THE RELATIONSHIP BETWEEN AUDITING EXPECTATIONS GAP AND VOLUNTARY CORPORATE DISCLOSURE: EGYPTIAN EVIDENCE

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By

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DECLARATION

This is to attest that no material from this thesis has been included in any work submitted for examination at this or any other university.

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ABSTRACT

The thesis consists of two main parts. First, the thesis is examining the level of voluntary corporate disclosure of the Egyptian companies' annual reports during the period of 2004-2005 and 2005-2006. The examined level is justified by the impact of two groups of determinants; firm characteristics, including firm size, firm profitability, and industrial membership, and corporate governance characteristics, including board size and role duality. The findings of this part of the thesis indicate a relatively low level of voluntary corporate disclosure. Moreover, it is found that firm characteristics have a significant impact of the level of voluntary disclosure, while corporate governance characteristics have an in significant impact on the level of this sort of disclosure. In addition, the thesis examined these relationships not only on the total level of voluntary disclosure, but also for each category of this examined disclosure.

Second, the thesis is examining the existence of the auditing expectations gap in Egypt through the different stakeholders' perceptions. The findings indicate the existence of this sort of gap in Egypt. Therefore, the thesis is investigating the usefulness and effectiveness of the traditional methods, including audit report form, user's education, and standards settings, in comparison to each other in reducing the existing gap. In addition, the thesis provides the theoretical bases for selecting the voluntary corporate disclosure auditing as an effective method of reducing such existing gap. Therefore, the thesis is investigating the usefulness and effectiveness of voluntary corporate disclosure auditing, as a proposed method of reducing the existing expectations gap, in comparison to the traditional methods. The findings of this part of the thesis indicate that voluntary disclosure auditing is an effective method of reducing the auditing expectations gap in comparison to the traditional methods.

Furthermore, the thesis points the most important categories of voluntary disclosure that would be worth it to begin with as have a countable impact on reducing the expectations gap. However, it is noted that the relatively important categories of voluntary disclosure that would effectively contribute to the reduction of the auditing expectations gap are characterized by scoring a relatively low level of disclosure. Therefore, the thesis is suggesting two stages to reduce the auditing expectations gap through voluntary disclosure auditing. First, is to increase the level of voluntary disclosure of these categories in the Egyptian companies' annual reports. Second, is auditing these categories of voluntary disclosure as an introductory stage of launching the concept of voluntary disclosure auditing.

Finally, it is recommended by the thesis to introduce this new area of auditing of voluntary disclosure. However, this new area of auditing needs further research concerning the qualifications and procedures required to apply this new paradigm to make it ready to be in action. Moreover, auditing voluntary disclosure does not mean that it would be obligatory for the companies to have this sort of disclosure, as this would affect the voluntary nature of these disclosures, but if the companies have chosen to disclose this sort of information voluntarily, so it is obligated to audit these disclosures as a matter of securing the stakeholders against any manipulated information that may direct them towards making wrong decisions.

CHAPTER ONE

INTRODUCTION AND OVERVIEW

1.1 BACKGROUND AND MOTIVATION

Information is considered to be the cornerstone of the decision-making process. Therefore, information gains a respectable amount of value to the different users. As the decision-making process is a critical issue, the quality of this process is dependent to a great extent on the reliability and validity of the provided information.

As the decision process is getting more complicated, the provided information needs to be completed from one side, and assured from the other side. Therefore, completeness and assurance of information are vital characteristics that are reflected on the reliability and validity of this sort of information. Moreover, the evolution of the agency theory to include other diversified stakeholders, beside the management and shareholders, to end with the stakeholder theory, presents a pressure on the preparers of information to satisfy diversified and conflicting needs. Therefore, stakeholder theory explains the conflicts of interest and strategic organizational behavior. As a result of this diversification and conflict, the information needs to include different perspectives as a matter of completeness satisfaction. While on the other hand, the source of the provided information requires a great attention to ensure that this information is enough assured to be reliable for the decision making.

With respect to the accounting information, the financial accounting standards are developed to ensure that stakeholders are provided with relevant, reliable, and timely information on which they can make their decisions (Canibano *et al.*, 1999). Therefore, to satisfy the completeness criteria it is required to include financial and non-financial information. However, the majority of the accounting standards require that the firms disclose financial information. Therefore, as a matter of fact, the firms voluntarily disclose additional information to satisfy their stakeholders' needs. This voluntary disclosure includes financial and non-financial information in order to fulfill the completeness of the provided information. This disclosed information varies in between the different firms, as there are no standards that regulate this sort of disclosure due to its voluntary nature, resulting in different levels of voluntary disclosure from one region to another, even from one firm to another within the same region.

Voluntary disclosure is considered to be a non–Generally Accepted Accounting Principals (GAAP) report or Enhanced Corporate Reporting (ECR). The Enhanced Corporate Reporting (ECR) is less constrained than the Generally Accepted Accounting Principals (GAAP) reporting by standards and regulations containing more qualitative disclosures and non–financial information (Gibbins and Pomeroy, 2006).

Moreover, voluntary disclosures level diversification is considered to be a struggling issue as to identify the determinants that affect the disclosure's level. Therefore, voluntary disclosure level is affected by some characteristics either related to the firm itself, firm characteristics, or related to the firm governance body, corporate governance characteristics. The association between voluntary disclosures level and these determinants still debatable, as the relationships vary between the different regions and cultures.

As a normal consequence, the more disclosed information would be associated with more costs of voluntarily disclosing additional information. However, there are different motives and advantages that make the firms bear the cost of disclosing such information. The Financial Accounting Standards Board (FASB)'s report identified several benefits of voluntary disclosures. First is reducing cost of capital. Second is enhancing credibility. Third is improving investors' relationship with the firm. Fourth is improving investment decisions and getting access to liquid markets (Boesso, 2002).

Accordingly, firms voluntarily disclose additional information that it believe that they satisfies the interests of the diversified stakeholders. Therefore, the suitable categories and level voluntary disclosures are still a questionable issue that is not satisfied by the previous literature. The majority of the previous studies examine the voluntary disclosure level and relationships on its aggregated level, ignoring the different categories of voluntary disclosure and its relationships with the different determinants of this sort of information.

With respect to the information assurance criteria, the auditing process plays a vital role to provide the different stakeholders with assured accounting information. However, the auditing process is considered to be limited to the provision of assurance for the mandatory disclosures identified by the auditing standards. Therefore, auditing failed to cope with the evolution in the disclosure improvements.

It is believed that voluntarily disclosing additional information to satisfy the stakeholders' needs is not performed effectively due to the failure of the auditing practices to cope with these improvements in the disclosure practices.

Moreover, it is noted that the auditing practices are not satisfying the needs of the different stakeholders, which results in the existence of an auditing expectations gap. This expectations gap exists in developed as well as developing countries. Several studies examined the existence of this gap, and in each study it proofs that this gap still exists, although there are various efforts to reduce it. The literature conducted three different methods to reduce this gap. First is to expand the audit report, and depend on the long form instead of the short form auditing report. Second is to educate the users towards the auditor's roles and responsibilities to reduce their expectations regarding the tasks performed. Third, is setting additional standards to expand roles and responsibilities of the auditors.

Additionally, the previous studies are restricted to two methodologies of research. First is examining the existence of auditing expectations gap in a specific country as a representative of a certain region. Second, is investigating the effectiveness of a specific method of reducing the existing expectations gap. The literature has not identified any comparative research between the effectiveness of more than one method at the same time. Therefore, I believe that any method examined individually reflects the usefulness of this entire method rather its effectiveness.

Regarding the Egyptian context, there is a shortage in research concerning the completeness of the provided accounting information by voluntarily disclosing additional information. In addition, there is lack of research regarding the assurance of the provided information which fails to meet the diversified stakeholders' needs, resulting in the existence of the auditing expectations gap. However, the only study applied on Egypt by Dixon *et al.* (2006) has only examined the existence of auditing expectations gap in Egypt, but the study has not proposed or investigated the effectiveness of any of the methods that could contribute to the reduction of the existing expectations gap.

Moreover, the relationship between auditing expectations gap and voluntary disclosure is a mutual relationship. The auditing of voluntary disclosures provides assurance to this sort of disclosure which enhances the credibility of it, leading to the ability to rely on this sort of information to make different decisions. On the other hand, voluntary disclosure auditing expands the role of auditor to include the auditing of additional information which satisfies the stakeholders' expectations leading to the reduction of the existing expectations gap.

1.2 RESEARCH CONTRIBUTIONS TO KNOWLEDGE

I am the first in my research area to link between the financial accounting and auditing areas of research. I have employed the voluntary corporate disclosure to solve the existing auditing expectations gap problem. This is considered to be a breakthrough in both areas of research. Moreover, I have introduced, for the first time in the area of auditing, a new branch entitled 'Voluntary Corporate Disclosure Auditing'. The current research provides the conceptual model for this new branch and the empirical evidences regarding the feasibility of this new area of auditing which opens the door for various researches in relation to the required techniques and codes for implying this sort of auditing.

Consequently, the thesis contributes to the accounting and auditing knowledge in three main areas:

First, the thesis is the first to provide updated examination to the level of voluntary information disclosed through the annual reports of the Egyptian companies during the most recent period of time. Moreover, the process is not limited to the examination of the total disclosure, but includes, as well, the level of each category of disclosure and its contribution to the total disclosure level.

Second, the thesis investigates the impact of two groups of determinants, firm characteristics and corporate governance characteristics, on the examined level of voluntary disclosure and identified the significant and insignificant relationships between this level and the disclosure's determinants. In addition, the impact of voluntary disclosure's determinants is investigated towards each category of the examined voluntary disclosure. The thesis is the first study to apply this sort of comprehensive investigation for all the categories of voluntary disclosure.

Third, the thesis suggests that voluntary corporate disclosure is considered to be an effective method in reducing the auditing expectations gap through expanding the roles and responsibilities of the auditor to include auditing the voluntarily disclosed information by the companies in their annual reports. This is considered to be the first study to recommend this proposed solution to reduce the auditing expectations gap and provide a conceptual model, evidencing its effectiveness in performing this role in addition to the examination of this role empirically in comparison to the other traditional methods.

The thesis argues that the level of voluntary disclosure in the annual reports is relatively considered to be low. Therefore, a checklist is adapted from the previous literature and validated to fit with the nature of the Egyptian companies; the checklist contains eight different categories of voluntary disclosures which are considered to be the benchmark of measuring the level of such disclosures. The results of this empirical part, based on descriptive statistical parameters, indicate that there is a low level of voluntary disclosure compared to the checklist items. Moreover, the thesis showed in this part the contribution of each category of disclosure towards the total level of disclosure.

As a matter of fact, the examined level of disclosure is justified by the impact of two groups of determinants on the examined level of voluntary corporate disclosure. The first group of voluntary disclosures determinants are firm characteristics, including firm size, firm profitability, and industrial membership, while the second group of determinates are corporate governance characteristics, including board size and role duality. The results argues that there is significant impact of firm characteristics on the voluntary disclosure level, while on the other hand there is in significant impact of corporate governance characteristics on the level of voluntary disclosure. It is argued that the larger and profitable companies, voluntarily discloses additional information more than the smaller and less profitable ones. In addition, the Egyptian services (non-manufacturing) companies discloses more information more than the manufacturing ones. This paradigm is emphasized using the stakeholders – agency theory, as the aim of disclosing this sort of information is to satisfy the different stakeholders by providing them with their needs of information to facilitate the decision-making process.

The results of the first part of the empirical analysis are derived using multiple Ordinary Least Squares (OLS) regression cross sectional panel data with fixed–effects regression as the data is gathered based on selective criteria (50 most active companies). A robust standard error is employed as the examined data is not normally distributed, which needs to be tested using a non-parametric test. Therefore, robustness test is used to overcome this problem. Moreover, a sensitivity analysis is applied using multiple Ordinary Least Squares (OLS) pooled regression with robust standard error to examine the sensitivity of the results towards changing the statistical test which ensure the reliability of the driven results.

The second part of the thesis investigates the problem of the auditing expectations gap. This problem still exists in most of the countries whether developed or developing countries. This gap exists between the annual reports' users (stakeholders) from one side, and the auditors from the other side. Stakeholders expect that the auditor, when performing the auditing procedures, is providing them with completely assurance that the annual reports present the firm's financial situation fairly and truly. The problem stems from the stakeholder's over-expectation regarding the auditor's roles and responsibilities, as there is a degree of error that might takes place due to depending on samples in performing the audit procedures and other analytic tasks progressed by the auditor.

As a result, the current auditing roles and responsibilities can not satisfy the stakeholders' expectations which are reflected on the existence of an auditing expectations gap (see for example: Gay *et al.*, 1998; Frank *et al.*, 2001; Gowthrope and Porter, 1999; Humphrey *et al.*, 1993; Fadzly and Ahmad, 2004; Best *et al.*, 2001; Dixon *et al.*, 2006; and Chowdhury *et al.*, 2005). Therefore, different methods were proposed to reduce such gap by the previous literature; these methods are summarized in to three methods. Firstly, is expanding the audit report by depending on the long form audit report instead of the short term as to increase the awareness of the stakeholders towards the auditor's roles and responsibilities (see for example: Schelluch and Gay, 2006; Almer and Brody, 2002; and Manson and Zaman, 2000). Secondly, is educating the annual reports users (stakeholders) towards the auditor's roles and responsibilities (see for example: Epstein and Geiger, 1993; Monroe and Woodliff, 1993; and Pierce and Kilcommins, 1996). Thirdly, is setting auditing standards to expand the auditor's roles and responsibilities to include additional performed tasks (see for example: Dewing and Russell, 2002). Each method seems to be effective in reducing such gap when it is examined individually. The previous studies have not examined the effectiveness of theses methods in comparison to each other as to suggest the most effective method.

To do so, the thesis examines the existence of the auditing expectations gap in Egypt to ensure that the problem still exists and this in comparison to the applied study by Dixon *et al.* (2006) but with the expansion of the examined sample. The results argued that the gap still exists. Therefore, based on the stakeholders – agency theory, the thesis examined the usefulness and effectiveness of the three traditional methods from the view of the perceptions of the different stakeholders in comparison to the auditors' perceptions. The empirical analysis differentiated between the usefulness and effectiveness of the different methods towards reducing the auditing expectations gap.

The thesis indicates that for any method being useful in reducing the existing gap do not mean that it is effective in doing so. Based on this argument, the empirical analysis identified the usefulness and effectiveness of each method in comparison to the other ones. The results are driven using the non-parametric Mann–Whitney U test, as the data is not normally distributed, to identify the significant different between two groups of samples, auditors and non–auditors groups. Moreover, the test was employed to examine the sensitivity of the results towards changing the statistical test which enhance the reliability of the driven results.

The thesis argued that expanding the auditor's roles and responsibilities to include voluntary corporate disclosure auditing would contribute to the reduction of the existing auditing expectations gap. Based on the stakeholder –agency theory, it is emphasized by the previous literature that the voluntary disclosure is playing a vital role in reducing the information expectations gap and solving the information asymmetry problem which is referred to the accountability of annual reports (Gray *et al.*, 1987, 1988, 1988, 1991; Laughlin, 1988; Woodward *et al.*, 1996). However, it is argued that this voluntarily disclosed information satisfies only the completeness criteria and ignored the reliability one (Doane, 2000; Swift and Dando, 2002; Dando and Swift, 2003).

The thesis argued that the voluntary disclosure lack reliability as a result of missing the credibility of this sort of disclosure. Therefore, the voluntary disclosure credibility would be provided by independent auditing. The assurance of voluntary disclosures requires expanding the auditor's roles and responsibilities to audit this sort of information. As a result, the audited voluntary disclosures would play dual roles. First, it effectively reduces the information expectations gap between the stakeholders and the directors by providing completed and reliable information. Second, it effectively reduces the auditing expectations gap due to the expansion of the auditor's roles and responsibilities which meets the stakeholders' expectations.

Accordingly, reducing both information and auditing expectations gaps, would contribute to the improvement of the financial reporting quality. This is illustrated by the conceptual model suggested by the thesis that shows the interaction between the audited voluntary disclosure and both gaps, information and auditing expectations gap.

Accumulatively, the results of the two empirical parts of the thesis state that, according to the stakeholders' perceptions, it is worthy to begin launching voluntary disclosure auditing to specific categories of this sort of disclosure rather than auditing the whole categories of voluntary disclosure. However, it is concluded that the recommended categories of voluntary disclosures to be audited are characterized by having low level of disclosure. Therefore, voluntary disclosure auditing would be applied on two stages. First, is increasing the disclosure level of the recommended categories. Second, auditing these recommended categories of voluntary disclosure.

From the previously mentioned expected contributions, the following main research questions will be investigated:

1 What is the nature and level of the total voluntary corporate disclosure in the annual reports of the Egyptian companies? What is the nature and level of each category of voluntary disclosure? What is the trend of the total voluntary disclosure and each category of this sort disclosure in the period of 2004-2005 and 2005-2006?

2 What is the association of the total voluntary corporate disclosure and its different categories, with the firm characteristics, including firm size, firm profitability, and industrial membership, and the corporate governance characteristics, including board size and role duality, during the examined period of time?

3 Is there still an existence of auditing expectations gap in Egypt? Which of the traditional methods, including audit report form, user's education, standards settings, is more effective in reducing such gap?

4 Is voluntary corporate disclosure considered to be an effective method in reducing the auditing expectations gap? If so, which categories of voluntary disclosure are more critical to begin with?

The answer of the previously stated research questions are provided by the thesis using theoretical evidences and empirical findings.

1.3 STRUCTURE OF THE THESIS

This section provides brief overview of the contents of the thesis. Chapter two includes an Egyptian background about the Egyptian economy including the different sectors of the economy and the economic reform program and the indicators of its performance. Moreover, this chapter includes information about the Egyptian stock market, Cairo and Alexandria Stock Exchange (CASE), and the main regulations and governing bodies that manage the stock exchange's operations and transactions. Finally, the chapter includes a framework about the regulatory bodies of the Egyptian accounting and auditing standards.

Chapter three provides updated literature review for the previous studies regarding the auditing expectations gap. The first part of this chapter presents the studies that examined the existence of auditing expectations gap in the developed countries in compared to those applied in the developing countries. The second part includes the previous studies regarding the investigation of the different methods of reducing the existing auditing expectations gap.

Chapter four represents the theoretical framework of the entire thesis which is composed of three different parts. First is presenting the different theories of voluntary disclosure including the stakeholder–agency theory which is the main theory of the thesis. Second is indicating the relationship between voluntary disclosure and information expectations gap. Third is emphasizing the relationship between auditing expectations gap and voluntary disclosure, which is the main relationship that is examined empirically in the following chapters.

Chapter five presents the research methodology of the thesis. This chapter is divided in to two main parts. The first part is the methodology of examining the level and determinants of voluntary disclosure which presents the quantitative part of the thesis depending on secondary data analysis. The second part is the methodology of investigating the auditing expectations gap and effectiveness of the different methods of reducing this gap presenting the qualitative part of the thesis depending on primary data.

Chapter six is the first empirical part of the thesis which is composed of two main parts. The first part is the examination of the level of total voluntary corporate disclosure and the level of each category of voluntary disclosure's categories of the Egyptian companies. The second part is the investigation of the relationship between voluntary disclosure and firm characteristics from one side, and between voluntary disclosure and corporate governance characteristics from the other side.

Chapter seven is the second empirical part of the thesis which is composed of five different parts. The first part is investigating the existence of the auditing expectations gap in Egypt. The second part is examining the effectiveness of the audit report form in reducing the existing auditing expectations gap. The third part is examining the effectiveness of educating users towards the auditor's roles and responsibilities in reducing the existing gap. The fourth part is investigating the effectiveness of setting standards that expands the auditor's roles and responsibilities in reducing the gap. The final part is investigating the effectiveness of voluntary disclosure auditing in reducing the existing gap as a proposed solution by the entire thesis.

Chapter eight is the thesis conclusion showing the results and findings of the thesis. The chapter also shows the implications to management and the limitations and future research of the thesis.

CHAPTER TWO
BACKGROUND INFORMATION ON THE EGYPTIAN ECONOMY

2.1 INTRODUCTION

Egypt is considered to be the most populous nation in the Arab World, and has the second largest economy in the Arab world after Saudi Arabia. Strong growth over the 1990s helped to reduce poverty and support an expanding middle and professional class transforming Egypt into an emerging modern economy. This could be observed from the economic indicators of Egypt, as its Gross Domestic Product (GDP) is $91.7 billion and per capita GDP $4,282, while its annual growth rate 4.8%.

Egypt has passed over different stages of economic improvements, specially the economic reform program in 1992, which affects its corporate governance framework. During the 1960s, the central auditing organization became the governmental agency which is responsible for auditing in the public sector, due to the movement toward economic management based on central planning, nationalization, and expansion of the public sector.

In the mid-1970s, the Egyptian government applied the "open-door" policy which leads to the liberalization of the national economy until the government launched the comprehensive economic reform program supported by the World Bank and the International Monetary Fund (IMF). As a result to this economic reform program, the Egyptian government launched several initiatives to reform corporate financial reporting and disclosure requirements as well as accounting and auditing standards for governing the financial practices.

2.2 THE GEOGRAPHIC LOCATION OF EGYPT

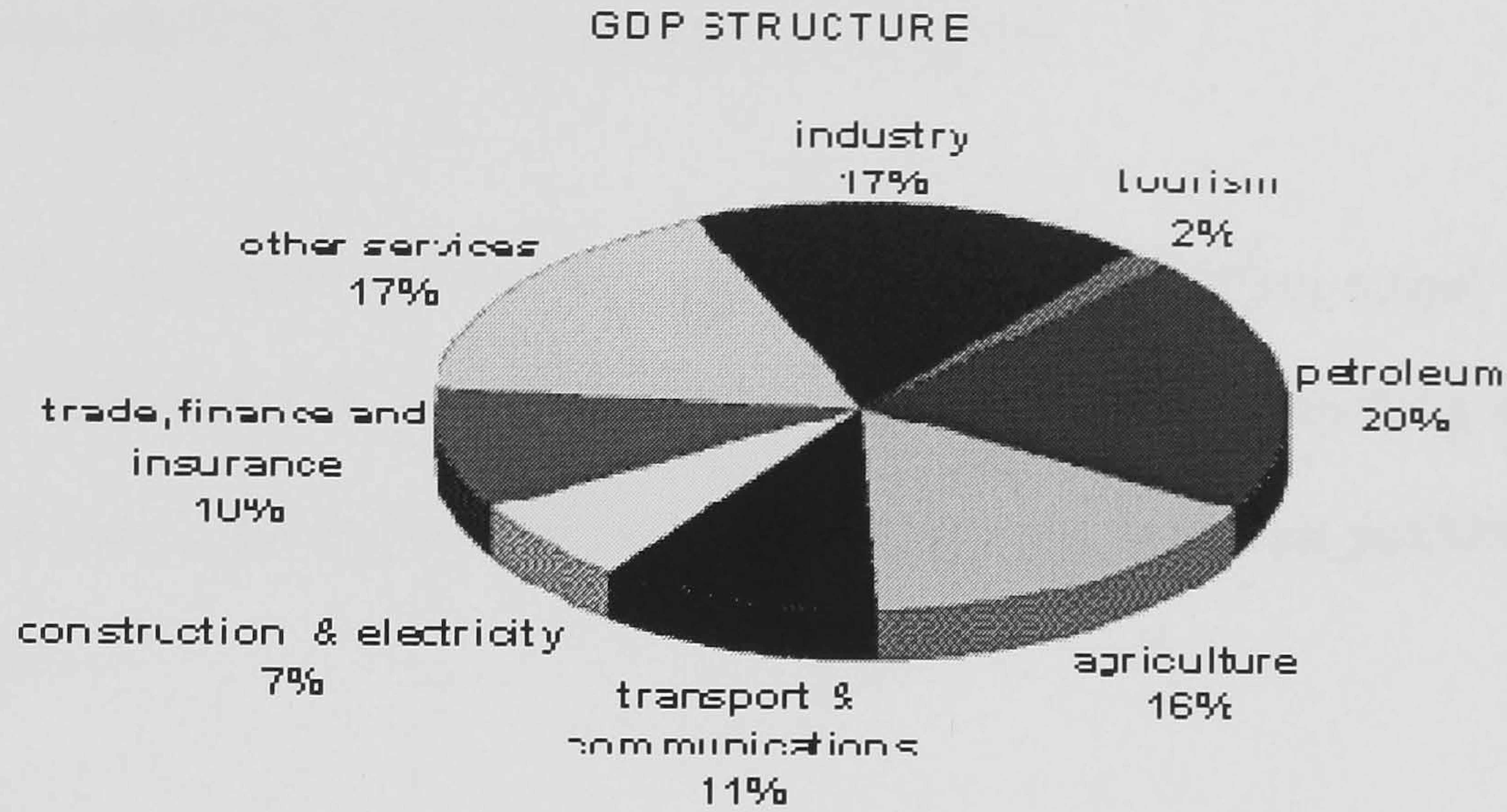
The Arab Republic of Egypt is located on the north eastern coast of Africa, and borders the Mediterranean Sea between Libya and the Gaza Strip. Egypt is basically a desert nation; only four percent of the country's total land area of one million km is arable. Egypt most notable geographical feature is the Nile River, and almost 99 per cent of Egypt population lives in the River Valley and the fertile Nile Delta, north of the capital, Cairo (Roquette and Kourouma, 2004).

2.3 THE MAIN SECTORS OF EGYPTIAN ECONOMY

Egypt has a fully diversified economy with potentially high growth across all of its sectors. And these sectors could be represented by the following chart:

Figure 2.1

The GDP Structure of Each Sector of the Egyptian Economy



Source: Country Commercial Guide for Egypt, International Copyright, US & Foreign Commercial Service and US Department of State, 2004.

The different various sectors could be represented as follows:

2.3.1 Energy

The oil & gas sector is considered to be the fifth important source of foreign exchange. Reserves of oil could remain for about fifty years. Natural gas production ad reserves have been growing by 10% or more each year. Egypt already generates most of its electricity from natural gas. With new discoveries of gas, after satisfying the demand of the domestic the market, Egypt is searching for new export markets and to develop export capacity of gas. The oil and gas sector is being one of the most important resources of foreign investments in Egypt such as: British Gas, BP, ENI, and Shell.

In addition, Egypt contains great natural resources which includes petroleum, natural gas, phosphates, and iron ore. Moreover, in the Gulf of Suez and in the Western Desert crude oil was found, while natural gas is found mainly in the Nile Delta, off the Mediterranean Seashore, and in the Western Desert. Oil and gas contributes about 12% of the GDP: exports of petroleum and related products (including bunker and aviation sales) equals to $2.7 billion in fiscal year 2003-04.

Moreover, the petroleum products are increasing from 16.8 million metric tons in 1983 to 25 million metric tons, and the Egyptian government is working on new discovery to satisfy the domestic demand and develop this important product of the energy sector.

The other source of energy is electricity, which is considered one of the most important infrastructure resources that attracts the foreign investments to the Egyptian economy. Always there is additional generation of the electricity capacities to meet the required demand. The electricity sector invites the private ownership and operations of new electricity power generating facilities up to 20% of total planned capacity.

2.3.2 Agriculture

Agriculture is one of the key sectors of the Egyptian economy as it represents 16% of GDP and 28% of total employment. However, all the agricultural prices are decontrolled except for cotton and sugar cane and all agricultural subsidies were removed, but there was a combination of improved incentives and introduction of new high-yield varieties that led to a good response that may be proved by the growth in the agricultural sector by 3-4% in recent years.

In addition, approximately one-third of Egyptian labour is engaged directly in farming, and the other related jobs, including processing and trading of agricultural products. The agricultural operations take place in about 2.5 million hectares (6 million acres) of fertile soil in the Nile Valley and Delta. However, Egypt expands the agricultural lands by constructing "Toshka" project that will be owned by the private sector to grow fresh fruits and vegetable to be exported to Europe in winter months.

2.3.3 Tourism

Tourism is one of the sub sectors of the service sector that represents about 50% of the GDP of Egypt and considered to be the key engine of growth of Egypt and the largest foreign exchanger as it represents about 3% of the GDP of Egypt. Tourism is an important source for Egypt of foreign currencies. Egypt earns a competitive advantage in this sector due to the variety of tourist locations and attractions. Therefore, Egypt is concerned with the development of these locations and attractions as this sector also offers various employment opportunities with acceptable returns.

2.3.4 Construction

This sector represents 7% of the GDP of Egypt, as it plays dual roles: it is considered to be the main sector that is participated in the development and maintenance of the infrastructure , and the demand on this sector creates demand on the steel and cement industries besides being an important sector in solving the unemployment problem.

2.3.5 Manufacturing

Manufacturing sectors contributes about 20% of GDP and about 13.4% of employed workforce. There are key industrial sectors in Egypt includes textiles and clothing, food and beverages, furniture, and metallurgy. However, there are other several sub-sectors that are characterized by a rapid growth, including steel production food processing industry, textiles and garments industry, pharmaceuticals, automotive assembly, and electronics industry.

Egypt is still one of the most important industrial countries in the Middle East and Africa, as it has attracted different multinational companies beside the domestic industrial companies, and that is a result of the facilities that the Egyptian government has offered for the industrial investors, including suitable infrastructure, the tax allowances, and the exports support.

2.3.6 Transportation and Communication

The service sector contributes over 50% of GDP, which includes sub-sectors as tourism, financial services and the receipts from the Suez Canal. This sector is characterized by being so sensitive to any external shocks and political tensions.

The Transportation and Communication sector is one of the most important service sectors in Egypt and represents about 11% of its GDP. The most important transportation channel is the Suez Canal, as its revenue is considered to be increasing revenue due to the globalization of markets and the increase of exports and imports between the foreign countries. But, as mentioned, the revenues of this source are sensitive to any political or economic shocks.

The focus has been on the development of the information technology sector and the telecommunication, which has attracted a lot of multinational companies to work in the Egyptian market. This sector is rapidly growing and considered to represent a switch from the manual culture to an electronic culture due to the introduction of the electronic commerce and the well-established technology, especially in the field of phone services and electronic networks.

2.3.7 Trade, Finance, and Insurance

This sector is considered to be a service sector and represents 10% of the GDP of Egypt. This sector includes the banking sector, which is composed of four governmental banks besides a variety of private multinational banks under the supervision of the Egyptian Central Bank (ECB). The different multinational banks are designed to activate investments in Egypt, which was the most important reason that made the Egyptian government think about the privatization of the four governmental banks. The government has privatized one of the four banks.

This sector also includes the Egyptian capital market whish is named The Cairo and Alexandria Stock Exchange (CASE), and it is taking a great consideration from the government for its establishing and development as it is the most important motivator of the economy as a whole, therefore, it would be discussed in a separate point by itself in this chapter.

2.3.8 Other Services

The other services represent 17% of the Egyptian GDP, and include some additional services that by themselves represent small contribution, such as insurance companies which represents only 1.1% of the GDP of Egypt.

Finally, it was observed that the Egyptian economy relies basically on tourism, oil and gas exports, and Suez Canal revenues, most of these sub sectors are controlled by the public sector.

2.4 THE ECONOMIC REFORM PROGRAM

In the 1990s, the government of Egypt began to apply an economic reform program to improve its economical situation, was designed to be applied in different phases; the first phase had focused on stabilizing the economy, improving the exchange rate and public finance and to stabilize the inflation rate. The second phase is concentrating and focusing on the trade and investment issues, and restructuring the private sector and the banking sector (Egyptian ministry of investment report, 2005).

The reform in both phases is applied with full support from the International Monetary and the World Bank and targeted to improve both the monetary and fiscal policy, as the economical indicators showed that the Egyptian economy suffers from a hyper-inflation rate of more than a 20%, negative real interest rate, which is about minus 6%, and a large budget deficit more than 20% as a percentage of the Egyptian GDP (Omran, 2001).

As mentioned, the economic reform program was applied gradually on two different stages: the programs aims to restore fiscal balance reorient both external and internal prices to more realistic levels and liberalize the Egyptian economy. These economic liberalization policies were in exchange for a foreign debt relief package (Monique Roquette and Kourouma, 2004).

Egypt applied this reform in a relatively successful way as the success of Egypt in the application of its reform program could be illustrated by the following table:

Table 2.1

Some Economic Indicators Before and After the Economic Reform Programme

Description	1990/91	1997/98
Total external debt	US $ 49.2 billion	US $ 26.6 billion
Total external debt as a percentage of GDP	151%	37.7%
Real interest rates	(6%)	5%
Inflation rate	21.2%	4.1%
Total foreign reserve (Billions of US$)	3.6	21.8
Budget deficit as a percentage of GDP	18.2%	0.06%
Real GDP growth rate	3.6%	5.7%

Source: Central Bank of Egypt, the Egyptian Cabinet Information and Decision Support Centre (Cairo: CBE and IDSC, Various issues, 1992-1998).

Moreover, Egypt has achieved valuable efforts in decreasing its total external debt from US $ 49.2 billion to US $ 26.6 billion, a decrease of 46%, and that decline is due to the debt forgiveness from the Gulf States, the United States and Paris Club rescheduling agreement (Omran, 2001).

However, as a result of the decline in the total external debt, the percentage of the total external debt to the GDP has decreased from 151% to 37.7% by a higher rate of decrease of 75% than the decrease of the external debt itself, which shows the higher consequences of the decline of the external debt (Omran, 2001).

In addition, it is included that the real interest rate ratio has been increased from (6%) to 5% which is a good indicator of the Egyptian economy as this increase caused the change of the situation of the interest rate from being a negative rate to a positive interest rate (Omran, 2001).

Concerning the inflation rate, there is a significant decrease from %21.2 to 4.1% which means that there is a decrease by a rate of 85% which means that the inflation rate after the reform program is being more controllable and acceptable (Omran, 2001).

From table 2.1 it could be seen that the total foreign reserve has increased from US $ 3.6 billion to US $ 21.8 billion by a rate of increase of more than 500%, which is considered to be a high rate of increase that reflects the Egyptian policies to attract the foreign currencies and exchange them with the domestic Egyptian pounds which means more investment opportunities that are available for foreign investors in Egypt during the period of the reform program of Egypt.

Regarding the budget deficit percentage, it has decreased from 18.2 % to 0.06%, which indicated a sharp decrease by 97%, which means a good improvement in the Egyptian government overall performance (Omran, 2001).

Finally, as a result of all the previous improvements, there is an improvement of the real GDP growth rate from 3.6% to 5.7% by about 58% which is considered to be a good improvement for the Egyptian economy during this period of time.

During the mid 1990s there was a progress done towards lower inflation rate, but despite of this decline in the inflation rate, the real (GDP) growth declined between 1999 and 2002, but in 2001 there was an accelerated rate of GDP growth per capita that have reached US$3,520, while the unemployment rate remained consistently high at 8-9%, representing a significant deviation from the targeted rate of 7.3% outlined in the fourth five-year plan of 1997/98 – 2001/02 (Roquette and Kourouma, 2004).

The Egyptian economic reform program co-operated with the public enterprises reform program in 1991 by the application of law 203 for the year 1991. This reform program is the privatization program which includes several areas of reform, mainly the sale of public assets and shares, and the restructuring of the companies as long as they remain owned by the state by comprising technical, financial, and labour restructuring.

Since 1991, the Egyptian government has achieved valuable progress in the reform program of its macro-economics program. This improvement can be shown by the progress of different economic indicators, the decrease of the fiscal deficit from 17%

of GDP to only 5%, import tariff rates have been reduced from a maximum of 120% to only 70% and are expected to go lower. Finally, the inflation rate has been reduced from 17% to less than 10% (Youssef, 1996).

In addition, the foreign exchange rate is freely determined, that causes the stabilization of the Egyptian pound over three years. The total foreign reserves are still stable at US $17 billion (Youssef, 1996).

The reform actions were applied directly through policy changes, and indirectly through educational and other measures to improve economic and social welfare. The reform policies are based on four dependent dimensions: investment, savings, institutional reform, and exports promotion (Elregal, 2003).

Moreover, the Egyptian reform program is concentrating on the encouragement of the private policy participation by offering initiative measures in the economic legal, monetary, and financial and institutional spheres. As a result, the new economic policy and business environment offers the investors attractive initiatives and opportunities (Elregal, 2003).

Therefore, the industrial cities and duty-free zones benefit from the advanced infrastructure, stable economy, and liberalization of trade. These developments have attracted an increasing number of multinational corporations (Elregal, 2003).

One of the most important constraints of privatization and the reform program is that Egypt still lacks the appropriate business environment. The important constraint on the government choices in the privatization options is the serious unemployment situation and social problems that may result from the transfer of ownership. There is also a belief that in efficiency exists in both, public and private ownership, therefore the inefficiency is due to managerial disqualifications rather than the form ownership (Youssef, 1996).

The privatization program was applied selling only the minority shares, which means that the majority ownership of most of the companies still remains in the hand of the state. The Egyptian structured reform program aimed to improve the performance of the privatized companies to maximize its profit or to change its situation from being loss-making to profit-making status which is considered to be a short term objective (Youssef, 1996).

The Egyptian government applied a diagnostic process on the companies that are decided to be sold. The diagnosis process aimed to identify whether the problems are due to external factors or internal factors. In other words, the main objective of this diagnostic process of the Egyptian economic reform program is to identify the symptoms and causes of the internal and external problems, as to change the status of these companies from losing companies to profitable companies to be attractive companies when selling them (Youssef, 1996).

The performance of the Egyptian privatization program could be shown by the following table:

Table 2.2

Number of Privatized Companies in Egypt

Companies sold to the public (through the stock market).	34
Companies sold to anchor investors.	8
Companies sold to labour unions	15
Number of companies of which more than 51 % of equity sold to private sector.	57
Number of companies sold as assets	17
Number of companies of which more than 40% of its equity sold through the stock market	9
Number of companies of which less than 40 % of equity sold through the stock market	9
Number of companies of which less than 50 % of equity sold to date	18
Total number of companies covered by the privatization programme	92

Source: The Egyptian Ministry of Public Enterprise Sector, Privatization Programme performance from the start to 24-5-1998, Unpublished Report, (Cairo: MPES, 1998).

It was noticed that the total number of the privatized companies in Egypt, either fully or partially, was 92 out of the total number of companies of Egypt which is 314 companies, that means that 28% of the state-owned enterprises have been privatized fully or partially (Omran, 2001).

Finally, there were many investment incentives that had been settled by the Egyptian government to attract investors to Egypt. This included the unified tax law number 187 in 1993 that reduced the marginal tax rates and simplified tax structure and administrative, besides the tax allowances. In addition, there was the introduction of the sales tax to reduce the budget deficit, reducing the exports tariff from a maximum of 120% to only 50%, and the establishing of the social fund of development by the president decree number 40 (Omran, 2001).

2.5 THE EGYPTIAN STOCK MARKET

The stock market is considered to be an essential prerequisite for the achievement of a significant growth rates of economies, and this stock market needs to be well established and at the same time to be developed and updated to be well-ranked compared to the other stock markets in the other different economies.

Cairo and Alexandria Stock Exchange (CASE) is the Egyptian stock market, which is considered to be a self-regulatory authority and is managed by an elected board of directors under the supervision of the Capital Market Authority (CMA). This board is composed of eleven members: the chairman is assigned by the Council of Ministers, six members represents the stock exchange brokers, two members represents banks, one member is appointed by the Central Bank of Egypt, and one is from the CMA (The Ministry of Foreign Trade, 2004).

The Stock exchanges were established in 1883 and 1903 respectively, and reached their historical peak in the 1940s when they, together, ranked as the fifth largest stock exchange market in the world. After several years of decline in the performance of the Egyptian stock exchange market, the stock market started growing again in 1992 with the economic reform program, privatization, and the regulatory changes in the Egyptian environment (The Ministry of Foreign Trade, 2004).

Egypt established its capital market by regulating the Capital Market Law 95 of 1992 (CML) that regulates the capital market framework and the supervision and control of the stock market and the market intermediaries that deals with the Egyptian stock market. In addition, new regulations and rules were established as decrees of the minister of foreign trade to address other issues including disclosure requirements, stock exchange listing requirements, minority stockholders rights, and securitization (The Ministry of Foreign Trade, 2004).

The Central Depository Law 93 of 2000 (CDL) regulates the stockholders record keeping, clearing and settlement. In addition, in 2003 the National Democratic Party (NDP) approved the reforms to the company and accounting / auditing laws (The Ministry of Foreign Trade, 2004).

Accordingly, Egypt established a new capital market law in year 2001. The new law aims to provide greater protection to the investor, and offering a code of conduct for the operations of the brokers and portfolio managers.

The regulations of the Egyptian stock market are settled by the Capital Market Authority (CMA), which is reporting to the Minister of Foreign Trade (MOFT). The CMA has wide administrative powers, including diversified actions as warnings, delisting, suspending and revoking license, imposing monetary penalties, cancelling transactions, conducting inspections, and suspending shareholder decisions (The Ministry of Foreign Trade, 2004).

The CMA is composed of seven board members, two of them, including the chairman, are appointed by the President for a renewal three year term, the others are appointed by the Prime Minister for a two-year renewal term Moreover, the CMA budget is derived from the fee income of the stock market (The Ministry of Foreign Trade, 2004).

After the Egyptian economic reform program, which was co-operated with the privatization program in the 1990s, there was a rapid growth in the Egyptian stock market. At the end of 2002, market capitalization as a percent of GDP was 29%, which increased from 21% in 1996, and decreased from 37% in 1999. Depending on this measure, the Egyptian stock market is considered to be smaller than the other stock markets in Jordan, Bahrain, and Saudi Arabia, but comparable to Morocco (The Ministry of Foreign Trade, 2004).

In terms of absolute size, the Egyptian stock market is performing well, as the Egyptian stock market index in local currency terms rose by almost 97.1% through September 2003, while the increase of the Egyptian stock market index in US Dollars is somehow lower of about 51.4% (The Ministry of Foreign Trade, 2004).

The Egyptian stock market is characterized by a large number of listed companies due to the tax advantages associated with the listing in the stock market: 1148 companies were listed at the end of 2002, increasing from 656 listed companies in 1992. However, the number of listed companies declined to 1079 by the end of September 2003 due to the enforcement of strictly listing requirements. At the end of 2003, up to 300 companies were expected to be deleted and 800 companies to remain listed (The Ministry of Foreign Trade, 2004).

CASE has three listing schedules: the official schedule, the unofficial schedule 1, and the unofficial schedule 2. Public enterprises are listed in the official schedule, while the foreign securities were listed on the unofficial schedules. There are no differences between the three schedules concerning the tax advantages or the listing requirements, but this classification to encourage the listing of companies with special conditions as: partially privatized companies, closed, companies, or technology companies (The Ministry of Foreign Trade, 2004).

2.6 THE EGYPTIAN LEGAL FRAMEWORK

The Accounting Practice law (133/1951) and its amendments govern professional accountants and auditors, especially in the private sector. This law governs the registration and licensing of accountants and auditors, and provides a framework for bookkeeping and financial reporting, and gives the authority to the ministry of finance to develop a standardized chart of accounts and detailed instructions on the accounting treatments and reporting formats. The main objective of this law is to create a uniform accounting system and auditing practices, and to develop and apply the accounting standards that are the prerequisite for the introduction of high-quality financial reporting to the market economy (Wahdan *et al.*, 2005a).

The Accounting Practice Law is followed by establishing the company law (159/1981) and its executive regulations. This law requires all the registered companies under the company law to maintain accounting records and present annual audited financial statements. In addition, this law requires that the annual meeting of the shareholders should evaluate the performance of the auditor and appoint a new auditor or renew the appointment of the existing auditor (Wahdan *et al.*, 2005a).

Moreover, the company law required that the following points must be satisfied in the auditor report that is presented in the shareholders' meeting: (a) the company maintain proper accounting records, (b) all legal requirements have been applied to all of the accounts, (c) all the information (evidence) for accomplishment of the auditor's duties has been collected, and (d) the financial statements represents the financial condition and results of operations in a fair and true view. Therefore, there are four main characteristics that are found in the Egyptian listed companies: (a) there is a separation between the owners and the managers of the listed companies; (b) considerable state ownership in privatized companies, (c) weak board independence, and (d) disclosure is not a common practice (Wahdan *et al.*, 2005a).

Egypt has had a stock exchange market since 1882. This stock exchange market was considered to be the fifth most active market in the world in the 1950s, but in the late 1950s the stock exchange activity decreased and remained inactive for 30 years. In the 1990s, with the launching of the economic reform program, the Egyptian government decided to refresh its capital market by issuing a new capital market law (No.95 of 1992) which regulates the capital market practices, and provides the legal framework. For the Cairo and Alexandria stock exchange, and regulates the incorporation and operations of market participants (Wahdan *et al.*, 2005a).

According to the capital market law, all listed companies are required to follow and apply the Egyptian accounting standards. At the beginning of applying the capital market law the listed companies are required to prepare financial statement incompliance with the international accounting standards. Then the ministerial decree (503/1997) mentioned that the listed companies are required to use the Egyptian accounting standards and in the absence of the Egyptian accounting standards regarding the accounting treatment, the requirements set by international accounting standards were applied (Wahdan *et al.*, 2005a).

