditor–client relationships evolve Khurana & Raman (2004); Casterella et al. (2007); Donelson et al. (2021).

The financial statement impact of tax disputes can be substantial. Reclassifying contingent exposures into provisions may eliminate reported profits, as shown for Big Four–audited firms in Jesus and Souza (2016), where fully provisioning certain contingencies would have driven a 100% profit reduction for 60% of the sample. Under NBC TG 25, professional judgment regarding recognition versus disclosure governs how such effects are presented and reflected in the financial statements. This prompts boards to reassess whether the incumbent audit firm is aligned with the company's risk profile.

Compliance architecture plays a critical role in shaping audit outcomes. Programs that combine internal controls with periodic external reviews reduce disputes and improve process reliability Almeida (2018); Vitalis & Lamy (2022). In this context, some companies opt to change audit firms to bolster perceived audit quality—selecting providers with deeper tax expertise or a demonstrable record of rigorous reviews—which can enhance transparency and strengthen financial integrity Oliva & Silva (2018).

Independence constraints influence auditor selection. When the same provides audit services and extensive tax consulting, the risk of selfreview threatens independence; the literature cautions against such arrangements and links them to more aggressive tax positions Dhiyaulhaq & Fadjarenie (2023). Clear boundaries between audit and consulting preserve transparency Mukoffi et al. (2022). Audit firms, for their part, price and select engagements with litigation exposure in mind, which can lead to disengagements or client transitions Choi et al. (2008). Consistent with this, perceived litigation risk is associated with heightened audit scrutiny Choi et al. (2008).

These arguments suggest a positive association between tax litigation intensity and voluntary audit firm rotation: firms with greater exposure are more likely to adjust their auditor choice to manage risk and signal governance quality. The empirical analysis below quantifies this relationship while controlling for firm size, financial condition, and auditor attributes (e.g., Big Four vs. nonBig Four), and accounting for macroeconomic conditions such as the COVID19 crisis.

3 METHODOLOGICAL ASPECTS

3.1 Sample and Data

A quantitative, descriptive study was conducted of Brazilian listed companies, focusing on factors associated with voluntary audit firm changes under tax litigation. The initial sample comprised all firms listed on B3 from 2014 to 2023. For comparability, we excluded financial institutions due to their distinct regulatory environment. The analysis focused on industrial, consumeroriented, and technologyintensive sectors, which, by prior observation, face greater compliance complexity and potentially higher taxdispute risk.

Based on the criteria, the final sample includes ≈30 firms observed over a tenyear period. We constructed an unbalanced panel using financial statements and Formulário de Referência filings obtained from the Brazilian Securities

Commission (CVM). After screening for data availability, the authors retained ≈260 firmyear observations with complete information.

Voluntary audit firm changes were identified by handcollecting disclosures in the “Auditors” section of the reference forms and notes. Each event was classified as mandatory (timelimit rotation) or voluntary (e.g., board decision, resignation, or other nonregulatory reasons). The researchers recorded 24 voluntary changes, which were coded as 1 (the dependent variable); all other firmyears were coded 0 (no change or mandatoryonly rotation). This procedure isolates the phenomenon of interest.

The period of this study also encompasses the COVID19 crisis (2020–2021). A dummy variable for these years was included to capture the shock’s potential influence on auditfirm switching behavior. Table 1 Table 1 provides the definitions of the variables, their expected signs, and the references that support each construct.

Table 1 – Description of the Research Variables

Variable	Name	Expected Sign	Description (Calculation)	Selected References
Tax Litigation	TL	+	Tax provisions + Contingent tax liabilities, scaled by total assets (ratio)	Khurana & Raman (2004); Khaoula & Moez (2019); Bédard & Paquette (2021); Ling (2023); Dhiyaulhaq & Fadjarenie (2023); Lopo Martinez et al. (2024)
Size	Size	+	Natural log of total assets	Martinez & Sonegheti (2015); Dash & Raithatha (2017); Waheed et al. (2022); Lopo Martinez et al. (2024); Bastos & Nakamura (2009); Medeiros & Daher (2008)
Indebtedness	LEV	+	(Current Liabilities + Non-Current Liabilities) / Total Assets	Rajan & Zingales (1995); Brito et al. (2007); Nakamura et al. (2007); Bastos & Nakamura (2009); Medeiros & Daher (2008); Campos et al. (2015); Dash & Raithatha (2017); Arena et al. (2021); Lopo Martinez et al. (2024)
Return on Assets	ROA	–	Net Income / Total Assets	Waheed et al. (2022); Arena et al. (2021); Akonye et al. (2020); Dash & Raithatha (2017)