Moreover, the capital market law required all listed companies to publish financial statements in two widely-distributed newspapers and to establish an audit committee. In addition, recently the capital market authority has issued a new capital market law that has been activated since August 2002 to ensure that the prepared and presented financial statements comply with accounting, auditing, and legal requirements (Wahdan *et al.*, 2005a).

In addition, Egypt has established the banking law (163/1957) that requires all banks to follow the accounting and auditing requirements and guidelines that are set by the central bank of Egypt. Therefore, all banks in Egypt are required to report their financial statements following the Egyptian accounting standards and these statements required to be audited. The central bank of Egypt controls the audits of the financial statements and the auditor performance and also reviews the auditor report and annual financial statements prior to stockholder meeting (Wahdan *et al.*, 2005a).

The Banking law required that two auditors - it is allowed that they are from the same auditing firm - must audit bank financial statements and ensure the audit quality. Moreover, the banking law requires that individual auditors cannot sign audit reports for more than two banks per year. In addition, the Egyptian central bank requires banks to file annual, semiannual, and quarterly reports including financial statements (Wahdan *et al.*, 2005a).

Finally, the central auditing organization law (144/1988) governs the auditing of government departments and agencies (public sector enterprises, and companies in which ownership interest of public investment is not less than 25 per cent). The central auditing organization is considered to be an independent public organization that reports directly to the people assembly by submitting its reports to parliament. The most important role of the central auditing organization is the harmonization of public sector accounting and auditing standards with the internationally accepted standards.

2.7 THE EGYPTIAN PROFESSIONAL AND EDUCATIONAL ENVIRONMENT

2.7.1 Auditing Profession

The Egyptian society of Accountants and Auditors is considered to be the body of accounting profession in Egypt; it is an association of chartered accountants that develops educational and professional standards. It is composed of about 1,200 members, where about 700 members are actively involved in auditing practice. The society is a member of the International federation of Accountants (IFAC).

In 1946, a royal charter established the Egyptian society of Accountants and Auditors and it was given further statutory recognition by the ministerial order No.2280. The society is managed by the board of directors and is constituted under its own statutes. Members have been admitted when they satisfied one or more of the following conditions: (1) Membership in the institute of chartered accountants in England and Wales, or another accepted foreign professional body, (2) Doctoral degree in accounting or auditing with three years of full-time work experience in practice, (3) At least three years of full-time work experience in the office of a practicing Egyptian society of Accountants and Auditors member or equivalent and successful completion of the two-part examination (the first examination is performed after one-and-a-half years; and the second final part is taken at the end of three years).

The registration committee for Accountants and Auditors in the ministry of finance is responsible for registering professional Accountants and Auditors; this registration committee has a list of more than 80,000 registered accountants who provide auditing services.

The registration rules requires that to be registered as a trainee accountant he/she must be a graduate with a bachelor degree and a major in accounting. These trainees may qualify for first-level registration as accountants if they achieve three years of professional work in a practicing accountant office or equivalent, after that they have the authority to practice as auditors of sole proprietorship and partnership enterprises. The accountants may apply for the final registration certificates after additional five years of employment experience; this final registration certificate gives the authority to the accountant to act as auditor of joint stock companies.

In addition, to be qualified as auditor of joint stock companies can be done by registering directly through membership in the Egyptian society of Accountant and Auditors. However, many practicing auditors, of the Egyptian society of Accountants and Auditors, lack necessary professional competence for providing high-quality auditing service.

In Egypt, the code of ethics was established in 1958 and the ethics violation criteria (such as: Fraud) was discussed by the syndicate law (40/1972). However, the ministry of finance and syndicate law has played an important role to increase the awareness of legal requirements, but practically there is little awareness among many practicing auditors of international best practices concerning conflicts of interest and auditor independence (Wahdan *et al.*, 2005b).

2.7.2 Auditing Education

The Egyptian public universities quality needs to be improved as they suffers from the lack of modern courses and few qualified teachers to face the rising number of students. The accounting and auditing courses needs to be updated to include international standards and practices, but that may be faced by the lack of the appropriate learning text books and educational materials in international accounting and auditing.

Private universities in Egypt, such as AUC, BUE, GUC, now offer English-language accounting programs using internationally-comparable courses and English-language text books. But these universities are characterized by high tuition fees which restrict huge number of students to be accessed to these universities. In addition, some public universities began to introduce an English-language section in the accounting department (Wahdan *et al.*, 2005b).

Moreover, one of the most important weaknesses is the registration process, as one of its requirements is that the applicant must work for practicing licensed accountant or equivalent throughout the stipulated apprenticeship period. This requirement is evidenced by a letter from the employer and neither this letter subjected for verification or the applicant participation in any actual audit assignment during the apprenticeship period. In addition, the Accounting practice law does not require the audit practitioners to undertake any regular training or continuing their professional education. On the other hand, international best practice stipulates that every practicing auditor should complete at least 30 hours of continuing professional education per year to be updated with the new and recent development in the accounting and auditing practices (Wahdan *et al.*, 2005b).

In response to this problem of knowledge some universities offered some training programs using the upgraded text books and educational materials, but these programs may be eliminated by the difficulty of accessibility of these programs to all of the auditor professionals.

2.8 THE ACCOUNTING AND AUDITING STANDARDS IN EGYPT

The Ministry of Economy and Foreign Trade in May 1997 issued ministerial decree (478/1997) to establish the permanent committee for standards of accounting and auditing which are responsible for setting the accounting and auditing standards in Egypt. The settlement of the accounting and auditing standards in Egypt is done by selecting the international accounting and auditing standards that are applicable to the Egyptian situation (Wahdan *et al.*, 2005b).

The selected international accounting and auditing standards are translated in to the local language and are used to draft the Egyptian standard that reflects the requirements of the Egyptian laws and regulations. The draft is then submitted to the permanent committee to be discussed, finalized, and adopted. The final draft of the Egyptian standard is submitted to the Ministry of Foreign Trade to be issued by a ministerial decree (Wahdan *et al.*, 2005b).

The first time to introduce Egyptian Accounting standards was done by the ministerial decree 503/1997. By the end of May 2002, the ministry of Foreign Trade introduced ministerial decrees issued 22 Egyptian Accounting standards and six Egyptian Auditing standards, concentrating only on the presentation of the final audit report regardless the necessarily improvements of the whole process of auditing (Wahdan *et al.*, 2005b).

2.9 ENSURING COMPLIANCE WITH ACCOUNTING AND AUDITING STANDARDS

The Ensuring compliance with accounting and auditing standards is affected by a group of problems that may face the application of these standards in Egypt. One of the most important problems is the lack of the guidelines for the application of the Egyptian standards, also the lack of capacity of those who prepare and audit financial statements, and the lack of the regulatory mechanisms for imposing sanctions the accountants and auditors who fail to comply (Wahdan *et al.*, 2005b).

The capital market authority reviews the annual financial statements presented by the listed companies to ensure that these statements are filling the requirements of the preparation and the disclosure required by the capital market authority from one side, and from the other side making sure that these financial statements are prepared and audited following the Egyptian accounting and auditing standards (Wahdan *et al.*, 2005b).

However, the recent reviews of the capital market authority reveal that many listed companies have not complied with disclosure requirements, and the audit reports frequently were not in compliance with required reporting format. In the case of the violation of the financial statements of a listed company to the accounting and disclosure requirements, the capital market authority request that the company correct and redo its financial statements. If the company refuses, the capital market authority may get a third party to redo the financial statements and the cost must be paid by the company. Also, the capital market authority may cancel stock market of violators.

Despite that, the capital market authority has no authority to apply penalties for non compliance or incentives for compliance with financial reporting requirements.

The central Bank of Egypt has no mechanism for monitoring compliance with the accounting and disclosure regulations. The Banking supervision department depends on specific measures to enforce the accounting and reporting requirements. In addition, the external banking supervision department reports any violations of established standards, rules, regulations, and laws, but the central bank does not impose any effective penalties on auditors who fail to comply with the requirements (Wahdan *et al.*, 2005b).

In Egypt, auditors' performance is self-regulated as they issue their audit report without any quality assurance check by another reviewer, whether inside the auditing firm or outside the firm. Therefore the audit firms lack the incentives to implement appropriate quality controls (Wahdan *et al.*, 2005b).

Although shareholders have the authority to appoint, remove, and set the auditors, practically the company top management controls these decisions. Therefore, there is a considerable pressure on auditors to meet the wishes of the top management which may affect the independence of the auditors in performing their tasks and responsibilities of the auditing process (Wahdan *et al.*, 2005b).

2.10 AUDITING STANDARDS IN PRACTICE

Auditors in Egypt are following the six auditing Egyptian standards in the presentation and format of the auditors report, and any other international standard of auditing that relate to other aspects of auditing. Due to the difficulty of accessing the practice manuals, knowledge deficiencies constrain the degree of compliance, with applicable auditing standards varies among large and small firms, as large firms have greater capability to provide quality services (Wahdan *et al.*, 2005b).

The auditor report sometimes introduce a "clean bill of health" report for clients even when there are serious and material issues that should be explained in the report, but the auditor usually mention these serious and material issues in the long form report, this practice may results in distortion for the users of the audited financial statements.

2.11 CONCLUSION

Egypt is characterized by an exclusive location that is associated by a variety of economical sectors that each of them may direct the Egyptian economy towards achieving a competitive advantage over its sectors: it was concluded that there was a breakthrough that was achieved by Egypt during the 1990s by applying its economic reform program cooperated with the privatization program of the public enterprises, which may be reflected in the improvement of the economical indicators of the Egyptian economy.

As a prerequisite to completing the improvement framework, the Capital Market Law improved the performance of the Egyptian stock market that is considered to be the engine of the economy. If it continues development and updating the stock market, that could be reflected on the growth of the Egyptian economy as a whole with its different sectors.

CHAPTER THREE

LITERATURE REVIEW

3.1 INTRODUCTION

The auditing expectation gap is an important terminology that affects the quality of the decision-making process as the corporate annual reports are considered to be the main basis for many users to make different decisions. It is important that such reports meet the users' expectations in their decision making process. Many studies in different countries investigated the existence of the auditing expectation gap and recommended one or more theoretical approaches that would help to reduce this gap.

The current chapter critically evaluates the prior studies that examined the existence of the auditing expectations gap and the appropriate methods to reduce this gap. These approaches can be summarized in to three methods. First, the expansion of the audit report by using the long-form instead of the short-form audit report. Second, is increasing the degree of education of the annual reports' users in terms of the auditing process and the auditors' responsibilities. Third, is setting auditing standards that expands the auditors' functions and responsibilities to satisfy the needs and expectations annual reports' users.

The majority of previous studies suggested the above approaches without any empirical investigation for the effectiveness of such methods. One of the main objectives of the current study is to empirically measure the effectiveness of these approaches in reducing the auditing expectation gap and to examine the potential impact of the audited voluntary disclosure in reducing such gap in the Egyptian context.

This chapter is divided into four main parts: First, defining the auditing expectation gap. Second part is reviewing the previous studies which examined the existence of the gap in the developed countries. Third section is reviewing the prior studies which investigated the existence of the gap in developing countries. Final part is showing the different methods of reducing this gap.

3.2 AUDITING EXPECTATIONS GAP DEFINISIONS

Liggio (1974) is the first to define the expectation gap as the difference between the actual and the expected performance. This definition is extended by the Cohen commission (Commission on auditors responsibilities, 1978) where the expectation gap is represented by the gap between the public expectations and needs, and the expected accomplishment of the auditors. Moreover, the expectation gap could be defined as 'the difference between what the public and financial statement users believe auditors are responsible for and what auditors themselves believe their responsibilities are' (AICPA, 1992).

Monroe and Woodliff (1993) defined the expectation gap as the difference between the beliefs of auditors and those of the public concerning the auditors' responsibilities and duties. Jennings *et al.* (1993) argued that the expectation gap represents the difference between the public expectations about the responsibilities and duties of the auditing profession and what the auditing profession actually provides.

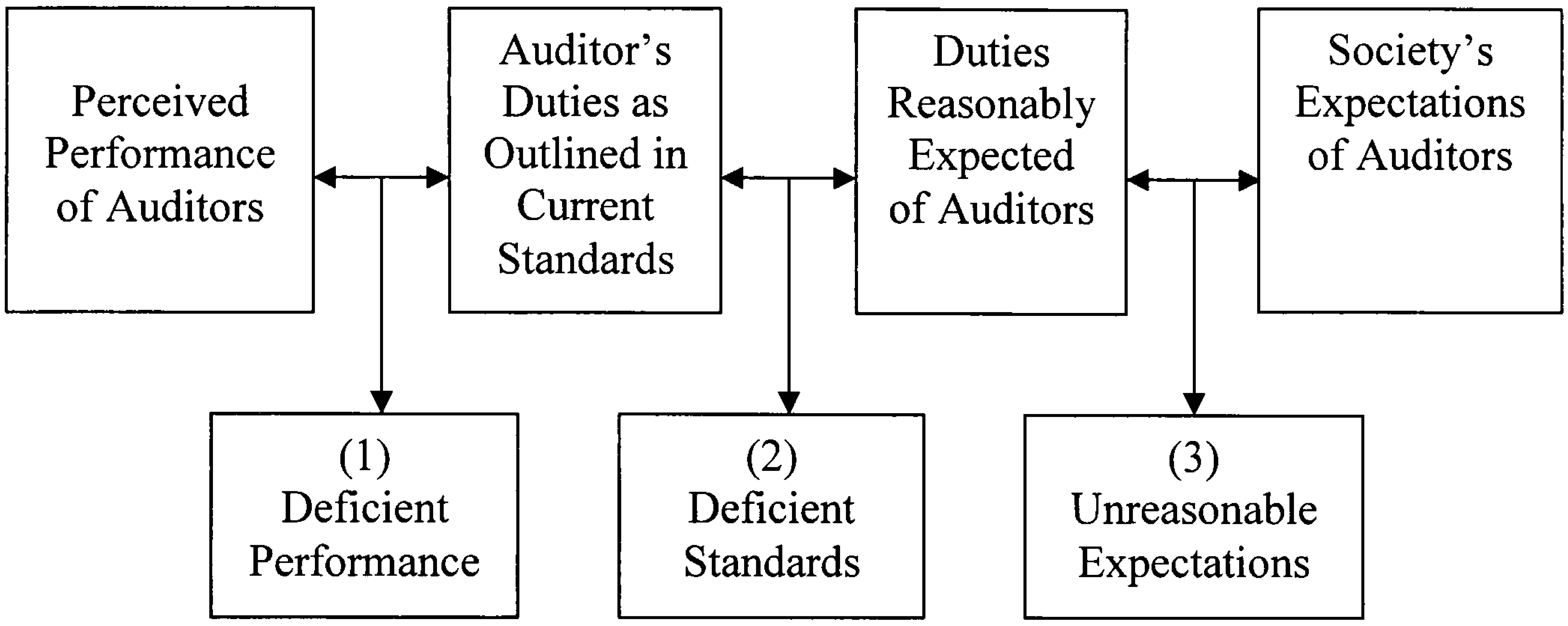
Porter (1993) defined the expectation – performance gap as the gap between the expectations of the society about the auditors, and the performance of the auditors. In addition, Porter identified that the expectation - performance gap is composed of two main components. First, the reasonableness gap which represents the gap between the society's expectations about the achievements of the auditors, and the reasonably expected accomplishment of the auditors. Second, the performance gap which represents the gap between the reasonably society's expected accomplishment of the auditor's, and the perceived achievement of the auditors.

Moreover, Porter (1993) subdivided the performance gap into two gaps. First, the deficient gap, which is the gap between the reasonably auditors expected duties, and the existing auditors' duties that are identified by the law and professional promulgation. Second, the deficient performance, which is the gap between the expected auditors' performance standard of the existing duties, and auditors' performance as expected and perceived by society.

Moreover, the auditing expectation gap has three main components (Thomas *et al.*, 2004). First, the deficit performance gap which shows the difference between the actual performance of the auditor and the proposed performance as outlined by the Generally Accepted Auditing Standards (GAAS) and quality control standards. Second, the deficit standards gap which shows the difference between the settled standards and the public reasonable requests from the auditor. Third, the unreasonable expectation which represents the unrealistic and not necessarily public's expectations regarding the auditor's performance.

Figure 3.1

The Nature of the Auditing Expectations Gap



Source: C. William (Bill) Thomas, Juan Alejandro JR, and Marchall K. Pitman (2004) 'The audit expectation gap of the 21st Century' *Today's CPA,* July/August 2004.

Tricker (1982) defined the expectation gap as 'the result of a natural time lag in the auditing profession identifying and responding to continually evolving and expanding public expectations'. However, Epstein and Geigere (1994) defined the expectation gap as the difference between the public expectations from the accounting profession and the actual performance of the accounting profession, and that is due to the public failure to know about the nature and limitations of an audit.

On the other hand, Humphrey (1997) defined the expectation gap as 'a representation of the feeling that auditors are performing in a manner at variance with the beliefs and desires of those for whose benefit the audit is carried out'. He also identified that the expectation gap could be defined more narrowly as a "role – perception gap" which represents that users expectations are capable of comparison with a predetermined notion the reasonably expected from the auditors to provide. As a result this leads to the "ignorance gap" that the expectation gap could be narrowed or even closed by the users' education.

In addition, other researchers identified that the expectation gap exists when there are different beliefs hold by the auditors and the public related to the auditor's duties and responsibilities and the messages conveyed by audit reports (Wollf *et al.*, 1999; Koh and Woo, 1998; Frank *et al.*, 2001). Moreover, according to Godsell (1992) the expectation gap exists when 'there is a widespread belief that a person who has any interest in a company (shareholders, potential investors, take-over bidders, creditors, etc.) should be able to rely on its audited accounts as a guarantee of its solvency, propriety and business viability. Hence, if it transpires, without any warning that the company is in serious financial difficulty, it is widely felt that somebody should be made accountable for these financial disasters, and this somebody is always perceived to be the auditors'. While Innes *et al.* (1997) defined the expectation gap from the auditors' and users' perspectives as the gap between the normative view (what the auditors should do) and the positive view (what auditors are actually doing), while Wolf *et al.* (1999) defined the expectation gap as the difference between the desires of the public from the auditors and the understood role of the auditors to be encompassed.

Moreover, Shaikh and Talha (2003) defined the expectation gap as 'the gap between society's expectations of auditor and auditor's performance as perceived by society', and they mentioned that the causes of this gap might be due to that the auditing is characterized by being probabilistic, the misunderstanding and unreasonable expectations of the non-auditors about the audit function, the unavailability of the evaluation of the audit performance depending on the data and the information after the audit completion, the time lags in responding to the changing expectations due to the development of the audit responsibilities, the new expectations and accountability requirements due to the corporate crises, and the professions efforts to control and maintain the expectation gap.

Regarding the reasons of the existence of the auditing expectation – performance gap, Sweeney (1997) classified the issues that results in the expectation gap into seven classes are: going concern, fraud and illegal acts, and warning of impending collapse, accuracy, management performance, independence, and duty of care, while Monroe and Woodliff (1993) classified these issues into only three classes are: auditor's responsibilities, reliability of the audited financial statements, and prospects of the audited entity. Finally, Best *et al.* (2001) agreed with Schelluch (1996) that the reasons of the existence of the expectation gap may be related to the areas of the responsibilities, and reliability and decision usefulness of audited financial statements.

3.3 EXAMINING THE EXISTENCE OF THE AUDITING EXPECTATIONS GAP

There are many studies that examined the existence of the auditing expectation gap in developed and developing countries. These studies are shown below.

3.3.1 Developed Countries

Gay *et al.* (1998) investigated the existence of the audit expectation gap in Australia by using a seven-point Likert scale questionnaire that is distributed over a sample of 581 Australian auditors selected randomly from members of the institute of chartered accountants in Australia, 304 company secretaries / accountants randomly selected from Australian business monthly top 500 business entities as well as the top 110 finance companies/entities, and 495 shareholders. But before distributing the questionnaires, a pilot study was applied by 200 auditors. The questionnaire measure the perceptions of the different categories of the sample regarding auditor responsibilities, financial statements reliability, and the decision usefulness of financial statements which are the same variables used by Schelluch (1996).

The study used the Mann-Whitney U-tests to calculate the significant differences in responses perceptions, the results of the test indicated the existence of high level of perception significant differences of the three groups of the sample, which is considered to be evidence to the existence of the auditing expectation gap in Australia. However, the study has not added any contribution to the work of Schelluch (1996) in proving the existence of the auditing expectation gap using the same variables; even the study has not recommended any proposed approaches that may cause the reduction of this auditing expectation gap in Australia.

Frank *et al.* (2001) examined the existence of the auditing expectation gap in the USA by distributing a questionnaire that is designed on a 10-point scale to a sample of 100 auditors, a sample of 100 prospective jurors, and a sample of 100 accounting students.

The distributed questionnaires aim to identify the significant differences of the perceptions of the 3 samples regarding the audit knowledge, the auditor's role, and the general attitudes toward the profession. The study used Kruskal-Wallis parametric test to examine the mean differences between the three groups of the samples, the test shows significant differences between the perceptions of the three samples regarding the three independent variables which indicates the existence of the expectation gap in the USA. The study examined the existence of the auditing expectation gap without any evidence showing how wide this gap or the effective approaches (if any) that could reduce this gap in the USA.

Gowthrope and Porter (1999) examined the existence of the auditing expectation - performance gap in New Zealand compared to the auditing expectation – performance gap in the United Kingdom in 1999 (cross sectional study), compared to the auditing expectation – performance gap in New Zealand in 1989 (longitudinal study). The study concentrates on 3 main variables; the structure, the composition, and extend of the auditing – performance gap. The study is applied using questionnaire that was mailed to 1610 selected members of four groups; auditors, auditees, and audit beneficiaries from inside, and from outside, the financial community in the UK, and 1534 members of the same groups in New Zealand. The study found that there is a wide auditing expectation – performance gap in the United Kingdom and New Zealand. However, the study has recommended different solutions to narrow this gap but without examining any of these solutions, and which solution is more effective in the United Kingdom, and in New Zealand, as the results would be different in between the two countries depending on the cultural differences of both of them.

McEnroe and Martens (2001) supported their study in (1992) by examining the existence of the auditing expectation gap in the United States by distributing a questionnaire composed of two groups of respondents; 500 audit partners from the 66 largest public accounting firms in revenue, their response rate was 23.4 %, and 500 investors from the American Association of Individual Investors with response rate of 86%. The questionnaire is designed to investigate the auditing expectation gap based on different dimensions: oversight responsibilities, the economic viability of the entity, and fraud. The results of the study are derived using a two-tailed t-test, F-test and the wave technique.

The study depends only on investigating the existence of the auditing expectation gap and recommending that the public education would reduce the auditing expectation gap. These results are driven but examining how valid and effective applying this solution would be regardless of whether or not there may be other solutions that can reduce this gap more effectively than education. Moreover, the sample is limited to only two groups (one of them is the preparer of the auditing report) regardless the other users which affects the ability to generalize the results of the study over the perceptions of the other users.

Humphrey *et al.* (1993) investigated the existence of the auditing expectation gap in the United Kingdom. The study used the questionnaire technique to gather the data from the different groups of respondents; accountants in public practice, corporate finance directors, investment analysis, bank leading officers, and financial journalists. The examination of the auditing expectation gap is examined regarding the role of the auditor, the prohibitions and regulations placed on audit firms, and the decisions auditors expected to make.

However, the study used a simple regression to identify the significant differences between the different groups of respondents towards the independent variables of the study. The results of the study indicated that there are wide significant differences between the different respondents which lead to concluding the existence of the auditing expectation gap in the United Kingdom. The study has not applied a robust test, which means that the results of the study could be defective. Also the study has not recommended or examined the effectiveness of the different methods that could solve the problem, as the study addressed the problem and offered the evidence of its existence without solving it.

The previous studies are summarized in table 3.1 as follows:

Table 3.1

Examining Auditing Expectations Gap in the Developed Countries

Author (s)& Date	Independent Variable(s)	Dependent variable(s)	Sample Size	Analysis & General Results
Gay *et al.* (1998)	Auditor responsibilities, financial statements reliability, and the decision usefulness of financial statements.	Auditing expectation gap.	581 Australian auditors, 304 company secretaries / accountants, and 495 shareholders.	Analysis Mann-Whitney U-tests. Results The existence of the auditing expectation gap in Australia.
Frank *et al.* (2001)	The audit knowledge, the auditor's role, and the general attitudes toward the profession.	Auditing expectation gap.	100 auditors, 100 prospective jurors, 100 accounting students.	Analysis Kruskal-Wallis parametric Results The existence of the auditing expectation gap in the USA.
Gowthrope and Porter (1999).	The structure, and composition, and the extent of the auditing – performance gap.	Auditing expectation gap.	Mailed to 1610 selected members of four groups; auditors, auditees, and audit beneficiaries from inside, and from outside, the financial community in the UK, and 1534 members of the same groups in New Zealand.	Analysis Mann-Whitney U-tests. Results The existence of the auditing expectation gap in the United Kingdom and New Zealand.

Author (s)& Date	Independent Variable(s)	Dependent variable(s)	Sample Size	Analysis & General Results
McEnroe and Martens (2001).	Oversight responsibilities, the economic viability of the entity, and fraud.	Auditing expectation gap.	500 audit partners from the 66 largest public accounting firms in revenue, and 500 investors from the American Association of Individual Investors.	Analysis 1- Two-tailed t-test. 2- F-test. 3- Wave technique. Results The existence of the auditing expectation gap in the United States of America.
Humphrey *et al.* (1993).	The role of the auditor, the prohibitions and regulations placed on audit firms, and the decisions auditors expected to make.	The Auditing expectation gap.	Accountants in public practice, corporate finance directors, investment analysis, bank leading officers, and financial journalists.	Analysis Simple regression analysis. Results The existence of the auditing expectation gap in the United Kingdom.

3.3.2 Developing Countries

Fadzly and Ahmad (2004) investigated the existence of the auditing expectation gap in Malaysia based on the work of Monroe and Woodliff (1993), when examining the effect of education on reducing the expectation gap in Australia. They used survey questionnaires which is comprised of two parts; the first part of the questionnaire is to examine the existence of the audit expectation gap, while the second part is related to the effect of the reading materials (in the form of brochures) on the respondent's expectations by applying the post-test method as having two groups: treatment groups (with brochure) and control groups (without brochure). In both parts of the questionnaire, it was based on the instruments used by Best *et al.* (2001) and Schelluch (1996) in investigating the expectation gap in Singapore, as the questionnaire is designed that the respondents would make their responses on a seven point bipolar Likert scale. The questionnaire of Fadzly and Ahmad (2004) concentrates on three main areas: responsibility, reliability, and decision usefulness.

Moreover, the questionnaire was distributed among a sample of 1300 individuals consists of 300 auditors and the major users of the financial statements: 300 bankers, 400 investors (including 100 as experimental), and 300 stockbrokers. However, the responded questionnaires were 398, which results in a response rate of 30.6 %. The study concluded that a wide gap was found regarding the auditor's responsibilities toward fraud detection and prevention, preparation of financial statements, and internal control, in addition to the auditor's scope gap of legal responsibility and culpability in fraud related business failure. Regarding this study, it may suffer from the limitation of generalizing its results due to the dependency on a convenience sampling to obtain the investor's sample in experimental and non-experimental procedures. Besides, using the post-test method instead of the pre-test-post-test method which may eliminates the strength of the study results.

Koh, and Woo (2001) examined the existence of the auditing expectation gap in Singapore between auditors and managers, the study identified five determinants that may exists this gap; the auditing knowledge, the years of working experience, the management position in the organization, and the functional area. The study is based on the questionnaires that are designed on a seven-point Likert scale and distributed over a randomly selected sample of 500 auditors in the big 6 auditing firms in Singapore, and 500 managers of the top 1000 companies in Singapore.

The statistical analysis of the study is divided into two parts; the first part examining the existence of the auditing expectation gap between the auditors and managers is done by applying the Logit analysis. The second part of the statistical analysis is aiming to test the relationship of the existing auditing expectation gap and its determinants by applying *n*-way ANOVA besides the Duncan multiple comparisons to study the differences in expectations between the auditors and managers over the determinants of the auditing expectation gap. The study offered evidence of the existence of the auditing expectation gap between the managers and auditors in Singapore, therefore the study is limited to one category of users which restricts the ability of the results to be generalized over the expectations of the other categories of the financial reports in Singapore, therefore the results lost its generalization power over other users or other geographic places.

The study of Best *et al.* (2001) applied on Singapore used a research methodology identical to the study used by Schelluch (1996) in developing an instrument that measure the messages communicated by the short form report audit report in Singapore, without comparing it to the effect of the long form report to show the effectiveness of the long form audit report in reducing the audit expectation gap. The sample consists of 300 subjects distributed equally over three groups of respondents; auditors, bankers, and investors (whom represented by general public 30 subjects, financial analysts 35 subjects, and brokers 35 subjects). The sample is characterized by being small as to be well representative of the whole population of the three selected categories of respondents.

Best *et al.* (2001) used the same methodology of Schelluch (1996) to measure the expectation gap by examining the message that is communicated to the users by using the short – form audit report in Singapore. The study examined the expectation gap using a seven point Likert scale questionnaire that was introduced to three main categories; auditors, bankers and investors with different levels of experience and accounting knowledge in order to measure three different factors; responsibility, reliability, and decision usefulness. The significant differences between the different categories of respondents are tested using the Mann-Whitney *U*-test besides using the Kolmogorov-Smirnov test to examine the normality of distribution of the collected data.

The results that are achieved by Best *et al.* (2001) indicated that there is a quite wide audit expectation gap in Singapore, but the study's results have not offered an evidence about the effectiveness of using the long form audit report instead of the short form audit report, which is considered one of the objectives of the study that has not been achieved by its results. However, using Best *et al.* (2001) the same methodology of Schelluch (1996) may not be acceptable as the two studies are applied on two different countries, Singapore and Australia, so the cultural differences between the two countries may affect the results of the study which is considered one of the important limitations that the study suffers from.

Dixon *et al.* (2006) investigated the existence of the auditing expectation gap in Egypt using the research methodology used by Schelluch (1996), Best *et al.* (2001), and Fadzly and Ahmad (2004) to measure the message communicated by the audit report form. This study concentrates on the same independent variables, responsibility, reliability, and decision usefulness, to examine the existence of audit expectation gap in Egypt. The questionnaire is distributed over a sample of the same three categories of respondents used by Best *et al.* (2001), auditors, bankers, and investors, with a sample size of 300 respondents distributed equally to the three categories.

Based on the existence of the significance differences between the mean test scores of the auditors from one side, bankers, and investors from the other sides, it indicates the existence of a wide expectation gap in Egypt without examining the effectiveness of any of the existence approaches that may reduce the audit expectation gap in Egypt, or recommending a proposed approach that may be the root of the audit expectation gap in Egypt and at the same time could be the solution for reducing this existing audit expectation gap. Moreover, the results are identically driven as with Fadzly and Ahmad (2004), Best *et al.* (2001) using the same tests. In addition the same limitation that affects their studies concerning the limited sample size (300 respondents).

Besides that, the study suffers from the limited ability to generalize the results due to the cultural differences that exists between Egypt, Malaysia, and Singapore.

Chowdhury, and Innes (1998) applied an exploratory study to identify whether or not an auditing expectation gap exists in the public sector of Bangladesh. The study is a qualitative research as it is depending on a semi-structured interview (face-to-face interview). The exploratory nature of the study made it only limited to identifying the existence of the audit expectation gap, but extents the study to investigate the causes of this auditing expectation gap. The sample used in this research is composed of 17 Comptrollers and Auditor Generals (CAG), 15 members of the Public Accounts Committee (PAC) of parliament, and nine senior representatives from the five International Funding Agencies (IFA). It examines the effect of the auditor accountability, auditor independence, auditor competence, auditor materiality and audit evidence, true and fair, and performance audit as independent variables on the audit expectation gap.

The study shows significant differences in the perceptions of the different categories of the study sample which indicates the existence of auditing expectation gap in Bangladesh. The study goes further and illustrated the reasons of the expectation gap in the public and the private sectors of Bangladesh; regarding the private sector, the study depends on the previous literature to identify that the causes of auditing expectation gap are related to the fraud detection, true and fair view, auditor independence, the relationship between auditors and users. On the other side, regarding the public sector, the auditing expectation gap may results from the independency from ministry, absence of formal communication, the scope of performance audit, the format and contents of report, auditors' competence, objectives of audited entities, and timeliness of reporting. However, this study can be criticized because it concentrates on the investigation of the auditing expectation gap in the public sector then generalizes the results about the existence of the auditing expectation gap in this sector on the private sector, depending on qualitative analysis on a sample of public sector respondents which is considered to be a restriction. Moreover, the study depends on the semi-structured interviews without any quantitative research assisted by statistical analysis to support this qualitative analysis that may lead to some biased results. Finally, the study suffers from the relatively small number of respondents which also affects the ability of the generalization of the results of the study.

To overcome the previous limitations, Chowdhury *et al.* (2005) applied the same study of Chowdhury and Innes (1998), but extended it to include, beside the applied qualitative analysis in the form of semi-structured interviews, a quantitative analysis by distributing over the same sample a questionnaire of different questions about the dimensions of audit concepts tested before using the semi-structured interview. The questionnaire is designed based on seven-point Likert scale, and is analyzed using the Mann-Whitney U-test which is a non-parametric test equivalent to the *t*-test to fit with the ordinal measurements as to be able to use the ranks. The results of the current study support the results of the previous studies concerning the existence of the expectation gap in Bangladesh. In spite that this study overcame the limitation of the previous studies concerning applying a quantitative analysis to support the results of the qualitative analysis the problems are generalizing the results of the existence of the audit expectation gap in the public sector over the private sector without applying any examination of this sector, besides the relatively small number of respondents as mentioned in the limitations of the previous study.

Siddiqui, and Nasreen (2004) examined the existence of auditing expectation gap in Bangladesh b y concentrating on three independent variables; audit responsibility, audit reliability, decision usefulness of audited financial statements, and these variables are similar to the independent variables of the studies of Schelluch (1996), Best *et al.* (2001), and Fadzly and Ahmad (2004). The study is applied using the questionnaire approach which is constructed on the base of a seven point Likert scale. This questionnaire is distributed over a sample of 100 undergraduate students in the department of Accounting & Information systems, university of Dhaka, who completed a course in auditing and they represents only the academic view, while 115 former students of the same department who qualified as charted accountants and working in different companies as accountants or internal auditors represent both the academic and professional views.

The results of the study, built on using the F-test and the t-test to identify the significant differences between the two categories of the collected sample, indicated the existence of wide auditing expectation gap in Bangladesh in terms of the tested three independent variables, However, this study suffers from the relatively small sample, and the limited categories tested as the users diversify in their education, knowledge, and experience, but this diversification was not taken in consideration in this study which limits the generalization power of the results over the diversified users.

Lin and Chen (2004) investigated the existence of the auditing expectation gap in China with respect to audit objectives, auditor's obligation to detect and report fraud, auditor independence, and third party liability of auditors. The investigation is applied using a questionnaire that is based on a 5-point Likert scale and distributed over a sample of audit beneficiaries as: investors, creditors, government officials, business management, and academics from one side, and the public practitioners in China from the other side.

There are 800 questionnaire distributed over the two groups of the sample, 300 questionnaires were sent to external user-groups of financial analysts from investment institutions, credit and loan officers at commercial banks, and government officials in charge of business financing and accounting at various government authorities. Another 300 questionnaires were sent to business management subjects in State Owned Enterprises (SOEs) and Public Listed Companies (PLCs) randomly selected from the China industrial enterprises and the China listed companies' reports respectively, with mail questionnaires sent to the general managers or controllers (or chief accountants) in the sample enterprises. A total of 120 questionnaires were mailed to practicing public accountants at the accounting/auditing firms listed in the China securities yearbook. Finally, 80 questionnaires sent to educators engaged in auditing teaching and research at the universities across the country.

The study applied a Mann-Whitney ranked test to compare the mean of the responded questionnaires, besides using the *t*-test to examine the significant differences between the different categories of the sample. Based on the previous analysis of the sample, the study offered an evidence of the existence of the auditing expectation gap in

China. However, this study is suffering from an important limitation which is that the members of the auditing firms were originally certificate public auditors who were mainly staff of the state audit bureaux, therefore their perceptions would be biased towards the government and would be similar to the perception of the government respondents, and so do not show any significant difference than their perceptions due to the bias toward the government. Moreover, in spite of the diversification of the categories of the sample, there is a low response rate of 24.8% which may affect the generalization of the results of the study over the whole population.

Desira and Baldacchino (2005) examined the existence of the auditing expectation gap in Malta based on the methodology used by Schelluch (1996), Best *et al.* (2001), and Fadzly and Ahmad (2004) to measure the significant differences between the different categories of the study sample regarding the auditor responsibility, the reliability of the audited financial statements and usefulness of financial statements to examine the existence of the auditing expectation gap in Malta.

The study used the questionnaire technique which is distributed over a sample of 100 potential jurors with the exemption of members of parliament, police and armed forces, and any person falling within the exempted categories was disregarded during the sample creation stage. Another 100 questionnaires were distributed over warranted Maltese auditors. The results are driven by applying the Chi–squared test to illustrate the significant differences between the two groups of samples, besides performing the Mann-Whitney U-test to check for the statistical differences between the same groups of samples. The previous tests show that there is significant difference in the perceptions of the two groups, which means the existence of the auditing expectation gap in Malta. Although, this study is criticized by applying the same methodology of Fadzly and Ahmad (2004) in Malaysia on the context of Malta which may result in misleading results due to the different cultures between Malaysia and Malta. Moreover, the study is characterized by having a very low response rate of the jurors sample (18%) compared to a high respond rate of the auditors sample (56%) which may affect the consistency of the samples and so affects the accuracy of the driven results.

Concerning Saudi Arabia, Hudaib and Haniffa (2003) investigated the existence of the expectation gap by collecting data in three different stages. The first stage is applying pilot semi-structured interviews with a number of auditors, credit mangers, financial analyst, shareholders, financial directors and governmental body representatives. The second stage is applying mail questionnaires to 350 subjects comprising large auditors, small auditors, financial directors, credit managers, investment analysts and funds managers, substantial shareholders, other shareholders, and governmental bodies. The final stage is applying depth face-to-face interviews with 48 selected respondents representing the previously mentioned eight groups.

However, the designed questionnaires are similar to those used by Porter (1993) and Humphrey *et al.* (1993). The study concentrates on the relation of the auditors' role, and the audit environment, with the auditing expectation gap. This relation is concluded by applying the Kruskal-Wallis one-way analysis of variance by ranks as a non-parametric test using the SPSS package. The results indicate the existence of the expectation gap in Saudi Arabia. The results of the study could not be reliable as they are built on the same questionnaire that is applied by Porter (1993) in New Zealand,

and Humphrey (1993) in the United Kingdom. Therefore, there may be some cultural differences that may affects the results and reduce its validity as when applying the questionnaire on different culture it needs a sort of adaptation to fit with the culture it is applied on. From the other side, the study offered the evidence of the existence of the expectation gap in the Saudi Arabia without examining the effective solution (if any) that would fits with the Saudi Arabia culture.

In addition, Al-Twaijry (2006) examined the existence of the auditing expectation gap in Saudi Arabia by applying a qualitative analysis using the face-to-face interviews. The study is applied on a sample of 100 companies selected from the largest 1000 Saudi Arabia companies. The sample is composed of academic staff, directors of internal audit departments, external auditors, governmental, accounting and internal auditing bodies.

Based on the applied interviews with the different categories of the sample, it was concluded that the auditing expectation gap in Saudi Arabia is composed of five categories: the gap between what corporate management expects external auditors to do when performing the independent audit and what their real task is, the gap between how corporate management should appreciate its internal auditing and how management recognizes the internal auditing in reality, the gap between what auditees expect corporate auditors searching for when doing their duties and what the internal auditors real job is, the gap between what the business sector required in internal auditors (qualification and experience) and what internal auditors real qualifications and background are, and the gap between the scope of internal auditing as expected by the professional standards (SPPIA) and what the internal auditors are really doing.

The study depends only on the qualitative analysis to evidence the existence of the auditing expectation gap and that may have some disadvantages such as the biased perceptions of the interviewers while running the interview or analyzing the data. Moreover, the study has not recommended the solutions to reduce the gap and which of these solutions would be more effective and fits with the environment of the Saudi Arabia.

The previous studies are summarized in table 3.2 as follows:

Table 3.2

Examining Auditing Expectations Gap in the Developing Countries

Author (s) & Date	Independent Variable(s)	Dependent Variable(s)	Sample Size	Analysis & Results
Fadzly and Ahmad (2004).	Responsibility, reliability, and decision usefulness	Auditing expectation gap.	300 auditor, 300 bankers, 400 investor (including 100 as experimental), and 300 stockbroker.	Analysis Mann-Whitney U-test. Results A wide gap regarding the auditor's responsibilities toward fraud detection and prevention, preparation of financial statements, and internal control, auditor's scope gap of legal responsibility and culpability in fraud related business failure.
Koh and Woo (2001).	The auditing knowledge, the years of working experience, the management position in the organization, and the functional area.	Auditing expectation gap.	500 auditors in the big 6 auditing firms in Singapore, and 500 managers of the top 1000 companies in Singapore.	Analysis 1. Logit analysis. 2. n-way ANOVA. Results The existence auditing expectation gap between the managers and auditors in Singapore.
Best *et al.* (2001).	Responsibility, reliability, and decision usefulness	Auditing expectation gap.	300 subjects distributed equally over three groups of respondents; auditors, bankers, and investors.	Analysis 1. Mann-Whitney U-test. 2. Kolmogorov-Smirnov test. Results Existence of audit expectation gap in Singapore.

Author (s) & Date	Independent Variable(s)	Dependent Variable(s)	Sample Size	Analysis & Results
Dixon *et al.* (2006).	Responsibility, reliability, and decision usefulness.	Auditing expectation gap.	100 auditors, 100 bankers, and 100 investors.	<u>Analysis</u> Mann-Whitney *U*-test. <u>Results</u> The existence of wide auditing expectation gap in Egypt.
Chowdhury and Innes (1998).	Auditor accountability, auditor independence, auditor competence, auditor materiality and audit evidence, true and fair, and performance audit	Auditing expectation gap.	17 Comptroller and Auditor General, 15 members of the Public Accounts Committee of parliament, and 9 senior representatives from the five International Funding Agencies.	<u>Analysis</u> Exploratory study. <u>Results</u> Existence of auditing expectation gap in Bangladesh.
Chowdhury *et al.* (2005).	Auditor accountability, auditor independence, auditor competence, auditor materiality and audit evidence, true and fair, and performance audit	Auditing expectation gap.	17 Comptroller and Auditor General, 15 members of the Public Accounts Committee of parliament, and 9 senior representatives from the five International Funding Agencies.	<u>Analysis</u> 1. Mann-Whitney U-test. 2. t-test. <u>Results</u> Existence of auditing expectation gap in Bangladesh.

Author (s) & Date	Independent Variable(s)	Dependent Variable(s)	Sample Size	Analysis & Results
Siddiqui and Nasreen (2004).	Audit responsibility, audit reliability, decision usefulness of financial statements.	Auditing expectation gap.	100 undergraduate student, and 115 charted accountants.	Analysis 1. F-test. 2. t-test. Results Existence of wide auditing expectation gap in Bangladesh.
Lin and Chen (2004).	Audit objectives, auditor's obligation to detect and report fraud, auditor independence, and third party liability of auditors.	Auditing expectation gap.	300 external user-groups of financial analysts (investment institutions, credit and loan officers at commercial banks, and government officials), 300 business management subjects (SOEs) and (PLCs), 120 public accountants, and 80 educators.	Analysis 1. Mann-Whitney test. 2. t-test. Results Existence of the auditing expectation gap in China.
Desira and Baldacchino (2005).	Auditor responsibility, the reliability of the audited financial statements, decision usefulness of financial statements.	Auditing expectation gap.	100 potential Jurors, and 100 warranted Maltese auditors.	Analysis 1. Chi – squared test. 2. Mann-Whitney U-test. Results Existence of the auditing expectation gap in Malta.

Author (s) & Date	Independent Variable(s)	Dependent Variable(s)	Sample Size	Analysis & Results
Hudaib and Haniffa (2003).	Auditor's role and the audit environment.	Auditing expectation gap.	Depth face-to-face interviews with 48 and mail questionnaires to 350 large auditors, small auditors, financial directors, credit managers, investment analysts and funds managers, substantial shareholders, other shareholders, and governmental bodies.	Analysis Kruskal-Wallis one-way analysis of variance by ranks. Results Existence of the auditing expectation gap in Saudi Arabia.
Al-Twaijry (2006).	None.	None.	100 companies selected from the largest 1000 Saudi companies, the sample is composed of academic staff, directors of internal audit departments, external auditors, governmental, accounting and internal auditing bodies.	Analysis Face-to-face interviews. Results Existence of the auditing expectation gap in Saudi Arabia.

3.4 THE ROLE OF THE AUDIT REPORT FORM IN REDUCING THE AUDITING EXPECTATIONS GAP

The auditing report has passed over different decades of changes and improvements as to improve the communicated messages that are sent by the reports to the users of the annual reports. The audit report has been changed from 1948 to 1988, as there was a concern that users might not be correctly interpreting the auditors' intended messages.

Therefore, in 1978, the commission on auditors' responsibilities known as the Cohen Commission, identified several possible deficiencies in the auditors' report and suggested the use of standardized language may have made the report a symbol which was not carefully read, considered and fully understood by users. Moreover, the Cohen Commission suggested that the auditors' report should be revised as to ensure that it describes the role and responsibilities of the auditor. Therefore, the audit report needs to be corrected by applying the standard audit report (Boyd *et al.*, 2001).

After a while, exactly January 1, 1989, a new audit report was introduced, as the traditional two paragraph report was expanded to three paragraphs that explains the nature of an audit, the differences between this report and the old one are the title and in the introductory, scope and opinion paragraphs of the report. Moreover, the new report labeled as the "Independent Auditor's Report" (Boyd *et al.*, 2001).

Post to 1989, there was introductory paragraph that extracted from the scope paragraph of the old report. This introductory paragraph of the new report includes entity audited, the financial statements presented, and the time period of the financial statements. Also, the word 'examined' was replaced by the word 'audited' in the audit report, and two sentences were added to the introductory paragraph identifying the responsibilities of both management and the auditor (Boyd *et al.*, 2001).

In addition, there were other modifications that are applied to the scope paragraph of the old report, as it includes that the examination was made in accordance with GAAS, and that the auditor performed the necessary tests in the circumstances. This sentence has been deleted by the new report and instead of it a new paragraph is presented including new five phrases which are newly added to the auditor's standard report (Boyd *et al.*, 2001).

However, the new report has eliminated the phrase "presents fairly" and exchanged it with the phrase "in all materials respects" indicating that the materiality concept was used by both the management in the preparation of financial statements, and the auditors in the audit of financial statements. Furthermore, SAS No. 58 revised the reporting standards of GAAS to require a separate explanatory paragraph in the audit report when accounting principles have not been applied consistently. Finally, Referred to the SAS No.95, the "changes in financial position" was replaced by the statement of cash flows.

Chung (1995) conducted an experiment on two groups of auditors from the big six public accounting firms and six smaller firms in the USA. The experiment requires examining the clients account balances in six different cases. In the first case, 32 auditors were selected depending on their availability and willingness to participate in the experiment with at least two years experience. The second case, 26 auditors selected on the same selection base of the first case with average auditing experience of 4.36 years. The two groups were trained before applying the experiment. Using the inter quartile index and the surprise index to analyze the results, it was concluded that the first group of auditors showed a mixture of under-confidential and good calibration, while the second group showed a mixture of good calibration and over confidence. The aggregation of the two results shows tendency towards under-confidence.

Hatherly *et al.* (1997) investigated the existence of the auditing expectation gap in the United Kingdom, besides examining the effect of the long form audit report on the perceptions of the MBA students at the University of Edinburgh. This is done by designing a questionnaire based on a seven point Likert scale and is distributed over 500 auditors, 140 MBA students. The researchers distributed the short form audit report with the other reports to 70 students, and distributed the long form report with the other reports to the other 70 students. This questionnaire was pilot tested by 12 part-time MBA students and comments were also received from a number of academics and practicing auditors.

The questionnaire is concentrating on examining the effect of the expanded report on the perception of the sample (auditing expectation gap) concerning 14 dimension of auditing; auditors' independence, auditor's judgment, fraud, auditor accountability, extent of audit, management of company, investment / disinvestment, purpose of audit, management's representation, specific versus whole, performance monitoring, accounting standards, credibility, conflict between management and auditors, satisfaction, management / auditor responsibility, variability of company, and proper accounting records.

The study used stem and leaf plots, chi-squared goodness, and Bartlett's test of homogeneity of variances to calculate the significance levels of students' perceptions, besides using a non-parametric test which is Wilcoxon and Mann-Whitney. The results indicated a significant difference between the two groups of MBA students. This significant difference results from the different audit report forms that are distributed for each group. Therefore, the audit report form affects the perception of the readers and could be used to reduce the existing auditing expectation gap that exists between the auditors and the users in the United Kingdom.

However, the study concentrated on an academic category of users regardless the other categories of users which may have no accounting or even business backgrounds and may not react actively as the MBA students reacted. The different audit report forms caused significant differences in the perception of the students may not be evidence that it would be an effective approach to reduce the audit expectation gap. That is because the researchers have not mentioned why they have chosen this approach to reduce the auditing expectation on the expense of the other approaches. Therefore, the results could not be reliable as they may be other solution (if any) that may be more effective for the reduction process.

Best (1999) examined the effect of the long form audit report on reducing the auditing expectation gap in Singapore. The study used a research methodology identical to that which applied by Schelluch (1996) in Australia. The Likert seven-point scale questionnaire is designed to measure the messages communicated by the short-form audit report to the different users of the annual reports in Singapore. The questionnaire, a covering letter, a sample of audit report, and a prepaid envelope were sent to a randomly selected sample of 300 subjects consisting of 100 auditors, 100 bankers, and 100 investors. The response rate that was achieved was 35% for auditors, 26% for bankers, and 36% for investors.

The study measured the existence of the auditing expectation gap in Singapore and the effect of the long-form audit report using the following factors; responsibility, reliability, and decision usefulness. The results of the study were driven using the Mann Whitney-U test to examine the significant differences between the different subjects of the sample, besides using Kolmogorov-Smirnov test to examine the normality of distribution of the data. The results of the study evidence the existence of the auditing expectation gap in Singapore, and that the long-form audit report offers better understanding of the nature of the auditing function.

However, the study is limited to a small sample size of the subjects tested by the study: 300 subjects may not identify a better representation of the tested population. Furthermore, the methodology of the study is identical to that of Schelluch (1996) applied in Australia which may expose the study to the effects of the different cultural differences between Australia and Singapore. On the other hand, the study indicated that the long-form audit report would have a great impact on the understanding of the users to the nature of auditing function without offering confident evidences that supports this conclusion. Therefore, it needs further tests to evidence this issue besides examining whether this method would be more effective than other methods to reduce the expectation gap, or there may be other proposed methods that would be more effective in reducing the auditing expectation gap in Singapore.

Manson and Zaman (2000) investigated the usefulness of the new long-report audit form based on SAS 600 in aligning the views of auditors, preparers, and users. The study aims to determine to which extent the respondents are satisfied by the new form, how it is useful to include different issues, including corporate governance, in the auditors report, and whether there are any differences in the perceptions of the three groups of respondents. A questionnaire based on seven-point Likert scale is introduced to 400 auditors in big 5, top 40 (excluding big 5), 400 preparers (finance directors) of selected 200 UK companies, and 200 users including investment analysts and corporate bankers. The response rate was 41%, 30%, and 23% respectively, which results in having overall response rate of 33%.

The questionnaire focuses on the measurement of different dimensions to achieve the objectives of the study; general auditors responsibilities, the nature of auditors' work, the extent of auditors responsibilities, going concern and fraud or illegal acts, non-financial information in annual reports, Internal control and materiality, issues arising during the audit, and corporate governance.

The study used the t-test and a Mann-Whitney to drive its results. These results indicate that there are lower significant differences between the different subjects of the sample concerning the study dimensions. This indicates the usefulness of the expanded audit report form introduced by SAS 600 in understanding the audit functions and to satisfy the users' needs towards the annual reports supported by the expanded report form.

The study suffers from the limitations of the problems associated with using the questionnaire technique. The study has not compared the expanded report form introduced by SAS 600 to the old short report form. Therefore, it would not show the effectiveness of the new report over the old one. Furthermore, the study has not examined the effectiveness of this expanded report form to other different methods that may improve the perceptions of the different users towards the auditors' functions and responsibilities.

Schelluch and Gay (2006) examined the significant differences in beliefs about messages communicated by both negative and positive assurance audit reports between different subjects of auditor, users, and preparers concerning the effect of changing the wordings of the auditing report. The subjects tested include 580 auditors, 301 company secretaries/chief accountants, and 496 shareholders. The response rate of the subjects was 59%, 36%, 43% respectively. These respondents were mailed a copy of the questionnaire, a covering letter, and a prepaid return envelope. The study is concerned by the reliability statements, the responsibilities of auditors and management, and the future prospects of entity.

Furthermore, the study was using a seven-point Likert scale questionnaire which includes 15 bipolar adjectival statements. The responds of the sample subjects were analyzed using Mann-Whitney U-test to compare the different groups of respondents from one side, and between the negative and positive assurance report from the other side. The results of the study indicate that the change of the wording of the audit report may cause significant differences between the respondents concerning the different reports. This shows that the form of the audit report may change the beliefs of the users of the annual report which results in the reduction of the auditing expectation gap.

However, the study concentrated on the significant differences towards the different reports, which does not mean that the existence of different response towards the different forms of reports may be effective in reducing the auditing expectation gap. At the same time, there might be other methods to reduce the auditing expectation gap rather than using the different audit form. There must be an investigation of the effectiveness of the different methods of reducing the auditing expectation gap compared to the change in the audit report form.

Almer and Brody (2002) applied a simulated experiment to examine the effect of the rephrasing of the audit report. The examination is applied by sending the experiment materials, which consists of financial statements and a summary of financial ratios relevant to going concern judgments, profitability, leverage, liquidity, capital intensiveness, and cash position, to a sample of 14 people at six big public accounting firm locations and bankers at 13 bank locations. A total of 57 auditors' and 69 bankers' responses were received resulting in a response rate of 36% and 55% respectively. The auditors were asked to identify the status of their client, while the bankers were asked to assume that they had received annual financial statements and the related modified audit report for an existing borrower, and it was requested from both groups to provides a numeric association for 'substantial doubt' in the context of the company.

The variables that are examined in the study are two groups of variables: independent variable which is represented by the ownership structure of the company, and dependent variables which are the participants' general numeric association for 'substantial doubt' tested by ability to continue (0% probability of failure) or no ability to continue (100% probability of failure), second participants' numeric associations within the context of the tested company. Therefore, the study is based on three basic hypotheses. The first is H1. Auditors' general numeric associations for a going concern modification will be lower than bankers' general numeric associations for a going concern modification. The second is H2B. Auditors' numeric associations for a going concern modification will be higher for public companies than for private companies. The third is H2B. Bankers' numeric associations for a going concern modification will not be different for public companies and private companies.

The hypotheses of the study were tested using one-way ANOVA and the results indicated that when auditors issue a modified report, they believe that the entity has lower probability of failure than bankers believe when they receive the audit report. Therefore, the auditors' and bankers' understanding of the modified audit report were differentially affected by ownership structure as the auditors reported higher numeric associations under public ownership structure, while bankers did not. These results indicated that the modified audit report was understood in different ways due to the differences between the auditors and bankers perceptions towards the message conveyed by the same report.

Accordingly, the modified audit report has not decreased the differences of perceptions between the two types of users. Therefore, there is an existence of an auditing expectation gap, and the modified report has not been able to reduce this auditing expectation gap between the different users. Moreover, the reaction of the respondents toward an experiment could not be recognized when they are dealing with the real case. The diversification of locations of the auditors and bankers selected for the experiment might eliminate the ability to generalize the results over the auditors and bankers. Furthermore, the experiment has not included any other alternatives that might reduce the auditing expectation gap and to examine its effectiveness towards the other methods that may be able to reduce the auditing expectation gap.

The previous studies are summarized in table 3.3 as follows:

Table 3.3

The Role of Audit Report Form in Reducing the Auditing Expectations Gap

Author (s) & Date	Independent Variable(s)	Dependent Variable(s)	Sample Size	Analysis & Results
Hatherly *et al.* (1997).	Audit long form report	Auditing expectation gap (Users perception).	500 auditors, 140 MBA students. The researchers distributed the short form audit report with the other reports to 70 students, and distributed the long form report with the other reports to the other 70 students.	Analysis 1- stem and leaf plots 2- chi-squared goodness, 3- Bartlett's test of homogeneity of variance. 4- Wilcoxon-Mann-Whitney. Results 1- Existence of auditing expectation gap in the United Kingdom. 2- Audit report form could be used to reduce the existing gap.
Best (1999).	Responsibility, reliability, and decision usefulness.	The Auditing expectation gap.	300 subjects consisting of 100 auditors, 100 bankers, 100 investors.	Analysis 1- Mann Whitney-U test. 2- Kolmogorov-Smirnov. Results 1- The existence of auditing expectation gap in Singapore. 2- The usefulness of long-form audit report.

Author (s) & Date	Independent Variables	Dependent Variable	Sample Size	Analysis & Results
Manson and Zaman (2000).	General auditors responsibilities, the nature of auditors' work, the extend of auditors responsibilities, going concern and fraud or illegal acts, Non-financial information in annual report, Internal control and materiality, issues arising during the audit, and corporate governance.	Users' expectations.	400 auditors, 400 preparers (finance directors), and 200 users including investment analysts and corporate bankers.	Analysis 1- t-test. 2- Mann-Whitney test. Results The usefulness of the audit expanded form introduced by SAS 600 in understanding the audit functions and to satisfy the users needs towards the annual reports supported by the expanded report form.
Schelluch and Gay (2006).	The reliability statements, the responsibilities of auditors and management, and the future prospects of entity	The auditing expectation gap.	The subjects tested include 580 auditors, 301 company secretaries / chief accountants and 496 shareholders.	Analysis Mann-Whitney U-test. Results The change of the wording of the audit report results in the reduction of the auditing expectation gap.

Author (s) & Date	Independent Variable (s)	Dependent Variable (s)	Sample Size	Analysis & Results
Almer and Brody (2002).	Ownership structure of the company.	Participants' general numeric association for 'substantial doubt' tested by ability to continue (0% probability of failure) or no ability to continue (100% probability of failure), second participants numeric associations within the context of the tested company.	A total of 57 auditors and 69 bankers responses were received resulting in a response rate of 36% and 55% respectively.	Analysis One-way ANOVA. Results The modified audit report has not decrease the differences of the perceptions between the two types of users, therefore, there is an existence of an auditing expectation gap and the modified report has not been able to reduce this auditing expectation gap.

3.5 THE ROLE OF THE USERS EDUCATION IN REDUCING THE AUDITING EXPECTATIONS GAP

Epstein and Geiger (1993) argued that the auditing expectation gap could be narrowed partly by increasing the public understanding of the audit nature and its limitations. This means the role of educating the financial statements' users towards the auditors' functions and responsibilities. Moreover, the study recommended that the AICPA should increase the educational efforts with clients and audit committees at shareholders' meetings in professional and organizations. To ensure that the education may reduce the auditing expectation gap, the study applied a survey regarding the level of assurance the auditors should provide for detecting material misstatements as a result of error (unintentional misstatements), and as a result of fraud (intentional misstatements), over a sample of different investors who owned 100 or more shares of a stock listed on the American or New York stock exchange. The respondents obtained were 246 representing individuals from all 50 states.

The study survey found that, in general, the more educated an investor was regarding accounting, finance and investment analysis (including using the auditor's report), the less likely to require absolute auditor assurance. However, the study focused only on one category of users (investors) and did not include the other categories of the users. The study is limited to describe the data without any further parametric or non-parametric data that may give more significant results that could be generalized over the whole population of investors. Therefore, the study is characterized by being limited and having low generalization power.

Monroe and Woodliff (1993) suggested that the users' education would reduce the audit expectation gap. The study examined the effectiveness of the users' education on reducing the expectation gap. The study used a semantic differential scales regarding the auditor responsibility, the auditor reliability, and the future prospects. The study includes: 141 auditing students at the beginning of the semester, 43 marketing students at the beginning of the same semester, 74 auditors, 114 auditing students at the end of the semester, and 30 marketing students at the end of the same semester.

Moreover, the marketing students are used as a control group sample as they have no previous auditing background. The scale was filled by the students at the beginning of the semester and another time at the end of the same semester. The data is analysed at the beginning and at the end of the semester using Kruskal-Wallis one-way analysis of variance to test the differences in responses between the five reports within each subject group, besides using the Chi-Square statistics to examine the significant levels between the samples.

The results of the study showed that at the beginning of the semester there were significant differences in beliefs between auditors and both groups of students which represent the existence of the expectation gap. At the end of the semester, the students' beliefs had changed due to the perceived information about the responsibilities of the auditors, which results in reducing the auditing expectation gap.

However, the results of this study could not be generalized, as the examined sample includes students whom are not considered to be a group of the annual reports' users.

Students could be a controllable sample to accept educating which would be more difficult to do so with the users. In addition, the number of students at the beginning of the semester is different than the number of student at the end of the semester which may affect the consistency of the study and the ability to compare the results. Moreover, the study examined the effectiveness of education without comparing it to the effectiveness of the other methods that could reduce the auditing expectation gap more effectively.

Hussain (2003) argued that the solution that fits with reducing the auditing expectation gap is the education of users about auditors' functions and responsibilities. The study depends on using the same instruments of Humphrey *et al.* (1993) study of examining the expectation gap in Britain. The study used 7-point Likert scale questionnaire, and distributed over a sample of 35 students in Sultan Qaboos University (Oman) before attending the audit class and the same number of students after attending the audit class. The questionnaire is focusing on questioning about auditors and auditing process, auditors' role with respect to audited financial statements, auditors' role with respect to audited company, and auditor's responsibility to owners and creditors.

The study used the paired t-test to drive the results of the responses of the students before and after the auditing class. The results show that the perception of the students changed as a result of attending the auditing course. Therefore, the study argues that the change in the students' perceptions is due to the auditing education which reduces the expectation gap between the students and the auditors.

However, the study solved the problem of Monroe and Woodliff (1993), which is the ability to compare the results after and before the education, as in this study the number of students before the beginning of the auditing class equals the number of students after attending the auditing class, but the study depends on the students to examine the effect of education in reducing the auditing expectation gap instead of examining the effect of education on the users of the annual reports. The other problem is not comparing the effect of education in reducing the auditing expectation gap to the effect of the other solutions as to recommend the most effective method that fits with the culture of Oman.

Pierce and Kilcommins (1996) examined the availability to offer evidence that the provision of auditing courses contributed to reducing the auditing expectation gap. The study depends on the questionnaire survey which was completed by five groups of students at the beginning of the academic year and again at the end of the same academic year. The five groups include 133 business studies year one students, 112 accounting and finance year one students, 93 accounting and finance year two students, 47 accounting and finance year three students with elective course of auditing, and 43 accounting and finance year three students without elective course of auditing.

The questionnaire is designed based on a five-point Likert scale concentrating on the duties, ethical and legislative framework, liability, and audit report. The data of the questionnaires are tested using the mean scores to rank the main issues included in the questionnaires at the beginning of the semester and at the end of the same semesters. The study indicates that there are considerable benefits of education, as the results before having the auditing courses differs after having the auditing courses, which gives a signal to the importance of the education in changing the perceptions of the students towards the auditors' responsibilities. Therefore, the education is considered to be effective in reducing the auditing expectation gap.

However, the study is criticized by having the same faults of the other studies. It is depending on the students instead of the users of the financial statements whom are not controllable as much as the students to be educated. Also the analysis is depending on a mean score which is considered a descriptive analysis rather than applying other statistical test to drive the relations between the different variables of the study. Furthermore, the study has not examined the other solutions of the auditing expectation gap to compare it with the education method as to identify the most effective method that would be able to reduce the auditing expectation gap more effectively.

Gay (2002) argued that the education would be an effective method that results in reducing the auditing expectation gap. The study focused on four groups of respondents; 581 auditors randomly selected from members of the institute of Chartered Accountants in Australia, and other three groups of students, 169 second year financial accounting students at the beginning of the first semester, 143 third year auditing students at the beginning of the second semester, and 110 at the end of the same semester.

The respondents were sent a covering letter, prepaid return envelope, and a copy of the questionnaire which is built on a seven-point Likert scale measuring the effect of education on the auditing expectation gap regarding responsibility, reliability, and decision usefulness. The study results indicate that education reduces the auditing expectation gap. These results are driven by applying Mann-Whitney U tests of comparison between the groups, and between review and audit reports within each group.

However, the study focuses on a sample of students who are not users of the annual reports of the companies and would accept to be educated while the users may refuse to do so. Furthermore, the number of the students at the beginning of the study is not equal to their number at the end of it which may affect the effectiveness of the study. In addition, the study examined how effective the education in reducing the auditing expectation gap without comparing this method to the other methods of reducing the auditing expectation gap to identify the most effective method that could be used if there is any more effective method that could be used.

The previous studies are summarized in table 3.4 as follows:

Table 3.4

The Role of Users Education in Reducing the Auditing Expectations Gap

Author (s) & Date	Independent Variable(s)	Dependent Variable(s)	Sample Size	Analysis & Results
Epstein and Geiger (1993).	The level of assurance the auditors should provide for detecting material misstatements as a result of error (unintentional misstatements), and as a result of fraud (intentional misstatements).	Users Education.	Different investors who owned 100 or more shares of a stock listed on the American or New York stock exchange, the respondents obtained were 246 representing individuals from all 50 states.	Analysis Descriptive analysis. Results The more educated an investor was regarding accounting, finance and investment analysis (including using the auditor's report), the less likely to require absolute auditor assurance.
Monroe and Woodliff (1993).	Auditor responsibility, the auditor reliability, and the future prospects.	The Auditing expectation gap.	141 auditing students at the beginning of the semester, 43 marketing students at the beginning of the same semester, 74 auditors, 114 auditing students at the end of the semester, 30 marketing students at the end of the same semester.	Analysis 1-Kruskal-Wallis one-way analysis of variance. 2-Chi-Square test.

Author (s) & Date	Independent Variable(s)	Dependent Variable(s)	Sample Size	Analysis & Results
Hussain (2003).	Auditors and auditing process, auditors' role with respect to audited financial statements, auditors' role with respect to audited company, and auditor's responsibility to owners and creditors.	Auditing expectation gap.	35 Students pre audit class, 35 students post audit class.	Analysis Paired t-test. Results The change in the perception of the students is due to the auditing education which reduces the expectation gap between the students and the auditors.
Pierce and Kilcommins (1996).	Duties, ethical and legislative framework, liability, and audit report.	Auditing expectation gap.	133 Business studies year one students, 112 accounting and finance year one students, 93 accounting and finance year two students, 47 accounting and finance year three students with elective course of auditing, 43 accounting and finance year three students without elective course of auditing.	Analysis Mean scores analysis. Results The education is considered to be effective to reduce the auditing expectation gap.

Author (s) & Date	Independent Variable(s)	Dependent Variable(s)	Sample Size	Analysis & Results
Gay (2002).	Responsibility, reliability, and decision usefulness.	Auditing expectation gap.	581 auditors randomly selected from members of the institute of Chartered Accountants in Australia, and other three groups of students; 169 second year financial accounting students at the beginning of the first semester, 143 third year auditing students at the beginning of the second semester, and 110 at the end of the same semester.	<u>Analysis</u> Mann-Whitney U tests. <u>Results</u> The study results indicate that the education reduces the auditing expectation gap.

3.6 THE ROLE OF THE STANDARDS SETTINGS IN REDUCING THE AUDITING EXPECTATIONS GAP

In 1988 the Audit Standards Board (ASB) issued its nine statements on Auditing standards, these standards known as "The Expectation Gap Standards" which could grouped in to the following categories:

1 Detection of fraud and illegal acts: SAS No.52, 'The Auditor Responsibility to Detect and Report Errors and Irregularities,' and SAS No. 54 'Illegal Acts by Clients'.

2 More effective audits: SAS No. 55, 'Consideration of the Internal Control Structure in a Financial Statement Audit,' SAS No. 56 , 'Analytical Procedures,' SAS No. 57, 'Auditing Accounting Estimates'.

3 Improved external communications: SAS No. 58, 'Reports on Audited Financial Statements,' SAS No. 59, 'The Auditors' Consideration of Equity's Ability to Continue as Going Concern'.

4 Improved internal communications: SAS No. 60, 'Communication of Internal Control Structure Related'.

5 Matters noted in an audit, SAS No. 61, 'Communication with Audit Committees' (Giacomino, 1994).

Dewing and Russell (2002) investigated the existence of the expectation gap in the UK and the possibility to reduce this gap. The study depends on designing a five-point Likert scale questionnaire that is concerned with the independence, audit value-added, audit quality, and auditors' liability. The questionnaire is validated by applying a pilot study by conducting 13 interviews to obtain a range of views about the validity of the questionnaire.

Moreover, after validating the questionnaire by applying the pilot study, the questionnaire was distributed over the study sample which consists of 81 Institutional Fund Managers Association (IFMA) members. The response rate of this sample was 37 per cent which is composed of accountant and non-accountant fund managers. The results of the study are derived using descriptive analysis indicating that the expectation gap phrase is frequently described by the sample. Furthermore, there are required reforms regarding the strengthen of the auditors' independence, the frequent auditors rotation, the extension of the scope and responsibilities of the auditors, the need for more independency in monitoring of auditors' work, and strengthening the public regulations of the auditors.

However, the study focuses only on one part of the problem which is the managers regardless of the other categories of the different users. The study recommended the solutions that would reduce the auditing expectation gap without examining the comparability of this method to the other approaches that may be more effective in reducing this gap. Furthermore, the study depends on the descriptive analysis which may not get significant results that may support the results of the study.

The previous studies are summarized in table 3.5 as follows:

Table 3.5

The Role of Standards Settings in Reducing the Auditing Expectations Gap

Author (s) & Date	Independent Variable(s)	Dependent Variable(s)	Sample Size	Analysis & Results
Dewing and Russell (2002).	Independence, audit value-added, audit quality, and auditors' liability.	The auditing expectation gap.	81 Institutional Fund Managers Association (IFMA) members.	Analysis Descriptive analysis. Results Expectation gap phrase is frequently described by the sample, and that there are reforms regarding the strengthen of the auditors' independence, the frequent auditors rotation, the extension of the scope and responsibilities of the auditors, the need for more independency in monitoring of auditors' work, besides strengthening the public regulations of the auditors, are required.

3.7 CONCLUSION

It is concluded from the previous discussion of the literature review regarding the auditing expectation gap that this gap is still an existing problem whether in the developed or in the developing countries which requires more efforts to reduce this existing gap. This existence of this problem affects the decision making process of the different users who get benefit from the published annual reports of the different companies.

The prior studies are classified to two groups. First group of studies examined the existence of the auditing expectations gap in a specific context. Most of the studies included in this group examined the gap existence using the questionnaire survey. Most of the studies employed the same questionnaire regardless the different cultures of the different contexts. Therefore, this group of studies ignored the cultural effects of the different countries, and so applied the previously used questionnaires with out any sort of adaptation as a matter of validation for the employed data gathering technique. Therefore, the current research will overcome this problem by adapting the employed data collection technique, questionnaire or checklist, on the Egyptian context to ensure the validation of the derived results based on these techniques.

Moreover, it is concluded that there is only single research that was applied on the Egyptian context by Dixon *et al.* (2006) regarding the auditing expectations gap problem. However, it suffers of the same defects of the previously mentioned studies which would be overcome by the current research, which is the most updated research in the Egyptian context, as it would be seen in the following chapters.

The second group of studies is concerned by the appropriate solution for the reduction of the auditing expectations gap. There are three different appropriate solutions that are recommended by the prior studies. First solution is expanding the audit report and using the long form audit report instead of the short form audit report. Second solution is educating the financial statements' users towards the auditor's roles and responsibilities. The third solution is concerned with the required standards settings expending the auditors' roles and responsibilities.

The second group prior studies select one of the three approaches and investigated the effect of the selected method on the auditing expectations gap. As a matter of fact, the three methods would have a positive impact on the reduction of the expectations gap. However, knowing the appropriate and effective method needs to examine the impact of the three methods simultaneously at the same time as to maintain the consistency of the comparison. None of the previous studies applied this sort of comparison between these methods. Also, the single research that is applied on the Egyptian context has not examined the effectiveness of any of the different solutions that would contribute to the reduction of the expectations gap. Therefore, the current research would examine the effectiveness of the different methods in comparison to each other.

Moreover, the research would propose a forth solution, audited voluntary disclosures that was not examined before by the prior studies, and compare its effectiveness to the traditional solutions in reducing the expectations gap. Therefore, the current research would overcome the defects of the prior studies and contribute to the knowledge through recommending another solution that is believed to be more effective in reducing the auditing expectations gap.

As a matter of fact, this additional solution requires a theoretical base to support the argument that this solution would be more effective in reducing the auditing expectations gap in comparison to the traditional methods which would be introduced in the next chapter. The examination of the different traditional methods in comparison to the proposed method would be applied over the Egyptian context as a unique situation passed over different reform programs which are shown in the previously presented chapter of the Egyptian economy background.

CHAPTER FOUR

THEORETICAL FRAMEWORK

4.1 INTRODUCTION

The theoretical framework of the current study focuses on reducing the information expectations gap and the auditing expectations gap using the audited voluntary corporate disclosure. The importance of theory is that theories enable us to understand in general terms how the world works, to move around, mentally, among the objects and relationships to which they relate, and to act in ways that, as far as we can tell, will not defeat our reasonable expectations. A theory will not save us from unreasonable expectations nor from the vagaries of chance in any form. A theory will not tell us what to do; but it will tell us what it is possible to do and what is not possible to do. In that way it removes countless things from consideration when we are confronted with the necessity of choosing or acting (Chambers, 1996).

Different prior studies focused on the role of the voluntary disclosure in reducing the information expectations gap and solving the information asymmetry problem. These studies provide evidence that this solution is restricted to the degree of assurance and credibility associated with the voluntary disclosure. It is a vital issue to rely on a credible sort of disclosure to make different decisions. Therefore, the usefulness of the provided disclosure depends on the credibility and assurance of this sort of information not just the information completeness.

The current study argues that the lack of voluntary disclosures' credibility would affect the effectiveness of this sort of disclosure in reducing the information gap or solving the information asymmetry problem. Therefore, the current research argues that voluntary disclosure requires to be assured by an independent third party. This sort of assurance service is more appropriate to be provided by auditors, which in turn would expand their roles and responsibilities leading to raising the degree of stakeholders' satisfaction and approaching their expectations leading to the reduction of the expectations gap between auditors and users. Therefore, the current chapter provides theoretical framework of evidences that support this argument.

Corporate voluntary disclosure is considered to be the heart of the current study. Therefore, this chapter will include its definition, its different categories and the incentives and constraints of disclosing voluntary information. In addition, there are different theories explaining the different motives of the voluntary disclosure. This chapter would give a brief idea of such theories. However, the study would rely on the stakeholder-agency theory that would fit with the nature and scope of the empirical work.

Moreover, the following discussion will include the previous studies' evidence regarding the role of voluntary corporate disclosure in reducing the information expectations gap. Based on the stakeholder-agency theory, there are different studies that provided evidence arguing that expanding the role of the auditor will satisfy the needs of the stakeholders, and in turn this study argues that the there is a vital role of the audited voluntary corporate disclosure in reducing the auditing expectations gap.

4.2 THEORIES OF VOLUNTARY CORPORATE DISCLOSURE

Positive accounting theory 'is concerned with explaining accounting practice. It is designed to explain and predict which firms will and which firms will not use a particular method, but it says nothing as to which method a firm should use' (Watts and Zimmerman, 1986, p.45). The stakeholder theory (managerial version) and legitimacy theory provide alternative explanation to the positive accounting theory about the drivers that make the organization make particular disclosures without prescribing particular actions, or methods of disclosure (Deegan, 2000).

According to Guthrie and Parker (1990) 'The political economy perspective perceives accounting reports as social, political, and economic documents. They serve as a tool for constructing, sustaining, and legitimizing economic and political arrangements, institutions and ideological themes which contribute to the corporation's private interests. Disclosures have the capacity to transmit social, political, and economic meanings for a pluralistic set of report recipients' (p.166).

The perspectives of the legitimacy theory and stakeholder theory are seen to be consistent and build on the assumptions of the political economy perspective (Deegan, 2000; Gray *et al.*, 1996). Thus, it is stated that legitimacy theory and stakeholder theory are two theories referred to as system-oriented theories where 'a system-oriented view of the organization and society permits us to focus on the role of information and disclosure in the relationship(s) between organizations, the state, individuals and groups' (Gray *et al.*, 1996, p.45). Therefore, the important advantages of the voluntary disclosure by the firms for both firms and managers are explained by three main theoretical theories: legitimacy theory, signaling theory, and agency theory (Watson *et al.*, 2002).

4.2.1 Legitimacy Theory

Legitimacy is considered to be 'a generalized perception or assumption that the actions of the entity are desirable, proper, or appropriate within some social constructed system of norms, values, beliefs and definition' (Suchman, 1995, p.574). Mathews (1993) stated that 'the social contract would exist between corporations (usually limited companies) and individual members of society. Society (as a collection of individuals) provides corporations with their legal standing and attributes and the authority to own and use natural resources and to hire employees. Organizations depend on community resources and output both goods and services and waste products to the general environment. The organization has no inherent rights to these benefits, and in order to allow their existence, society would expect the benefits to exceed the costs to society' (p.35).

The survival and growth of the company depends on its ability to distribute economic, social, or political benefits to the different groups that represents the source of its power (Shocker and Sethi, 1973). Early accounting theory identified the users of accounting information as shareholders and creditors, and the annual report's disclosure was directed to serve only the interests of these two groups of users (Gray, 1995).

Moreover, the legitimacy theory assumes that the company would not survive unless it is congruent with the society in which it operates (Dowling and Pfeffer, 1975). However, there is a social contract between the company and its society of operations. The social contract contains explicit terms in the form of legal requirements, and implicit terms in the form of non – legislated social expectations (Gray *et al.*, 1996). A number of researchers invoked legitimacy theory to explain disclosures in environmental and social disclosure (Guthrie and Parker, 1989; Patten, 1992; Deegan and Gordon, 1996).

However, Deegan and Rankin (1996) mentioned that the failure to comply with society expectations leads to revocation of the contract mentioned by Gray *et al.*, 1996). Deegan (2000) stated that 'organizations continually seek to ensure that they operate within the bonds and norms of their respective societies, that is, they attempt to ensure that their activities are perceived by outside parties as being legitimate' (p.253). It is indicated that the social expectations would encompass economic, environmental and social factor relationships (Elkington, 1997).

Therefore, legitimacy theory presents that corporate disclosure reacts to environmental factors (economical, social, political) and that disclosures legitimate action (Preston and Post, 1975; Hogner, 1982; Lehman, 1992; Lindblom, 1994). However, Guthrie and Parker (1989) provided evidences that the legitimacy theory is not adequate as means of explaining the social disclosure during a specific period of time. This is based on the absence of any reaction of economic, social or political events as a result of the social disclosures.

Based on legitimacy theory, social disclosures are one of the methods used by the firm to influence the public policy process. This can be done directly by addressing public and/or legislative concerns, or indirectly, by projecting company's image as socially aware. Therefore, the greater the company is exposed to the social and political environment, the greater the need to attempt to influence the process through social disclosure (Patten, 1992). Moreover, according to Guthrie and Parker (1989), legitimacy theory argues that the corporate disclosures are made as reactions to environmental pressures (economical, social, and political) and to legitimate the company's existence and actions.

Lindblom (1994) differentiates between legitimacy as a status or condition and the legitimating as a process. According to Lindblom (1994), the legitimacy is defined as 'a condition or status which exists when an entity's value system is congruent with the value system of the larger social system of which the entity is part. When a disparity, actual or potential, exists between the two value systems, there is a threat to the entity's legitimacy' (p.2).

Moreover, Tinker and Neimark (1987) states that 'the public in general, become increasingly aware of the adverse consequences of corporate growth. They pressured both business and government to make outlays to repair or prevent damage to the physical environment, to ensure health and safety of consumers, employees, and those who reside in the communities where products are manufactured and wastes are dumped, and to be responsible for the consequences of technological unemployment and plant closings' (p.84). Moreover, the evidence suggests that the society's confidence in business has decreased. Therefore, businesses are forced to respond to the diversified social issues that are consequences of their activities (Tinker and Neimark, 1987).

Moreover, based on legitimacy theory, the organization is said to be a part of a wide social construct that has different expectations that must be met to maintain the ongoing of its operations (Ratanajongkol *et al.*, 2006). Corporate social disclosure is motivated by the legitimacy activities (Horgner, 1982). Legitimacy theory forms a sort of stress on the corporations to react to the community's expectations (Guthrie and Parker, 1989). Therefore, the community's expectations are satisfied by additional disclosure of social information (Wilmshurst and Frost, 2000).

Additionally, under the previously stated stress of the community, the annual report is an evaluation for the responsiveness of the management to the different environmental issues that affects the corporation's performance. Hence, the voluntary disclosure of the environmental and social issues is not limited to the role of offering information, but also shows the perception of the management towards considering satisfying the expectations of the stakeholders (Deegan and Rankin, 1996).

The studies of Patten (1992) and Deegan and Rankin (1996) on the Australian companies showed that the increasing of the concern about the community that the companies are operating in, including the stakeholders expectations and interests, increased the level of the social responsibility information in the annual reports. This response is believed to be a supporting evidence for the legitimacy theory in the form of corporate reaction to the society to gain its approval for the company's existence and growth.

Legitimacy theory is based on perceptions, and any response of the management would be in the form of disclosure. Hence, the measurement of the stakeholders' perceptions indicates their interests and expectations which need to be satisfied. The management satisfies these expectations in terms of additional voluntary disclosure that is not motivated by standards or regulations, but motivated by the incentive to satisfy the stakeholders' expectations and change their perceptions towards the management's response to the social and environmental issues. Using the disclosure by the management to satisfy the stakeholder's needs reduces the expectations gap between the two parties (Cormier and Gordon, 2001).

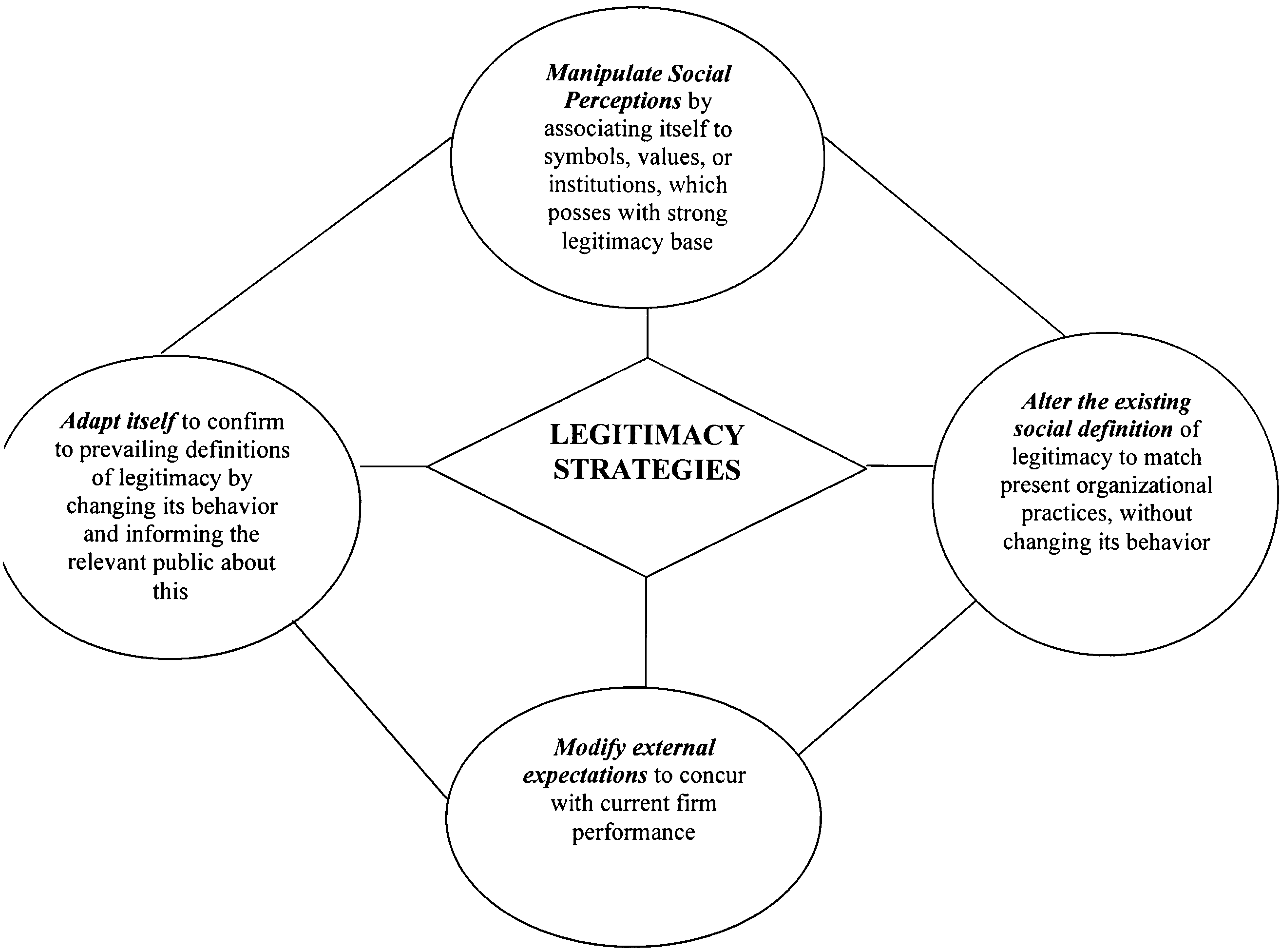
Legitimacy theory includes four strategies. First, the organization is seeking to inform and educate its key stakeholders about actual changes in the organization's performance and activities. This strategy was initiated as a response to the existence of the legitimacy gap due to the actual failure of the organization's performance. The social disclosure is used to apply the four strategies. The second and fourth strategies are concerned with the expectations of the stakeholders. The difference between these two strategies is that both of them are willing to correct and change the stakeholders' expectations, but the second strategy is willing to do that without any changes in the behavior of the organization, while the fourth strategy is accepting to act in other behavior to do so. Therefore, the two strategies having the same objective but the first using a negative approach, while the second strategy acting positively (Lindblom, 1994).

To this extent the legitimate strategies present the key stakeholders' expectations. The success of implementing any legitimate strategy will involve the addressing of the current values of either the corporation's society, or the business key stakeholders (Lewis and Unerman, 1999). This shows that the legitimate strategies are stakeholders' oriented.

The previously stated strategies of the legitimacy gap are shown in the following figure:

Figure 4.1

Organizational Legitimacy Strategies



Source: Khor, A.K. (2002) 'Social Contract Theory, Legitimacy Theory and Corporate Social and Environmental Disclosure Policies: Constructing a Theoretical Framework' Nottingham University Business School.

However, it is noted that 'a relationship between legitimacy theory and disclosure was only marginally supported for environmental issues, unconfirmed for energy and community issues and subject to contradictory evidence for human resources issues' (Guthrie and Parker, 1989, p.351). In addition, Wilmshurst and Frost (2000) concluded that legitimacy theory provides limited explanation for the decision to disclose environmental information. It is observed that firms refer to legitimacy theory through voluntary disclosures as a fear from violating the social contract (Joseph, 2007).

Furthermore, given that the legitimacy theory is dealing with perceptions, the legitimacy theory has not provided an appropriate measure of the effect of disclosure changes in the perception of the relevant publics in isolation from other influences and events in the society (Campbell *et al.*, 2003). Therefore the theory has not provided any attention to the conflict of interests of the stakeholders, and so it assumed that the voluntary disclosure is likely to be credible and reliable, which is somehow considered to be questionable issue.

4.2.2 Signaling Theory

Another theoretical approach used in the definition of voluntary disclosure is signaling theory. The development of this theory is to explain behavior in the labour markets, but it is also used for voluntary disclosure. Signaling is a reaction to information asymmetry as managers have more information than investors have. The information asymmetry can be reduced if the party with more information signals to others. This is done as the higher quality firms' managers distinguish themselves from the lower quality ones. In order to signal successfully, managers should use credible signals (Eccles *et al.*, 2001).

It is argued that when information is costless, the seller will disclose both good and bad information, as buyers would put the worst interpretation on non-disclosure (Grossman, 1981). Likewise, disclosing favorable information by the firms is done as non-disclosure will result in users inferring content of such information as unfavorable (Milgrom, 1981; Jung and Kwon, 1988). Such disclosure provides credible signals about a firm's value as the firm would be penalized if the firm provides misleading information (Hughes, 1986). Furthermore, managers voluntarily disclose both good and bad news, as the good news signals quality and bad news is signaled to prevent a decline in the firm's share price (Skinner, 1994).

Information plays an important role in the agency relationship because the agent's rewards and compensation may be based not just on the realized outcome but also on the results signaled by the accounting information system. Therefore, accountability information work perfectly only if the signals from the accounting system endeavors of the agent (Bromwich, 1992). In addition, signaling theory predicts that the healthy firms are likely to disclose more information than the distressed firms (Ross, 1979).

4.2.3 Stakeholder - Agency Theory

Agency theory 'may help to explain the lack of existence of a comprehensive accounting theory. It implies that a framework of accounting theory cannot be developed because of the diverse interests involved in financial reporting. However, there is an even more basic reason why agency theory will have limited direct impact on financial accounting. Agency theory is a descriptive theory in that it helps to explain why a diversity of accounting practices exists. Therefore, even if subsequent testing supports this theory, it will not identify the correct accounting procedures to be used in various circumstances, and thus accounting practice will not be changed' (Schroeder and Clark, 1995, p.45). Moreover, agency theory provides a necessary explanation of why the selection of particular accounting method would affect the organization (Deegan, 2000).