Continues

Table 1 – Description of the Research Variables

Continuation				
Variable	Name	Expected Sign	Description (Calculation)	Selected References
Big Four Auditor	Big4	+	Dummy: 1 if the company is audited by a Big Four firm (PwC, Deloitte, EY, KPMG), 0 otherwise	Khurana & Raman (2004); Khaoula & Moez (2019); Bédard & Paquette (2021); Ling (2023); Dhiyaulhaq & Fadjarenie (2023); Lopo Martinez et al. (2024)
Economic Crisis (COVID-19)	Crisis	–	Dummy: 1 for years 2020–2021 (pandemic period), 0 otherwise	Martinez et al. (2023)
Market Valuation	VALUE	–	Market value of equity (market capitalization, in BRL)	Moraes et al. (2021)
Voluntary Audit Firm Change	VAC	Dependent	Dummy: 1 if a voluntary audit firm change occurred in the year, 0 otherwise	Martinez et al. (2023)

Source: Adapted from Martinez et al. (2023) and Lopo Martinez et al. (2024), with additions by the authors

3.2 Data Collection and Variable Measurement

Data on audit firm changes were handcollected from companies' annual *Formulário de Referência* and financial statement notes filed with the CVM. For each firm year, the "Auditors" section was examined to identify whether an audit firm change occurred and if it was due to mandatory rotation or other reasons. Changes solely attributable to the 5-year rule (CVM Instruction 308/1999) were not considered voluntary. A voluntary change was coded when disclosures indicated a Board of Directors' decision, audit firm resignation, or another nonregulatory motive Martinez et al. (2023). In these cases, VAC = 1; otherwise, VAC = 0.

Financial data for the independent variables were obtained from audited financial statements and notes. The key independent variable, Tax Litigation (L_Trib), is the sum of provisions for tax litigation plus contingent tax liabilities, scaled by total

assets. These figures were taken from the notes where firms recognize probable losses and disclose losses as required by NBC TG 25 (aligned with IAS 37). As a proxy, *L_Trib* reflects the accounted for exposure to tax disputes (e.g., *L_Trib* = 0.05 indicates tax contingencies of 5% of assets). The researchers acknowledge that the proxy may not capture every nuance of ongoing disputes; this limitation is discussed later.

The control variables are defined as follows. Size is the natural logarithm of total assets. Indebtedness (*End*) is total liabilities (current + noncurrent) divided by total assets; values above 1 reflect negative equity, which was observed in a few cases. Return on Assets (*ROA*) is net income divided by total assets; negative values denote losses. Big Four (*Big4*) is a dummy variable equal to 1 if the company was audited by PwC, Deloitte, EY, or KPMG in the year, and 0 otherwise (information from the reference forms). Economic Crisis (*Crisis*) is a dummy variable equal to 1 for 2020–2021 (COVID19 period) and 0 otherwise. Market Valuation (*VALUE*) is the yearend market capitalization (BRL), as reported or computed from price and shares outstanding. Missing data, such as from illiquidity or delistings, may reduce the effective sample size for this variable. All monetary amounts (assets, liabilities, market value) were inflationadjusted to 2023 BRL for comparability, before being used to compute ratios or logtransformed as appropriate. To limit the influence of outliers, such as extreme negative equity or exceptional profit years, selected ratios (e.g., *ROA*, *End*) were winsorized at the 1% tails.

3.3 Econometric Model: Panel Data Logistic Regression

A logistic (logit) model was used to estimate the probability that a firm **voluntarily changes its audit firm** as a function of the covariates described above. This model is appropriate for a binary dependent variable (**VAC**).

$$VAC_{it} = \beta_0 + \beta_1 TL_{it} + \beta_2 + \beta_3 LEV_{it} + \beta_3 ROA_{it} + \beta_5 BigFour_{it} + \beta_6 CRISIS_{it} + \beta_7 Value_{it} + v_{it} + u_i$$

Where:

- *VAC*: dichotomous variable that assumes 1 (one) if there is a voluntary audit firm change and 0 (zero) otherwise;
- *TL*: tax litigation;
- *Size*: company size;
- *LEV*: indebtedness;
- *ROA*: return on total assets;
- *Big Four*: *dummy* that assumes 1 (one) company audited by the Big Four group and 0 (zero) otherwise;
- *Crisis*: *dummy* that assumes 1 (one) in the Covid-19 health crisis period and 0 (zero) otherwise;
- *Value*: *valuation of companies*;
- v_{it} : model error term; and u_i : unobserved heterogeneity.