Jensen and Meckling (1976) emphasized that the agency theory shows the contract between one party (principal) and another party (agent). By means of this contract, the principal will delegate the authority to the agent to make different decisions on the behalf of this principal. Using the terms of agency theory, there is a contract between the shareholders (principal) and the management (agent) regarding managing and operating the organization on the behalf of them. Moreover, there is another contract that is between the shareholders (principal) and the auditor (agent) regarding controlling and auditing the disclosures of the management about the organization's performance.

Auditing may be useful where the information is issued by the agent, who may be better informed than the principal or may provide information which puts him/her self in the best possible situation. Auditing helps in verifying and validating such information (Bromwich, 1992).

The relationship between the shareholders (principal) and the corporate managers (agent) created much uncertainty due to various information asymmetries (Deegan, 2000). Agency theory explains why managers voluntarily disclose information. It is assumed by the agency theory that managers and shareholders have different interests (Chow and Wong-Boren, 1987; Cooke, 1989a, 1989b, 1992, Firth, 1980; Hossain *et al.*, 1994). Shareholders will seek to control managers' behavior through bonding and monitoring activities. Therefore, managers may have an incentive to try and convince shareholders. Through greater disclosure, companies attempt to reduce cost of capital by reducing investor uncertainty (Ball and Foster, 1982; Watson *et al.*, 2002). Moreover, agency theory indicates that managers will disclose social information if it increases their welfare, by means that the benefits of this disclosure overweigh its associated costs (Ness and Mirza, 1991).

Agency theorists argue that corporations are structured to minimize the costs of getting some participants (agents) to do what other participants (principals) desire. Therefore, participants agree to co operate with each other within the organization rather than dealing with each other through the market (Donaldson and Preston, 1995).

There are two kinds of managerial failures that restrict the agent from acting perfectly towards the principals (shareholders). Firstly, failures of managerial competence related to unwitting mistakes in the discharge of managerial control. Secondly, failures of managerial integrity related to willful behaviors on the part of managers negatively impact the value of firm's assets (Moldoveanu and Martin, 2001).

4.2.3.1 Agency Costs

The separation of the ownership and management that occurs between the principal and the agent results in a variety of agency problems and different agency costs including monitoring costs, bonding costs, and residual loss (Jensen and Meckling, 1976).

4.2.3.1.1 Monitoring Cost

The monitoring costs are paid by the principal to measure, observe, and control the agent's performance (Fama and Jensen, 1983a, 1983b). Denis *et al.* (1997) described the monitoring as a process that is restricted to certain groups. The monitoring process must have necessary expertise and incentives to monitor the management, and provide credible thread to management's control of the company. Therefore, the cost of undertaking an audit is referred to as a monitoring cost (Deegan, 2000). However, too much monitoring would results in constricting the managerial initiative (Burkat *et al.*, 1997).

Moreover, critics of Cadbury (1992) showed that the high level of monitoring may act as deterrent to managerial entrepreneurship. However, it is required to have an optimal level of monitoring the agent's performance in a way that does not restrict the agent from performing his stewardship role. Thus, the stewardship theory indicates that the performance variations arise from whether the structural situation facilitates the effective actions by the management (Donaldson, 1988).

The small board of directors' size and the role duality of the chairman of the board of directors being the Chief Executive Officer (CEO) at the same time, as corporate governance characteristics, would facilitates the decision making process and achieve the stewardship role. On the other hand, the small size and role duality's benefits would be on the expense of the other shareholders' interests and the whole performance of the organization. Therefore, the monitoring of the agent's performance needs to be tied to a degree that does not affect his stewardship role. This balance would have a positive effect on the agent's performance (Donaldson and Davis, 1991).

4.2.3.1.2 Bonding Costs

The bonding costs are adhered to the agent's compensation systems when they act in a manner of behavior that satisfies the interests of the principal (shareholders). The agents need to disclose additional information to show their shareholders that they are acting in a satisfactory behavior that fits with their interests. Managers are bonding themselves to prepare financial statements. This is costly, and referred to the positive accounting theory as a bonding cost (Deegan, 2000).

Moreover the agents would accept bearing the bonding costs as to reduce the monitoring costs (McColgan, 2001). The optimal bonding contract would satisfy the shareholders interests. However, the agent would not satisfy all the request of the shareholders, therefore there would not be a perfect bonding contract that satisfies all the needs of the shareholders (Denis, 2001).

4.2.3.1.3 Residual Loss

The existence of the residual or agency loss is due to the existence of the monitoring costs and bonding costs. This residual loss is due to the imbalance between the monitoring cost and the bonding cost. That means the failure of the agent to satisfy the needs of the shareholders regarding monitoring the agent's performance and so the agency contract is imperfectly satisfied (McColgan, 2001).

4.2.3.2 Agency Conflicts

As a result of the conflicts of interests between the principal and the agent contract there are four problematic areas; moral hazard, earning retention, risk aversion, and time horizons (McColgan, 2001).

4.2.3.2.1 Moral Hazard Agency Conflicts

The single manager who owns the firm consumes private perquisites rather than investing in positive net present value as his ownership stake in the company decreases. Therefore, the investment decision is considered to be dependent on the ownership structure (Jensen and Mecking, 1976).

Jensen (1993) argued that moral hazard problems are likely to appear in larger companies as increasing firm size increases its complexity and the difficulty of monitoring which increases the monitoring costs. The corporate size is considered to be an indicator for the complexity and higher monitoring cost.

4.2.3.2.2 Earnings Retention Agency Conflict

The different studies found that director remuneration is an increasing function of corporate size, which incentives management to focus on size growth rather than shareholders' return growth (Brennan, 1995b). Moreover, Jensen (1986, 1993) argues that managers prefer to retain earnings to have size growth, greater prestige, and ability to be awarded high levels of remuneration, while shareholders prefer higher cash dividends. This indicates increasing conflict of interest between the management and the shareholders.

4.2.3.2.3 Time Horizons Agency Conflict

The conflict between the management and the shareholders concerning the timing of cash flows. The shareholders are concerned with the cash flow in the future, while the management concerned with the cash flows for their employment term in the short term. This conflict would affect the research and development expenditures. It is noted that the managers reduces the research and development expenditures, while the shareholders requires increasing these research and development expenditures (McColgan, 2001).

Dechow and Sloan (1991) examined the research and development expenditures near the retirement of the top management. It is found that the research and development expenditures are reduced which indicated that the management is concerned by the short term, while the shareholders are concerned by the long term benefits of the research and development expenditures.

4.2.3.2.4 Managerial Risk Aversion Agency Conflicts

The majority of company directors are tied to the company they are working in, and their income is depending on the performance of the company. Therefore, the managers prefer minimizing the risk of their company's stock, and avoid the investment decisions which increase the risk of the company (Denis, 2001).

4.2.3.3 Stakeholder Theory

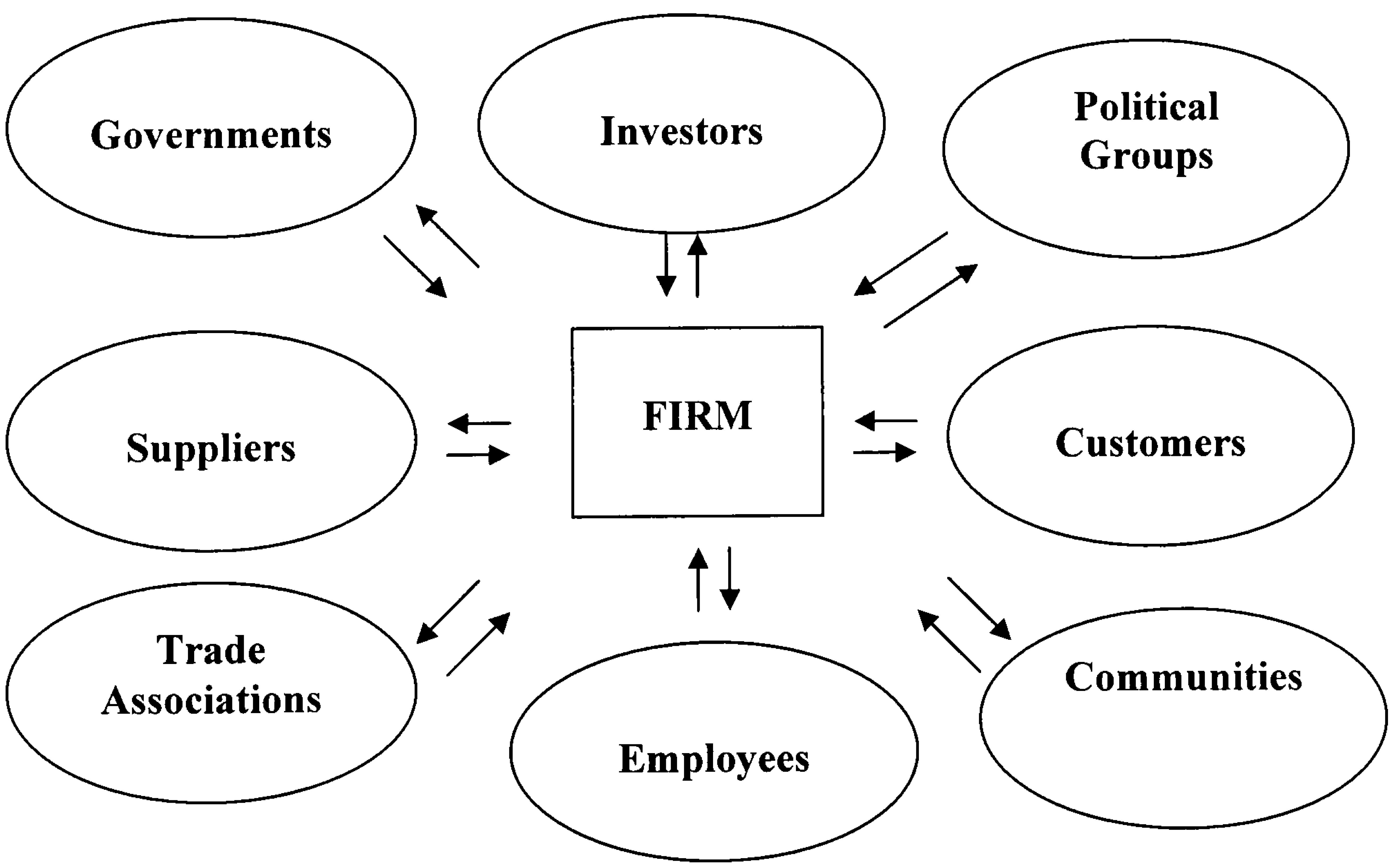
There are many similarities between legitimacy theory and stakeholder theory. Therefore, Gray *et al.* (1995b) state that 'it seems to us that the essential problem in the literature arises from treating each as competing theories of reporting behavior, when stakeholder theory and legitimacy theory are better seen as two overlapping perspectives of the issue which are set within a framework of assumptions about political economy' (p.52).

Stakeholder theory involves the recognition and identification of the relationship between the company's behavior and the impact on its stakeholders (Ansoff, 1965). Gray, *et al.* (1995b) stated that 'the corporation's continued existence requires the support of the stakeholders and their approval must be sought and the activities of the corporation adjusted to gain that approval. The more powerful the stakeholders the more the company must adapt' (p.55). Atkinson *et al.* (1997) suggested that the term 'stakeholder' recently introduced in conjunction with the development of new performance measures for better strategic planning. While Gray *et al.* (1996) state that 'a 'stakeholder' is any human agency that can be influenced by, or can itself influence, the activities of the organization in question' (p.33). Since the organization has many stakeholders, therefore, it owes accountability to all its stakeholders (Gray *et al.*, 1996). In addition, it is stated that the more important the stakeholder to the organization, the more effort will be made to manage and manipulate this relationship. This is done by offering more information, especially voluntary disclosures, to gain the support and approval of these stakeholders. Freeman (1984) suggested that stakeholder theory explains the relationship of the firm to its external environment.

Moreover, Stakeholder theory states the 'all persons or groups with legitimate interests participating in an enterprise do so to obtain benefits and that there is no prima facie priority of one set of interests and benefits over another' (Donaldson and Preston, 1995, p.68). Thus the stakeholder model is shown in the following figure:

Figure 4.2

The Stakeholder Model



Source: Donaldson, T, and Preston L. (1995) 'The Stakeholder Theory of the Corporation: Concepts, Evidence, and Implications' Academy of Managerial Review, Vol. 20, No. 1, 69 – 91.

The stakeholder theory can be , and has been used and presented in different ways that are distinct involving various methodologies, types of evidence, and criteria of appraisal. Therefore, stakeholder theory is justified in literature explicitly or implicitly using three different approaches. First, the descriptive approach which attempts to show that the theory's concepts are corresponding to observed reality. Second, the instrumental approach which points to evidence connection between stakeholder management and corporate performance. Third, the normative approach aims to appeal to underlining concepts such as individual or group rights, social contract and social corporate responsibilities (Donaldson and Preston, 1995). The normative approach is considered to be the central core of the theory. The instrumental is the second level of the theory which predicts if certain practices are carried out, then certain results are obtained. The external shell of the theory is its descriptive aspects explaining the observed relationships in the external world. The descriptive accuracy of the theo resumes the truth of the core normative conception.

Therefore, stakeholder theory has been advanced and justified based on 'its descriptive accuracy, instrumental power, and normative validity' (Donaldson and Preston, 1995, p.69). These aspects are interrelated and quite distinct that they involve different evidences and have different implications (Donaldson and Preston, 1995).

Moreover, the theory is considered to be a moral and philosophical guide for the organization (Donaldson and Preston, 1995). It is argued that the company should serve only the interests of the shareholders of the corporation (Wijnberg, 2000). There are two perspectives concerning the disclosure to the stakeholders of the corporation. First, is the ethical (moral or normative) branch of stakeholder theory where all the stakeholders have the right to get a full disclosure of the corporation and its impact upon them regardless using this information or not. Moreover, Hasnas (1998) states that, according to the normative stakeholder theory, management must give equal consideration to the interests of all stakeholders and, when these interest conflict, manage the business so as to attain the optimal balance among them. This, of course, implies that there will be times when management is obliged to at least partially sacrifice the interests of stockholders to those of the other stakeholders. Hence, in its normative form, the stakeholder theory does imply that business has true social responsibilities' (p.25).

Second, the corporation satisfies only the needs of the powerful stakeholders, and this power could be in the form of political power by the government, or political power by other stakeholders. Information is a major element that can be employed to manage (manipulate) the stakeholders to gain their support and approval, or distracting their opposition and disapproval (Gray *et al.*, 1996; Deegan, 2000). Therefore, organizations would have the incentive to disclose information about their programs and initiatives with respect to the powerful stakeholders' expectations (Deegan, 2000). Consequently, information disclosure programs help in reducing information asymmetries, which in turn affect the relative political power of different actors (Grant, 1997).

Stakeholders are classified into two groups: primary stakeholders, whose continuing participation is necessary for the survival of the corporation, and secondary stakeholders, who are not essential to the survival of the corporation although their actions and responds can significantly damage or benefit the corporation (Freeman, 1984; Clarkson, 1995). In addition, stakeholder theory also recognizes the existence of trade-offs in resource allocation between competing stakeholders (Hill and Jones, 1992). However, the rights of stakeholders should be considered to be equal (Freeman, 1994). The stakeholder's concept is satisfied by designing non financial measures (Logsdon and Lewellyn, 1998). Furthermore, stakeholders' theory arises due to the rejection of the concern about maximizing the benefits of a single stakeholder (shareholders) (Wijnberg, 2000).

Moreover, Atkinson *et al.* (1997) stated that 'a model for measuring company's performance helps all members – customers, suppliers, employees, and community – understand and evaluate their contributions and expectations. By focusing on the secondary processes for achieving primary objectives, such as profit, the system provides a tool for monitoring implicit and explicit contractual relationships with stakeholders' (p.25). Donaldson and Preston (1995) provides a theoretical foundation of the stakeholder theory. The main hypothesis of this theory is the existence of a connection between an action and an outcome. The predictions of the normative assumption mentioned that all the stakeholders deserve moral consideration. Moreover, stakeholder theory differs from other theories that it is intended to explain and to guide the structure and operation of the established corporation.

Many authors suggested that 'the trust between managers and key shareholders can lead to competitive advantage for firms' (Berman, 1998, p.45). The competitive advantage that the organization can achieve is the output of the connection between the organization and its stakeholders. Accordingly, the competitive advantage's degree is measured and disclosed using the voluntary disclosure. This outcome is an item of the market disclosure in the list of the different categories of the voluntary disclosure. Therefore, this disclosure shows the outcome that indicated the success of the action. Furthermore, directors can communicate with stakeholders using voluntary disclosure (Watson *et al.*, 2002).

The stakeholder theory's main advantage is providing a means for dealing with multiple stakeholders with multiple conflicting interests. The organization is not focusing on the interests of the individual stakeholder. It is believed that the satisfaction of interests of the different stakeholders is achieved using system centered theory (Freeman, 1984). Moreover, Rowley (1997) theoretically argued that the way the organizations are treating their multiple interdependent stakeholders is influenced by the structure of a stakeholder relationship network.

The interaction of the organizations with their stakeholders is determined by two structural factors of stakeholder networks. First, the interaction between the organization and its stakeholders is determined by the density of stakeholders' network which measures the degree of interconnectedness between an organization's stakeholders. Second, the interaction between the organization and its stakeholders is determined by the focal organization's centrality in the stakeholders' network which measures the degree to which an organization in a network falls on a path between its stakeholders in the network (Rowley, 1998).

The high density network allows the exchange of information and the coordination between the different activities among the stakeholders. Therefore, high density network provides the opportunity for the stakeholders to interact with each other effectively (Oliver, 1991). Thus, the product of the highly density network is efficient communication and the shared expectations across the network. In contrast, the less dense network does not create shared behavioral expectations between the different stakeholders (Mintzberg, 1983). If the focal organization's centrality is high, by means that the organization is centralized between the different stakeholders, that would influence the formation of shared behavioral expectations and facilitates information exchange (Rowley, 1997).

Furthermore, stakeholder theory addressed the relationship between the organization and the external environment including its corporate social responsibility and corporate social performance. The stakeholders are the parts that have the ability to affect (directly or indirectly) the resources of the organization. On the other hand, they are affected by the different economical, technological, social, political, and managerial perspectives of the organization. Therefore, the theory is concerned by the congruency between the organization and its stakeholders (Freeman, 1984).

Regarding the explanation of the environmental, social, and ethical disclosure, stakeholder theory explains the observable relationships in the real world based on its descriptive aspect (Donaldson and Preston, 1995). Using the managerial branch of the stakeholder theory, the disclosed 'information is a major element that can be employed by the organization to manipulate the stakeholder in order to gain their support and approval, or distract their opposition or disapproval' (Gray *et al.*, 1996, p.46).

Therefore, this managerial aspect focuses on the relationships and interactions between the organization and the various stakeholders who compose the organizational environment, rather than considering the whole organizational environment, and assuming the homogenous of stakeholders' perception and expectations as legitimacy theory does (Laan, 2006). As a result, stakeholder's priorities may not necessarily be homogenous. Some stakeholders may acquire stocks in firm with intend to exercise them influencing social action, while others may acquire the firm's stocks to advance the firm's financial performance (Wolfe and Putler, 2002). Thus, Lev (1988) stated that 'the usefulness of information is clearly an adequate standard in a 'multi-person' setting of many users with varied preferences and objectives' (p.2).

Moreover, stakeholder theory considering the heterogeneity of stakeholders, and the inability to provide all information needs, results in the occurrence of conflict between these stakeholders. The resolution of this conflict reflects the amount of power stakeholder group hold in the organization's environment (Miles, 2002; Mitchell *et al.*, 1997; Tilt, 1994). From the view of stakeholder theory, the organization's objective is to balance the conflict demands of various organization stakeholders (Roberts, 1992). Therefore, under the management branch of stakeholder theory, environmental, social, and ethical disclosure, as a category of the voluntary disclosure, 'assumed to assist in gaining, maintaining or restoring organizational legitimacy in the eyes of those stakeholder groups whose needs have been addressed' (Laan, 2006, p.25).

Stakeholder theory focuses on two core questions. First, it asks, what is the purpose of the firm? The answer of this question encourages managers to share the sense of the value they create, and bring their key stakeholders together. This result in generating outstanding performance which is determined in terms of its purpose and marketplace financial metrics. Second, stakeholders' theory asks, what responsibility does management have to stakeholders? The answer to this question requires managers to identify how they want to do business regarding kinds of relationships they want and need to create with their stakeholders to achieve their purpose. Therefore, stakeholders are important constituent and profits are critical feature of this activity, but concern for profits is the result rather than the driver in the process of value creation (Freeman *et al.*, 2004). Moreover, Stakeholder theory begins with the assumption that values are necessary and explicitly a part of doing business, and rejects the separation between ethics and economics. This separation results in a narrow view of the theory that cannot possibly do justices to the panoply of human activities that is value creation and trade (Freeman, 1994).

Furthermore, government agencies, investors, and other stakeholders are demanding more disclosure of company environmental information due to their interest in the environmental issues and its related costs and liabilities (Mastrandonas and Strife, 1992). In respond to this demand, many corporations are issuing voluntary environmental reports independent of the traditional annual financial reports (CFO, 1996). Moreover, over the last two decades, environmental issues entered in the consideration of stakeholders' risk and return (Neu *et al.*, 1998).

Based on stakeholders theory the larger companies disclose more information in order to attract capital in financial market (Cooke, 1991), while using stakeholders theory makes the economic performance and profitability is the motive to voluntary disclose information (Gray, 1995). In addition, Deegan and Gordon, 1996, discussed the effect of type of industry on the voluntary disclosure decisions.

Ramanathan (1976) state that 'the political economy perspective is deriving the concept of a 'social contract', suggesting the existence of an organization relies on the support of society in general (p.517). Clarkson (1995) has referred evaluating corporate social performance to the stakeholders' satisfaction instead of in terms of corporate social responsiveness or satisfying corporate social responsibility.

The stakeholder theory is used to clarify the corporate social responsibilities' benefits for corporations. This is based on the assumption that the corporation depends on various groups for resources and survival. Therefore, the corporations need to satisfy such groups. Otherwise they would withdraw their support causing the corporate decline and may be death. The stakeholders are groups or individuals with diversified preferences and interests. Therefore, the corporate social reporting role is reporting the positive (good) and negative (bad) effects on the society arising from the organization's operations to the key stakeholders as a fulfillment of the corporation's social contractual obligations (Ramanathan, 1976; Gray *et al*., 1988).

Furthermore, the provision of the voluntary corporate disclosure is a motivated by the stakeholders' demands to achieve strategic objectives (Freeman and Reed, 1983). Therefore, corporate voluntary disclosure might be seen in the context of strategic decision making (Ullmann, 1985). Beside the traditional stakeholders (owners and investors, managers, employees, customers, and suppliers) the community is defined as a stakeholder (Boehm, 2002). Therefore, developing stakeholder theory provides structure for the social issues of the relationship between stakeholders (including the community) and business corporations (Joseph, 2007).

However, Gray *et al.* (1995b) stated that 'stakeholders and legitimacy theory are overlapping perspectives which are set within a framework of assumptions about political economy implying that the differences are in levels of resolution of perception rather than arguments for and against competing theories as such' (p.52). As mentioned before, with regard to legitimacy theory the audience of interests is defined as the society. Within the descriptive managerial branch of stakeholder theory, it is considered that organization is a part of a wider social system that includes other groups of stakeholders whom should be best managed if the organization is to survive. Moreover, as legitimacy theory, stakeholder theory believes that expectations of different stakeholder groups affect the operating and disclosure policies of the organization. The organization would not respond to the stakeholder groups equally, but rather, respond to those who deemed to be powerful (managerial perspective of stakeholder theory) (Deegan, 2000).

Finally, Hill and Jones (1992) integrated the stakeholder concept with agency theory by enlarging the standard principal–agent paradigm of financial economics to create stakeholder–agency theory which is considered to be a generalized theory of agency. In the sense of contractual perspective, stakeholder theory expands agency relationship to include other stakeholder. Accordingly, managers can be seen as the agents of all other stakeholders. It is observed that stakeholders differ among themselves with respect to their importance to their stake in the firm, and their power towards the managers. A similar emergence of theories is done by Freeman and Evan (1990) through the emerging of the firm-as-contract analysis with the stakeholder concept. Freeman and Evan (1990) stated that 'managers administer contracts among employees, owners, suppliers, customers, and the community. Since each of these groups can invest in asset specific transactions which affect the other groups, methods of conflict resolution or safeguards must be found' (p.352).

Moreover, integration of the agency theory and firm–as–contract theory with the stakeholder theory gives attention to the special role of managers towards all stakeholders. The 'information asymmetry' between managers and other stakeholders expands the management's role to include a duty of safeguarding the welfare of the abstract entity that is the corporation and of balancing the conflicting claims of multiple stakeholders to achieve this goal. This argument raises the importance of monitoring devices that have the effect of reducing information asymmetry and enforcement mechanisms (Hill and Jones, 1992).

4.3 VOLUNTARY CORPORATE DISCLOSURE

It is observed that from 1994, several accounting organizations have issued different reports focusing on the different types of voluntary disclosure. The first issued report was by the Jenkin's Committee, AICPA (1994) and the ISA 38 entitled 'Intangible Assets'. Moreover, the financial accounting standards board (FASB) issued a report in January 2001 concerning the voluntary disclosure entitled 'Improving Business

Reporting: insights into enhancing voluntary disclosure'. This report does not state that non-financial performance must be disclosed but the firms are encouraged to voluntarily report this type of information. Another report issued by the Steering Committee entitled 'Improving Business Reporting. A Customer Focus: Meeting the Information Needs of Investor and Creditors'.

Meek *et al.* (1995) defined the voluntary disclosure as in excess disclosure of requirements representing free choices of the company's management to provide accounting and additional information relevant to the needs of their annual reports' users for making decisions.

Depoers (2000) defined the voluntary disclosure. It said 'an item of information is considered as discretionary whenever it goes beyond the compulsory information for shareholders. Compulsory information has to be understood as all the items whose publication is duly required but also the items which the firms must send to shareholders who ask for them (for example, social reporting). Whether its nature be qualitative, financial or anything else, voluntary disclosures covers all data which concern both subsidiaries and the group itself' (p.246). While Adrem (1999) defined the voluntary corporate disclosure as 'information disclosed over and above existing regulations' (p.5).

The voluntary disclosure is defined in FASB perspective as 'disclosures primarily outside the financial statement that are not explicitly required by GAAP or SEC rule'. The purpose of the AICPA's reports is to identify the information needs of the financial statement's users and to determine the types of the information considered to be useful in predicting earnings and cash flows. To do so, the AICPA suggested new types of voluntary disclosures. The suggested types are non-financial and qualitative that assists the different stakeholders in predicting the financial companies' performances (Boesso, 2002).

The AICPA committee emphasized few points that are critical for the disclosure of 'private information, operational measures, forward-looking information and new definitions of performance':

1 Providing the market with safe and reliable information.

2 The cost of preparing these detailed business reports, compared to the benefits of this type of communication.

3 The problems associated with auditing investigation of these types of information in the absence of well-defined accounting and auditing standards.

Moreover, the FASB's report correlates several benefits with the voluntary disclosure: 'lower average cost of capital, enhanced credibility, improved investor relations, access to more liquid markets and better investment decisions'. On the other hand, there are some costs related to the voluntary disclosure: 'competitive disadvantage, bargaining disadvantages and litigation from merit less suits attributable to information disclosure' (Boesso, 2002).

Kaplan and Norton (1992) introduced the Balanced Scorecard, based on the theory of stakeholders, as performance measurement approach that is based in integrating the non-financial measures with the financial ones. Kaplan and Norton (1993) linked the non-financial measures to the strategy. Moreover, Kaplan and Norton (1996) emphasized that the Balanced Scorecard is an approach that assists creating and developing intangible measures such as: customer relationships, innovative products and services, high quality and responsive operating processes, and skills and knowledge of the workforce. Moreover, the use of accountability turned into competitive advantage (Epstein *et al.*, 2000). Furthermore, providing the stakeholders with the proper and expected information supports this relationship which represents the main source of competitive advantage (Boesso, 2002).

Voluntary disclosure is considered to be non-GAAP report or enhanced corporate reporting (ECR). The ECR is less constrained than the GAAP reporting by standards and regulations, and contains more qualitative disclosures and non-financial information (Gibbins and Pomeroy, 2006). Moreover, Gray (1994b) state that 'accounting should be social rather than a strictly economic concept and that a broader concept of accountability would recognize a wide range of groups or individuals that have the potential right to more information that is not strictly measurable in monetary terms and is of a voluntary nature. Shareholders, employees, customers and society in general have a right to financial and non-financial information.' (p.27).

In addition, the annual report's preparers can decide to have one of two approaches. First is following a negative approach by providing the minimum information required by the regulations (mandatory disclosure). Second is presenting a corporation's financial performance in the most favorable way by disclosing more information than required by these regulations (voluntary disclosure) (Myburgh, 2001).

4.3.1 Incentives of Voluntary Corporate Disclosure

Voluntary disclosure takes different forms: press releases, investor and analyst meetings, conference calls, monthly newsletters, and field visits with existing and potential institutional investors (Graham *et al.*, 2005). There are five motivations that drive managers to voluntary disclosure decisions: information asymmetry, increased analyst coverage, corporate control contests, stock compensation, and management talent (Healy and Plepu, 2001). Graham *et al.* (2005) introduced the limitations of mandatory disclosures as a driver of the voluntary disclosure.

4.3.1.1 Information Asymmetry

The importance of information asymmetry to accounting theory is that security markets are exposed to the information asymmetry problems due to the inside information and insider trading (Scott, 2003). Barry and Brown (1985, 1986) and Merton (1987) argue that if the available information to the managers (insiders) more than the investors (outsiders), the investors requests an information risk premium. The firm can reduce information risk by reducing the cost of capital through the increase of voluntary disclosure.

Increasing voluntary disclosure reduces information asymmetry, and thus increases the liquidity of firm's stock (Diamond and Verrecchia, 1991; Kim and Verrecchia, 1994; Baiman and Verrecchia, 1996). Graham *et al.* (2005) emphasized that voluntary disclosure reduces the information risk due to the predictable earnings of the company. Moreover, non-financial information improves decision-making due to the decrease of the information asymmetry (Fama and Laffer, 1971; Wallace, 1988).

4.3.1.2 Increased Analyst Coverage

Information is the inputs of the firm analysis that is done by the analysts. The efficiency of the analysis depend on variety of diversified factors, the most crucial one is the amount and type of information available for the analysis process. The amount of information available for the analysts depends on the level of disclosure, especially the voluntary disclosure.

If the required disclosures are not fully disclosing management's private information; then voluntary disclosure reduces the cost of information acquisition for analysts and increases the amount of available information, which increases the number of analysts (Bhushan, 1989; Lang and Lundholm, 1996). Therefore, voluntary disclosure influences the attraction of analysts, by the provision of attractive level of disclosure.

4.3.1.3 Stock Price Motivations

The stock price is an important indicator for firm's performance and acts as criteria of management's performance evaluation. The poor stock and earnings performance result in the risk of job loss motivates managers to use voluntary corporate disclosure to reduce the need to explain the poor earnings performance (Healy and Palepu, 2001).

Graham *et al.* (2005) indicates that unprofitable and young firms care more about voluntary disclosure than profitable and older firms. Thus, developing and improving voluntary disclosure have a positive impact on the share's market price of the company (Fishman and Hagerty, 1989).

4.3.1.4 Stock Compensation

Voluntary disclosure is linked to compensation of employees, but managers might act in the interest of the current shareholders by reducing the contracting costs associated with new employees' stock compensation. Therefore, new employees will demand risk premium to cover them from the information advantage acquired by the management.

Furthermore, the managers are having incentives to reduce contracting costs associated with stock compensation for new employees by increasing the voluntary disclosure (Aboody and Kasznik, 2000; Miller and Piotroski, 2000).

4.3.1.5 Management Talent Signaling

The managers diversify from each others in terms of qualifications and talents. Therefore, there are two distinguished types of management. First, managers with poor talents and qualifications, and in this case they would avoid any voluntary or additional disclosure. Second, managers with highly qualifications and talents and motivated to make voluntary disclosure as to represent and signal their talents to the stakeholders (Trueman, 1986).

However, Graham *et al.* (2005) indicates that this motive is restricted to the managers of the small or high growth firms as the management is still not well known yet and needs to represent themselves in the form of achieving good performance, and presenting this performance voluntarily in the form of additional disclosure.

4.3.1.6 Limitations of Mandatory Disclosures

Voluntary disclosures fill in the gaps in the usefulness of the mandatory disclosures and satisfy the needs of the stakeholders that can not be satisfied by the mandatory disclosure (Graham *et al.*, 2005). Furthermore, literature has shown that neither stakeholders nor companies are satisfied with the mandatory financial reporting disclosures as a sole source of corporate information (Holland and Doran, 1998; Holland and Stoner, 1996; Holland, 1997).

4.3.2 Constraints on Voluntary Corporate Disclosure

Voluntary disclosure is constrained by the reporting standards and stock exchange rules and the informal costs (Holland, 2006). There are four constraints on voluntary disclosure: litigation risk, proprietary costs, political costs, and agency costs. However, Graham *et al.* (2005) introduced additional constraint of voluntary disclosure which is the hardness to maintain the disclosure precedent setting.

4.3.2.1 Litigation Costs

Litigation threat affects the voluntary disclosure in two ways. First, litigation can induce managers to disclose information, especially bad news. Second, litigation can reduce the incentives of the managers to disclose future forecast information (Skinner 1994, 1997; and Francis *et al.*, 1994). While Graham *et al.* (2005) provided a strong support for delaying bad news to allow analysis and interpretation.

4.3.2.2 Proprietary Costs

Firms are not fully disclosing their information due to the existence of the proprietary costs associated with the firm's competitive position in the product market (Verrecchia, 2001; and Dye, 2001). The proprietary costs are an effective barrier to the voluntary disclosure, as the firms do not prefer to be exposed to the competitors, although they can get such information from other sources such as: trade journals or trade conferences (Graham *et al.*, 2005). Competitors are using the disclosed information to change their product plans which restricts the level of voluntary disclosure (Lev, 1992; and Daeeough, 1995). The proprietary costs appear if the company is surviving in an increased competition or government regulations (Meek *et al.*, 1995).

Proprietary costs arise due to the existence of proprietary information. Proprietary information is value-relevant private information to the price of firm's shares, or traded debt in capital markets (Cormier and Gordon, 2001). Proprietary information may be used by third parties (e.g. employees, customers, suppliers, and competitors) to enhance their interests. Therefore non-disclosure of proprietary information can result in lower third party costs (Cormier and Megnan, 1999).

The proprietary cost is an incentive not to disclose information that might affect the firm's competitive position, even if it faces a high cost of capital. Therefore, this constraint is sensitive to the nature of competition in the firm's product market (Verrecchia, 1983; Darrough and Stoughton, 1988; Wagenhofer, 1990; Feltman and Xie, 1992; Newman and Sansing, 1993; Darrough, 1993; Gigler, 1994).

4.3.2.3 Political Costs

It is stated that 'economists have questioned whether the public interest assumption is consistent with observed phenomena. They have proposed an alternative assumption- that individuals involved in the political process act in their own self interest (the self-interest assumption). This assumption yields to implications that are more consistent with observed phenomena than those based on the public interest assumption' (Watts and Zimmerman, 1979, p.283).

Voluntary disclosure makes the regulators pay more attention to the firm and that would costs the firm such costs that they could avoid by not disclosing this type of information (Watts and Zimmerman, 1978, 1986). Firms with high inside ownership are more concerned about regulatory costs (Graham *et al.*, 2005). Furthermore, voluntary social disclosures can be explained as effort to reduce the political costs of the disclosing entities (Ness and Mirza, 1991; McComiskey, 1995).

4.3.2.4 Agency Costs

The agency problem justifies the lack of full disclosure and avoiding the voluntary disclosure. The managers limit the voluntary disclosures to avoid unfavorable attention of stakeholders (Nagar *et al.*, 2003; Berger and Hann, 2003).

4.3.2.5 Disclosure Precedent

One of the main constraints of voluntary disclosure is the desire to avoid setting disclosure precedent that might be difficult to be maintained in the future (Graham *et al*, 2005). That indicates that the management should be aware that the level of disclosure in a specific time would lead to having at least the same level or above, and that the stakeholders would not accept any level below the previously disclosure level in the previous period.

The disclosure precedent constraint is viewed in a similar way to the commitment cost associated with increasing voluntary disclosure (Diamond and Verrecchia, 1991; Verrecchia, 2001). Therefore, there is the cost of losing the firm's reputation towards its stakeholders by not maintaining the same level of voluntary disclosure level they are used to before.

4.4 THE ROLE OF VOLUNTARY CORPORATE DISCLOSURE IN REDUCING THE INFORMATION EXPECTATIONS GAP

Liggio (1974) defined the expectations gap as 'the difference between the levels of expected performance as envisioned by both the independent accountant and by the user of financial statements' (p.27). There are many items that are not disclosed in the annual reports resulting in the existence of information gap between stakeholders' expectations and the disclosures provided by the firm (Hooks *et al.*, 2002). Stakeholder theory is concerned with how the organization manages its stakeholders. Thus, the disclosed information is assumed to be part of legitimacy and/or social construction process. That's justifying the voluntary disclosure that is released by the organizations to satisfy their stakeholders (Gray *et al.*, 1997).

Verdi (2006) defined the financial reporting quality as the role of financial reporting in providing information about firm's operations, especially cash flows, to be offered to the stakeholders. The FASB Statement of Financial Accounting Concepts No.1 described that the financial reporting should 'provide information that is useful to present and potential investors in making rational investment decisions and provide information to help present and potential investors in assessing the amounts, timing, and uncertainty of prospective cash receipts' (par. 34 & 37). However, Parker (1986) mentioned that the corporate annual reports represent a process of mass communication.

Furthermore, the financial accounting standards are developed in order to ensure that the stakeholders are provided with relevant, reliable, and timely information on which they can make their decisions. There are barriers that contradict the provision of such information to the stakeholders found in the information asymmetry problem and the agency theory (Canibano *et al.*, 1999). Information asymmetry assumptions are underpinnings of agency theory and when applied to stakeholder theory, it explains the conflicts of interest, and strategic behavior of the organization (Eisenhardt, 1989). Therefore, information provision, or access to it, is considered to be a proxy of power (Huse and Eide, 1996). Power differentials occur not only between different types of stakeholders, but also within the same stakeholder category. The large firms' sizes and the dispersal of stakeholders increased information asymmetry between more informed and less informed stakeholders, as large investors (more powerful) acquire monopoly over information (Lev, 1988).

Accountability is defined as 'the duty to provide an account (by no means necessarily a financial account) or reckoning of those actions for which one is held responsible' (Gray *et al.*, 1996, p.38). Therefore, annual reports and financial statements are considered to be mechanisms for discharging accountability. The process of providing information is based on the society defined relationship between directors and shareholders, which provides these shareholders with a right to information (Gray *et al.*, 1996). Therefore, accountability 'focuses on the impact of actions of the entity on the stakes of individuals, and information that relates to these stakes'. The nature of the information would depend on the type of actions based on the size and industry of the entity (Joseph, 2007). However, unless the principal can enforce the accountability, then no accountability is to be provided, which is considered to be 'positive accountability' (Tricker, 1983; Stewart, 1984).

The information provision is referred to the accountability which is defined as 'the provision of information between two parties where the one who is accountable, explains or justifies actions to the one to whom the account is owed' (Gray *et al.*, 1997, p.333). The accountability framework is described in principal and agent terms, where principal refers to one who holds to account, and agent refers to the one who is held accountable. This framework assumes the existence of contractual obligation between the two parties (Gray *et al.*, 1987, 1988, 1991; Laughlin, 1988; Woodward *et al.*, 1996).

Accountability information covers different areas of accounting. The traditional use of information is the fulfillment of the stewardship objectives. This area includes that corporate resources actually exist are used for legitimate and legal purposes, and that assets and resources have been accounted in a proper way. Auditors play a vital role in this area by validating and verifying the organization's stewardship reports (Bromwich, 1992). Using an agent–principal model, the selection information systems for accountability purpose differ from those for selecting information systems for decision making (Gjesdal, 1981).

Moreover, accountability also is related to the 'social contract', the idea that business owes its existence to society, which is part of the normative approach of the stakeholder theory (Gray *et al.*, 1988; Donaldson, 1982; Donaldson and Preston, 1995). However, the accountability's definition tends to be more inclusive of other stakeholders in recognition of the social contract, as it explain and justify the acts and omissions for which one is responsible to people with legitimate interest (ISEA, 1999). Therefore, accountability referred to whether stakeholders have sufficient, accurate, understandable and timely information on which to rely in their different actions (Cohen, 1995). The accountability framework extends the current framework by including supplement information to assists accounting bodies to create the supplement reports (Joseph, 2007).

The Global Reporting Initiative (GRI) states that 'A primary goal of reporting is to contribute to an ongoing stakeholder dialogue. Reports alone provide little value to inform stakeholders or support a dialogue that influences the decisions and behavior of both the reporting organization and its stakeholders' (GRI, 2002, p.9). Thus, accountability supports stakeholders' relationship with the firm by providing information for different decision. Despite of the provided unnecessary information for other stakeholders, this information would provide assurance that the firm is operating in the interest of the society as a whole (Joseph, 2007). Therefore, accountability narrows the information asymmetry between the management and different stakeholders, and in between the different categories of stakeholders (Lev, 1989). Thus, accountability would increase the awareness towards the complexity of information disclosures and reduce the information asymmetries. In doing so, accountability would also serve to narrow asymmetries of power between different classes of stakeholders (Joseph, 2007).

Miller and Bahnson (2002) stated that 'if management truly views shareholders as partners, and places creating value for them near or at the top of its primary responsibilities, then it should treat them as such. Management should give shareholders information on strategic plans and performance and activity solicit their feedback on both. If shareholders don't like the strategies and register dissatisfaction with the company's performance, management should listen to their complaints and quickly learn what has caused them' (p.25).

Jensen and Meckling (1976) defined an agency relationship as 'a contract under which one or more persons (the principal (s)) engage another person (the agent) to perform some service on their behalf which involves delegating some decision making authority to the agent' (p.5). This contract requires the firm (agent) to disclose relevant information that enables the investors (principal) to monitor compliance and the contractual agreements, and to ensure whether the firm is managing the resources in the interest of the investors (Healy and Palepu, 2001). There are monitoring costs associated with the monitoring process. These costs are paid by the principal to measure, observe, and control the agent's performance (Fama and Jensen, 1983).

However, Burkat *et al.* (1997) viewed that too much monitoring would results in constricting the managerial initiative. Moreover, the agent may provide voluntary information to reduce the bonding costs (expenses incurred to ensure that the agent does not undertaking actions not in the principal's interest) and attract future investors to invest in the company (Barako *et al.*, 2006).

The new entrepreneurs and the existing companies would like to attract household savings to fund their business ideas and future investment opportunities. Matching savings to investment opportunities faces two complications. First, entrepreneurs have better information than savers about the different investment opportunities. Therefore, there is an existence of information problem due to the information asymmetry or 'lemons' problem between the entrepreneurs and the savers. Second, there is an agency problem between the entrepreneurs and the savers due to the conflict of interests of the two parties (Healy and Palepu, 2001).

Scott (2003) differentiated between two major types of information asymmetry. The first type is the adverse selection which occurs when the firm managers and other insiders having information advantage by acquiring more information about the current condition and the future forecasts than the investors and the other outsiders. The second type is the moral hazard which occurs as a result of the separation of ownership and control that characterizes the large sized firms, as the insiders can observe the business transactions than the outsiders. The two types of information asymmetry are considered to be the main agency problems.

The equity shares of the firm are sold to the investors to raise cash required for investment opportunities. To do so, the firm is exposed to transaction cost which is referred to the information asymmetry component of the cost of capital. In perfect competition the well informed investor will be able to exchange assets with the firm with low cost of capital. In other words, the higher transaction costs, the less the investors would be willing to buy the firm's shares which reduce the available liquidity and increase the cost of capital (Verrecchia, 2001).

Epstein and Palepu (1999) provided additional evidence about the existence of the information gap between financial reporting practices and financial statement's users. They considered that the solution is to provide more voluntary disclosures that 'tell the corporate story' to the users. It is believed that companies tend to disclose the required information unless they have good news to be disclosed. Taking in consideration corporate disclosure credibility, full disclosure must occur whether having good or bad news.

Moreover, the main motivation to disclose information by the management is to reduce the cost of capital, as additional information reduces investors' uncertainty (Gray *et al.*, 1995b). Scott (2003) stated that 'we can think of financial reporting as a device to reduce the adverse selection problem, thereby improving the operation of securities markets and reducing incompleteness' (p.55). This is applied by adopting full disclosure policies to increase the usefulness of financial reporting, and to expand the available information for the public to reduce the ability of insiders to profit from their information advantage.

In addition, the information dialogue is defined as the type of dialogue where the company aims to be transparent about its activities and policies and inform stakeholders about them. It is 'dialogue' only in so far as the stakeholders are able to respond by asking questions of clarification'. However, it is not expected that the company learn from stakeholders, and little or no expectation to manipulate or educate stakeholder's view. Most early the corporate social and environmental reports have satisfied the minimal stakeholder dialogue over the relevance and materiality of the information provided (Bendell, 2000). Moreover, one of the most visible drivers to disclose the positive social and environmental performance is that releasing such information provides market signals and corporate financial gains (Murphy and Bendell, 1999).

Some researchers have analyzed the connections between information disclosure and political behaviour. They found that the people are not motivated by the information itself, but instead they are motivated by the relationship between the information and their prior expectations. Meanwhile, if the new information does not conflict with prior expectations, it would not be expected to see a change in behaviour. Otherwise, new information differs than the people prior expectations, would considered to be a motive to change the behaviour and act in a different way (Stephan, 2002).

Information asymmetry between the firm and investors is important driver of firm's cost of raising capital required to finance its investment opportunities (Verdi, 2006). Furthermore, Information asymmetry prevents the efficient selection of the worthy investments. As based on the principal – agent conflict, the investors would select the investment opportunities that maximize their welfare regardless the interest of the shareholders. Therefore, the firm has the incentive to reduce information asymmetry to reduce the cost of capital (Berle and Means, 1932; Jensen and Meckling, 1976). Moreover, the primary role of voluntary disclosure is to correct investor's perceptions (expectations) regarding current or future performance (Graham *et al.*, 2005).

Diamond and Verrscchia (1991) and Baiman and Verrscchia (1996) indicated that the greater disclosure the lower cost of capital. While Bushman *et al.* (1996) showed that the less than full disclosure include risk sharing and agency costs, while increasing disclosure is associated with proprietary costs. The regulated disclosure is motivated by concerns other than market failure (Leftwich, 1980; Watts and Zimmerman, 1986). Moreover, the Accounting Standards Committee (ASC) (1986) considered the historical cost information may appear adequate for stewardship role, but it would be unsatisfactory for decision making. Therefore, the regulated disclosure individually would not reduce the information asymmetry.

The firms disclose more information in order to attract capital in financial market (Cooke, 1991). While Berman (1998) argued that 'the trust between managers and key shareholders can lead to competitive advantage for firms' (p.54). However, the regulatory mandates raise the disclosure levels, but the higher disclosure companies already have voluntary disclosures which provide those companies with competitive advantage over the other competitors. Therefore, the mandate of the voluntary disclosure would not enhance the disclosure, but results in loosing this competitive advantage (Einhorn, 2005). Firms release voluntary disclosures motivated by their wish to inflate the investor's expectations about the firm value and thereby maximizing the firm's stock price (Einhorn, 2005).

Voluntary disclosure may signal company value as managers have judged the disclosure to have value than its cost. But if disclosure is mandated, it does not signal value as the reason of this disclosure is just following the regulations without any clear implications that the benefits are more than the cost. Therefore, voluntary disclosure is enhanced, but that may not achieve the expected advantage as the managers may vary from any performance criteria implied by it (Ferreira and Rezende, 2006). Information disclosure create value in two ways; directly by narrowing the information gap (asymmetry) by decreasing investor's uncertainty (agency costs), and indirectly by enhancing value-creating through the reduced cost of capital (Lev, 2000).

Voluntary disclosure reduces information asymmetry (information gap). This reduction occurs as a result of the investor's relative confidence that the stock transactions occur at a fair price which increase the stock liquidity (Diamond and Verrecchia, 1991; Kim and Verrecchia, 1994). Better disclosure practice improve analyst's forecast accuracy of next year's earnings (Lang and Lundholm, 1996).The financial information alone did not correlate with stock prices and returns, but the non-financial information alone (such as: population size and market penetration) did (Amir and Lev, 1996).

Some information are proprietary, so investors accept not releasing it, but if they believe that managers have non-proprietary information that is not released they would have the impression that it is unfavourable or bad news. Therefore, the investors believe that the market value of the company is overstated which results in the fall of the stock price of the firm (Verrecchia, 1983; Dye, 1985).

Regarding the credibility of the environmental reports, KPMG (1993) states that 'disclosing the bad news as well as good is very important if companies want to gain credibility for their reports. Otherwise, the reports can appear biased and akin to public relations tools. Even if there is considerable data, an otherwise 'good' report will invite suspicion on all its disclosures if companies are not "up front" about the problems they are facing, including fines and prosecutions'.

However, the greater voluntary disclosure should lower information asymmetry, and therefore reduce the cost of capital (Diamond and Verrecchia, 1991). In addition, voluntary disclosure reduces uncertainty and therefore reduces the information asymmetry problem and lead to the reduction of the cost of external financing (Healey and Palepu, 1993, 2001).

Referred to the previous discussion, it can be concluded that voluntary corporate disclosure is a proxy of the existence of the information expectations gap as an indicator of the occurrence of the information asymmetry problem. Therefore, the level of disclosure in the Egyptian annual reports would be able to justify the presence of the information asymmetry problem.

4.5 THE ROLE OF AUDITED VOLUNTARY CORPORATE DISCLOSURE IN REDUCING THE AUDITING EXPECTATIONS GAP

The expectations that assurance affect investors' judgment stem from the argument that independently audited information reduces information asymmetry and decreases uncertainty (Wallace, 1987). Therefore, investors increase reliance on voluntary disclosure when assurance is provided on this type of information (Coram, 2004). Furthermore, Abdel-khalik (1993), Chow (1982), and Watts and Zimmerman (1983) provides significant evidence that shows the increasing demand for auditing regulated and unregulated information to provide assurance to stakeholders. Hunton *et al.* (2000) found that auditor provided electronic commerce assurance has a positive impact on earning forecasts and stock price estimates.

Reporting growth, especially the environmental, social, and sustainable reporting, is driven by a realization that growing levels of disclosure are being undetermined by a credibility gap arising from the lack of confidence in both data and the reporting organizations (Doane, 2000; Swift and Dando, 2002; Dando and Swift, 2003). In addition, there is a concern about the provided information, especially voluntary disclosures, which is the credibility and the verification of the accuracy of this information in the absence of any mandatory requirements, and the caution concerning the bias towards disclosing only the good news (Deegan, 2005; Deegan *et al.*, 2002; Guthrie and Parker, 1990; Neo *et al.*, 1998).

In the absence of credible information, stakeholders tend to assume the worst. As a result, stakeholders will discount the firm's stock prices, and would not react passively to the lack of information. However, they would choose to privately collect and analyze data. Due to the high cost of collecting and analyzing such data, only sufficient stakeholders with available resources would do so. Consequently, unsophisticated stakeholders are driven out of the market that becomes less efficient. The remaining stakeholders in the market would face high transaction cost, lower trading volume and illiquidity. Therefore, they bid down a firm's stock price (Karpoff, 1986; Lev, 1988).

Agency theory provides the best link between the voluntary disclosure and audit quality. Accordingly, one monitoring device that shareholders can use to observe manager's behavior is appointing external auditors. An audit firm influences the amount information disclosed in financial statements (Singhvi and Desai, 1971). Moreover, referred to the accountability paradigm, the agent or the management cannot be trusted to provide information that may serve stakeholders interests. Therefore, accountability is not essentially concerned with discretionary or voluntary disclosure (Swift, 2001). Furthermore, the use of reputable auditor is a reflection of the associated agency costs with the disclosure decisions and a signal to the market that the information disclosures are of high quality (Craswell and Taylor, 1992).

In order to enhance trust in reporting assurance, providers need to be well connected to the stakeholders and understand their issues well (Henriques, 2003). Therefore, key stakeholders must be identified clearly as addressing assurance statement to specific stakeholder has implications for assurance on materiality of the information provided. The information is deemed material if its omission or misrepresentation could influence the decisions and actions of stakeholders (Owen and O'Dwyer, 2004). In terms of stakeholders, materiality is a crucial issue in the area of assurance. It is stated that 'if stakeholders don't think the information is relevant or material, it just won't count' (Zadek, 2003).

Moreover, KPMG (2002) suggests that the verification arises from 'the demand for reliable and credible information from management, for managing the company's environmental and social risks, and from stakeholders who want assurance that the report truly represents the company's efforts and achievements' (p.18). The Association of Chartered Certified Accountants (2003) states that 'all organizations want to show themselves in the best possible light. ACCA believes that independent external assurance is a vital part of the credibility and trust building process. The role of independent assurance is to insure that the reporter presents an account that is fair, complete, unbiased and relevant' (p.7).

Auditing has different objectives, such as the provision of independent opinion upon the company's financial statements, improving management performance, and controlling and monitoring the company's activities. The studies addressed the importance of auditing in providing credibility to accounting information which assists the different stakeholders in making their decisions (Owen et al., 2000; Burnet-Hall, 1994(a); Wood, 1991; Brown, 1962; Gwilliam, 1988;; Wallace, 1987; Show *et al.*, 1980; Coopers and Lybrand). The great importance of the auditing function to investors is that it facilitates the raise of corporation's capital and conducting their business affairs (Schuetze, 2004). Auditors play an important role in verifying and validating the enterprise's stewardship reports (Bromwich, 1992). Therefore, the purchase of audit results in having reported information likely free from misrepresentation and thus more credible (Barton and Waymire, 2003).

In addition, Karapetrovic (2002) defined a universal audit as 'an independent and documented system for obtaining and verifying material audit evidence, objectively examining the evidence against the stated audit criteria based on audit risk and reporting the audit findings to the client' (pp.150-151). Such audit definition includes not only financial audit, but includes other diversified types of audits including the voluntary disclosures.

Miller and Bahnson (2002) stated that 'incomplete information can be caused by omissions, misrepresentations, or simply lack of trustworthiness. Even if the managers are actually telling the truth, no one will act on it if they don't trust the reports' (p.23). Moreover, the uncertainty about the past and present leads to uncertainty and lack of confidence about the future predictions. Therefore, the investors and creditors are demanding a higher rate of return to compensate for the uncertain outcome representing high cost of capital for the managers. Furthermore, to reduce the information asymmetry, the investors and other outsiders are served by relevant information that enables them to assess the firm's future. In addition the provided information needs to be reliable and free from bias or other management manipulation (Scott, 2003). In the sense of agency theory, voluntary disclosure presents an excellent opportunity for managers who have access to firm's private information to make credible and reliable communication to the market, which in turn optimizes the value of the firm (Barako, 2006).

The attribution theory explains how users perceive the voluntary disclosure of non-financial information (Kent and Martinko, 1995). Koonce and Mercer (2002) used the attribution theory to show the users' perception towards the voluntary disclosures. It is expected that investors would discount positive disclosures as self-serving but would not do so for the negative disclosures as they are considered not to be self-serving. Based on the attribution theory, users would be more uncertain about the validity of the self-serving information and discount it. Thus, owners face moral dilemmas due to the inaccuracy to evaluate and determine the value of decisions made. That's because the agent takes advantage of the lack of observability of his actions and practices to enhance his personal goals referred to the agent-principal conflicts (Barako, 2006).

Assurance would have positive effect on users' stock price estimates and forecasts in case of the positive disclosures due to the reduction of uncertainty using information assurance. While in case of negative disclosures assurance would not make any difference to users (Coram, 2004). Furthermore, audited information is more credible than un-audited information (Johnson *et al.*, 1983; Libby, 1979; Pany and Smith;

1982). Provision of assurance increases user's perceptions of non-financial reliability as the independently audited information reduces information asymmetry and decrease uncertainty. Therefore, the value of assurance on disclosure is not independent of signal provided by disclosure (Coram, 2004).

Investors found it difficult to evaluate the impact of the voluntary un-audited disclosures on future earnings (Rajgopal *et al.*, 2003). Furthermore, the Elliott Committee (1997) suggested that there are new opportunities for assurance services to add value to the external audit as a result of the new types of information used by decision makers. It defines assurance services as 'independent professional services that improve the quality of information, or its context, for decision makers'.

Voluntary enhanced annual report disclosure does not affect the informative power of the current stock prices. This result shows that the usefulness of voluntary disclosure is a questionable issue (Gelb and Zarowin, 2002). Investors evaluated the audited financial reporting as more credible than the un-audited information were more optimistic about firm's future earnings based on the audited financial reporting (Hodge, 2001). Therefore, information relevance includes the traits of timeliness and predictive value for decision making, while reliability contains the traits of representational faithfulness, verifiability, and neutrality which differ with respect to the nature of items. Such traits are easy to attain for financial information but not for intellectual capital and social costs which needs to be quantified (Joseph, 2007).

Auditing is a way to ensure information reliability and credibility. Therefore, managers making voluntary disclosure might also voluntarily hire an auditor.

Moreover, having an audit makes manager's disclosures are more credible to users than they would be without an audit. Hence, the society requires auditing voluntary disclosures than GAAP audit, which provides greater protection of users (Power, 1997, 1999; Jamal and Sunder, 2006). Furthermore, auditors, as well as users, needs to pay more attention to non-financial information, but perhaps more attention is paid by auditors to focus on GAAP (Bell *et al.*, 1997).

The firm incurs a disclosure cost in case of disclosing private information. The disclosure costs include the preparation costs in addition to the cost of contracting an auditor (Verrecchia, 1983). Incurred auditing cost insures the trustfulness of the private information as it is the only way to make voluntary disclosure credible to the public. The importance of auditing of voluntary disclosure is that bad information is kept private while good information is publicity disclosed. Therefore, cost of disclosure increases more as information becomes not valuable for disclosure (Suijs, 2005). The manager's incentive for disclosing bad information is driven by firm's reputation and litigation threats besides the proprietary costs that face the firm (Skinner, 1994).

Voluntary disclosures have low and in some cases negative coefficient with future earnings which indicates that voluntary disclosure misleads analysts' perception regarding the firm's future. These results raised a question about the value relevant information about the future earnings (Banghøj and Plenborg, 2006). In the sense of agency theory, the managers who have better information than the other outsiders can make credible and reliable communication to the market to enhance the value of the company. This enhancement of the company's value in the market reduces monitoring costs and in turn reduces the agency costs. Therefore, the more accurate and reliable information the companies disclose, the better companies' perception received by the public (Barako *et al.*, 2006). The accounting reports can affect the real decisions made by managers and other users, rather than just reflecting the results of these decisions. This argument illustrates the importance of disclosure in directing stakeholders to different decisions stimulating the relative importance of disclosure credibility (Zeff, 1978).

Audit effectiveness adds value for investors as research shows that capital providers require firms to hire an independent auditor as a condition of financing, even when it is not required by regulation (Healy and Palepu, 2001). Moreover, banks require firms to present audited financial information, even for private companies. This shows that capital providers regard auditors as enhancement for the credibility of the presented information (Leftwich, 1983).

Voluntary disclosure reduces information asymmetry between the managers and outside investors. Reduction of information asymmetry reduces the cost of capital by reducing information risk but this solution is restricted by the costs associated with credibility of voluntary disclosure (Barry and Brown, 1985, 1986; Merton, 1987). The value of the voluntary disclosure in the capital market depends on the degree of credibility of the disclosed information. As the voluntary disclosure is self-serving, it is not clear whether these disclosures are credible (Healy and Palepu, 2001).

In contrast, Jensen and Meckling (1976) argued that agency theory explains why accounting reports are provided voluntarily to creditors and stockholders, and why independent auditors are engaged by management to testify and verify the correctness and accuracy of the provided reports. It is clear that managers are willing to incur costs in order to improve the credibility of accounting reports before doing so as a law requirement. Moreover, in the sense of agency theory, minimizing agency monitoring costs is considered to be economic incentive for managers to report reliable accounting reports to the ownership (Wolk and Tearney, 1997).

Most of the studies as Waymire (1984), Ajinkya and Gift (1984), and Pownall and Waymire (1989) found that stock prices react positively to the management forecasts of earnings increases, and vice versa. It is observed that the credibility of voluntary disclosure is measured by the accuracy and stock prices effects of management forecasts. However, management forecasts accuracy can easily be verified by investors by actual earnings realization without need for the voluntary disclosures.

Dye (2001) stated that 'the theory of voluntary disclosure is a special case of game theory with the following central premise: any entity contemplating making a disclosure will disclose information that is favorable to the entity, and will not disclose information unfavorable to the entity' (p.184). Managers may disclose information that reduces a firm's stock price and delay disclosing information that increases firm's stock price (Aboody and Kaznik, 1999). Furthermore, managers are disclosing bad news prior to management buyout, or prior to union negotiations. This shows that voluntary disclosure is acting as stock prices control instrument rather than reducing information asymmetry (Liberty and Zimmerman, 1986). Moreover, the presence of multiple audience (stakeholders), besides the investors in the capital market, such as competitors in the product market, consumers, suppliers, employees, labor unions, creditors, and regulatory authorities, managers may disclose bad news to inflate the investor's expectations by deflating the expectations of the other audience (Darrough and Stoughton, 1990; Wagenhofer, 1990).

Watts and Zimmerman (1982) stated that 'an audit will be successful in changing expectations and hence reducing the opportunistic behavior costs (agency costs) borne by the managers only if it is expected that the auditor will report some discovered breaches of contract. The probability that the auditors will report a discovered breach is effectively enhancing the auditing profession's definition of independence' (p.11). Moreover, Elliott (1998) stated that 'the audit provides assurance that an information set presented to investors and creditors is reliable. But the market place need for high-quality information is far greater than just the need for reliable historical cost-based financial statements' (p.2). Moreover, the Elliott Committee (1997) identifies the opportunity to provide assurance services in relation to risk assessments, business performance measurements, and information system reliability. The heart of the minimum auditing is to create value by reducing investors' uncertainty and this improves the overall financial reporting quality rather than just attesting to management compliance with GAAP, and this causes their clients satisfaction (Miller and Bahnson, 2002).

The market places a stock price premium on independently audited information (Dopuch *et al.*, 1986; Willenborg, 1999). Therefore, the provision of information assurance services is a natural extension of the traditional financial audit role (Elliott, 1998). Quality financial reporting revolution is an important key to increase the auditors' ability to add value by reducing uncertainty about the quality of information included in management's reports rather than just ensuring management's compliance with technical GAAP (Miller and Bahnson, 2002). Under the disclosure principle, the released information must be credible. One way to secure the credibility is that the released information attested to by third party as an auditor (Scott, 2003). However, it is stated that 'more assurance will not necessarily mean more and better accountability, but merely more 'value added' for management as they manage key risks imposed by various stakeholders group who need to be controlled' (Power, 1997, p.127).

The Global Reporting Initiative's Sustainability Reporting Guidelines (GRI 2002) emphasized the need for independent assurance to add to the credibility of sustainability reports: 'A range of factors influences the perceptions and expectations of users about the credibility of an organization's sustainability report. Consultation with stakeholders is the best way to ascertain stakeholder perceptions and expectations about building credibility' (pp.17-18). One of the key criticisms of the voluntary social, ethical and sustainability reports is the existence of the huge audit expectations gap (Kamp-Roelands, 1999). Therefore, the assurance provision for social and environmental reporting, as one of the voluntary disclosure categories, is necessary to add credibility and reduce the audit expectations gap (Gonella and Woo, 2000; Lewellyn, 2000).

Moreover, the stakeholders are the main concern of the auditor in performing his duties towards assuring the credibility of the voluntary disclosure. Therefore it is stated that 'the assurance provider evaluate whether the reporting organization has responded to stakeholders concerns, policies and relevant standards and adequately communicated these responses in its report' (AccountAbility, 2003, p.18). However, the agency problem of adverse selection or hidden information appears if the auditors do not discover this information. To overcome this problem, auditors seek to signal to their quality by their actions in offering quality services (Bromwich, 1992).

Furthermore, the need for external verification and assurance is supported by several key assertions. First, external verification improve environmental reporting because of the scrutiny inherent in such an examination. Second, external verification of periodic environmental reports will provide additional credibility and assurance to the annual financial reports with environmental considerations. Third, the threat of litigation and other actions by shareholders or regulatory authorities for misrepresentations in the periodic environmental reports may be reduced by third party verification. Therefore, external verification may prevent corporations from disclosing inaccurate or misleading information and ensuring that the disclosure is reliable. Fourth, without credibility offered by the external verification, some investors may consider the environmental reporting is a sort of 'green wash' (Aeppel, 1993; Greer and Bruno, 1996). In addition, the corporations in order to secure their reputations against the risk of disclosing untruthful information, many of them now have their disclosure verified (audited) by independent experts in social, environmental, and ethical field (Lann, 2006).

The auditing profession should widen its scope to encapsulate environmental issues as to keep its position as a source of credibility of information for the diversified stakeholders. Therefore, there is a crucial need to activate the role of audit profession regarding the environmental issues remain to maintain the auditor report of being reliable by the diverse users (Mousa, 2004). The auditor's role in reducing the uncertainty about the low-quality information in GAAP financial statements would not be useful as providing a greater degree of comfort in consuming and relying on the unregulated reporting. It is believed that the new supplemental unregulated reporting offers a special opportunity to auditors to add much more value to their clients (users) by quality financial reporting consultation services (Miller and Bahnson, 2002).

The Federation des Experts Comptables Europeens (FEE), the body of accounting professions in Europe have published its assurance on sustainability report and stated that 'the assurance provider issues a report that enables users to place more credibility on the information reported by the company. Each user of the report may benefit through being able to take decisions based on information in sustainability report with less uncertainty about the information'. Moreover, the FEE report desire is to avoid creating an expectation gap 'whereby a user mistakenly assumes that there is more assurance than is actually present' (FEE, 2002, p.17).

Moreover, only the supply of financial information leads to unproductive behaviors and outcomes, while providing the information demanded by the capital markets produce changes in the roles played by managers, auditors, financial statement users, standards setters, and regulators (Miller and Bahnson, 2002). Adams and Evans (2004) provided some assurance guidelines as key principles for the assurance of ethical, social, and environmental reports. The aim of these guidelines is to reduce the audit expectations gap. To apply such assurance the stakeholders need more power to issue such appointment of auditors.

Based on the previous discussion, it can be argued that expanding the auditor's role and responsibility, to include the auditing of voluntary disclosure, is expected to reduce the audit expectations gap more effective rather than the traditional approaches (ie. auditor's report, users' education, and standards settings).

4.6 CONCLUSION

It is concluded from the previously presented chapter that there are different theories that justifies the different voluntarily disclosure practices. First theory is legitimacy theory which argues that the different organizations are disclosing more information voluntarily as to satisfy the community and environment it is operating in. Therefore, legitimacy theory argue that any sort of additional environmental disclosure would satisfy the organizational environment regardless the conflict of interests that could occur in between the stakeholders whom part of the organizational environment assuming that they got equal power and same interests. Moreover, legitimacy theory the organizational community would be satisfied by environmental, social and ethical disclosures regardless the role of the other categories of voluntarily disclosed information.

Second theory is signaling theory which indicates that additional disclosures would signal to the relevant parties and the capital market that the organization is disclosing such information to reduce information asymmetry. However, signaling theory ignored the credibility of these disclosures and the way it is going to be perceived by the relevant parties.

Third theory is conjunction between stakeholder and agency theories to form the stakeholder-agency theory. Agency theory would justifies the agent-principal relationship which leads to the existence of information expectations gap between management (agent) and shareholders (principal) from one side, and auditing expectations gap between auditors (agent) and shareholders (principal) from the other side. Hence, it is shown that shareholders are considered to be the common principal for both gaps. However, both agents, management and auditor, are required to satisfy not only the interests of the shareholders, but they are required to satisfy the conflicting interests of the different stakeholders. Therefore, agency theory alone would not describe these conflicting interests of other stakeholders, besides shareholders, which requires conjunction between stakeholders and agency theory where it is stated by Hill and Jones (1992) that stakeholder-agency theory is considered to be a generalized theory of agency. This would be comprised in the methodological chapter when selecting the research sample that reflects the different perceptions of stakeholders with their different backgrounds and interests.

The previous discussion specified the meaning of the voluntary corporate disclosure its incentives, constraints, and its main categories in the light of the stakeholder-agency theory. The presented studies provide different evidences regarding the role of this audited voluntary disclosure in reducing both information expectations gap and auditing expectations gap. Many studies focused on the role of disclosure in reducing the information gap and solving the information asymmetry problem. The interesting point is that due to the agency conflicts, some studies showed that this role is still questionable due to the credibility and reliability of this type of disclosure.

Moreover, such studies requested the provision of an accepted degree of credibility and assurance to the voluntary disclosure to be reliable. At this extent appears the need for a third independent party to be involved in the voluntary disclosure provision process. This party is the auditor whom required extending his role to include auditing the voluntary disclosure and providing assurance services to his/her clients. Therefore, the need for the voluntary disclosure is associated with the need for additional auditing and assurance services to ensure the credibility of the disclosure and its usefulness for the decision-making.

As a result of expanding the role of the auditor to include additional services towards satisfying the needs of the users, regarding the assurance of the voluntary disclosure, leads to reaching some of the user's expectations towards his roles and responsibilities. It is expected that this approaching from satisfying some of the users' needs and expectations would reduces the auditing expectations gap. To this extent, the research argues that the audited voluntary disclosure is playing dual roles. First, reducing the information expectations gap and solving the problem of information asymmetry. Second, role is expanding the auditor's role to include the provision the auditing and assurance services for such disclosure, which in turn might result in the reduction of the auditing expectations gap.

Therefore, it is concluded that theoretically voluntary disclosure needs to be audited as to provide assurance for this type of disclosure. Consequently, credible voluntary disclosure would reduce the information expectations gap and solve the information asymmetry. While auditors performing the extended roles and responsibilities to provide voluntary disclosure assurance, they would satisfy the diversified annual reports' users and in turn reduce the auditing expectations gap.

As a result of this conclusion by prior studies, this argument needs to be examined empirically. The next part of the study is concerned by examining the validation of this theoretical argument. However, the empirical study needs to link between the audited voluntary disclosure as a proposed solution, and the auditing expectations gap as an existing problem that needs to be solved.

CHAPTER FIVE

RESEARCH METHODOLOGY

5.1 INTRODUCTION

The cornerstone of the current research is the existence of the auditing expectations gap in Egypt investigated recently by Dixon *et al.* (2006). Therefore, the research would try to provide new solution for this problem.

It is expected that the results of the research would be limited to the Egyptian context. The Egyptian economy is considered to be a unique system which has passed over different reform programs restructuring the Egyptian business culture as shown before in chapter two entitled background information on the Egyptian economy. The research would examine the effectiveness of the different solutions, beside the proposed solution, of reducing the auditing expectations gap. Therefore it would depend on primary and secondary data when applying the empirical analysis.

The main objective of this chapter is to justify the used methodology that would be followed in the study's empirical analysis in the light of the research ontological and epistemological positions that stems from the employed theoretical background of the research shown by the theoretical framework chapter. Also the methodology shows the linkage between the two investigated empirical studies and justifies the vital importance of exploring the two sequential empirical chapters in the presented form.

Moreover, the research focuses on measuring the level of voluntary disclosures included in the annual reports of the Egyptian companies. It is argued that auditing this sort of voluntary disclosures would be a proposed solution for the reduction of the auditing expectations gap in Egypt investigated by Dixon *et al.* (2006). The first part of the empirical study depends on the designing a checklist that includes the main issues of the voluntary disclosure. Furthermore, the results of the checklist would form the index of the voluntary disclosure.

Furthermore, the research justifies the investigated level of voluntary disclosure by examining the different determinants of this sort of disclosure. The determinants are classified into two groups: firms' characteristics (firm size, firm profitability, and industrial membership), and corporate governance characteristics (board size and role duality). Finally, the research used the questionnaire technique to examine the effectiveness of the traditional methods of reducing the auditing expectations gap compared to the auditing of voluntary disclosures as a proposed solution.

5.2 RESEARCH PHILOSOPHY

There are different layers that link the basic assumptions to the employed methodological techniques. These layers range from the ontological and epistemological ones to the methodological techniques used to examine the research theoretical perspectives. These linked layers form a 'justification of our choice and particular use of methodology and methods is something that reaches into the assumptions about reality that we bring to our work' (Crotty, 1998, p.2).

The research process includes five layers named the research process 'onion'. The first layer is the research philosophy. Second, the research approach layer. Third, layer is the research strategy layer. Fourth, layer referred to the research time horizons. The fifth layer, data collection methods. Each layer includes different set of choices that the researcher is required to choose to imply his/her research (Saunders, 2003).

Referring to the discussion of the first research layer, it is argued by Ruddock (2001) that 'ontology and epistemology are significant in that they illustrate how research begins by outlining theoretical suppositions that are taken as given by the research. Ontology relates to how we understand the nature of reality...epistemology refers to a theory of knowledge. It is related to ontology in that the nature of the reality you set out to explore influences the sort of knowledge that you can have of it ...methodological implications follow. Observations, measurement and interpretation depend on the understanding of the ontological and epistemological nature of the work at hand' (p.27)

Therefore, the choice of the suitable research philosophy that fits with the nature of the research is based on the ontological position of this sort of research. Ontology is described as 'claims and assumptions that are made about the nature of social reality, claims about what exists, what it looks like, what units make it up and how these units interact with each other. In short, ontological assumptions are concerned with what we believe constitutes social reality' (Blaikie, 2000, p.8). Therefore, the research ontological position is referred to the answer of the question of what is the nature of the investigated social and political reality; it is a theory of being (Marsh and Stoker, 2002). There are two ontological positions objectivism (realism) and subjectivism (constructionism) (Burrell and Morgan, 1979; Hirschheim, 1985; Chua, 1986; Hirschheim and Klein, 1989; Weber, 2003).

Objectivism 'is an ontological position that implies that social phenomena confront us as external facts that are beyond our reach of influence' (Bryman, 2001, p.16). The Organization is considered to be social entities that have got a tangible reality. Therefore, it is characterised by being an object with an objective reality. On the other hand, subjectivism or construction asserts that 'social phenomena and their meanings are continually being accomplished by their social actors. It implies that social phenomena and categories are not only produced through social interaction but that they are in a constant state of revision' (Bryman, 2001, p.18). The subjectivism position argues that there is no objective reality. Therefore, this ontological position requires the construction of the research objective.

It is noted that objectivists view the organisation's culture as something that the organisation 'has'. On the other hand the subjectivist's view the culture as something that the organisation 'is' as a process of continuing social enactment (Smircich, 1983).

Epistemology is described as 'the possible ways of gaining knowledge of social reality, whatever it is understood to be. In short, claims about how what is assumed to exist can be known' (Blaikie, 2000, p.8). In other words, epistemology is the 'theory or science of the method or grounds of knowledge' (OED 2004). Therefore, the epistemological position is considered to be the technical term of the theory of knowledge, and refers to how the world is seen. In other words, it is the theory of knowledge (Marsh and Stoker, 2002). There are two main epistemological positions: positivism and interpretivism.

Positivism refers to 'working with an observable social reality and that the end product of such research can be law-like generalisations similar to those produced by the physical and natural scientists' (Remenyi *et al.*, 1998, p.32). According to this position the main objective of the theory is to generate hypotheses that can be examined. Hence, the role of research is to test theories and develop these theories if possible (Bryman and Bell, 2003). To do so, the researcher would employ highly structured methodology to facilitate replication (Gill and Johnson, 2002).

Therefore, to generate a research strategy to collect the research data it is likely to use an existing theory to formulate the research hypotheses. These hypotheses are examined and confirmed, as a whole or partly, or refused, leading to further development of the examined theory (Saunders *et al.*, 2003). The positivist approach assumes that 'the researcher is independent of and neither affects nor is affected by the subject of the research' (Remenyi *et al.*, 1998, p.33). This is considered to be a critical assumption for the data collection process and the validity of the research's results.

Interpretivism refers to 'the details of the situation to understand the reality or perhaps a reality working behind them' (Remenyi *et al.*, 1998, p.35). Interpretivist epistemology indicates that researchers have to adopt 'empathetic stance' which is considered to be a challenging task to enter the social world of the research subjects and understand their world from their point of view. This epistemological position is associated with the constructionism ontology. Interpretivist argues that generalisation is not of crucial importance (Saunders *et al.*, 2003).

Moving to the second layer, research approaches are classified in to deductive (testing theory) approach and inductive (building theory) approach (Saunders *et al.*, 2003). The deductive approach is considered to be the dominant approach in the natural sciences where 'laws provide the basis of explanation, permit the anticipation of phenomena, predict their occurrence and therefore allow them to be controlled' (Hussey and Hussey, 1997, p.52).

Moreover, Robson (2002) lists five sequential stages through which deductive research will progress:

1. deducing a hypothesis (a testable proposition about the relationship between two or more events or concepts) from the theory;
2. expressing the hypothesis in operational terms (that is, ones indicating exactly how the variables are to be measured), which propose a relationship between two specific variables;
3. testing this operational hypothesis (this will involve an experiment or some other form of empirical inquiry);
4. examining the specific outcome of the inquiry (it will either tend to confirm the theory, or indicate the need for its modification);
5. if necessary, modifying the theory in the light of the findings.

Therefore, the deductive research beginning point is the search to explain causal relationship between variables leading to the hypothesis development. Consequently, it is required to collect quantitative data, or even qualitative data, to test the developed hypothesis using a highly structured methodology to facilitate replication of the findings (Gill and Johnson, 2002).

The other alternative is the inductive approach. This approach begins with collecting and then analysing the data, the result of this analysis would lead to the formulation of a theory. Alternatively, the researcher may end with the same theory, but he/she would have gone about the production of that theory in an inductive way. Therefore, it is noted that theory would follow data rather than vice versa as in the deductive approach (Saunders *et al.*, 2003).

The current research argument is based on the agency-stakeholders theory which is considered to be an important part of the positive accounting theory (descriptive research). This sort of research has dominated since 1970s replacing normative accounting theory (prescriptive theories) prior to this date (Gaffikin, 2007). It is referred to the positive accounting theory as a neo-empirical research. That is due to the reliance on empiricism to establish theory from the best practices, as it is a systematic use of empirical evidence (Henderson *et al.*, 1992).

Ontologically neo-empirical research (positive accounting theory) adopts a strong realist (objective) position. It is believed that there is an objective reality that exists independent of any human agency (human involvement). As a result, human beings are viewed as interacting parties with reality passively, by means that they do not create reality but have to live around it. Therefore, human behaviour can be objectively observed and predicted as a respond to real world. Consequently, social order is controllable and manageable (Gaffikin, 2005).

The empiricism (positivism) is the epistemological foundation of positive accounting theory. The positivist epistemology is built on an assumption of dualism between subject and object. This position believes that it is possible to separate between the subject and the object that is required to be reached (Keat and Urry, 1975). Which indicates that role of the researcher is neutral showing that he/she does not influence what is being observed. This position is called 'theory-neutral observational language' (Gill and Johnson, 1991).

Both ontological and epistemological positions have direct impacts to the employed methodological approach. Accordingly, if the philosophical assumptions of positivism and its consequent of epistemological prescriptions are accepted, a nomothetic methodology would be suitable which means that it set out to establish law-like generalizations (Gill and Johnson, 1991).

It is argued by Zimmerman (2002) that positive accounting theory advocates believe a theory is 'succinctly stated, a theory explains what has been observed, tests empirically the hypothesis derived from the theory, and then predicts what is yet to be observed' (pp. II 417-418).

Consequently, based on the objectivist ontological position and positive epistemology, it would be suitable to use the hypothetico-deductive methodology. This methodological approach start with the development of a set of hypotheses, deduce what follows from them and then tests the conclusions to determine whether they are in fact correct.

Hypothetico-deductive methodological approach argues that data collection without hypothesis development is blind. Positivist epistemology is concerned with directly observed phenomena and with hypothetico-deductive testing of theories. The positivists develop a theory about the phenomenon and then test the theory. If the observation from the field and the theory match, the theory is true and if not, the theory is false (Keat and Urry, 1995; Giddens, 1979).

As a key underlying assumption in whether quantitative or qualitative research approaches would be appropriate. It is believed that quantitative research considers objectivity not only desirable but rather an essential aspect of this type of research. On the other hand, qualitative research believed that objectivity is not possible therefore subjectivity is acknowledged for this sort of research. Consequently, with reference to the objective ontological position of the current research, it is believed that the quantitative research would be appropriate to test the developed hypotheses deduced from the stakeholder-agency theory employed by the study.

The variable is considered to be central to quantitative research. Therefore, quantitative research uses the language of variables and is primarily concerned with the relationships between them to establish the causal structure of the variables. As this sort of research is based on the realist (subjective) ontology, variables are representation of the real world and can objectively determine the established causal relationship where the outcome can be generalized to other (similar) situations (set of variables). Moreover, while employing quantitative research the researcher remain separate from data in order to maintain objectivity (Gaffikin, 2005).

The survey technique is appropriate to this type of quantitative research and usually associated with the deductive approach (Saunders *et al.*, 2003). Surveys give a picture of what many people think or report doing and are often used in descriptive or explanatory research (Neuman, 1997). The survey technique facilitates the research of the 'what' question in the form of 'how many' or 'how much' (Yin, 2003). The logic of the traditional survey technique is strictly positivistic and the assumption of positivism is concerned with answering the 'how many' or 'how much' questions (Remenyi *et al.*, 1998).

Analytic or explanatory surveys aim to test a theory using the logic of experiment out of the laboratory into the field (Gill and Johnson, 2002). Surveys allow the collection of large amount of data from a sizable population in an economical way and give the researcher more control over the research process (Saunders *et al.*, 2003).

As a result, I am adopting an objectivism ontology and positive epistemological position because the current research is considered to be a neo-empirical research adopting a positive accounting theory (descriptive research) represented by the stakeholder/agency theory. Therefore, I am using a H ypothetico-deductive methodological approach because it fits with testing the employed theory by setting a set of research hypotheses.

Consequently, I am employing a quantitative research to be appropriate with the objectivist ontological position to examine the set of developed hypotheses.

Strategically, the research is using the survey method to gather the required data based on two time horizons, longitudinal and cross-sectional, through two different sources, secondary and primary data respectively. The previously mentioned positions are presented in figure 5.2.

5.3 RESEARCH PARADIGM

Paradigm is a way of examining social phenomena from which understandings and explanations can be gained (Saundres *et al.*, 2003). Research paradigm is based on the ontological and epistemological positions discussed above. Burrell and Morgan (1979) illustrate four research paradigms by the following figure:

Figure 5.1

Four Paradigms for the Analysis of Social Science

Radical Change

Subjectivist

Radical Humanist	Radical Structuralist
Interpretive	Functionalist

Objectivist

Regulation

Source: Developed from Burrell and Morgan (1979, p. 22).

The previous figure shows four paradigms: functionalist; interpretive; radical humanist; and radical structuralist. The four paradigms are arranged in correspond to four dimensions: radical change; regulation; subjectivist; and objectivist. Subjectivist and objectivist dimensions are discussed previously in the research philosophy section, where they present the research ontological positions. Radical change dimension adopts a critical perspective on organizational life. Regulatory perspective is less judgmental and critical. Regulations explain the way organizations are regulated and provide suggestions as to how they may be improved at present. On the other hand, radical change dimension explains organizational problems from the viewpoint of the existing state of affairs (Burrell and Morgan, 1979).

The purposes of the four paradigms are noted by Burrell and Morgan (1979) as follows:

1. Assisting researcher clarifying their assumptions regarding the nature of science and society;
2. Offering useful understanding of the way in which researchers approach their work;
3. To help researchers plotting their own route of research, to understand where it is possible to go and where they are going.

In the top left corner the radical humanist paradigm is located within the subjectivist and radical change dimensions. Burrell and Morgan (1979) indicate that this is the state 'to articulate ways in which humans can transcend the spiritual bonds and fetters which tie them into existing social patterns and thus realise their full potential' (p. 32). The ontological position that would fit with this state is subjectivist.

In the right corner of the quadrant is the radical structuralist paradigm. In this state, the researcher concern would be to approach the research with a view of fundamental change based upon an analysis of specific organizational phenomena (Saunders *et al.*, 2005).

The bottom left corner of the quadrant contains the interpretive paradigm. Burrell and Morgan (1979) stated that this paradigm refers to that 'everyday life is accorded the status of miraculous achievement' (p. 31). This state does not require the researcher to achieve change in the order of things, but it would be to understand and explain what is going on.

Finally, the bottom right corner of the quadrant is the functionalist paradigm. It is noted by Burrell and Morgan (1979) that this paradigm 'is often problem-oriented in approach, concerned to provide practical solutions to practical problems' (p. 26). This paradigm assumes that organizational are rational entities, in which rational explanations provide rational solutions to rational problems. Objectivism is the ontological position that fits with this paradigm. Referred to the research philosophy discussion, objectivism is the current research ontological position. Therefore, functionalist would be the appropriate paradigm that fits with the current research nature and philosophy.

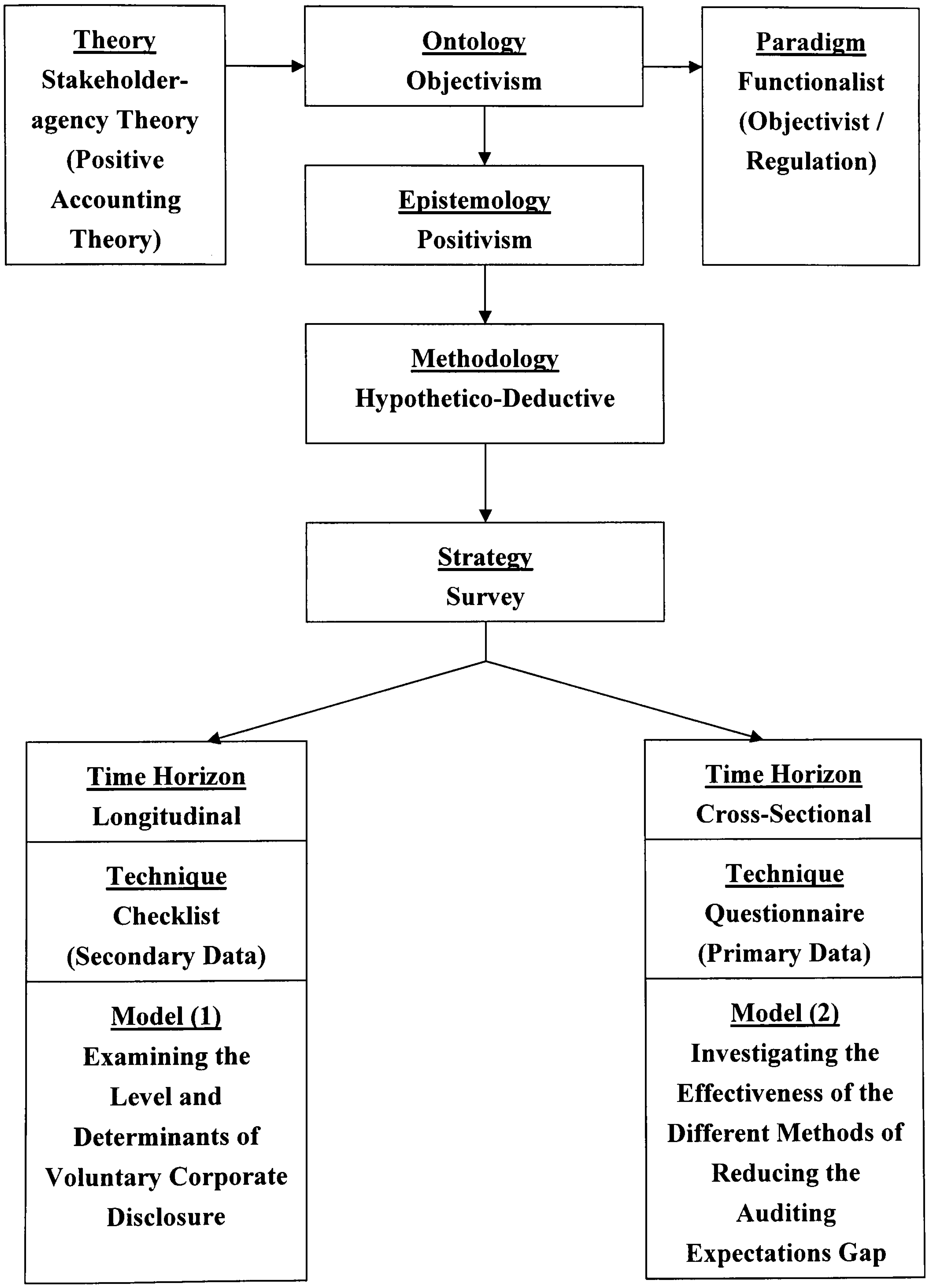
Consequently, the thesis would include two research models. The differentiation is based on the data collection method employed to perform the research objectives. The first method is secondary data collection using a checklist of different items that forms a secondary data index. The second method is a questionnaire that is employed to gather primary data from the different survey respondents.

Moreover, the two research models are classified based on the survey time horizons. The first model is considered to be a longitudinal survey for the selected sample. On the other hand, the second model is a cross-sectional survey over the different selected groups of respondents.