The dependent variable *VAC* equals 1 when a voluntary audit firm change occurs in year t and 0 otherwise. The main explanatory variable is *TL* (tax litigation), which is complemented by the following control variables: *Size* (log of total assets), *End* (indebtedness), *ROA* (return on assets), *Big4* (indicator for PwC, Deloitte, EY, or KPMG), *Crisis* (indicator for 2020–2021), and *VALUE* (market capitalization). Unobserved, time invariant firm characteristics are treated as firm level heterogeneity; in the pooled specification, they are absorbed by the intercept, whereas in the random effects specification, they are modeled explicitly.

Logit coefficients are reported in logodds. To facilitate interpretation in probability terms, we present marginal effects. For continuous regressors, these indicate the change in the predicted probability associated with a one unit increase (and, where specified, with a one standard deviation change). Indicator variables such as *Big4* and *Crisis* represent the discrete change in probability from 0 to 1, holding other variables constant.

Model adequacy is assessed using several diagnostics. Overall significance is evaluated by the Likelihood Ratio (LR) test for the joint null hypothesis, which shows that all slope coefficients are zero. Predictive performance is summarized by classification accuracy, sensitivity (true positive rate), and specificity (true negative rate) under two thresholds: the conventional 0.50 and a cutoff close to the sample base rate of auditor changes (approximately 0.08). The area under the ROC curve (AUC) is reported as a measure of discrimination (values near 1 indicate strong predictive power; 0.5 indicates no better than chance).

As observations span multiple years per firm, the necessity of a panel logit was evaluated. A rho (intraclass correlation) test indicated that the proportion of variance attributable to firmlevel effects was not statistically significant. Accordingly, pooled logit results are reported for clarity and parsimony, noting that estimates are robust to randomeffects logit, which yielded similar coefficients.

Beginning with the full specification, a stepwise refinement procedure was applied to improve parsimony, following Fávero and Belfiore (2017). Variables with *p* values exceeding 0.10 were removed iteratively, and the model was reestimated after each step. The final specification retains L_Trib, Size, Big4, and Crisis as the principal predictors. End, ROA, and VALUE were not statistically significant in any specification ($p > 0.10$) and are excluded from interpretation, consistent with the recommendations in Fávero and Belfiore (2017).

4 RESULTS

4.1 Descriptive Statistics

Firm-year observations with and without a voluntary audit firm change are compared to assess whether observable characteristics differ across groups. Table 2 presents summary statistics for each subset.

Table 2 – Descriptive Statistics by Presence or Absence of Voluntary Audit Firm Change (2014–2023)

No Voluntary Audit Firm Change							
Variables	Number of observations	Average	Median	Minimum	Maximum	Deviation	Coef. of Variation
TL	258	6,360	0,053	0	1.122,2	70,75	1112%
SIZE	289	13,982	13,974	6,873	17,463	1,71	12%
LEV	287	6,460	0,336	-4,4449	1.655,88	98,26	1521%
ROA	289	0,741	1,96	-1.459,9	1.549,22	149,60	20189%
Big Four	297	0,552	1	0	1	0,50	90%
Crisis	296	0,419	0	0	1	0,49	118%
Valuation	270	4.287.706	325.198	2.132	161.300.000	12841127,00	299%
Presence of Voluntary Audit Firm Change							
Variables	Number of observations	Average	Median	Minimum	Maximum	Deviation	Coef. of Variation
TL	24	6,456	0,057	-0,001	85,21	21,505	333%
SIZE	25	14,711	15,038	11,994	17,611	1,591	11%
LEV	25	0,267	0,41	-1,923	1,9477	0,8205	306%
ROA	25	-2,527	1,774	-50,321	24,119	16,752	-663%
Big Four	26	0,5	0,5	0	1	0,51	102%
Crisis	26	0,192	0	0	1	0,402	209%
Valuation	24	4.728.169	760.226	13.316	28.393.540	7.200.453	152%

Source: Survey data (2025)

Note: All Monetary values are expressed in BRL. “Litigation” denotes the ratio of taxrelated contingent liabilities and provisions to total assets (expressed in percentage terms for readability). For variables with extreme outliers (e.g., Litigation and Indebtedness), large standard deviations and minima/maxima reflect a few cases of exceptionally high tax risk or negative equity. Big Four and Crisis are dummies; proportions can be read as percentages.

Tax litigation (TL): The mean TL is comparable across groups (6.456 vs. 6.360), but dispersion is substantially greater among firms that do not change audit firms (coef. var. 1,112% vs. 333%). This suggests greater heterogeneity in taxrisk exposure among firms that do not change audit firms. The presence of substantial outliers (exceptionally large maxima and standard deviations) warrants caution when interpreting mean values. Nonetheless, the data confirm material tax risk on both sides, consistent with links between tax risk and auditor–client dynamics noted in prior studies Khurana & Raman (2004); Khaoula & Moez (2019); Bédard & Paquette (2021); Ling (2023); Dhiyaulhaq & Fadjarenie (2023).

Size: Firms that change audit firms are larger on average (higher mean and median SIZE), aligning with the view that complexity and regulatory scrutiny scale with size and may prompt governance actions such as auditfirm switching Martinez & Sonegheti (2015); Dash & Raithatha (2017); Waheed et al. (2022).

Indebtedness: The mean LEV is lower in the change group; however, the median values move in the opposite direction (0.410 vs. 0.336). Extreme values (including negative equity cases) drive substantial variance, so leverage shows no clear monotonic pattern here—an issue we revisit in the multivariate analysis.

Profitability: The change group exhibits a negative mean ROA and a lower median than the nochange group, suggesting weaker performance around change events. Given the outliers, this pattern is treated as indicative rather than conclusive, consistent with work relating performance pressure to governance adjustments Arena et al. (2021); Waheed et al. (2022).

Auditor tier and crisis period: The proportion of firms audited by Big Four is similar across groups ($\approx 55\%$ vs. 50%), offering no strong descriptive signal ex ante. The Crisis indicator (2020–2021) is less frequent among change observations (0.192 vs. 0.419), consistent with fewer voluntary changes during the COVID19 period Martinez et al. (2023).

Market valuation: Differences in Valuation are not decisive, given high skewness and dispersion (means driven by a few exceptionally large firms). Median valuation is higher in the change group, consistent with the observed size pattern. However, regression analysis is used to isolate effects.

Taken together, the descriptive evidence suggests: (i) material taxrisk exposure in both groups with greater dispersion where no change occurs; (ii) larger firm size and weaker profitability are more prevalent in the change group; (iii) voluntary changes were rarer during the COVID19 years. Given outliers and overlapping distributions, multivariate analysis is necessary to quantify associations (see Section 4.2).

4.2 Regression Results

Table 3 presents the logit estimates for the likelihood of a voluntary audit firm change (VAC) following stepwise refinement. The initial specification included Indebtedness (End), ROA, and VALUE, but these variables did not improve model fit and were excluded following the parsimony guidance of Fávero & Belfiore (2017). The final model retains Tax Litigation (denoted TL in the table, consistent with L_Trib used elsewhere), Size, Big Four, and Crisis, with coefficients, robust standard errors, and marginal effects reported in percentage points.

Table 3 – Logistic Regression Results - Determinants of Voluntary Auditor Change (Final Stepwise Model)

Variable	Coefficient (β)	Std. Error	Marginal Effect	p-value
Tax Litigation (TL)	0.0258345 **	0.0125	+2.58 p.p.	0.021 **
Size (ln Assets)	0.5992936 **	0.2721	+6.00 p.p.	0.028 **
Big Four Auditor	-1.035745 *	0.5529	-10.36 p.p.	0.067 *
Economic Crisis 2020–21	-0.9808165 *	0.5684	-9.81 p.p.	0.083 *
Constant	-10.23976 ***	3.123	–	0.001 ***
Model Statistics				
Number of observations	260			
LR χ^2 (df)	29.45 (4)			p < 0.001
Pseudo R ²	0.234			
Log-Likelihood	-48.52			
Sensitivity (true 1's correctly predicted)	66.7%			
Specificity (true 0's correctly predicted)	59.4%			
Overall Correct Prediction Rate	60.0%			
AUC (ROC curve)	0.7105			
Rho (panel var. fraction) – LR Test	~0 ($\chi^2=0.46$)			p = 0.499