Referred to the previous research philosophy and paradigm discussion, the following figure shows the research positions and models:

Figure 5.2

Research Philosophy and Models



5.4 MODEL (1) EXAMINING THE LEVEL AND DETERMINANTS OF VOLUNTARY CORPORATE DISCLOSURE

First model of the current thesis examines the level of voluntary disclosure in the Egyptian firms' annual reports. Moreover, the model justifies the examined level of voluntary disclosure by investigating the determinants of this sort of disclosure. The investigated determinants are classified in to two groups. First group of determinants is firm characteristics including; firm size; firm profitability; and industrial membership. Second group of determinants is corporate governance characteristics including; board size; and role duality.

5.4.1 The Model Instrument

This model is applied on the annual reports of the Egyptian companies using a pre-designed checklist that is referred to previous studies in which it is adapted and validated to fit with the Egyptian context. The employed checklist is constructed based on different studies that have examined the practices of one or more of voluntary disclosure categorise (see for example: Bar ako *et al.*, 2006; Lajili and Zeghal, 2005; Gray *et al.*, 1995a; Entwistle, 1999; Collett *et al.*, 2005). The checklist would form a disclosure index that shows the level of voluntary corporate disclosure. The checklist is adapted to fit with the Egyptian culture through interviewing 10 academic members regarding the validity of the checklist items to ensure that the items would be appropriate for the Egyptian companies' disclosures. The outcome of these interviews is the deletion of some items commonly indicated that they are not fitting with the Egyptian companies' disclosure practices. Therefore, the revised checklist is reliable and valid to act as a benchmark for the Egyptian companies. The model aims to measure the disclosure level using un-weighted disclosure index or dichotomous scores to examine the presence or absence of the different items of the checklist using binary codes. The presence of the item in the annual reports is represented by (1), while the absence of the item in the annual reports is represented by (0). The checklist is composed of different sections showing the whole voluntary disclosure categories. The disclosure level is measured using the percentage of the present items over the whole disclosure index items.

The voluntary corporate disclosure checklist is shown in the following table:

Table 5.1

Voluntary Corporate Disclosure Checklist

No	Items
1	**General Disclosure**[1]
1.1	Mission & vision.
1.2	Statement of corporate strategy.
1.3	Top management names / experience.
1.4	Majority of stockholders. (composition of shareholdings)
1.5	Organization structure.
1.6	Statement of corporate goals and objectives.
1.7	Presentation of annual reports in Arabic & English.
2	**Market Disclosure**[2]
2.1	Industry size.
2.2	Product (s) information.
2.3	Customers' information.
2.4	Supplier information.
2.5	Market (s) information.
2.6	Market share.
2.7	Competitive environment.
2.8	Productivity capacity.
2.9	Productivity indicators.
2.10	Marketing networks.
2.11	Physical outputs.
3	**Risk management Disclosure**[3]
3.1	Financial risk (interest rate, currency, credit & fin. Instruments).
3.2	Political risk (international business).
3.3	Market risk (competition, market share).
3.4	Technology risk (rapid change)
3.5	Environmental risk (laws & regulations).
3.6	Weather risk (climate conditions).
3.7	Government regulation risk (control, regulation, taxation).
3.8	Seasonality risk (natural seasonal patterns).
3.9	Operational risk (technical, accidents, human error & loss).

[1] adapted from Barako, D., *et .al.* (2006).

[2] adapted from Barako, D., *et .al.* (2006).

[3] adapted from Lajili, K. and Zeghal, D. (2005).

3.10 Cyclicality risk (natural cyclical trend).
3.11 Supplier risk (key supplier).
3.12 Natural resources risk (reserves quality and quantity).

4 Financial Disclosure[4]

4.1 Financial ratios & statistics.
4.2 Industry ratios.
4.3 Using charts, graphs, photos.
4.4 Market Share price.
4.5 Bank loans, mortgages and their uses.
4.6 Information of capital structure.
4.7 Information of dividends policy.
4.8 Reasons and effects of acquisions / disposals on past results.
4.9 Information of foreign sales.
4.10 Financial information on quarterly basis.
4.11 Changes in inventory level.
4.12 Dividends per share compared with previous years.

5 Human Resources Disclosure[5]

5.1 Consultation with employees.
5.2 Employee share ownership.
5.3 Employment data.
5.4 Pension commitment.
5.5 Employees' health & safety.
5.6 Average compensation of employees.
5.7 Percentage of foreign and national labour force.
5.8 Information of training and employee development.
5.9 Number of employees trained.
5.10 Amount spent on training.

6 Research & Development Disclosure[6]

6.1 Inputs: Product.
6.2 Inputs: People.
6.3 Input: Infrastructure.
6.4 Outputs: Actual achievements (Product development).
6.5 Outputs: Actual achievements (Beyond Product development).
6.6 Outputs: Potential achievements.
6.7 Output: Product timing.

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[4] adapted from Barako, D., *et .al.* (2006).

[5] adapted from Gray, R., *et. al.* (1995a).

[6] adapted from Entwistle, G. (1999).

6.8 Future expenditures.
6.9 Financing Past, Present, Future.
6.10 Accounting/ financing (Comparing prior years, competition, budget).
6.11 R&D ratios.
6.12 R&D as explanatory.
6.13 Explaining R&D changes.
7 Environmental, Social, and Ethical Disclosure[7]
7.1 Environmental reports.
7.2 Value added statement.
7.3 Social activities & contributions.
7.4 Environmental health safety.
7.5 Energy information.
7.6 Community information.
7.7 Charitable donations information.
7.8 Using photocopy of awarded certificates.
7.9 Methods of provisions computation.
7.10 Employment of disabilities.
7.11 Ethical actions.
8 Corporate Governance Disclosure[8]
8.1 Major share ownership and voting rights.
8.2 List of board members.
8.3 Picture of chairperson and/or other members.
8.4 Board member qualifications.
8.5 Number of shares held by members of the board.
8.6 Remuneration policy for board members and key executives.
8.7 Audit committee members: names, addresses, experiences.
8.8 Corporate governance codes, policies, implementation extent.
Total Corporate Voluntary Disclosure
Total Corporate Voluntary Disclosure percentage (%)

[7] adapted from Gray, R., *et. al.* (1995a).

[8] adapted from Collett, P., *et .al.* (2005).

5.4.2 The Sample Population

The shown checklist is applied on the annual reports of the Egyptian companies in the most recent two years 2004–2005 and 2005-2006 that shows disclosure level of the corporate voluntary disclosure. The selected companies are the 50 most active Companies based on the disclosure books issued by the Egyptian stock market (Cairo & Alexandria stock market) in June 2005 and June 2006. However, there are nine companies in 2004-2005, and 10 companies in 2005-2006 excluded from the sample which are the financial institutions, as they have their own regulations concerning the mandatory and the voluntary disclosures, so they are excluded to maintain the consistency of the annual reports of the different companies.

The most active companies have been selected based on the activity of companies' stocks in the last six months of each year. To be considered as active, the stock must be traded at the stock exchange at least 50% of the working days during the last six months of each year. Arguably, the most active companies represent the highest level of voluntary disclosure among the listed companies.

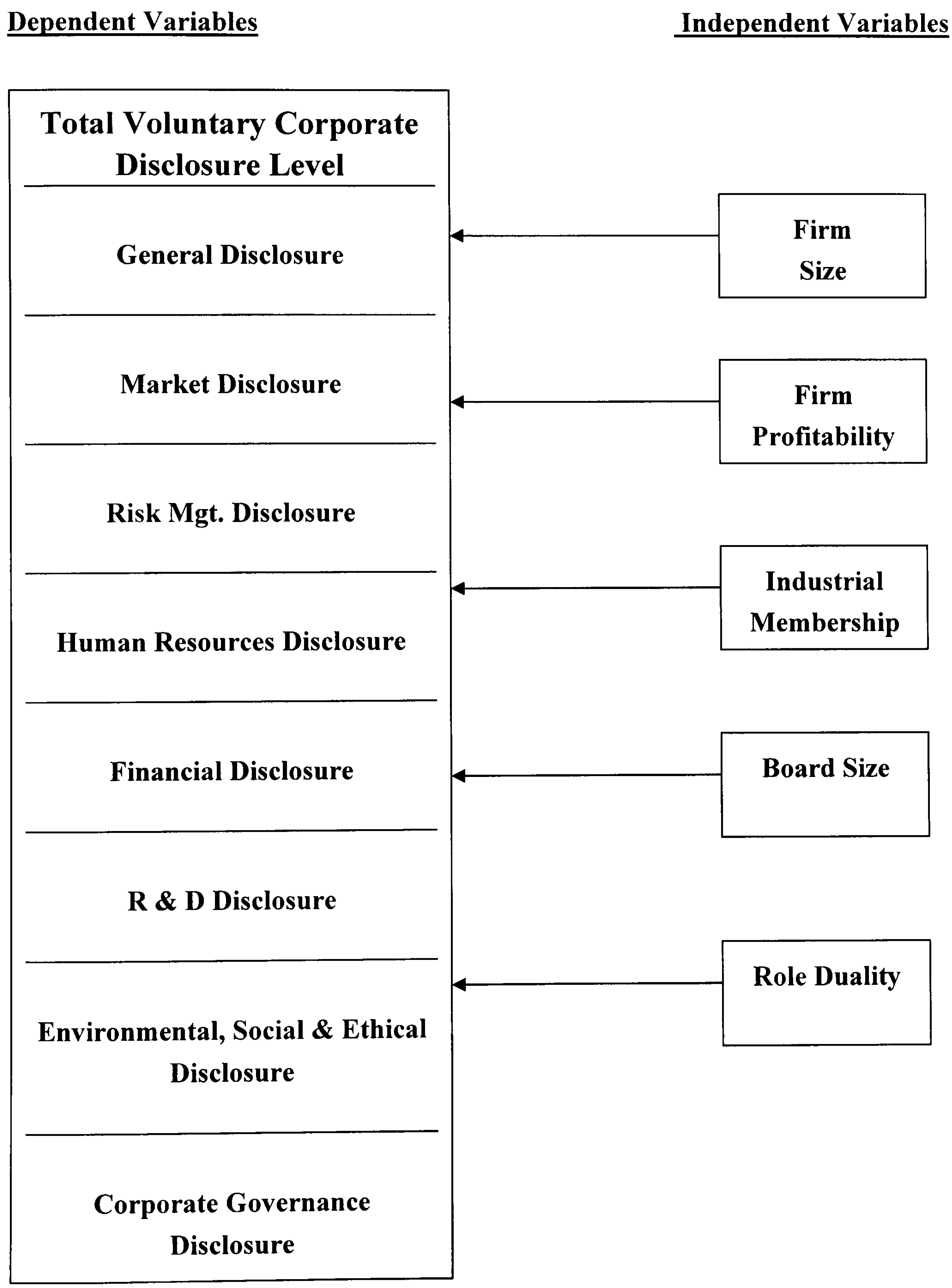
The self-selected companies based on the criteria of being most active, are restricted to the most recent two years as the capital market reform program and the disclosures standards updates are launched in year 2003 by preparing the first disclosure book of Cairo and Alexandria stock exchange in June 2003. Therefore, the most reliable data, consistent with these new disclosure reforms, are available from the beginning of year 2004 which is the selected research sample.

5.4.3 Model Dependent and Independent Variables

The variables of the model are shown by the following figure:

Figure 5.3

Examining the Level and Determinants of Voluntary Corporate Disclosure



5.4.3.1 Dependent Variables Definition and Measurement

The dependent variable of the current research is the Egyptian companies' total voluntary disclosure level. This variable is measured using the disclosure index of the Egyptian companies in the sample of the research. Moreover, the index is applied over a checklist that includes the different categories of the voluntary disclosure. The checklist includes all the possible categories of voluntary disclosure as the disclosure of the items of each group would contribute to the total voluntary disclosure's level.

Furthermore, the index is based on examining of the presence or absence of the entire item in the annual reports, where the presence of the item in the annual report is represented by (1), while the absence of the item would be represented by (0), therefore the measurement of the voluntary disclosure level is based on binary (1 and 0) scale. The different categories of total voluntary disclosure are presented as follows:

5.4.3.1.1 General Disclosure

The general disclosure includes additional illustration for the nature of the corporation. This disclosure is related to the format of the annual reports and its language. In addition, the main aspects of the corporation regarding the corporate strategy, objectives, and structure are included in the corporation's general disclosure (Barako *et al.*, 2006).

5.4.3.1.2 Market Disclosure

The corporation market disclosure includes different market indicators concerning the product, customers, suppliers, and markets information. These indicators reflect the competitive situation of the corporation. The disclosure is with a great importance for the corporation to identify the competitive opportunities and threats that affects the corporation. The voluntary disclosure regarding this type is dependent on the competitive status of the entire market (Barako *et al.*, 2006).

5.4.3.1.3 Risk Management Disclosure

The risk management disclosure reflects the management's effectiveness towards dealing with different types of risk that their corporation is exposed to. Also, the uncertainty that is correlated with the different types of risk causes the relative importance such types of risk. On the other hand, the corporation is getting a competitive advantage by overcoming the risk and reducing the degree of risk exposure. The risk management disclosure is examined by the average of the different components of this group shown in the checklist (Lajili *et al.*, 2005).

5.4.3.1.4 Financial Disclosure

The financial disclosure is represented by the voluntary financial disclosure regardless the mandatory financial disclosure. This group of disclosure shows the presentation of the financial information regarding the corporation's performance. In addition, this group includes the financial disclosures that are not obligated by the mandatory disclosure as to offer a full picture about the performance of the corporation (Barako *et al.*, 2006).

5.4.3.1.5 Human Resources Disclosure

The human disclosure is part of the company's social responsibilities. This disclosure represents the data concerning the employees of the corporation. Other information regarding the employees but having social perspective is included in the environmental, social, and ethical disclosure group (Gray *et al.*, 1995a).

5.4.3.1.6 Research and Development Disclosure

The research and development disclosure is focusing on the research and development expenditures in the future. The research and development is categorized in to different perspectives. These perspectives are related to inputs, outputs, future expenditures, financing, and accounting / financial (Entwistle, 1999).

5.4.3.1.7 Environmental, Social, and Ethical Disclosure

The environmental, social, ethical disclosure is the most important information regarding the society. This group of disclosure is reflecting how the corporation is dealing with its environment, the social responsibility of the corporation, and the ethical actions regarding the different parties that the corporation is dealing with (Gray *et al.*, 1995a).

The ethical reporting is defined as 'those factors which are used by ethical investment funds to form an opinion on the appropriateness of an organization's business practices. This may not include much of the information on employees that is generally considered to fall within the definition of "social reporting", but may include other issues which are generally considered as "social reporting". Environmental reporting is clearly a subset of ethical reporting and generally also considered a subset of social reporting, but as the most common type of social and ethical reporting, warrants a separate label' (Adams, 2004; p. 731).

As a result of the lack of ethical, social, and environmental reporting that may be reflected on the commitment to accountability and transparency (Gray, 1996; Elkington, 1997; Deegan, 2000; GRI 2002; Suggett and Goodsir, 2002). Therefore, there may be a significant expectation gap between users and preparers of the annual reports concerning the disclosure of the ethical, social, and environmental reporting (Corcoran, 1997). This expectation gap of ethical, social, and environmental reporting is also entitled "the green gap" (Gozali, 2000).

There are different reasons that are motivating the companies to disclose the ethical, social, and environmental events in their financial reports and that may act as mechanisms to reduce the ethical, social, environmental reporting expectation gap: survival (Deegan and Blomquist, 2001; Deegan, 2002); corporate image (Gray, 1988; Deegan, 2000); forestalling corporate change (Deegan and Blomquist, 2001; Deegan, 2002); unfavourable media attention (Neu, 1998; Hooghiemstra, 2000; Deegan, 2002); industry affiliation (Deegan and Gordon, 1996; Deegan and Rankin, 1996; KPMG 1999; Gray, 2001; Newson and deegan, 2002); financial performance (Clarke, 1998; Stanwick and Stanwick, 1998); corporate social responsibility (Gelb and Strawser 2001; Swift 2001); response to community and societal concerns (Gray, 1998; Clarke, 1998; KPMG 1999; Hooghiemstra, 2000; Wilmshurst and Forst, 2000; Deegan and Blomquist, 2001; Deegan, 2002); company size (Gray, 1995b; Deegan and Gordon, 1996; Hackston and Milne, 1996; Neu, 1998; Stanwick, 1998; KPMG 1999; Gray, 2001) and country of origin (KPMG 1999; Gray, 2001; Newson and Deegan, 2002).

5.4.3.1.8 Corporate Governance Disclosure

The Australian Stock Exchange (ASX) development listed rule required the listed companies to disclose in its annual reports a statement indicated the corporate governance practices followed during the reporting period. Similar rule was applied in the London Stock Exchange based on the recommendations of Cadbury Committee report (1992) concerning the corporate governance issues in the UK. The ASX rule has not mentioned practices to be disclosed but referred to an indicative list of items that are recommended to be disclosed in its issued 'Principles of Good Corporate Governance and Best Practice Recommendations'. However, Carson (1996) specified that the corporate governance disclosure would vary in terms of comprehensiveness and specificity (Collett and Harsky, 2005).

5.4.3.2 Independent Variables Definition and Measurement

The model includes two groups of determinants that affect the level of corporate voluntary disclosure as follows:

5.4.3.2.1 Firm Characteristics

The firm characteristics are vital determinants of the voluntary disclosure. There are increasing interests in the studies of accounting disclosures since the 1960s. Considerable academic research has investigated the relationship between corporate characteristics and voluntary disclosures in developed and developing countries (Alsaeed, 2006). Prior empirical evidence suggests that firm characteristics differentiate the level of voluntary disclosure by the different companies (e.g. Chandra, 1989; Lee and Morse, 1990; Ward, 1998).

Regarding this relationship between disclosure level and firm characteristics, there are many studies applied in the developed countries as in as in the UK (Spero, 1979; Firth, 1979); the USA (Buzby, 1975; Lang and Lundholm, 1993); Canada (Belkaoui and Kahl, 1978); Sweden (Cooke, 1989); Switzerland (Raffournier, 1995); Japan (Cooke, 1992); Mexico (Chow and Wong-Boren, 1987); and New Zealand (McNally *et al.*, 1982).

Few disclosure studies have been applied in the developing countries as in Egypt (Abd-Elsalam and Weetman, 2003; Hassan *et al.*, 2006); Jordan (Naser *et al.*, 2002); Nigeria (Wallace, 1987); Saudi Arabia (Alsaeed, 2006); Bangladesh (Ahmed and Nicholls, 1994); India (Singhvi, 1968); Malaysia (Hossain *et al.*, 1994); Zimbabwe (Owusu-Ansah, 1998); Kenya (Barako *et al.*, 2006) . In addition, some comparative studies have examined the relationship between corporate characteristics and voluntary disclosures (e.g. Barrett, 1977; Zarzeski, 1996; Camfferman and Cooke, 2002).

Among the different studies, each study selects firm characteristics to be examined in relation to the level of voluntary information disclosed by the entire companies. The research focuses on examining the relationship between voluntary disclosure and firm size, firm profitability, and industrial membership as representative of firm characteristics.

5.4.3.2.1.1 Firm Size

Regarding firm size, Jensen and Meckling (1976) assumed that the large sized firms have the incentive to disclose this sort of information to avoid political costs represented in the form of tight regulations and increasing tax and social obligations. Referred to the agency theory, larger firms disclose more information as they have higher agency costs and they are more sensitive to political cost (Jensen and Meckling, 1976; Leftwich, Watts and Zimmerman, 1981) Moreover, the advocates of stakeholder theory argues that firms are expected to have high level of voluntary disclosure in order to be registered in the stock market to attract more funds at lower cost of capital, as in this case they have greater responsibility to provide information to customers, suppliers, analysts and government (Choi, 1973; Cooke, 1991). It is mentioned that 'the variable most consistently reported as significant in studies examining differences across firms in their disclosure policy is firm size' (Foster, 1986; p. 44).

Moreover, most of the studies provide evidence that there is a significant positive relationship between firm size and level of voluntary disclosure (Buzby, 1975; Firth, 1979; Chow and Wong-Boren, 1987; Cooke, 1992; Wallace *et al.* 1994; Raffournier, 1995; Zarzeski, 1996; McNally *et* al., 1982, McKinnon and Dalimunthe, 1993; Hossain and Adams, 1995; Meek *et al.*, 1995; Ahmed and Courtis, 1999; Choon *et al.*, 2000; Lee and Morse, 1990; Ward, 1998). In addition to other studies suggested that there is a positive relationship between environmental voluntary disclosure and size of the entity (Hackston and Milne, 1996; Choi, 1999; Williams, 1999; Cormier and Magnan, 2003).

The firm size could be measured by different methods, depending on the previous studies; the number of shareholders, number of employees, total market value of the firm, total assets, sales volume (Salama, 2003). Regarding the research, the firm size would be measured using: total assets, as the examined sample is the 50 most active companies in the Egyptian stock market as the other measures would be redundant for these companies.

The firm size of a certain corporation is considered to be the most statistically significant variable examining the differences between voluntary reporting practices of firms (McNally *et al.*, 1982, McKinnon and Dalimunthe, 1993; Hossain and Adams, 1995; Meek *et al.*, 1995; Ahmed and Courtis, 1999; Choon, Smith and Taylor, 2000). Moreover, the previous literature offers evidences that the firm size is positively related to the voluntary disclosure level (Lee and Morse, 1990; Ward, 1998). Consequently, the model tests the following hypothesis:

Hypothesis 1.1 – *There is a positive significant relationship between firm size and voluntary corporate disclosure.*

5.4.3.2.1.2 Firm Profitability

Concerning the firm profitability, it is a reflection of the firm's performance for a specific year. Therefore, profitable firms choose to disclose more voluntary accounting information to distinguish themselves from the less profitable ones (Foster, 1986). It is suggested by Singhvi and Desai (1971) that stakeholder theory argues that the firm performing high profitability, induce management to disclose more information to attract the shareholders towards their high performance to increase their compensation. While on the other hand, low profitable companies avoid disclosing more information to hide their poor performance (Ullman, 1985; Richard, 1992, Meek *et al.*, 1995). However, there is unclear direction of the relationship between firm profitability and the level of disclosed information. It is emphasized that the firm profitability measures the level of disclosure in New Zealand (McNally *et al.*, 1982). On the other hand, it is found by Camfferman and Cooke (2002) that there is a significant negative relationship between firm profitability and the amount of information disclosed by the British firms. Finally, it is observed that there is no significant relationship between the disclosure of the Spanish firms and their profitability (Wallace *et al.*, 1994).

The profitability of the firm is mainly based on the revenues and the expenses of the entire accounting period, therefore profitability could be a major factor in the decision to produce summarized version of the annual reports (Gambino, 1987; Simon, 1988; Schneider, 1988; Hamilton, 1990; Lee and Morse, 1990) or detailed statements beside voluntary disclosure reports. In the current study the return on equity (ROE) is employed as a proxy for the firm profitability. Therefore, the firm profitability would be a representative justification for the level of the voluntary disclosure level by the Egyptian companies. Consequently, the model tests the following hypothesis:

Hypothesis 1.2 – *There is a positive significant relationship between firm profitability and voluntary corporate disclosure.*

5.4.3.2.1.3 Industrial Membership

A great attention was drawn towards the bandwagon effect that could be produced by the leading firms in certain industry on the level of disclosure of the other firms working in the same industry (Cooke, 1989). Previous studies have not provided clear relationship between type of industry and level of voluntary disclosure. Some studies emphasized that there is a significant relationship between industry type and voluntary disclosure (Ness and Mirza, 1991; Cooke, 1992; Deegan and Gordon, 1996; Hackston and Milne, 1996; Ward, 1998; Choi, 1999; Williams, 1999; Mahmood, 1999; Brown *et al.*, 2004). However, other studies found that there is insignificant relationship between voluntary disclosure level and industry type (Lee and Morse's, 1990; Gray *et al.*, 1995b; Ahmed and Courtis, 1999; Brown, 2005).

The industrial membership is an important factor that affects the level of the voluntary disclosure of the different corporations. Moreover, the firm's accounting policy, concerning the level of disclosure, is affected by the industry to which the firm belongs (Watts and Zimmerman, 1996).

Furthermore, the industrial membership in the annual reports of the Egyptian companies is represented by the sector that the companies are member of and these sectors could be represented by the following table:

Table 5.2

The Sectors of the 50 Most Active Companies

Sector	Number of Companies (2004 – 2005)	Number of Companies (2005-2006)
Building Materials & Constructions.	12	10
Chemical Industry.	4	5
Communications Industry.	3	3
Electric Equipments & Engineering.	2	1
Entertainment.	2	2
Food & Beverage.	3	2
Health & Pharmacy.	1	2
Housing & Real Estate.	2	4
Media.	1	1
Mills & Storage.	5	2
Mining & Gas.	1	1
Textiles & Clothing.	4	5
Canal Shipping Agencies	1	1
Information Technology	0	1
Financial services.	9	10
Total	**50**	**50**

Consequently, the model tests the following hypothesis:

Hypothesis 1.3 – *There is a negative significant relationship between industrial membership and voluntary corporate disclosure.*

5.4.3.2.2 Corporate Governance Characteristics

Agency theory represents the cornerstone of most of the studies regarding corporate governance characteristics, as these studies are employing the logic of the principal-agent relationship towards the effectiveness of the corporate governance practices leading to firm behaviors that are consistent with owners' expectations, and achieving superior firm performance due to the reduction of agency costs (Jensen and Meckling, 1976; Eisenhardt, 1985; Fama, 1980; Fama and Jensen, 1983a).

There are different definitions for the corporate governance, but the classical definition of corporate governance is 'the system by which organizations are directed and controlled. Moreover, the corporate governance has been described as 'the process and structure used to direct and manage the business affairs of the corporation with the objective of enhancing shareholder value' (Dey, 1994; p: 7).

5.4.3.2.2.1 Board Size

Regarding corporate governance characteristics, previous studies concerned with board size showed mixed findings. Board size represents the number of directors within the board. It is argued that the board size needs to be reduced to improve board effectiveness (Jensen, 1993; Lipton and Lorsch, 1992; Kesner and Johnson, 1990), while to maintain the agency theory logic it is recommended to raise the board size (Hermalin and Weisbach, 2003). At the same time, big boards would be more diversified that would help the companies to secure critical resources and reduce environmental uncertainties (Pfeffer, 1987; Pearce and Zahra, 1992; Goodstein *et al.*, 1994). Other studies mentioned that board size does matter on the corporate performance and corporate disclosures (Monks and Minow, 1995).

From stakeholder theory perspective, large board size is believed to enable a high degree of independency as it enables the election of a broad range of directors that lead to diversification of the board composition. This variation addresses wider scope for the stakeholder's interests, which leads to greater propensity to disclose more information (Williams, 2002). Moreover, it is argued that the large size of the board of directors increases the control and the opportunity to increase the manipulation by the management (Jensen, 1993). While, it is observed that larger board size makes it dysfunctional board which could limit the disclosure of information. Consequently, the model tests the following hypothesis:

Hypothesis 1.4 – *There is insignificant relationship between board size and voluntary corporate disclosure.*

5.4.3.2.2.2 Role Duality

Duality refers to the situation where the same person is holding the position of chief executive officer (CEO) and at the same time holds the position of Chairperson of the board of directors. In the sense of the stakeholder theory and the agency theory this situation affects the independency status and the bias as this person would accumulate much power by driving two critical positions at the same time (Williams, 2002).

Chief Executive Director (CEO) role duality means that the CEO is also holding the chairman position of the board of directors, so there are dual roles played by the same person (Finkelstein and D'Aveni, 1994). Agency theory argue that the separation between the two roles, the absence of role duality, provide monitoring and balances over managements' performance (Argenti, 1976; Rechner and Dalton, 1991; Donaldson and Davis, 1991; Forker, 1992; Shamser and Annuar, 1993, Stiles and

Taylor, 1993; Blackburn, 1994). However, there are other views, based on the stewardship theory, suggest that the existence of role duality would improve the board effectiveness in performing a good control on the board and selection of the other board members (Eisenhardt, 1989; Dahya *et al.*, 1996; Rechner and Dalton, 1991; Donaldson and Davies, 1991). Therefore, it is argued that the separation of the roles of chairman and chief executive will increase monitoring quality and improve the level of disclosure (Forker, 1992). However, some studies argue that there is no association between CEO duality and the extent of voluntary disclosure of information (Haniffa and Cooke, 2000).

Moreover, the relationship between the role duality and voluntary disclosure is arguable. Empirically, it is found that there is a negative relationship between role duality and voluntary disclosure (Forker, 1992). While in other study it is argued that there is no significant relationship between role duality and the amount of voluntary disclosure (Ho and Wong, 2001). Consequently, the model tests the following hypothesis:

Hypothesis 1.5 – *There is insignificant relationship between role duality and voluntary corporate disclosure.*

5.4.4 Model Specification

Econometric model (1.a) is shown as follows:

$$TVCD = \beta 0 + \beta 1\ FS + \beta 2\ FP + \beta 3\ IM + \beta 4\ BS + \beta 5\ RD + \epsilon$$

While, econometric model (1.b) is shown as follows:

$$VCDC = \beta 0 + \beta 1\ FS + \beta 2\ FP + \beta 3\ IM + \beta 4\ BS + \beta 5\ RD + \epsilon$$

Where:

TVCD = Total Voluntary Corporate Disclosure;

VCDC = Voluntary Corporate Disclosure Category;

$\beta 0$ = Intercept;

$\beta 1$ to $\beta 5$ = Coefficient of slope parameters;

ϵ = Error term;

FS = Firm Size;

FP = Firm Profitability;

IM = Industrial Membership.

BS = Board Size; and

RD = Role Duality.

5.4.5 Econometric Model Statistical Tests

The model is analyzed using descriptive statistics of the collected data using Pearson correlation to identify the correlation between the dependent and independent variables. Besides using Pie Chart figure to show the contribution of each disclosure category to the whole voluntary disclosure level.

The regression models would be applied on two dimensions. First, is investigating the association between total voluntary disclosure, as a dependent variable, and the different determinants of voluntary disclosure, as independent variables. Second, examination of the association between the different categories of voluntary disclosure, as dependent variables, and the different determinants of voluntary disclosure, as independent variables.

The hypotheses are examined using cross sectional panel regression. A dummy variable is used to differentiate between the two groups of the examined sample of the two years 2004 – 2005 (41 observations) and 2005 – 2006 (40 observations). A pooled ordinary least square (OLS) regression is applied in comparison to the panel regression as it deals with the whole observations as one unit with the same intercept and same error distribution. The standard error robust regression test would be used specially that the sample size is small (41 and 40 companies) and the data is not normally distributed. The data is analyzed under the assumption of a confidence level of 99%, 95%, and 90%. A dummy variable of 0 and 1 values is inhibited in the analysis to differentiate between the two panels as 0 represents year 2004–2005 (panel A), while 1 represents year 2005–2006 (panel B). The model is statistically analyzed using STATA 9 statistical package.

5.5 MODEL (2) INVISTIGATING THE EFFECTIVENESS OF THE DIFFERENT METHODS OF REDUCING THE AUDITING EXPECTATIONS GAP

Second model of the current thesis examines the existence of the auditing expectations gap in Egypt. Moreover, the model investigates the effectiveness of the traditional methods of reducing the existing gap including; audit report form; users' education; and standards settings. Also, the model examines the effectiveness of the traditional methods in comparison to the role of the voluntary disclosures auditing as a proposed solution by the current research.

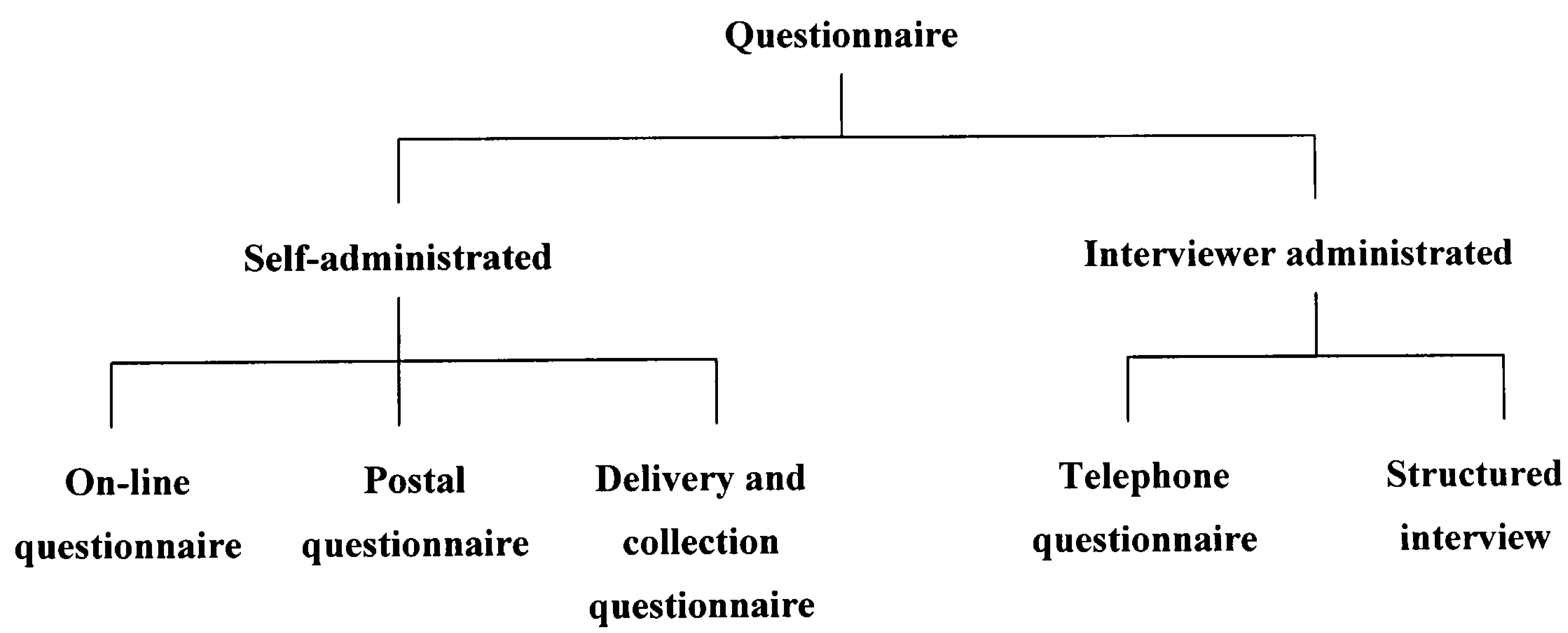
5.5.1 The Model Instrument

The model is applied using the questionnaire technique which is designed based on 5-Point Likert scale that include 5 different scales for the answers on the questions; strongly agree, agree, neutral, disagree, and strongly disagree. These answers are numbered from 1 to 5. 1 represents the strongly agree opinion, 2 represents the agree opinion, 3 is the neutral, 4 is the disagree opinion, and 5 is the strongly disagree opinion. The questionnaire aims to measure the perceptions of the different categories of the sample towards the different solutions of reducing the auditing expectations gap. The questionnaire is constructed based on previous studies that have examined the existence of auditing expectations gap and the different solution to reduce this gap The last section of the questionnaire, the role of voluntary corporate disclosure in reducing auditing expectations gap, is the checklist employed in the first model. This section is already validated and adapted to fit with the Egyptian context as previously mentioned. Moreover, the other sections were used before in different studies in different developing countries which would fit with the Egyptian context (see for example: Best and Buckby, 1999; Fadzly and Ahmad, 2004; Manson and Zaman, 2000; Dewing and Russell, 2002; Barako *et al.*, 2006; Lajili and Zeghal, 2005; Gray *et al.*, 1995; Entwistle, 1999; Collett *et al.*, 2005).

There are types of questionnaire to gather the research required data. The following figure provides a representation of the typology of questionnaires:

Figure 5.4

Types of Questionnaire



Source: Saunders *et al.* (2003, p. 282)

The current research used the self administrated delivery and collection questionnaire to distribute and then collect the questionnaire hand to hand as to ensure having acceptable response rate which affect the validity of the research results.

The questionnaire is validated by applying pilot study of randomly selected 10 subjects of each group of the sample that's to examine the reliability of the questionnaire. The results of the pilot study are similar to the findings of the analysis of the whole sample. The questionnaire is distributed in Arabic which is the formal language of Egypt. To overcome any translation problems back-to-back a translation is applied to the questionnaire to Arabic and then to English again to guarantee that the questionnaire is valid regarding the translation issue.

The model is used to test the last hypothesis of the study regarding the examination of different methods of reducing the auditing expectation gap effectiveness, including the proposed solution, simultaneously. The analysis includes comparing the effectiveness of the different methods to each other and examining whether the results satisfies the hypothesis. The agreement or disagreement upon the entire statement shows the usefulness of this item in reducing the auditing expectation gap. Although the statement is useful in reducing such gap, it could not be effective in performing the required reduction of the gap. Therefore, there is further test used to examine the effectiveness of each statement which shows the overall effectiveness of the examined method of reducing the existing expectations gap.

The Auditing expectations gap questionnaire is shown as follows:

Table 5.3

Auditing Expectations Gap Questionnaire

Dear respondent,

I wish to have your attention towards my research. It aims to investigate the existence of the auditing expectations gap in Egypt and the different methods that reduces this gap. The research uses the questionnaire technique as to capture the data about the different perceptions of different samples about this problem.

The questionnaire is designed to examine your perceptions concerning the auditing expectations gap in Egypt, and the effective solution to this problem. Your response would contribute to reaching the most effective solution that fits with the Egyptian context.

Finally, I would like to thank you for having your attention towards this questionnaire, which considered being the corner stone of the research results.

Thanks for your time and attention

The Researcher

Section I

Demographic Information[9]

Please tick in front of the answer that fits with your personal information:

1. Do you have Accounting qualifications?

   Yes [ ]   No [ ]

2. Do you have accounting experience?

   Yes [ ]   No [ ]

3. If yes, how many years?

   2 – 5 years [ ]   5 – 10 years [ ]   Over 10 years [ ]

4. What is your occupation?

   Auditor [ ]   Banker [ ]   Investor [ ]   Academic [ ]

5. How long have you been in your present occupation?

   2 – 5 years [ ]   5 – 10 years [ ]   Over 10 years [ ]

6. Do you wish to have a copy of the analyzed results emailed to you?

   Yes [ ]   No [ ]

7. If yes, please provide your email address.

   [   ]

---

[9] adapted from Best, P. J. and Buckby, S. (1999).

Section II

Investigating the Existence of the Auditing Expectations Gap[10]

Identify to which extent do you agree or disagree with the following statements:

Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
1-Management is responsible for producing the financial statements of the company.	1	2	3	4	5
2-The auditor is responsible for the soundness of the internal control structure of the company.	1	2	3	4	5
3-The auditors is legally responsible only to the shareholders.	1	2	3	4	5
4-The auditor is responsible for maintaining accounting records of the company.	1	2	3	4	5
5-The auditor is responsible for detecting all fraud.	1	2	3	4	5
6-Management should be held responsible if the company goes bankrupt due to fraud.	1	2	3	4	5
7-The auditor is responsible for preventing fraud.	1	2	3	4	5
8-The auditor is unbiased and objective.	1	2	3	4	5

[10] adapted from Fadzly, M. N. and Ahmad, Z. (2004).

Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
9-The financial statements give a true and fair view.	1	2	3	4	5
10-Users can have absolute assurance that the financial statements contain no material misstatements.	1	2	3	4	5
11-The company is free from fraud.	1	2	3	4	5
12-The extent of audit work performed is clearly explained in the audit report.	1	2	3	4	5
13-The extent of assurance given by the auditor is clearly indicated in the audit report.	1	2	3	4	5
14-The auditor is trustworthy.	1	2	3	4	5
15-The audited financial statements are useful in monitoring the company's performance.	1	2	3	4	5
16-The audited financial statements are useful for decision making.	1	2	3	4	5
17-The company is well managed.	1	2	3	4	5

Section III

The Role of Audit Report Form in Reducing the Auditing Expectations Gap[11]

Identify to which extent do you agree or disagree with the following statements in the light of reducing the auditing expectations gap:

Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
1-The inclusion of an audit report enhances the credibility of financial statement.	1	2	3	4	5
2-The purpose of the audit is clearly communicated in the audit report.	1	2	3	4	5
3-The audit report is readable document.	1	2	3	4	5
4-The audit report clearly summarizes the extent and nature of the evidence gathered in the formation of the audit opinion.	1	2	3	4	5
5-The audit report clearly indicates the role of judgment in the formation of the audit opinion.	1	2	3	4	5
6-The auditors' responsibility in relation to fraud is clearly indicated in the audit report.	1	2	3	4	5

[11] adapted from Manson, S. and Zaman, M. (2000).

Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
7-The auditors' responsibility in relation to any illegal acts performed by the client is clearly indicated in the audit report.	**1**	**2**	**3**	**4**	**5**
8-In the future there should be an explicit statement in the audit report of the auditors' assessment of the going concern status of the client.	**1**	**2**	**3**	**4**	**5**
9-In the future there should be an explicit statement in the audit report of the auditors' findings in relation to fraud or illegal acts.	**1**	**2**	**3**	**4**	**5**
10-It should be useful for the auditor to indicate either in the audit report or in a separate statement, the extent of their examination of the chairman's statement.	**1**	**2**	**3**	**4**	**5**
11-It should be useful for the auditor to indicate either in the audit report or in a separate statement, the extent of their examination of the director's report.	**1**	**2**	**3**	**4**	**5**

Statements	**Strongly Agree**	**Agree**	**Neutral**	**Disagree**	**Strongly Disagree**
12-It should be useful for the auditor to indicate either in the audit report or in a separate statement, the extent of their examination of the operating and financial review.	1	2	3	4	5
13- It should be useful for the auditor to indicate either in the audit report or in a separate statement, the extent of their examination of any other information included in the annual report but outside the financial statements.	1	2	3	4	5
14-The value of the audit would be enhanced if the auditor reported, either in the audit report or in a separate statement, in respect of each audit engagement the scope of their study of the client's internal control.	1	2	3	4	5
15-The value of the audit would be enhanced if the auditor reported, either in the audit report or in a separate statement, in respect of each audit engagement the extent to which they relied on internal controls.	1	2	3	4	5

Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
16- The value of the audit would be enhanced if the auditor reported, either in the audit report or in a separate statement, in respect of each audit engagement the materiality level they used.	1	2	3	4	5
17-The value of the audit would be enhanced if, for each audit, the report explained the most difficult issues arising in the audit and how they had been resolved.	1	2	3	4	5
18-An auditor should always report on corporate governance issues for which they have a responsibility.	1	2	3	4	5
19-The directors' statement in respect of corporate governance is useful.	1	2	3	4	5

Section IV

The Role of Users' Education in Reducing the Auditing Expectations Gap[12]

Identify to which extent do you agree or disagree that educating users towards the following issues would contribute to the reduction of the auditing expectations gap:

Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
1-The auditor's responsibility for the soundness of the internal control structure of the company.	1	2	3	4	5
2-The auditor's legal responsibility to the different users.	1	2	3	4	5
3-The auditor's responsibility for maintaining accounting records of the company.	1	2	3	4	5
4-The auditor's responsibility for detecting all fraud.	1	2	3	4	5
5-The auditor's responsibility for preventing all fraud.	1	2	3	4	5
6-The auditor's unbiased and objectivity.	1	2	3	4	5
7-The financial statements' true and fair view.	1	2	3	4	5
8-The assurance that the financial statements contain no material misstatements.	1	2	3	4	5
9-The extent of audit work performed explained in the audit report.	1	2	3	4	5

[12] adapted from Fadzly, M. N. and Ahmad, Z. (2004).

Statements	**Strongly Agree**	**Agree**	**Neutral**	**Disagree**	**Strongly Disagree**
10-The extent of assurance given by the auditor indicated in the audit report.	**1**	**2**	**3**	**4**	**5**
11-The auditor trustworthy.	**1**	**2**	**3**	**4**	**5**
12-The audited financial statements usefulness in monitoring the company's performance.	**1**	**2**	**3**	**4**	**5**
13-The audited financial statements usefulness for decision making.	**1**	**2**	**3**	**4**	**5**

Section V

The Role of Standards Settings in Reducing the Auditing Expectations Gap[13]

Identify to which extent do you agree or disagree that the following standards regarding extending the auditors' roles and responsibilities would contribute to the reduction of the auditing expectations gap:

Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
1- Increasing regulation governing auditor appointment.	1	2	3	4	5
2- Increasing regulation governing provision of non-audit services.	1	2	3	4	5
3- Increasing regulation governing rotation of audit partner.	1	2	3	4	5
4- Increasing regulation governing rotation of audit firm.	1	2	3	4	5
5-Extending auditor responsibilities as regards fraud detection.	1	2	3	4	5
6-Extending auditor responsibilities as regards going concern certification.	1	2	3	4	5
7-Extending auditor responsibilities as regards wider stakeholders.	1	2	3	4	5

[13] adapted from Dewing, I. P., and Russell, P. O. (2002).

Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
8- Assigning independent body responsible for monitoring of audit work.	1	2	3	4	5
9- Assigning independent body responsible for disciplining of auditors.	1	2	3	4	5
10- Joint and several liabilities of audit partners on its own provide assurance to the quality of auditors' work.	1	2	3	4	5
11- Liability of auditors should be restricted.	1	2	3	4	5

Section VI

The Role of Voluntary Corporate Disclosure Auditing in Reducing the Auditing Expectations Gap

Identify to which extent do you agree or disagree that expanding the auditors' roles and responsibilities to include the provision of assurance for the following voluntary corporate disclosures would contribute to the reduction of the auditing expectations gap:

Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
1. General Disclosure[14]					
1.1 Mission & vision.	1	2	3	4	5
1.2 Statement of corporate strategy.	1	2	3	4	5
1.3 Top management names / experience.	1	2	3	4	5
1.4 Majority of stockholders (composition of shareholdings).	1	2	3	4	5
1.5 Organization structure.	1	2	3	4	5
1.6 Statement of corporate goals and objectives.	1	2	3	4	5
1.7 Presentation of annual reports in Arabic & English.	1	2	3	4	5
2. Market Disclosure[15]					
2.1 Industry size.	1	2	3	4	5
2.2 Product (s) information.	1	2	3	4	5
2.3 Customers' information.	1	2	3	4	5
2.4 Supplier information.	1	2	3	4	5
2.5 Market (s) information.	1	2	3	4	5
2.6 Market share.	1	2	3	4	5

[14] adapted from Barako, D., *et al.* (2006).

[15] adapted from Barako, D., *et al.* (2006).

Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
2.7 Competitive environment.	1	2	3	4	5
2.8 Productivity capacity.	1	2	3	4	5
2.9 Productivity indicators.	1	2	3	4	5
2.10 Marketing networks.	1	2	3	4	5
2.11 Physical outputs.	1	2	3	4	5
3. Risk Management Disclosure[16]					
3.1 Financial risk (interest rate, currency, credit & fin. Instruments).	1	2	3	4	5
3.2 Political risk (international business).	1	2	3	4	5
3.3 Market risk (competition, market share).	1	2	3	4	5
3.4 Technology risk (rapid change)	1	2	3	4	5
3.5 Environmental risk (laws & regulations).	1	2	3	4	5
3.6 Weather risk (climate conditions).	1	2	3	4	5
3.7 Government regulation risk (control, regulation, taxation).	1	2	3	4	5
3.8 Seasonality risk (natural seasonal patterns).	1	2	3	4	5
3.9 Operational risk (technical, accidents, human error & loss).	1	2	3	4	5
3.10 Cyclicality risk (natural cyclical trend).	1	2	3	4	5

[16] adapted from Lajili, K. and Zeghal, D. (2005).

Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
3.12 Natural resources risk (reserves quality and quantity).	1	2	3	4	5
4. Financial Disclosure[17]					
4.1 Financial ratios & statistics.	1	2	3	4	5
4.2 Industry ratios.	1	2	3	4	5
4.3 Using charts, graphs, photos.	1	2	3	4	5
4.4 Market Share price.	1	2	3	4	5
4.5 Bank loans, mortgages and their uses.	1	2	3	4	5
4.6 Information of capital structure.	1	2	3	4	5
4.7 Information of dividends policy.	1	2	3	4	5
4.8 Reasons and effects of acquisions / disposals on past results.	1	2	3	4	5
4.9 Information of foreign sales.	1	2	3	4	5
4.10 Financial information on quarterly basis.	1	2	3	4	5
4.11 Changes in inventory level.	1	2	3	4	5
4.12 Dividends per share compared with previous years.	1	2	3	4	5
5. Human Resources Disclosure[18]					
5.1 Consultation with employees.	1	2	3	4	5
5.2 Employee share ownership.	1	2	3	4	5
5.3 Employment data.	1	2	3	4	5
5.4 Pension commitment.	1	2	3	4	5
5.5 Employees health & safety.	1	2	3	4	5

[17] adapted from Barako, D., *et al.* (2006).

[18] adapted from Gray, R., *et al.* (1995).

Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
5.6 Average compensation of employees.	1	2	3	4	5
5.7 Percentage of foreign and national labour force.	1	2	3	4	5
5.8 Information of training and employee development.	1	2	3	4	5
5.9 Number of employees trained.	1	2	3	4	5
5.10 Amount spent on training.	1	2	3	4	5
6. Research & Development Disclosure[19]					
6.1 Inputs: Product.	1	2	3	4	5
6.2 Inputs: People.	1	2	3	4	5
6.3 Input: Infrastructure.	1	2	3	4	5
6.4 Outputs: Actual achievements (Product development).	1	2	3	4	5
6.5 Outputs: Actual achievements (Beyond Product development).	1	2	3	4	5
6.6 Outputs: Potential achievements.	1	2	3	4	5
6.7 Output: Product timing.	1	2	3	4	5
6.8 Future expenditures.	1	2	3	4	5
6.9 Financing Past, Present, and Future.	1	2	3	4	5
6.10 Accounting/ financing (Comparing prior years, competition, budget).	1	2	3	4	5
6.11 R&D ratios.	1	2	3	4	5
6.12 R&D as explanatory.	1	2	3	4	5
6.13 Explaining R&D changes.	1	2	3	4	5

[19] adapted from Entwistle, G. (1999).

Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
7. Environmental, Social, and Ethical Disclosure[20]					
7.1 Environmental reports.	1	2	3	4	5
7.2 Value added statement.	1	2	3	4	5
7.3 Social activities & contributions.	1	2	3	4	5
7.4 Environmental health safety.	1	2	3	4	5
7.5 Energy Information.	1	2	3	4	5
7.6 Community information.	1	2	3	4	5
7.7 Charitable donations information.	1	2	3	4	5
7.8 Using photocopy of awarded certificates.	1	2	3	4	5
7.9 Methods of provisions computation.	1	2	3	4	5
7.10 Employment of disabilities.	1	2	3	4	5
7.11 Ethical actions.	1	2	3	4	5
8. Corporate Governance Disclosure[21]					
8.1 Major share ownership and voting rights.	1	2	3	4	5
8.2 List of board members.	1	2	3	4	5
8.3 Picture of chairperson and/or other members.	1	2	3	4	5
8.4 Board member qualifications.	1	2	3	4	5
8.5 Number of shares held by members of the board.	1	2	3	4	5

[20] adapted from Gray, R., *et al.* (1995).

[21] adapted from Collett, P., *et al.* (2005).

Statements	**Strongly Agree**	**Agree**	**Neutral**	**Disagree**	**Strongly Disagree**
8.6 Remuneration policy for board members and key executives.	**1**	**2**	**3**	**4**	**5**
8.7 Audit committee members: names, addresses, experiences	**1**	**2**	**3**	**4**	**5**
8.8 Corporate governance codes, policies, implementation extent.	**1**	**2**	**3**	**4**	**5**

5.5.2 The Sample Population

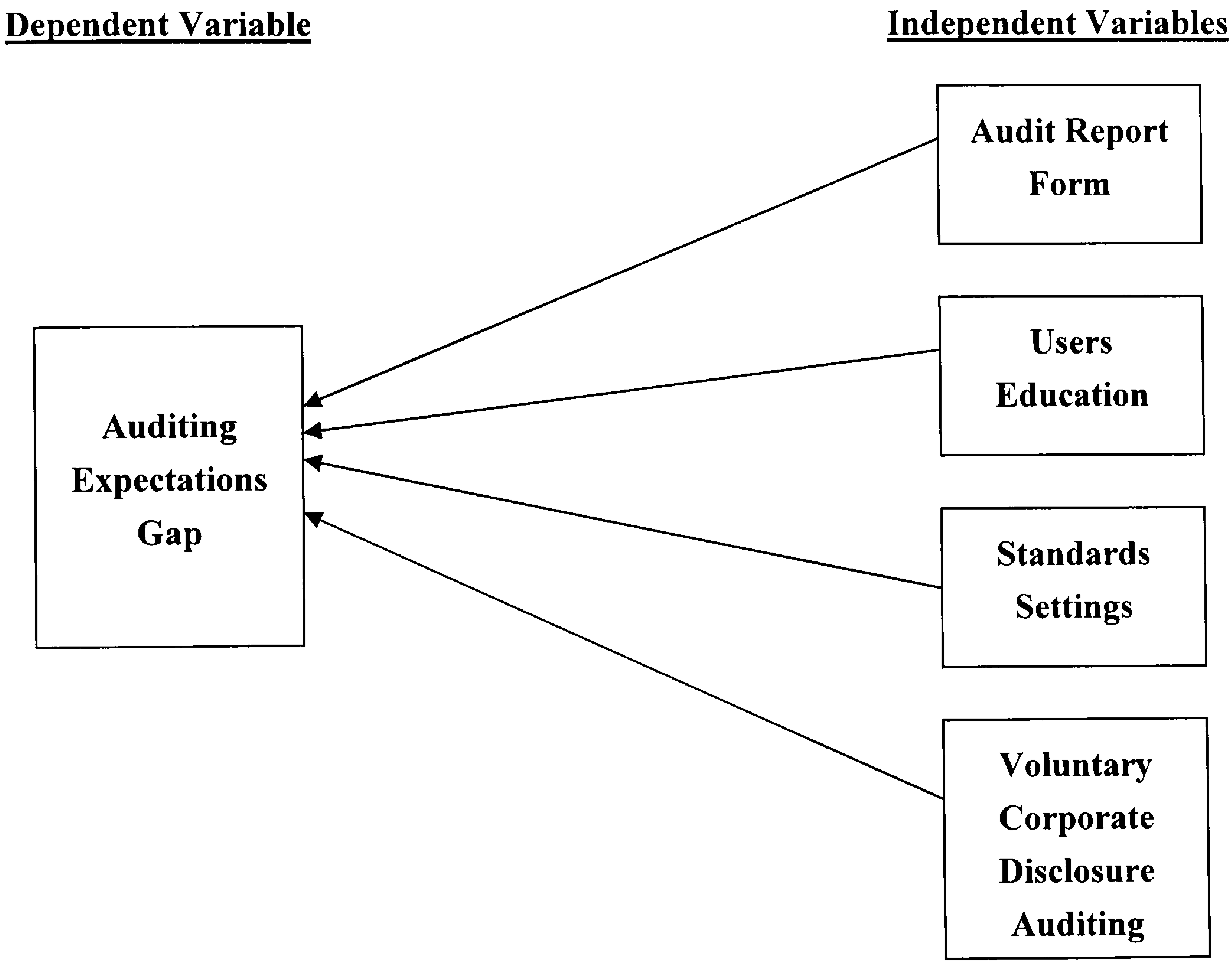
The current research is based upon the stakeholder-agency theory as previously mentioned. Therefore, the selected sample should be a representative of the different stakeholders with their various backgrounds, educations and empowerments. As a result, the current research is applied over the same sample that is applied by Dixon *et al.* (2006) which investigated the existence of the auditing expectations gap in Egypt using a sample composed of three groups of users; auditors, investors, bankers. The current research would add to the previously mentioned groups a sample of academics group. The academics are included in the sample as they play a consulting role in the standard setting process in Egypt. The four sample groups would have equal weights as to overcome any bias that may exists towards any category. Since the sample is categorized over four categories, therefore the sample size must be divisible equally by the 4 categories which may results in selecting a sample of 400 respondents (Dixon *et al.*, 2006; Manson and Zaman, 2000; Best, 1999; Fadzly and Ahmad, 2004).

5.5.3 Model Dependent and Independent Variables

The variables of the model are shown by the following figure:

Figure 5.5

Investigating the Effectiveness of the Different Methods of Reducing Auditing Expectations Gap



5.5.3.1 Independent Variables Definition and Measurement

As a matter of fact, any research needs to identify the thing that is going to be measured, and how to be measured. The model includes four independent variables as follows:

1 The audit report form.
2 The Users education.
3 The standards settings.
4 Voluntary corporate disclosure auditing.

5.5.3.1.1 The Audit Report Form

The audit report is one of the most important components of the annual reports and it is prepared by an independent external auditor who judges the trueness and fairness of the statements prepared by the company. The audit report could have the form of a short-form audit report with comprehensive view of his opinion about the statements of the company, or it takes the long-form view which shows in details the scope and responsibilities of his tasks to give his/her opinion in the statements and reports of the company.

The effect of the audit report form on the auditing expectations gap is measured using the questionnaire technique by measuring the perceptions of the examined sample on a 5-Point Likert scale (1 strongly agree – 5 strongly disagree). The data is collected from the different samples with their different perceptions. These perceptions are transformed to values from 1 to 5 which could then be analyzed using the proper statistical test to identify the relationship of the audit report form with the auditing expectation gap in Egypt. By analyzing the significant differences between the different categories' perceptions it could be measured how effective this method in reducing the audit expectations gap.

5.5.3.1.2 The Users Education

The users of the annual reports are characterized by having a variation of education backgrounds. However, it is not a prerequisite to have accounting and auditing backgrounds to be a user of the annual reports. Therefore, the user's education may have a vital role in understanding the annual reports and the auditors' scope and responsibilities regarding auditing the statements and reports of the annual reports. The education of the users, as a method of reducing the auditing expectations gap, is examined by the perceptions of the different categories of the sample population and how effective it would be a reducing method for the auditing expectations gap.

The perceptions of the respondents are measured by a 5-Point Likert scale (1 strongly disagree – 5 strongly agree) by using a questionnaire technique the perceptions are converted to values applicable to be analyzed using the suitable statistical analysis.

5.5.3.1.3 The Standards Settings

The standards are the regulations of the accounting and auditing profession that cannot be violated. Otherwise, it is considered to be legally a crime which might lead to cheating in the company's statements and the annual reports, creating a misleading impression for these reports' users and making wrong decisions. Therefore, the standards are considered to be the law of the accounting and auditing profession.

However, the research is concerned with the auditing standards as it is considered one of the methods of reducing the auditing expectations gap is to settle standards that expand the scope and responsibilities of the auditors towards the auditing process to increase the trustiness and fairness of the audited statements and reports. Therefore, the auditors could meet the users' expectations and reduce the auditing expectations gap.

This variable is measured by the perceptions of the examined population towards the effectiveness of this method to reduce the auditing expectations gap in Egypt. The perceptions are transferred to values using the 5-Point Likert scale (1 strongly disagree – 5 strongly agree). The values of the respondents' perceptions are examined to identify how effective this method in reducing the auditing expectation gap compared to the other methods (independent variables).

5.5.3.1.4 Voluntary Corporate Disclosure Auditing

The voluntary disclosure is considered to be additional disclosure by the companies to their mandatory disclosure that is regulated by the standards. This disclosure is useful to improve the decision making process of the different users. As mentioned before it is composed of different categories as: general information disclosure, human resources disclosure, extra financial analysis tools disclosure, risk management disclosure, research and development disclosure.

Voluntary disclosure auditing is considered to be a proposed method of reducing the auditing expectations gap. It is measured using the different perceptions of the different categories of the examined sample by a five-point Likert scale that transform the perceptions to values as to identify the effectiveness voluntary disclosure auditing in reducing the auditing expectations gap compared to the other different methods (independent variables).

5.5.3.2 Dependent Variable Definition and Measurement

The main variable of the research is the auditing expectations gap. The aim of the current research is to measure the auditing expectations gap and to examine the effective methods that would be able to reduce this gap.

The auditing expectations gap is measured using the same five-point Likert scale questionnaire used to examine the effectiveness of the different solutions to reduce the auditing expectations gap in Egypt. The relationships between the dependent variable and the independent variable would result in examining the most effective method for reducing the audit expectations gap.

The audit report form, the users' education, and the standards settings are considered to be the traditional solutions to reduce the auditing expectations gap. While voluntary disclosure auditing represents the proposed solution of the study. Therefore, the proposed solution is the main concern of the study to examine its effectiveness to reduce the auditing expectation gap compared to the effectiveness of the other three traditional solutions. Consequently, this model tests the following hypothesis:

Hypothesis 2 – *The voluntary corporate disclosure audit is more effective method of reducing the auditing expectations gap in Egypt than the traditional methods (i.e auditing report form, users' education, standards settings).*

5.5.4 Model Statistical Tests

The model would be examined using Mann-Whitney-U non-parametric test for significant difference between auditors and each non-audit group (academics, investors, and bankers) from one side, and between auditors and the overall non-audit groups from the other side. The Mann-Whitney-U non-parametric test was chosen as it examines the significant difference in response means between two populations based on the Z scores and *p* values of the examined variables without the need to test for normality as this test is used even if the distribution was normal. However, the normality of distribution is examined using Kolmogorov-Smirnov test (Best, 1999).

A t-test is applied over the examined sample as to examine the sensitivity of the results towards changing the type of the test by using a parametric test instead of the main Mann-Whitney-U non parametric test. The t-test is applied using a confidence level of 95%. A dummy variable of value 0 and 1 is inhibited in data analysis to differentiate between the two examined groups as 1 represents the auditor group while the 0 represents the non – audit group. The model is statistically analyzed using STATA 9 statistical package.

5.6 CONCLUSION

From the previous discussion it is concluded that the employed methodology is justified by the objectivist (realism) ontological position and the positive epistemology. This position is considered to be a consequence of the stakeholder-agency theory employed by the research and shown in the previously discussed chapter. The stakeholder - agency theory is considered to be a positive theory comprises the objective ontology. Therefore, the hypothetico-deductive approach (testing theory) would be the appropriate methodology to be employed with this type of research. Hence, the research uses two survey instruments to gather the data. First instrument is a pre-designed checklist used to gather the secondary data to examine the model's hypotheses through investigating the level and determinates of voluntary corporate disclosure. Second instrument is a valid and reliable questionnaire to gather the primary data used in investigating the effectiveness of the different methods of reducing the auditing expectations gap. Therefore, the current research includes primary and secondary data, beside using quantitative and qualitative analysis tests.

The methodology of the research includes two groups of hypotheses that are related to the voluntary disclosure. The hypotheses are examined by two different models. First, examines the hypotheses of the relationship between the voluntary disclosure and its determinants including firm characteristics (firm size, firm profitability, industrial membership) and the hypotheses of the relationship between the voluntary disclosure and corporate governance characteristics (board size, role duality, and board composition). Second, examining the hypothesis of the effectiveness of voluntary corporate disclosure auditing, compared to the effectiveness of the audit report form, users' education, and standards settings, towards reducing the existing auditing expectations gap in Egypt.

The research methodology is considered to be the bridge between the theoretical perspective and the empirical analysis of the research. The theoretical framework indicates that the research is employing the stakeholder-agency theory as a positive accounting theory. The employed stakeholder - agency theory justifies the used research methodology to examine the different hypotheses which are developed based the same theory. Therefore, the research is testing the theory through its hypotheses rather than building a theory which directs the research towards using the hypothetico-deductive methodology. The selected deductive methodology shows the sequential stages through which the empirical analysis will progress in the following chapters.

CHAPTER SIX

LEVEL AND DETERMINANTS OF VOLUNTARY CORPORATE DISCLOSURE

6.1 INTRODUCTION

The chapter has two main objectives. First objective is measuring the level of voluntary corporate disclosure and its different categories using descriptive analysis. Second objective is examining the determinants of voluntary corporate disclosure and testing the hypotheses of the association between these different determinants and the different categories of voluntary corporate disclosures. The level of voluntary disclosure in the annual reports of the Egyptian companies is characterized by being relatively low level whether in year 2004-2005 or in year 2005-2006. The findings of the empirical analysis showed the contribution of each voluntary disclosure category to the whole level of disclosure over the two examined years. These findings indicated that specific categories' level increase on the expense of the other group of disclosure categories.

The second part of this chapter investigates the association between the total voluntary disclosure and its determinants from one side, and the association between each disclosure category and the different determinants from the other side. The determinants are classified in to two groups. First group is firm characteristics determinants. Second group is corporate governance characteristics determinants.

Finally, a sensitive analysis is applied to identify the effect of changing the statistical test on the results and findings of the main applied test. The applied sensitivity analysis findings have not got significant differences from the main test ensuring that the selected test fits with the examined sample.

6.2 MEASURING THE LEVEL OF VOLUNTARY CORPORATE DISCLOSURE

The main objective of this analysis is examining the level of voluntary disclosure and its different categories. The empirical study of this model is considered to be a descriptive analysis that shows the average voluntary disclosure and the averages of the different components of this voluntary disclosure. The descriptive study includes three different panels. First panel includes the disclosures of year 2004 – 2005. Second panel includes the disclosures of year 2005 – 2006. Third panel includes the average total disclosures of the two panels.

The descriptive statistics of the different panels of voluntary corporate disclosure categories are shown in the following tables:

Table 6.1

Descriptive Statistics of Panel A: 2004 - 2005

Type of Disclosure	Mean (Median)	Standard Deviation	Min. (Max.)	Standard Skewness	Standard Kurtosis
Total Voluntary Disclosure	0.22 (0.20)	0.11	0.05 (0.54)	1.03	3.56
General Disclosure	0.24 (0.29)	0.21	0.00 (0.86)	1.04	3.70
Market Disclosure	0.39 (0.36)	0.19	0.00 (0.82)	0.52	3.77
Risk Management Disclosure	0.11 (0.08)	0.13	0.00 (0.50)	1.29	4.05
Financial Disclosure	0.27 (0.25)	0.15	0.00 (0.67)	0.65	3.37
Human Resources Disclosure	0.19 (0.20)	0.15	0.00 (0.60)	0.70	3.14
Research & Development Disclosure	0.20 (0.15)	0.19	0.00 (0.77)	1.47	4.50
Environmental, Social, & Ethical Disclosure	0.16 (0.09)	0.16	0.00 (0.64)	1.36	4.49
Corporate Governance Disclosure	0.19 (0.13)	0.19	0.00 (1.00)	2.07	8.97

Table 6.1 shows the descriptive statistics of the total voluntary disclosure level and the level of each of the voluntary disclosure's categories for the first panel of data at year 2004–2005. The total voluntary disclosure's level presents 22% of the examined checklist items which variant between 5% and 54% for the least and highest Egyptian companies disclosures respectively. Moreover, the market disclosure represents the highest disclosure level of 39%, while the risk management disclosure presents the lowest disclosure level of 11%. In addition, it is observed that the maximum disclosure is presented by the corporate governance disclosure of 100%. As common notice for the whole categories of disclosure is that the minimum disclosure for any category of disclosure is 0%, which means that at least one company of the examined companies miss at least one category of the presented categories of disclosure. This is an indicator that there is not yet a dominant category of voluntary disclosure that all companies in the examined sample agree to disclose.

Moreover, in relation to standard skewness statistics the presented data is not normally distributed. As a common rule, the standard skewness of the data needs to be within the range of ±1.96 (Haniffa and Hudaib, 2006). It is observed that the corporate governance standard skewness is 2.07 which exceed the range of ±1.96 evidencing that the data is not normally distributed. Additionally, with respect to the standard kurtosis the data is not normally distributed. The data is said to be normally distributed if the standard kurtosis fall in the range of ±3 (Haniffa and Hudaib, 2006). The standard kurtosis of the total voluntary disclosure and its different categories exceed the range of ±3 indicating that the data is not normally distributed. As a result any hypotheses test related to the entire data needs to use a robust analysis.

Table 6.2

Descriptive Statistics of Panel B: 2005 - 2006

Type of Disclosure	Mean (Median)	Standard Deviation	Min. (Max.)	Standard Skewness	Standard Kurtosis
Total Voluntary Disclosure	0.22 (0.20)	0.11	0.05 (0.5)	0.82	3.07
General Disclosure	0.25 (0.14)	0.22	0.00 (0.86)	0.95	3.20
Market Disclosure	0.40 (0.36)	0.20	0.00 (0.82)	0.18	3.33
Risk Management Disclosure	0.13 (0.08)	0.13	0.00 (0.5)	0.99	3.33
Financial Disclosure	0.26 (0.25)	0.15	0.00 (0.67)	0.76	3.60
Human Resources Disclosure	0.19 (0.15)	0.17	0.00 (0.60)	0.69	2.55
Research & Development Disclosure	0.21 (0.15)	0.19	0.00 (0.77)	1.24	3.95
Environmental, Social, & Ethical Disclosure	0.16 (0.09)	0.17	0.00 (0.64)	1.18	3.78
Corporate Governance Disclosure	0.19 (0 .13)	0.21	0.00 (1.00)	1.73	6.69

Table 6.2 shows the descriptive statistics of the total voluntary disclosure level and the level of each of the voluntary disclosure's categories for the second panel of data at year 2005 – 2006. These results indicate that the mean total voluntary disclosure is 22% which is considered a low level of voluntary disclosure. The highest component of the voluntary disclosure is the market disclosure of 40%, reflecting the severe competition between the different companies in the Egyptian market, as the market disclosure may act as a sort of promotion for the company. The lowest disclosure level is represented by the risk management disclosure of 13%, which is a bad sign that the company is exposed to high risk, that it is not disclosing their risk management activities and how they are dealing with the risk the company is exposed to.

The descriptive statistics shows the normality of the different variables data. It is noted that the corporate governance represents the maximum skewness of 1.73, while the market disclosure shows the minimum skewness of 0.18. This indicates that the minimum and maximum skewness are within the normally distributed range of ±1.96 (Haniffa and Hudaib, 2006). While the Kurtosis of the disclosure data indicate that most of the disclosure data is not normally distributed. The maximum Kurtosis is shown by the corporate governance disclosure of 6.69, while the minimum Kurtosis is shown by the human resources disclosure of 2.54. With reference to the Kurtosis most of the disclosure data is not normally distributed as they are out of the range of ±3 (Haniffa and Hudaib, 2006).

Table 6.3

Descriptive Statistics of Panel C: Average Total Disclosure

Type of Disclosure	Mean (Median)	Standard Deviation	Min. (Max.)	Standard Skewness	Standard Kurtosis
Total Voluntary Disclosure	0.22 (0.20)	0.11	0.05 (0.54)	0.92	3.30
General Disclosure	0.25 (0.14)	0.22	0.00 (0.86)	1.00	3.44
Market Disclosure	0.40 (0.36)	0.19	0.00 (0.82)	0.34	3.53
Risk Management Disclosure	0.12 (0.08)	0.13	0.00 (0.50)	1.14	3.66
Financial Disclosure	0.27 (0.25)	0.15	0.00 (0.67)	0.71	3.48
Human Resources Disclosure	0.19 (0.20)	0.16	0.00 (0.60)	0.69	2.81
Research & Development Disclosure	0.21 (0.15)	0.19	0.00 (0.77)	1.35	4.21
Environmental, Social, & Ethical Disclosure	0.16 (0.09)	0.16	0.00 (0.64)	1.27	4.11
Corporate Governance Disclosure	0.19 (0.13)	0.20	0.00 (1.00)	1.89	7.70

Table 6.3 presents the descriptive statistics of the average panel data (panel C) of years 2004 – 2005 (panel A) and 2005 – 2006 (panel B). The average total voluntary disclosure does not differ from the two panel averages which is 22% emphasizing that there is a sort of stability in the voluntary disclosure volume and practices over the examined period under study. Still the market disclosure scoring the highest disclosure level among voluntary disclosure categories of an average 40% showing that the companies are using this sort of disclosure as an effective method of advertising and promotion for their products and services. On the other hand, risk management disclosure presents the least disclosure level among the different categories of voluntary disclosure which may be either that the Egyptian companies are not exposed to different risks that make it worthy for them to disclose voluntarily additional information about these sort of risks, or that the companies are not yet recognizing their exposure to different types of risks that they need to disclose how they are managed and well prepared to face this sort of risk.

Moreover, the average maximum disclosure is 54%, while the minimum average disclosure is 5% indicating a high distortion in voluntary disclosure volume and practices between the examined companies. However, the maximum disclosure score is performed by the corporate governance disclosure which means that at least one company has disclosed all the required corporate governance items, while the minimum score of disclosure is common among the different categories of voluntary disclosure which is 0% indicating that at least one company totally missed disclosing any information about at least one of the voluntary disclosure categories.

It is observable that, based on the standard skewness parameter, the data is considered to be normally distributed as it falls within the range of ±1.96 (Haniffa and Hudaib, 2006). While with respect to the standard Kurtosis, the data is not normally distributed as all of the voluntary disclosure categories, except the human resources disclosure, exceeds the range of ±3 (Haniffa and Hudaib, 2006).

Since the data is not normally distributed, that would have some shadows over the selected test to examine the research hypotheses applied over the entire data. Therefore, a robust analysis should be employed when testing the research hypotheses in the further analysis.

The distribution of the different categories of voluntary disclosure in the different panels would be presented by the following pie charts:

Figure 6.1

Voluntary Corporate Disclosure Categories of Panel A: 2004 - 2005

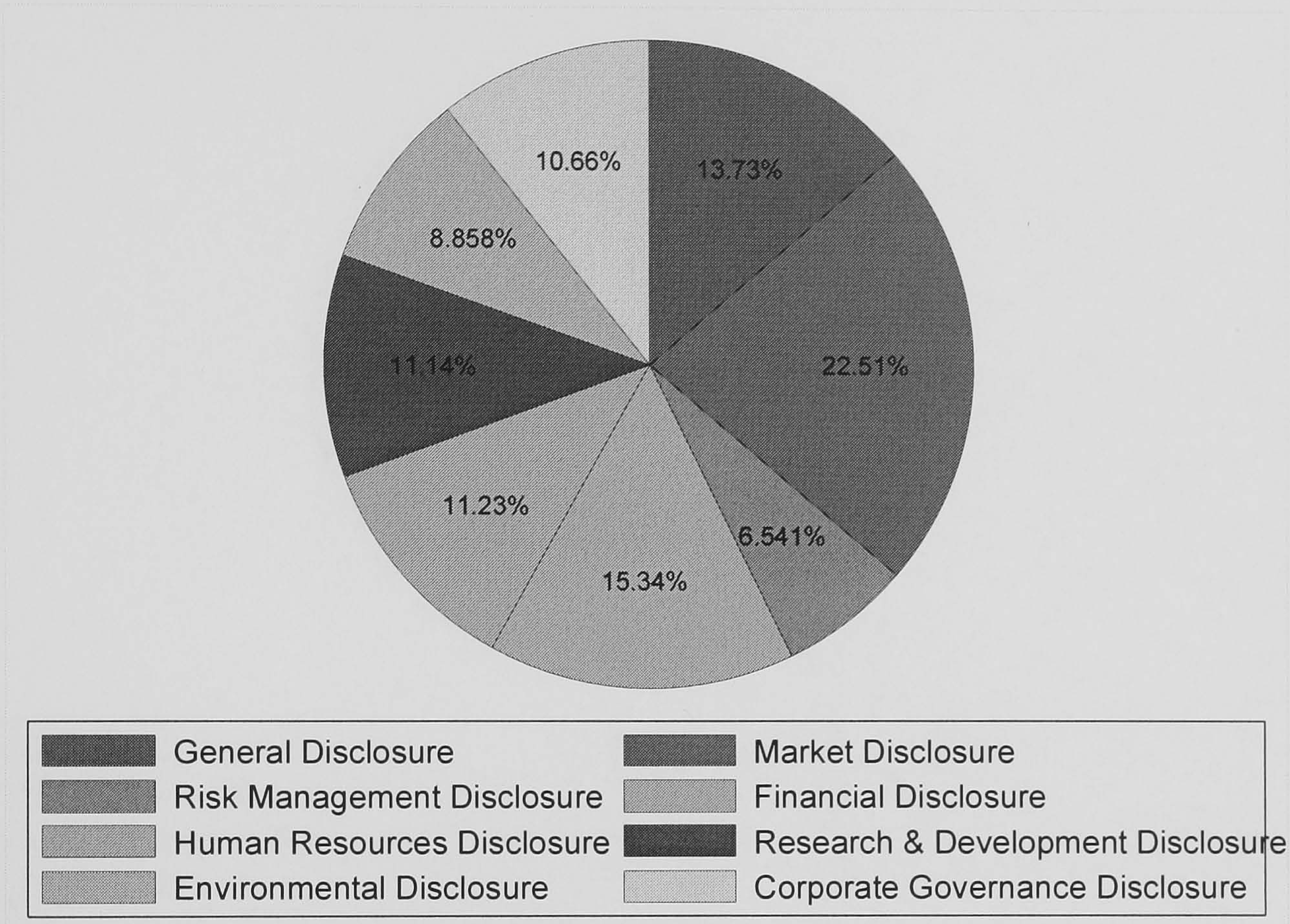


Figure 6.1 pie chart indicates the different percentages of the different categories of voluntary disclosure during the year 2004 – 2005 (panel A). The chart is built on an assumption that the total voluntary disclosure represents 100%. Therefore, the chart shows how this 100% is distributed over the different categories. It is observed that the largest portion of the total voluntary disclosure is the market disclosure of 22.51%, while the least portion is the risk management disclosure of 6.541%. This is an expected result as both categories achieved the highest and lowest levels of disclosures respectively shown in table 6.1. Environmental, social, and ethical disclosure level is relatively low level 8.86% of the total voluntary disclosure level regarding the need for the introduction of new incentives that are related the corporate social responsibilities of the companies dealing with the Egyptian culture.

Figure 6.2

Voluntary Corporate Disclosure Categories of Panel B: 2005 - 2006

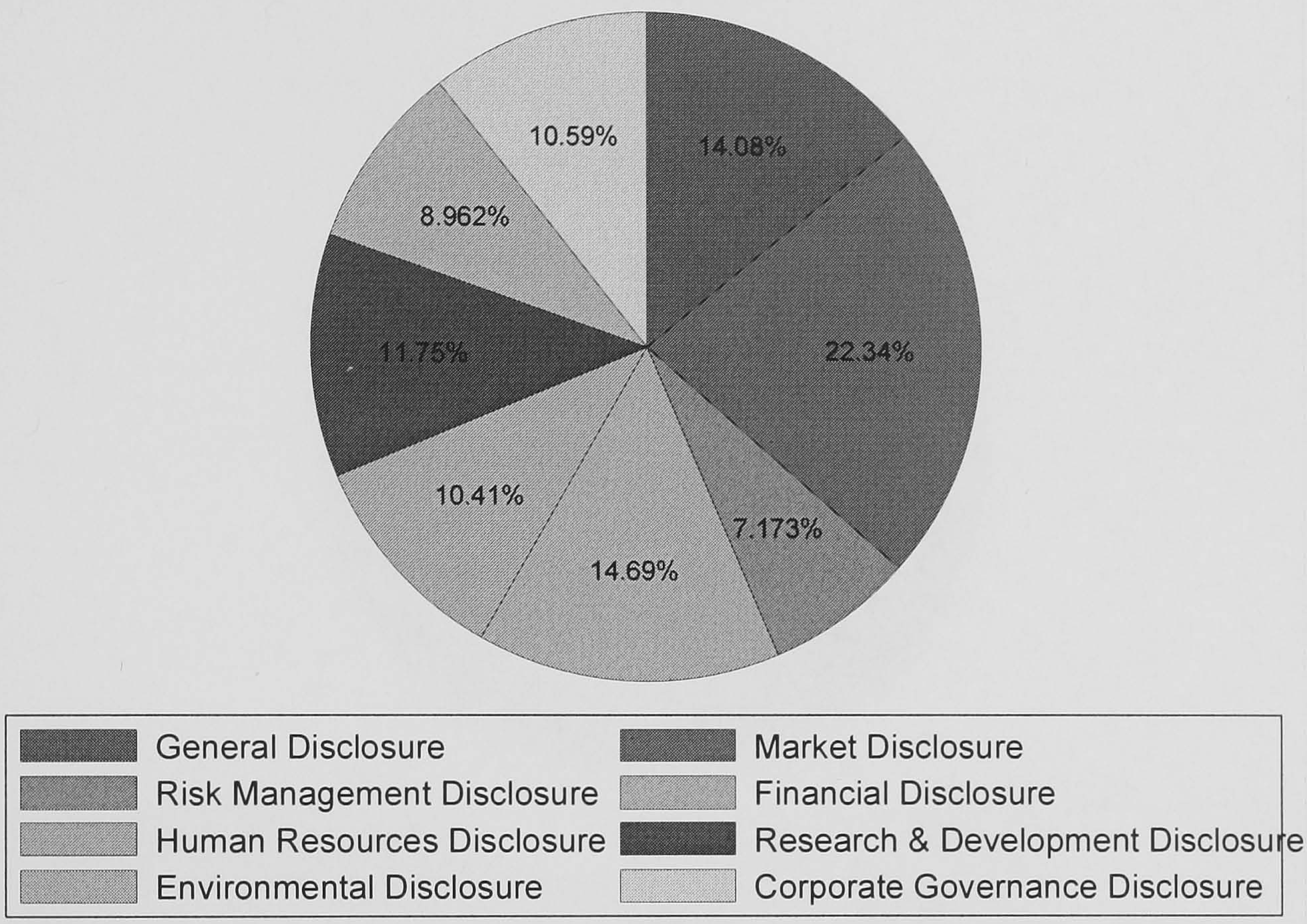


Figure 6.2 pie chart indicates the different percentages of the different categories of voluntary disclosure during the year 2005 – 2006 (panel B). It is observed that the largest portion of the total voluntary disclosure is the market disclosure of 22.34%, while the least portion is the risk management disclosure of 7.173%. This is an expected result as both categories achieved the highest and lowest levels of disclosures respectively shown in table 6.2. The disclosure structure did not change much since the previous year 2004 – 2005 (panel A) indicating a low rate of disclosure improvements over this period of time. Therefore, Egyptian companies needs some stimulations and incentives to improve their voluntary disclosure without introducing any obligatory procedures as that contradicts with the voluntary disclosure of this sort of disclosure.

Figure 6.3

Voluntary Corporate Disclosure Categories of Panel C: Average Total Disclosure

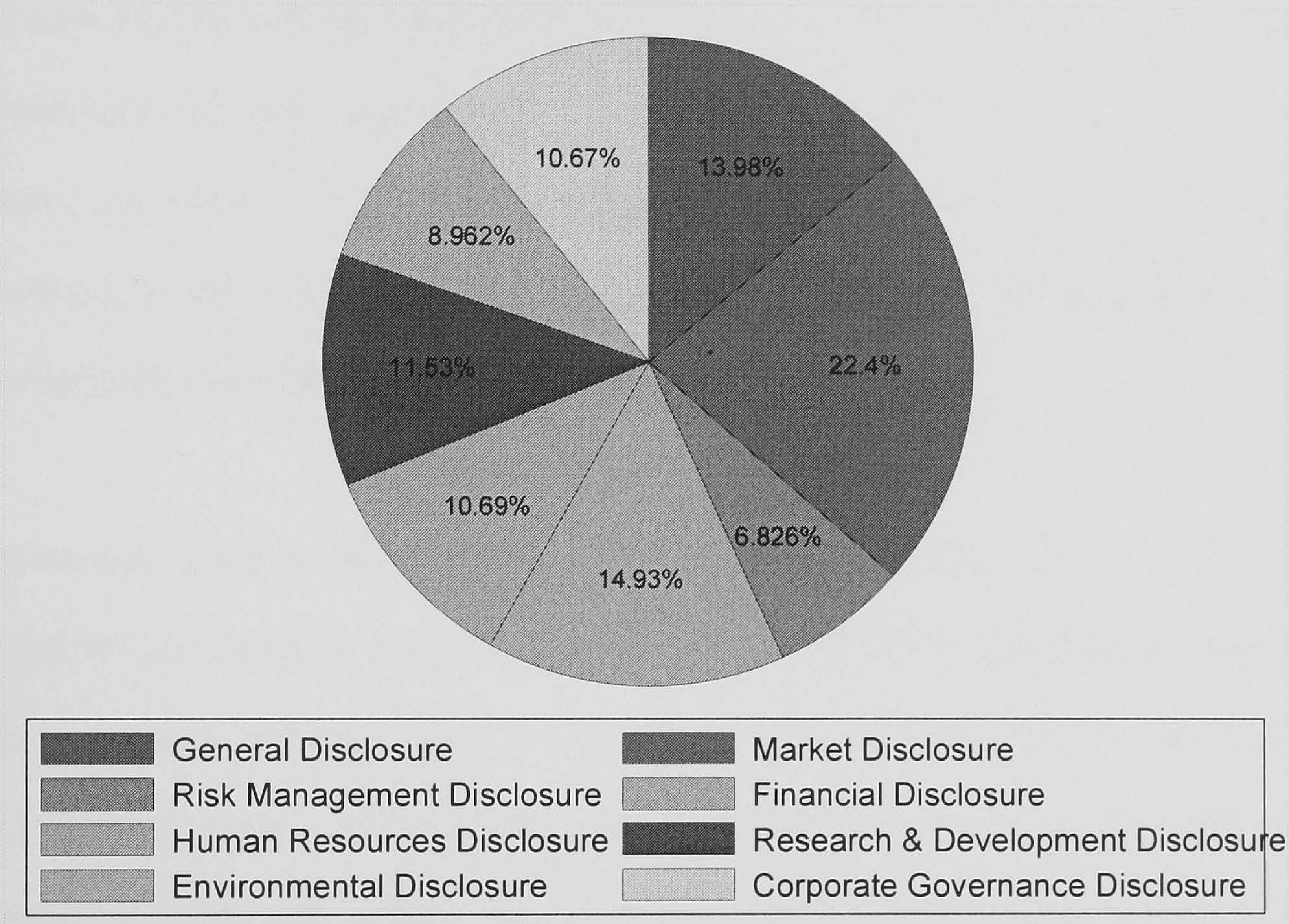


Figure 6.3 pie chart indicates the different percentages of the different categories of voluntary disclosure for an average (panel C) of year 2004 – 2005 (panel A) and year 2005 – 2006 (panel B). It shows that the maximum component of voluntary corporate disclosure is the market disclosure representing 22.4% of the total voluntary disclosure. This is an indicator to the highly competitive market in Egypt, as the market disclosure in this case is used as a sort of promotion of the company which is the motive for the highly concern with this component of the voluntary disclosure.

On the other hand, the risk management represents the minimum component of the voluntary corporate disclosure as it represents 6.826% of the total voluntary disclosure. The low level of the risk management may be a good sign or a bad sign. It is a good sign that it indicates that the companies are not exposed to high degree of risk so therefore it has a limited risk management disclosure. This is considered to be a theoretical case as one of the main indicators of the company's survival and growth is how it deals with and manages the risk it is exposed to. The bad sign is that the companies are not recognizing the risk they are exposed to and so they are not managing this risk, or the risk is recognized but the companies have no strategy to manage the risk it is exposed to. In both cases it would be a reason not disclosing with a respectable level about managing risk.

Moreover, the corporate governance disclosure is considered to be a low level of 10.67%. The corporate governance is a new phenomenon of controlling and directing the company's activities which is not yet introduced with an acceptable level by the Egyptian companies. The corporate governance disclosure indicates that the Egyptian companies need more efforts and concern for introducing this phenomenon to their activities. Therefore, the corporate governance is not yet considered to be effective in the Egyptian context. This point is more illustrated in model (2) by examining the significance of some corporate governance to the voluntary disclosure.

Accumulatively, the results are almost consistent in between the different panels indicating the stability of the voluntary disclosure volume and practices confirming that the selected sample is well representative to the whole population of the Egyptian companies registered in Cairo and Alexandria stock exchange.

6.3 MEASURING THE DETERMINANTS OF VOLUNTARY CORPORATE DISCLOSURE

The model is examining the relationship between voluntary disclosure level and the determinants of this voluntary disclosure. The determinants of the level of the voluntary disclosure that are examined in this model are classified in to two group: firm characteristics including firm size, firm profitability, and industrial membership, and the other group is the corporate governance characteristics including board size and role duality. The model is examined after transforming the firm size and firm profitability variables to overcome the effect of the wide range of the observations of both variables. The variables are transformed using Log firm size and Log firm profitability.

6.3.1 Descriptive Statistics

The descriptive statistics of model (2) is shown in the following tables:

Table 6.4

Descriptive Statistics of Voluntary Corporate Disclosure Determinants of Panel A: 2004 - 2005

Variables	Mean (Median)	Standard Deviation	Min. (Max.)	Standard Skewness	Standard Kurtosis
Firm Size	6.03 (5.93)	0.51	5.19 (7.39)	0.60	2.85
Firm Profitability	1.15 (1.28)	0.38	0.00 (1.76)	-1.19	4.06
Industrial Membership	0.83 (1.00)	0.38	0.00 (1.00)	-1.75	4.06
Board Size	8.20 (7.00)	3.70	3.00 (23.00)	1.54	7.19
Role Duality	0.71 (1.00)	0.46	0.00 (1.00)	-0.91	1.83

The descriptive statistics of the voluntary disclosure determinants shown in table 6.4 indicates that the determinants are grouped in to firm characteristics, including firm size, firm profitability, and industrial membership, and corporate governance characteristics including board size, and role duality. Referred to the standard skewness the data is considered to be normally distributed as it is in between the normality range of skewness of ±1.96 (Haniffa and Hudaib, 2006). On the other hand, with reference to the standard kurtosis the data is considered not to be normally distributed as the kurtosis of firm profitability, industrial membership, and board size exceeds the standard normality range of ±3 (Haniffa and Hudaib, 2006).

Table 6.5

Descriptive Statistics of Voluntary Corporate Disclosure Determinants of Panel B: 2005 - 2006

Variables	Mean (Median)	Standard Deviation	Min. (Max.)	Standard Skewness	Standard Kurtosis
Firm Size	6.10 (5.96)	0.55	4.90 (7.58)	0.59	3.36
Firm Profitability	1.30 (1.41)	0.45	0.08 (1.99)	-1.12	3.82
Industrial Membership	0.80 (1.00)	0.41	0 (1)	-1.5	3.25
Board Size	11.32 (11)	4.27	5 (24)	0.83	4.05
Role Duality	0.67 (1.00)	0.47	0 (1)	- 0.74	1.56

Table 6.5 shows the descriptive statistics of the different determinants of the corporate voluntary disclosure. The determinants are classified into two groups. First group of determinants are firm characteristics, including firm size, firm profitability, and industrial membership. Second group of determinants are corporate governance characteristics, including board size, and role duality. This model is justifying the low level of corporate voluntary disclosure of 22% by its determinants.