Notes: Coefficients are logodds; marginal effects are evaluated at sample means for continuous regressors and as the discrete 0→1 change for dummies. Robust standard errors. Significance: * p < 0.10, ** p < 0.05, *** p < 0.01

4.2.1 Main results

- Tax Litigation (TL /) is positively associated with VAC. A 1 p.p. increase in tax contingencies relative to assets raises the probability of change by approximately 2.58 p.p. This finding is consistent with prior evidence that litigation risk influences auditor–client dynamics Khurana & Raman (2004); Khaoula & Moez (2019); Bédard & Paquette (2021); Ling (2023); Dhiyaulhaq & Fadjarenie (2023).

- Size is positively related to VAC. A oneunit increase in $\ln(\text{assets})$ corresponds to +6.0 p.p. in the change probability, in line with the idea that larger firms face greater complexity and scrutiny Dash & Raithatha (2017); Waheed et al. (2022); Bastos & Nakamura (2009).

- Big Four status is negatively associated with VAC. The marginal effect is approximately –10.4 p.p., suggesting greater engagement stability among firms audited by Big Four auditors, consistent with credibility and riskscreening arguments Khurana & Raman (2004).

- Crisis (2020–2021) is negatively related to VAC. The likelihood of switching auditors was approximately 9.8 p.p. lower in the pandemic years, reflecting a preference for stability during macroeconomic stress Martinez et al. (2023).

Model diagnostics indicate adequate fit and discrimination (LR test, pseudo R^2 , and AUC). The rho test does not indicate significant panel structure, supporting the use of a pooled logit model, which is appropriate, with results robust to a randomeffects specification. Overall, the multivariate evidence identifies tax litigation and firm size as the main drivers of voluntary audit firm change, with Big Four engagement and the COVID19 crisis acting as dampening factors.

4.3 Discussion of Findings

The positive association between tax litigation and voluntary audit firm change supports the notion that litigation exposure shapes auditor–client dynamics, a mechanism anticipated in prior research on legal environments and audit behavior

Khurana & Raman (2004); Choi et al. (2008). In our setting, higher TL is linked to increased switching, consistent with two complementary channels documented in the literature. First, clients under tax pressure may seek auditors with greater tax expertise or a more conservative stance to reassess uncertain tax positions, echoing concerns about tax aggressiveness and auditor responses discussed by Martinez (2017) and by studies on resignation and risk screening in contentious contexts (Goh et al., 2013). Second, auditors actively price and manage engagement risk when litigation exposure rises, which can tighten acceptance and continuance decisions and indirectly elevate the incidence of client switching Choi et al. (2008); Khurana & Raman (2004).

The Brazilian evidence on the fiscal impact of tax contingencies helps explain why this link is economically meaningful. Jesus and Souza (2016) demonstrate that fully provisioning certain tax exposures can eliminate reported profits for a substantial proportion of firms audited by Big Four. Our results align with this mechanism. Where recognition and disclosure judgments under NBC TG 25 materially affect earnings, boards face stronger incentives to realign with an audit firm perceived as better suited to the firm's tax risk profile, which reinforces the compliance-driven interpretation of rotation.

The size effect we document aligns with prior studies linking organizational complexity and regulatory scrutiny with governance adjustments Bastos & Nakamura (2009); Dash & Raithatha (2017); Waheed et al. (2022). Larger firms exhibit a higher propensity to switch auditors, which converges with the notion that they face broader regulatory interfaces and require closer alignment between risk and external assurance. This pattern also helps reconcile mixed findings in the rotation literature. While rotation may renew professional skepticism and mitigate complacency (Parreira et al., 2020), benefits are not universally observed Azevedo & Costa (2012). The evidence suggests that size and litigation intensity jointly tilt the cost–benefit calculus toward switching in cases where the payoffs to enhanced tax scrutiny are highest.

The Big Four coefficient is negative, indicating lower switching probabilities for clients of these auditors after controlling for other factors. This is consistent with

credibility and riskscreening arguments advanced by Khurana and Raman (2004) and the view that highreputation auditors impose stricter monitoring where litigation exposure is salient. It complements results on audit committees, independence, and litigation risk in settings where auditorprovided tax services may complicate incentives Bédard & Paquette (2021). In parallel, caution in the literature regarding the joint provision of audit and extensive tax consulting Dhiyaulhaq & Fadjarenie (2023) aligns with a governance response in which firms separate roles or migrate to providers whose engagement model better supports their independence posture.

The COVID19 crisis years are associated with fewer voluntary changes, which dovetails with evidence that macroeconomic shocks reshape governance preferences and operational priorities Martinez et al. (2023). In a period of elevated execution risk, the cost of switching auditors increases, and the option value of continuity rises, even when tax disputes remain relevant. This temporal moderation offers insight into why some determinants that matter in normal times recede during systemic stress.

The confrontation of empirical results with prior literature yields three key insights. First, in an environment of elevated tax litigation, rotation appears primarily compliencedriven, not performancedriven, which helps explain why financial indicators such as ROA, leverage, and market value lose explanatory power once litigation and size are accounted for. Second, institutional features highlighted in Brazilian studies—material earnings effects from tax provisioning under NBC TG 25 and the salience of independence concerns—correspond closely to the empirical patterns observed, clarifying the mechanisms behind switching in this context Jesus & Souza (2016); Bédard & Paquette (2021); Dhiyaulhaq & Fadjarenie (2023). Third, the findings bridge two strands of the literature—rotation debates and taxrisk research—by demonstrating that litigation intensity serves as a concrete trigger for audit firm realignment, consistent with theories of riskbased auditor selection and with evidence on auditor behavior under heightened legal exposure Choi et al. (2008); Khurana & Raman (2004); Martinez (2017).

Taken together, the contribution lies in anchoring audit firm switching in measurable tax risk exposure within a setting where such exposure is exceptionally high. This framing clarifies when auditor rotation is most likely to be a rational governance response and how it interacts with auditor reputation, firm scale, and macroeconomic shocks.

5 CONCLUSIONS AND IMPLICATIONS

This study investigates the association between **tax litigation** exposure and **voluntary audit firm change** among Brazilian listed companies. Firms with higher tax-related contingencies exhibit a greater propensity to switch auditors, and this relationship remained after controlling for size, leverage, profitability, auditor tier, and macroeconomic conditions. The observed pattern supports the interpretation of audit firm rotation as a tool for managing compliance risk rather than a reaction limited to performance swings.

For managers and boards, the evidence supports interpreting midtenure audit firm changes as a strategic governance response to intensifying tax exposures. Engaging providers with deeper tax capabilities or a more conservative approach may facilitate disputes and enhance reporting credibility. For audit firms, the findings underscore the influence of client tax risk profiles on engagement continuity and call for deliberate acceptance and continuance policies calibrated to litigation exposure. For regulators, the findings suggest that prominent levels of tax litigation shape corporate behavior in ways that intersect with audit market dynamics. Efforts to streamline dispute resolution and to promote transparent disclosure of the reasons for audit firm changes can improve market understanding and reduce the tendency to interpret mid-tenure switches as automatic red flags.

For investors and analysts, context factors are crucial when interpreting audit firm changes. In environments characterized by substantial tax litigation, rotation can signal proactive governance rather than accounting problems. The size effect suggests that such changes in larger firms carry greater informational value for expected monitoring intensity and risk management.

The study has limitations. The sample restricted to publicly listed companies within a single jurisdiction and relies on accountingbased proxies for tax disputes, which may not fully capture earlystage controversies. Future research could incorporate case filings or outcomes. Additional avenues include examining postrotation consequences for reporting quality and fees and complement the quantitative evidence with interviews of audit committee members and engagement partners. Crosscountry comparisons would clarify how institutional features shape the relationship between tax risk and audit firm changes.

Overall, the results established a clear connection between tax dispute exposure and voluntary audit firm rotation among Brazilian listed companies. This evidence expands the empirical foundation for understanding how governance mechanisms adapt under regulatory pressure and offers practical guidance for boards, auditors, and policymakers.

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2. Development of hypotheses or research questions (empirical studies)	✓	✓			
3. Development of theoretical propositions (theoretical work)					
4. Theoretical foundation / Literature review	✓	✓			
5. Definition of methodological procedures		✓	✓	✓	
6. Data collection		✓	✓	✓	
7. Statistical analysis	✓	✓			
8. Analysis and interpretation of data		✓	✓	✓	
9. Critical revision of the manuscript	✓	✓	✓	✓	✓
10. Manuscript writing	✓	✓	✓	✓	
11. Supervision and critical guidance					✓

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