The skewness of the different determinants indicates that the data of the different variables is not normality distributed. The maximum skewness of 0.83is represented by the board size, while the minimum skewness of -1.5 represented by the industrial membership. The minimum and maximum skewness are within the skewness range of ±1.96 which indicates the normality of the variables data (Haniffa and Hudaib, 2006). Therefore, based on the skewness the data of the different variables is normally distributed and considered to be parametric data.

The kurtosis shows that the minimum kurtosis is 1.56 which is represented by the role duality, while the maximum kurtosis is 4.05 represented by the board size. Since the minimum and maximum kurtosis are not within the range of ±3 (Haniffa and Hudaib, 2006). Therefore the data is not normally distributed and the data is considered to be non parametric. These contradictions between the Skewness and kurtosis results indicate that the data would be not normally distributed or non-parametric data.

Table 6.6

Descriptive Statistics of Voluntary Corporate Disclosure Determinants of Panel C: Average Total Disclosure

Variables	Mean (Median)	Standard Deviation	Min. (Max.)	Standard Skewness	Standard Kurtosis
Firm Size	6.07 (5.95)	0.53	4.901 (7.58)	0.61	3.17
Firm Profitability	1.22 (1.31)	0.42	0.00 (1.99)	-1.02	3.78
Industrial Membership	0.81 (1.00)	0.39	0.00 (1.00)	-1.62	3.62
Board Size	9.74 (10.00)	4.27	3.00 (24.00)	1.04	4.56
Role Duality	0.69 (1.00)	0.46	0.00 (1.00)	-0.83	1.69

The average statistics of voluntary disclosure determinants (panel C) includes the determinants of year 2004 – 2005 (panel A) and year 2005 – 2006 (panel B). The data of determinants with reference to the Standard Skewness considered to be normally distributed as it falls in between the normality range of ±1.96 (Haniffa and Hudaib, 2006). On the other hand the data is not normally distributed as firm size, firm profitability, industrial membership, and board size exceeds the normally distribution range of ±3 (Haniffa and Hudaib, 2006).

The correlation between the different categories of voluntary disclosure and the determinants of disclosure is shown using Pearson correlation coefficients in the following tables:

Table 6.7

Pearson Correlation Coefficients between Categories and Determinants of Corporate Voluntary Disclosure of Panel A: 2004 - 2005

	TVD	GD	MD	RMD	FD	HRD	RDD	ESED	CGD	FS	FP	IM	BS	RD
TVD	1.00													
GD	0.69*	1.00												
MD	0.73*	0.57*	1.00											
RMD	0.62*	0.36*	0.50*	1.00										
FD	0.61*	0.35*	0.25	0.10	1.00									
HRD	0.37*	-0.09	0.10	0.42*	0.10	1.00								
RDD	0.76*	0.43*	0.46*	0.54*	0.31	0.25	1.00							
ESED	0.65*	0.22	0.30	0.19	0.44*	0.36*	0.42*	1.00						
CGD	0.68*	0.76*	0.50*	0.12	0.61*	-0.14	0.30	0.43*	1.00					
FS	0.49*	0.48*	0.25	0.01	0.35*	0.15	0.20	0.52*	0.62*	1.00				
FP	0.43*	0.32*	0.25	0.20	0.28	0.16	0.26	0.29	0.46*	0.19	1.00			
IM	-0.46*	-0.66*	-0.57*	-0.31*	-0.16	0.15	-0.27	-0.07	-0.48*	-0.30	-0.08	1.00		
BS	-0.07	-0.14	-0.23	-0.09	0.07	-0.05	-0.05	0.14	-0.01	-0.00	0.05	0.06	1.00	
RD	0.07	-0.13	0.06	0.15	0.01	0.11	0.00	0.15	0.01	0.03	0.05	-0.01	-0.16	1.00

* Significance at confidence level of 95%
TVD Total Voluntary Disclosure, **GD** General Disclosure, **MD** Market Disclosure, **RMD** Risk Management Disclosure, **FD** Financial Disclosure, **HRD** Human Resources Disclosure, **RDD** Research & Development Disclosure, **ESED** Environmental, Social, and Ethical Disclosure, **CGD** Corporate Governance Disclosure, **FS** Firm Size, **FP** Firm Profitability, **IM** Industrial Membership, **BS** Board Size, **RD** Role Duality.

The Pearson correlations in table 6.7 show the significance association between the total and different categories of voluntary disclosures with the different determinants of this type of disclosure during year 2004 – 2005 (panel A). The significance association is identified using confidence level of 95%. The results of the table shows that at this level of voluntary disclosure there is a significance association between the total voluntary disclosure and firm characteristics, including firm size, firm profitability, and industrial membership. Referred to the correlation coefficients, there is a positive relationship between total voluntary disclosure and firm size and firm profitability, while there is a negative relationship between total voluntary disclosure and industrial membership.

Concerning the corporate governance characteristics, there is insignificant relationship between total voluntary disclosure and board size and role duality. There is negative relationship between total voluntary disclosure and board size, while there is a negative relationship between total voluntary disclosure and role duality. The results of this table agree with research hypothesis regarding the association between total voluntary disclosure and the different disclosure's determinants.

Regarding the different categories of the total voluntary disclosure, there is a significant relationship between, general disclosure, financial disclosure, environmental, social, and ethical disclosure, and corporate governance disclosure, and firm size. There is a significant relationship between, general disclosure, and corporate governance disclosure, and firm profitability. Also there is a significant relationship between, general disclosure, marketing disclosure, risk management disclosure, and corporate governance disclosure from one side, and industrial membership from the other side. On the other hand, the findings show that there is insignificant relationship between the different categories of voluntary disclosure and corporate governance disclosure, including board size, and role duality.

Table 6.8

Pearson Correlation Coefficients between Categories and Determinants of Corporate Voluntary Disclosure of Panel B: 2005 - 2006

	TVD	GD	MD	RMD	FD	HRD	RDD	ESED	CGD	FS	FP	IM	BS	RD
TVD	1.00													
GD	0.66*	1.00												
MD	0.76*	0.58*	1.00											
RMD	0.59*	0.34*	0.47*	1.00										
FD	0.64*	0.33*	0.31*	0.12	1.00									
HRD	0.35*	-0.17	0.13	0.28	0.06	1.00								
RDD	0.75*	0.42*	0.48*	0.48*	0.36*	0.24	1.00							
ESED	0.63*	0.15	0.28	0.18	0.43*	0.41*	0.37*	1.00						
CGD	0.71*	0.78*	0.53*	0.20	0.65*	-0.15	0.30	0.40*	1.00					
FS	0.50*	0.45*	0.29	-0.01	0.35*	0.21	0.20	0.53*	0.57*	1.00				
FP	0.35*	0.33*	0.27	0.12	0.30	-0.00	0.13	0.30	0.41*	0.31*	1.00			
IM	-0.48*	-0.68*	-0.57*	-0.31	-0.23	0.19	-0.28	-0.02	-0.55*	-0.30	0.00	1.00		
BS	-0.09	-0.02	-0.14	-0.10	-0.20	-0.18	0.07	0.17	-0.10	0.17	-0.09	-0.08	1.00	
RD	-0.04	-0.17	-0.09	0.18	0.07	0.01	-0.07	-0.03	-0.07	-0.26	-0.10	0.05	-0.02	1.00

* Significance at confidence level of 95%
TVD Total Voluntary Disclosure, **GD** General Disclosure, **MD** Market Disclosure, **RMD** Risk Management Disclosure, **FD** Financial Disclosure, **HRD** Human Resources Disclosure, **RDD** Research & Development Disclosure, **ESED** Environmental, Social, and Ethical Disclosure, **CGD** Corporate Governance Disclosure, **FS** Firm Size, **FP** Firm Profitability, **IM** Industrial Membership, **BS** Board Size, **RD** Role Duality

The Pearson correlations in table 6.8 show the significance association between the total and different categories of voluntary disclosures with the different determinants of this type of disclosure during year 2005–2006 (panel B). The results of this panel of data do not differ significantly from the results of the previous panel of year 2004–2005 (panel A), except that there is insignificant relationship between risk management disclosure and industrial membership in year 2005–2006 (panel B) instead of the existence of significant relationship between the two variables during year 2004–2005 (panel A).

Moreover, the relationship between total voluntary disclosure and role duality is a negative relationship during year 2005–2006 (panel B) instead of the existence of positive relationship during 2004–2005 (panel A). This difference indicates that the direction between the two variables is not a clear relationship.

Table 6.9

Pearson Correlation Coefficients between Categories and Determinants of Corporate Voluntary Disclosure of Panel C: Average Total Disclosure

	TVD	GD	MD	RMD	FD	HRD	RDD	ESED	CGD	FS	FP	IM	BS	RD
TVD	1.00													
GD	0.67*	1.00												
MD	0.74*	0.58*	1.00											
RMD	0.61*	0.35*	0.49*	1.00										
FD	0.62*	0.34*	0.28*	0.11	1.00									
HRD	0.36*	-0.13	0.12	0.34*	0.08	1.00								
RDD	0.75*	0.42*	0.47*	0.51*	0.33*	0.24*	1.00							
ESED	0.64*	0.18	0.29*	0.19	0.43*	0.39*	0.39*	1.00						
CGD	0.70*	0.77*	0.51*	0.16	0.63*	-0.15	0.30*	0.41*	1.00					
FS	0.49*	0.46*	0.27*	0.00	0.35*	0.18	0.21	0.52*	0.59*	1.00				
FP	0.39*	0.33*	0.26*	0.17	0.28*	0.06	0.19	0.29*	0.43*	0.27*	1.00			
IM	-0.47*	-0.67*	-0.57*	-0.31*	-0.20	0.17	-0.27*	-0.05	-0.52*	-0.30*	-0.04	1.00		
BS	-0.06	-0.06	-0.16	-0.07	-0.07	-0.12	0.03	0.15	-0.05	0.11	0.04	-0.03	1.00	
RD	0.01	-0.15	-0.02	0.16	0.04	0.06	-0.04	0.06	-0.03	-0.12	-0.04	0.03	-0.09	1.00

* Significance at confidence level of 95%
TVD Total Voluntary Disclosure, **GD** General Disclosure, **MD** Market Disclosure, **RMD** Risk Management Disclosure, **FD** Financial Disclosure, **HRD** Human Resources Disclosure, **RDD** Research & Development Disclosure, **ESED** Environmental, Social, and Ethical Disclosure, **CGD** Corporate Governance Disclosure, **FS** Firm Size, **FP** Firm Profitability, **IM** Industrial Membership, **BS** Board Size, **RD** Role Duality.

The Pearson correlation coefficients in table 6.9 indicate that there is a significant relationship between total voluntary disclosure and firm characteristics, including firm size, firm profitability, and industrial membership, while there is insignificant relationship between total voluntary disclosure and corporate governance characteristics, including board size, and role duality.

The relationship between the firm's size and the firm's profitability, and the voluntary corporate disclosure is a positive relationship. While the relationship between the industrial membership, board size and role duality, and voluntary corporate disclosure is a negative relationship.

Regarding the different categories of total voluntary disclosure, there is significant relationship between, general disclosure, market disclosure, environmental, social, and ethical disclosure, and corporate governance disclosure, and firm size. There is a significant relationship between, general disclosure, market disclosure, environmental, social, and ethical disclosure, and corporate governance disclosure, and firm profitability. In addition, there is a significant relationship between, general disclosure, market disclosure, risk management disclosure, research and development disclosure, and industrial membership.

Finally, there is insignificant relationship between total voluntary disclosure and the different categories of this sort of disclosure, and the corporate governance characteristics, including board size, and role duality.

6.3.2 Test of Hypotheses

The model would be examined using multiple pooling ordinary least square (OLS) regression compared to the results using panel data regression. The examination of the hypotheses of the model is shown in the following tables:

Table 6.10

Voluntary Corporate Disclosure Determinants

OLS Cross Sectional Panel Regression Using Robust Standard Error

(Fixed - Effects Regression)

Number of Observations = 81 **Number of Groups (Panels) = 2**

Obs. per Group: Min = 40 : Average = 40.5 Max = 41

Dep. Var.	Cons. Coff. (t-stat.)	FS Coff. (t-stat.)	FP Coff. (t-stat.)	IM Coff. (t-stat.)	BS Coff. (t-stat.)	RD Coff. (t-stat.)	R^2 (Overall)
TVD	-0.19	0.07***	0.08***	-0.10***	-0.00	0.01	0.45
	(-1.19)	(2.75)	(4.37)	(-4.29)	(-1.21)	(0.71)	
GD	-0.09	0.09***	0.13***	-0.33***	-0.01	-0.05*	0.61
	(-0.40)	(2.64)	(4.30)	(-6.25)	(-1.51)	(-1.71)	
MD	0.43*	0.03	0.10**	-0.27***	-0.01***	-0.00	0.42
	(1.87)	(0.73)	(2.36)	(-5.16)	(-2.97)	(-0.06)	
RMD	0.33	-0.03	0.06**	-0.12**	-0.00	0.04*	0.17
	(1.87)	(-1.18)	(2.05)	(-2.87)	(-0.80)	(1.80)	
FD	-0.27	0.08*	0.08**	-0.04	-0.00	0.02	0.19
	(-1.02)	(1.93)	(2.55)	(-0.92)	(-0.75)	(0.69)	
HRD	-0.36	0.08**	0.00	0.10**	-0.00	0.03	0.11
	(-1.54)	(2.40)	(0.02)	(2.14)	(-1.47)	(0.72)	
RDD	0.02	0.03	0.07**	-0.12**	0.00	-0.01	0.12
	(0.06)	(0.65)	(2.26)	(-2.13)	(0.05)	(-0.13)	
ESED	-1.02***	0.16***	0.07**	0.05	0.01	0.05	0.34
	(-4.08)	(4.54)	(2.30)	(1.29)	(1.27)	(1.39)	
CGD	-0.75***	0.16***	0.15***	-0.20***	-0.00	0.01	0.58
	(-3.03)	(3.95)	(5.98)	(-4.02)	(-1.18)	(0.35)	

***$p \le 0.01$, **$p \le 0.05$, and *$p \le 0.10$.

TVD Total Voluntary Disclosure, **GD** General Disclosure, **MD** Market Disclosure, **RMD** Risk Management Disclosure, **FD** Financial Disclosure, **HRD** Human Resources Disclosure, **RDD** Research & Development Disclosure, **ESED** Environmental, Social, and Ethical Disclosure, **CGD** Corporate Governance Disclosure, **FS** Firm Size, **FP** Firm Profitability, **IM** Industrial Membership, **BS** Board Size, **RD** Role Duality.

Table 6.10 shows the results of the data using Multiple Regression with Ordinary Least Squares (OLS) cross sectional panel regression technique to test the hypothesis of the econometric model. The descriptive statistics showed that the data is not normally distributed. Therefore, the data analysis needs to be applied using non-parametric test that fits with this non parametric data not normally distributed. The OLS is a parametric test, so to fit with the non parametric data it needs to be employed using robust standard error.

The panel regression is used to differentiate between the data of year 2004 – 2005 (panel A) and year 2005 – 2006 (panel B). Therefore, two groups are examined. The minimum number of observations 40 companies representing the data of year 2005 – 2006 (panel B), while the maximum number of observations 41 companies representing the data of year 2004 – 2005 (panel A) resulting in average observation of 40.5 companies per each year.

The results show that the total voluntary disclosure is positively significant ($p \leq 0.01$) with firm size, firm profitability, and role duality, while it is negatively significant ($p \leq 0.01$) with industrial membership and board size. The positive relations mean that the voluntary disclosure increases with the increase of the firm size, firm profitability, and with the separation between the roles of the CEO and the chairman of the board of directors. On the other, hand, the negative relations mean that the voluntary disclosure increases in the non manufacturing companies rather than in the manufacturing companies, and with the small board size rather than the large board size.

However, the results indicate there is a significant relationship ($p \leq 0.01$) between the total voluntary disclosure and the firm characteristics, including firm size, firm profitability, and industrial membership. On the other hand, there is insignificant relationship between total voluntary disclosure and the corporate governance characteristics, including board size, and role duality. This means that the changes that occur in the total voluntary disclosure could only be explained using the firm characteristics rather than the corporate governance characteristics. The adjusted R Squared of the models explains how much of the changes in the dependent variable explained by the changes in the independent variables. The R Squared is 0.45 indicating that 45% of the changes of the total voluntary disclosure is explained by the changes its examined determinants.

Referred to the different categories of voluntary disclosure, there is a significant relationship between, firm size and general disclosure ($p \leq 0.01$), financial disclosure ($p \leq 0.10$), human resources disclosure ($p \leq 0.05$), environmental, social, and ethical disclosure ($p \leq 0.01$), and corporate governance disclosure ($p \leq 0.01$). There is a significant relationship between, firm profitability and general disclosure ($p \leq 0.01$), market disclosure ($p \leq 0.05$), risk management disclosure ($p \leq 0.05$), financial disclosure ($p \leq 0.01$), research and development disclosure ($p \leq 0.01$), environmental, social, and ethical disclosure ($p \leq 0.01$), and corporate governance disclosure ($p \leq 0.01$). Also, there is a significant relationship between, industrial membership and general disclosure ($p \leq 0.01$), market disclosure ($p \leq 0.01$), risk management disclosure ($p \leq 0.05$), human resources disclosure ($p \leq 0.05$), research and development disclosure ($p \leq 0.05$), and corporate governance disclosure ($p \leq 0.01$). It is observed that the majority of the voluntary disclosure categories have significant relationship with the firm characteristics which is supporting the significant relationship between the total voluntary disclosure and the firm characteristics.

Concerning the corporate governance characteristics, there is a significant relationship between board size and general disclosure ($p \leq 0.10$) from one side, and with market disclosure ($p \leq 0.01$) from the other side. Also, role duality has a significant relationship ($p \leq 0.10$) with both general and risk management disclosure. The rest of the relationships between the different categories of voluntary disclosure, and corporate governance characteristics are insignificant which is supporting the insignificant relationship between the total voluntary disclosure and corporate governance characteristics, including board size, and role duality.

The results of the panel regression analysis agree with the firm characteristics research hypotheses concerning the existence of positive significant relationship between voluntary disclosure and firm size (hypothesis 1.1), and firm profitability (hypothesis 1.2), and a negative significant relationship with industrial membership (hypothesis 1.3).

Moreover, the results of the panel regression analysis agree with corporate governance research hypotheses concerning the existence of insignificant relationship between voluntary disclosure and board size (hypothesis 1.4), and role duality (hypothesis 1.5).

6.3.3 Sensitivity Analysis

Table 6.11

Voluntary Corporate Disclosure Determinants

OLS Pooled Regression Using Robust Standard Error

Number of Observations = 81

Dep. Var.	Cons. Coff. (t-stat.)	FS Coff. (t-stat.)	FP Coff. (t-stat.)	IM Coff. (t-stat.)	BS Coff. (t-stat.)	RD Coff. (t-stat.)	R^2
TVD	-0.19	0.08***	0.08***	-0.10***	-0.00	0.01	0.45
	(-1.19)	(2.78)	(4.37)	(-4.32)	(-1.34)	(0.72)	
GD	-0.09	0.09***	0.13***	-0.33***	-0.01*	-0.05*	0.61
	(-0.39)	(2.67)	(4.25)	(-6.52)	(-1.80)	(-1.71)	
MD	0.42*	0.03	0.10**	-0.27***	-0.01***	-0.00	0.42
	(1.87)	(0.73)	(2.45)	(-5.20)	(-3.19)	(-0.06)	
RMD	0.32	-0.03	0.06**	-0.12***	-0.00	0.04*	0.17
	(1.84)	(-1.20)	(2.14)	(-2.90)	(-0.55)	(1.81)	
FD	-0.26	0.08*	0.08**	-0.04	-0.00	0.02	0.19
	(-1.02)	(1.95)	(2.54)	(-0.92)	(-0.94)	(0.70)	
HRD	-0.37	0.08**	0.00	0.10**	-0.00	0.03	0.11
	(-1.57)	(2.40)	(0.08)	(2.14)	(-1.40)	(0.72)	
RDD	0.02	0.03	0.07**	-0.12**	0.00	-0.01	0.11
	(0.07)	(0.65)	(2.30)	(-2.14)	(0.02)	(-0.13)	
ESED	-1.00***	0.16***	0.06**	0.05	0.00	0.05	0.34
	(-4.11)	(4.60)	(2.15)	(1.32)	(1.03)	(1.40)	
CGD	-0.74***	0.16***	0.15***	-0.20***	-0.00	0.01	0.58
	(-3.02)	(3.97)	(6.04)	(-4.03)	(-1.53)	(0.34)	

***$p \leq 0.01$, **$p \leq 0.05$, and *$p \leq 0.10$.

TVD Total Voluntary Disclosure, **GD** General Disclosure, **MD** Market Disclosure, **RMD** Risk Management Disclosure, **FD** Financial Disclosure, **HRD** Human Resources Disclosure, **RDD** Research & Development Disclosure, **ESED** Environmental, Social, and Ethical Disclosure, **CGD** Corporate Governance Disclosure, **FS** Firm Size, **FP** Firm Profitability, **IM** Industrial Membership, **BS** Board Size, **RD** Role Duality.

The main objective of the sensitivity analysis is to examine how sensitive the results and findings towards changing the statistical test. The used test is Ordinary Least Squares (OLS) pooled regression using robust standard error as the examined data is not normally distributed as stated before by the descriptive statistics. The pooled regression analysis deals with large number of observations as one unit without differentiating between the different groups of data as the panel data do. The results of the pooled regression showed the same adjusted R Squared as the panel data regression analysis indicating that the pooled regression has the same strength of the main panel regression. The pooled regression showed the same significant and insignificant relationship between the total voluntary disclosure and its categories with firm characteristics, and corporate governance characteristics.

The results of the pooled regression showed that the results of the panel data analysis are not sensitive to changing the type of the test. Hence, the selected panel data analysis is considered to be well matching with the examined data. Moreover, the results of this sensitivity analysis confirm the reliability of the results and findings which support the generalization of such results.

6.4 CONCLUSION

The chapter includes two stages of analysis. First, examining the level of voluntary disclosure over two different years 2004–2005 (panel A) and 2005–2006 (panel B). Second, investigating the association between voluntary disclosures and two groups of determinants, firm characteristics, and corporate governance characteristics.

The first part of the analysis found that the level of voluntary disclosures is characterized by being stable from one period of time to another. In addition, this level is considered to be relatively low. Regarding the different categories of voluntary disclosure, the disclosure structure is relatively stable where market disclosure scores about 23% of the voluntary disclosure level on the expense of the other voluntary disclosures. The environmental, social, and ethical disclosures are relatively low as a result of the unfamiliarity of the corporate social responsibility concepts and practices in the Egyptian culture. Similarly, corporate governance disclosures are relatively low due to the recent launch of the codes and procedures of corporate governance within the Egyptian business culture.

The second part of the analysis indicates that there is a significant relationship between the voluntary disclosures and firm characteristics, including firm size, firm profitability, and industrial membership, while there is insignificant relationship between the voluntary disclosures and corporate governance characteristics, including board size, and role duality.

Consequently, these results indicated that the Egyptian culture needs to make some efforts to be familiar with the corporate social responsibilities of the working companies towards their society. On the other hand, the Egyptian business culture still not enough aware of the codes and practices of corporate governance.

This chapter emphasized the different areas of disclosure that need improvements to raise the whole level of disclosure which satisfies the different users of the Egyptian annual reports whom represents the stakeholders of the companies, where the existence of survival of these companies is dependent on the degree of satisfaction of these stakeholders. Therefore, offering the adequate level of information satisfy these stakeholders which is the main source of financing for the company to ensure its existence and survival.

Accumulatively, it is concluded that the entire empirical study's results that the bigger and profitable the company, the higher level of information voluntarily disclosed in its annual reports. Also, the service sector companies' discloses higher level of voluntary disclosure than the manufacturing companies sector. However, the board size and role duality, as corporate governance determinants, do not justify any level of information disclosed voluntarily in the annual reports of the Egyptian companies.

CHAPTER SEVEN

AUDITING EXPECTATIONS GAP AND DIFFERENT METHODS OF REDUCING THIS GAP

7.1 INTRODUCTION

This chapter represents the second part of the empirical study which includes: first, investigating the existence of the auditing expectations gap in Egypt and second, examining the perceptions of the sample's respondents towards the traditional solutions to reduce this gap compared to their perceptions towards the proposed solution to reduce this gap. The analysis of the results expected to test the hypothesis related to the effectiveness of auditing voluntary corporate disclosure towards the reduction of the auditing expectations gap.

The results of this chapter differentiate between the usefulness of the different methods to reduce the existing expectations gap, and its effectiveness to perform this objective. The usefulness is identified by the agreement of the examined sample of respondents upon that the entire method would contribute to the expectations gap reduction. On the other hand, the effectiveness is measured by the significant difference between each non–auditor group and the auditor group from one side, and between the overall non–auditor group and the auditor group from the other side.

The objective of this empirical analysis is to illustrate the existence of the auditing expectations gap in Egypt, and the most effective methods that would contribute to the reduction of this existing gap. These methods includes traditional methods, including audit report form, users' education, and standards settings, in comparison to the voluntary disclosure auditing as a proposed method.

7.2 DESCRIPTIVE STATISTICS

The descriptive study shows the response rate of the study and the details of this response rate for each group of the examined sample. In addition, the analysis emphasizes the accounting qualification and past experience of the sample, and experience of each group in his/her occupation.

Table 7.1

Response Rates and Demographic Details of Participants

Group	Survey Sent	Response Received	Accounting Qualification		Accounting Experience	
			Yes	No	Yes	No
Auditors	100	31	31	0	31	0
Academics	100	33	33	0	33	0
Investors	100	34	18	16	15	19
Bankers	100	29	24	5	26	3
Total	400	127	106	21	105	22

The results in table 7.1 indicate that the overall response rate is 31.75 per cent which is an acceptable rate for using this type of data collection tool (Dixon *et al.*, 2006; Manson and Zaman, 2000; Best, 1999; Dewing and Russel, 2002; Fadzly and Ahmad, 2004). It is noted from the table that the auditors and academics groups have got accounting qualifications, while the bankers and investors groups vary between having accounting qualifications and not having accounting qualifications as nearly half the investors group sample have accounting qualifications while the second half not, which presents a variety of the sample qualifications. Moreover, similar to the accounting qualifications, all the auditors and academics included in the sample have accounting experience, while the majority of the bankers have got accounting experience. Although most of investors group have no accounting experience, the sample is considered to be balanced representing variety of different investors which supports the well representation of the sample for the whole population.

Table 7.2

Accounting Experience of Responses

Group	**None**		**2-5 Years**		**5-10 Years**		**More than 10 Years**	
	n	**Percent**	***n***	**Percent**	***n***	**Percent**	***n***	**Percent**
Auditors (*n*=31)	0	0	11	35.5	8	25.8	12	38.7
Academics (*n*=33)	0	0	14	42.4	2	6.1	17	51.5
Investors (*n*=34)	18	53	3	8.8	7	20.6	6	17.6
Bankers (*n*=29)	0	0	3	10.3	11	38	15	51.7
Total (*n*=127)	18	14.2	31	24.4	28	22	50	39.4

The results of table 7.2 present the variation of the accounting experience of the different respondents. Most of the auditors' sample had more than 10 years experience indicating the inclusiveness of senior members in the sample as indicator of the awareness of the relatively new terminologies included in the questionnaire. However, the sample includes other auditors with different experiences to ensure that the sample is well representative for the whole population. Regarding the academics group, it contains diversified groups of accounting experience to maintain the balance between the different experiences which is reflected on the perception of the respondent. However, the majority of the bankers sample had more than 10 years experience which indicates that the study focused on the perceptions of the senior bankers rather than the other categories of experienced bankers. Accumulatively, the overall sample is balanced between having no experience and having more than ten years' experience, indicating that the sample is representative of the whole population of the four examined groups.

Table 7.3

Occupational Experience of Responses

Group	2-5 Years		5-10 Years		More than 10 Years	
	n	Percent	*n*	Percent	*n*	Percent
Auditors (*n*=31)	12	38.7	15	48.4	4	12.9
Academics (*n*=33)	14	42.4	5	15.2	14	42.4
Investors (*n*=34)	28	82.4	4	11.8	2	5.8
Bankers (*n*=29)	8	27.6	11	37.9	10	34.5
Total (*n*=127)	62	48.5	35	27.5	30	24

The occupational experience of responses presented in table 7.3 shows the number of years each group of respondents still in his occupation as auditor, academic, investor, and banker. This table indicates that most of the auditors are in their career for 5–10 years, which is the period of the new reform regulations that affected the accounting and auditing structures and practices in Egypt and the new regulations of the Egyptian capital market (Cairo & Alexandria stock exchange). Therefore, the auditors group got most of their work experience during this period which is reflected on their perceptions. However, the academics sample is scattered over the scale as it includes equal proportion of the new fresher academics with 2-5 years academic experience, and the experienced academics with more than 10 years academic experience. That's reflected on the diversification of the academic perceptions. In contrast with the academic sample, the bankers sample is well distributed over the different ranges of experience, which guarantee that the sample represents the whole population.

However, the investors sample is concentrated on those whom are dealing with the stock market for 2-5 years which is a logical finding, as since the Egyptian stock market regulations and reforms the investors were attracted to invest in the capital market to get benefit of the different incentives offered by the government to refresh the stock exchange market as part of the Egyptian reform program (The Egyptian Ministry of Foreign Trade, 2004). Therefore, the sample is concentrated by this way to reflect the radical changes in the regulations and polices of the capital market on their perceptions. The overall sample is concentrated towards the 2-5 years experience with nearly equally distribution on the remaining experience ranges.

7.3 TEST OF HYPOTHESIS

The hypothesis examined by this analysis is that voluntary corporate disclosure auditing is an effective method of reducing the auditing expectation gap in Egypt, compared to the effectiveness of the other traditional method. Therefore, as a prerequisite for the study, it is useful to investigate the existence of the auditing expectations gap in Egypt before examining the effectiveness of the different methods of reducing this gap.

The hypothesis is tested based on the significant differences between the perceptions of the auditors' group compare to each non-audit groups including academics, investors and bankers. In addition it compares the significant difference of the auditors' group compared to the overall perceptions of the non-auditor groups. The perceptions of the different groups is measured using 5 point Likert scale, as 1 represents strongly agree, 2 agree, 3 neutral, 4 disagree, and 5 strongly disagree. Therefore, the analysis is based on the mean score of the different perceptions as a mean score below 3 presents that the perception tend to be towards the agreement perception, while a mean score beyond 3 presents that the perception tend towards the disagreement perception. Accordingly, using the Likert scale is useful in the analysis of the different perceptions as it has a cutting point, which is 3 in our case, a yardstick used to differentiate between the different perceptions.

Table 7.4

Investigating the Existence of the Auditing Expectations Gap in Egypt

(Comparative Mean Response)

Statements	Mean Responses				
	Auditors	Academics	Investors	Bankers	Overall
1-Management is responsible for producing the financial statements of the company.	1.42	2.24*#	1.50	1.45	1.74
2-The auditor is responsible for the soundness of the internal control structure of the company.	4.00	4.12	1.44*#	2.48*#	2.68*#
3-The auditors is legally responsible only to the shareholders.	4.23	3.76	1.68*#	4.03	3.10*#
4-The auditor is responsible for maintaining accounting records of the company.	3.77	4.24#	1.41*#	3.24*#	2.94*#
5-The auditor is responsible for detecting all fraud.	2.94	1.39*#	1.62*#	1.41*#	1.48*#
6-Management should be held responsible if the company goes bankrupt due to fraud.	2.00	1.76	1.44*#	1.69	1.63*#
7-The auditor is responsible for preventing fraud.	4.26	4.21	1.41*#	3.45*#	2.99*#
8-The auditor is unbiased and objective.	1.35	1.48	1.56	1.52	1.52
9-The financial statements give a true and fair view.	1.58	1.55	1.56	2.52*#	1.84
10-Users can have absolute assurance that the financial statements contain no material misstatements.	1.39	2.91*#	3.79*#	2.55*#	3.11*#
11-The company is free from fraud.	4.03	4.48*#	3.18*#	3.10*#	3.60*#
12-The extent of audit work performed is clearly explained in the audit report.	1.55	3.09*#	4.00*#	2.41*#	3.21*#

Statements	Mean Responses				
	Auditors	Academics	Investors	Bankers	Overall
13-The extent of assurance given by the auditor is clearly indicated in the audit report.	1.45	3.00*#	3.06*#	2.31*#	2.81*#
14-The auditor is trustworthy.	1.42	1.73	4.03*#	1.69*#	2.53*#
15-The audited financial statements are useful in monitoring the company's performance.	1.32	1.67*#	3.91*#	1.55	2.43*#
16-The audited financial statements are useful for decision making.	1.42	1.79*#	3.41*#	1.41	2.25*#
17-The company is well managed.	4.00	2.64*#	3.97	1.86*#	2.88*#

1 strongly agree, 2 agree, 3 neutral, 4 disagree, and 5 strongly disagree.
*Significantly different from auditors at $\rho \leq 0.05$ (Mann-Whitney U test)
#Significantly different from auditors at $t \leq 0.05$ (t-test)

The results in table 7.4 investigate the existence of the auditing expectations gap in Egypt. There is total agreement by the different groups that the management is responsible for preparing the financial statement (statement 1). Therefore, there is insignificant difference between the auditors and the non-auditors groups. However, there is significant difference concerning the responsibility of the auditor towards the internal control structure of the company (statement 2). There is high disagreement towards this statement by the auditors and academics group. While the investors and bankers require that the auditors need to be responsible for the internal control structure which results in this significant difference.

Moreover, an expected result indicated by statement 3 that the auditor is only responsible towards the shareholder, as there is a high agreement by the investors to get the greater attention of the auditors to satisfy their needs regardless the interests of the other stakeholders, which is, of course, disagreed by the academics, bankers, and even the auditors group', which results in the overall disagreement towards this statement.

Similarly, there is disagreement of the different groups concerning the responsibility of the auditor towards maintaining the accounting records of the company (statement 4), which is an internal task that needs to be performed by the company rather than the auditor, but the agreement of the investors' group results from the subjects included in the sample that have no accounting qualification and experience.

There is strong agreement by the different groups of stakeholders about the responsibility of the auditor to detect all fraud (statement 5). In contrast, it is not strongly agreed by the auditors group as this would result in expanding the responsibilities of the auditors to ensure the fulfilment of this task. Therefore, there is significant difference between the auditors group and each non auditors group and the overall non auditors group.

Interesting result indicated concerning the responsibility of the company if it goes to bankruptcy due to fraud (statement 6), the examined stakeholders groups strongly agreed towards this statement, while the auditors group agreed less strongly as they believe that they had to accept part of the responsibility towards this bankruptcy which results in the occurrence of significant difference between the auditors group and each non auditors group from ones side, and between the auditors' group and the overall non-auditors group from the other side. Referred to the results of the previous two statements, it is indicated that the auditors accept to be responsible for the fraud detection. Although, the auditors are responsible for fraud detection, they are not the only party responsible but the company involved in the responsibility of this issue.

In contrast, auditors group disagree strongly that they are responsible for the prevention of the existence of fraud (statement 7). To do so, the auditor needs to have full control over the company and that would contradict with his independence. It is observed that the academics and bankers groups agree with the auditors' group, indicating that if the auditor is having full control over the company that would lead to the violation of the auditor's independency standard. On the other side, investors strongly agree that the auditor is responsible for preventing fraud which represents the misunderstanding of the scope of the auditors' responsibilities as perceived by the investors group. This diversified perception results in the significant difference of the auditors' group and the overall non-auditors groups.

Moreover, there is strong agreement between the different auditors and non-auditors groups that the auditor is unbiased and objective (statement 8), which represents the main reason that the stakeholders requires more services and responsibilities from the auditors as they believe that due to their objectivity, the auditor's opinion is reliable for making their decisions. Therefore, the auditors and non-auditors groups' perceptions are insignificantly different from each other regarding the objectivity of the auditor's opinion.

Similarly, there is a strongly agreement that the financial statements give a true and fair view (statement 9). This perception is given under the assumption that these statements are audited by external independent auditor, as the main objective of the auditing process is to make the financial statements trustful and fairly presented. This supports the previous results concerned with the agreement that the auditor is objective and unbiased (statement 8). Therefore, the overall perceptions indicate insignificant difference between the auditors and non auditors groups.

Investors disagree that the financial statements have absolute assurance and get no material mis-statements (statement 10). This is related to the responsibilities and tasks performed by the auditors as investors believe in the objectivity of auditors (statement 8) but they think they need to expand their responsibilities to get absolute assurance about the fairness and trustiness of the financial statements. The other non-auditors groups agree to have this absolute assurance but within the limit of the responsibilities performed by the auditors. Therefore, there is significant difference between the auditors and non-auditors perception regarding this statement.

Moreover, there is a disagreement among the auditors and the non-auditors groups that the company is free from fraud (statement 11). This is a logical consequence to the failure of the auditor to guarantee the freedom or prevention of fraud. There is a significant difference between the perceptions of the auditors group and the non-auditors groups due to the different degrees of disagreement within the different groups.

There is an extreme differentiation between the auditors group and the non-auditors groups regarding the extent to which the audit work performed is clearly explained in the audit report (statement 12). There is strongly agreement by the auditors group, while there is disagreement by the non audit groups indicating an existing problem with the message communicated by the audit report showing that what is sent by the report is not perceived by the non auditors groups. Therefore, there is a significant difference between the auditors and each non auditors group's perceptions for one side, and between the auditors group and the overall non auditors groups' perceptions from the other side.

In contrast, there is significant difference between auditors group and non auditors groups regarding the extent of clearly indication of the assurance given by auditor in the audit report (statement 13). This result ensures that there is an existing problem with the message conveyed by the audit report to the different non auditors groups.

Regarding the auditor's trustworthiness (statement 14), the investors disagree that the auditor is trustworthy while the other groups agree that the auditor is trustworthy. This differentiation indicates the investors' awareness concerning the trustworthiness of the auditor resulting in the significant difference between the auditors group's perception and the perception of the overall non-auditors groups. This problem reflected on how the investors perceive the usefulness of the audited financial statements in monitoring the company's performance (statement 15) and for decision making (statement 16). The differentiated results of the investors from the other groups, resulting in the overall significant difference, indicates the effect of the lack of accounting qualification and experience, which needs to be overcame by the detailed audit report which is directed to the different users with the different needs and qualifications. However, investors and auditors disagreed that the company is well managed (statement 17), which contradict with perceptions of the academic and bankers groups resulting in the overall significant difference of perceptions.

Accumulatively, the analysis shows major significant differences in the perceptions of the auditors group and the non auditors groups indicating the existence of a gap between what the stakeholders, represented by academics, investors, and bankers, expects to be performed by the auditors, and the actual auditor's performance. This results in the existence of an auditing expectations gap that needs to be reduced effectively.

Table 7.5

The Role of Audit Report Form in Reducing the Auditing Expectations Gap

(Comparative Mean Response)

Statements	Mean Responses				
	Auditors	Academics	Investors	Bankers	Overall
1-The inclusion of an audit report enhances the credibility of financial statement.	1.29	1.48	1.94*#	1.51	1.65*#
2-The purpose of the audit is clearly communicated in the audit report.	1.23	2.58*#	1.88*#	1.83*#	2.09*#
3-The audit report is readable document.	1.26	1.76*#	1.74*#	1.66*#	1.72*#
4-The audit report clearly summarizes the extent and nature of the evidence gathered in the formation of the audit opinion.	2.48	2.91	1.41*#	1.37*#	1.88*#
5-The audit report clearly indicates the role of judgment in the formation of the audit opinion.	4.26	3.94	1.47*#	2.20*#	2.52*#
6-The auditors' responsibility in relation to fraud is clearly indicated in the audit report.	4.29	3.55#	1.32*#	1.69*#	2.17*#
7-The auditors' responsibility in relation to any illegal acts performed by the client is clearly indicated in the audit report.	4.29	2.82*#	1.38*#	2.43*#	2.21*#
8-In the future there should be an explicit statement in the audit report of the auditors' assessment of the going concern status of the client.	1.81	3.82*#	1.26*#	1.31*#	2.11

Statements	Mean Responses				
	Auditors	Academics	Investors	Bankers	Overall
9-In the future there should be an explicit statement in the audit report of the auditors' findings in relation to fraud or illegal acts.	1.58	3.67*#	1.68	1.40	2.23#
10-It should be useful for the auditor to indicate either in the audit report or in a separate statement, the extent of their examination of the chairman's statement.	4.13	2.30*#	1.44*#	1.26*#	1.66*#
11-It should be useful for the auditor to indicate either in the audit report or in a separate statement, the extent of their examination of the director's report.	2.81	1.82*#	1.32*#	1.46*#	1.53*#
12-It should be useful for the auditor to indicate either in the audit report or in a separate statement, the extent of their examination of the operating and financial review.	2.74	2.67	1.24*#	1.46*#	1.77*#
13- It should be useful for the auditor to indicate either in the audit report or in a separate statement, the extent of their examination of any other information included in the annual report but outside the financial statements.	4.10	1.64*#	1.65*#	1.32*#	1.53*#
14-The value of the audit would be enhanced if the auditor reported, either in the audit report or in a separate statement, in respect of each audit engagement the scope of their study of the client's internal control.	1.48	3.33*#	1.82*#	1.34	2.15*#

Statements	Mean Responses				
	Auditors	Academics	Investors	Bankers	Overall
15-The value of the audit would be enhanced if the auditor reported, either in the audit report or in a separate statement, in respect of each audit engagement the extent to which they relied on internal controls.	1.55	2.88*#	1.76	1.49	2.03*#
16- The value of the audit would be enhanced if the auditor reported, either in the audit report or in a separate statement, in respect of each audit engagement the materiality level they used.	1.61	2.39*#	1.53	1.69	1.86
17-The value of the audit would be enhanced if, for each audit, the report explained the most difficult issues arising in the audit and how they had been resolved.	1.97	2.52*#	1.29*#	1.31*#	1.70*
18-An auditor should always report on corporate governance issues for which they have a responsibility.	2.39	2.67	1.35*#	1.71*#	1.90*#
19-The directors' statement in respect of corporate governance is useful.	1.84	3.12*#	1.32*#	1.54*#	1.98

1 strongly agree, 2 agree, 3 neutral, 4 disagree, and 5 strongly disagree.
*Significantly different from auditors at $\rho \leq 0.05$ (Mann-Whitney U test)
#Significantly different from auditors at $t \leq 0.05$ (t-test)

Table 7.5 shows the role of the audit report form in reducing the auditing expectations gap. The audit report could be articulated either in a short brief form or in a long detailed form. The aim of this analysis is to indicate how effective changing the form of the audit report would contribute to the reduction of the auditing expectations gap.

Regarding the effect of including an audit report in the enhancement of the credibility of financial statements (statement 1), all the examined groups agree on this issue. However, there is a significant difference between the overall non-auditors groups and the auditor group due to the different degrees of agreement among the different groups.

Moreover, the examined sample groups agreed with different degrees that the purpose of the audit is clearly communicated in the audit report (statement 2) and whether the audit report is a readable document (statement 3) reflecting how each group perceives the audit report. Due to the different qualifications and experiences of the different groups, there are significant differences between the auditors group and each group of non-auditors, resulting in the overall non-auditors groups in a significant difference from the auditors group.

Similarly, the different auditors and non-auditors groups agreed that the audit report clearly summarizes the extent and nature of the evidence gathered in the formation of the audit opinion (statement 4). It is observed that the investors and bankers groups' degree of agreement are stronger than that of auditors and academics, which results in the significant different between the auditors group and the other overall groups.

An interesting finding is derived from the significant difference between auditors group and non-auditors groups regarding the role of judgment in the formation of the audit opinion indicated by the audit report (statement 5), the auditor's responsibility in relation to fraud as indicated in the audit report (statement 6), and the indication of the audit report regarding the auditor's responsibility in relation to any illegal acts performed by the clients (statement 7). The previously presented statements indicate how effective do the audit report communicates a certain message from the auditors to the stakeholders.

It was shown that the auditors strongly disagree with the previously mentioned statements, while the other non-auditors groups, specifically investors and bankers, agreed with these statements. This indicates that the auditors are concerned about the message conveyed by the audit report and it needs to be modified, while the other groups are satisfied by this unqualified audit report, from the auditors own view, which means that the non-auditors did not realize that this report needs some improvement and this shows how vague is the audit report that the non-auditors could not judge it in a right way. Consequently, this phenomena takes place due to the existing of the wide auditing expectations gap realized in the previous analysis.

Regarding the future, the auditors and non auditors groups (except academics group) strongly agree with inclusion of an explicit statement in the audit report of the auditor's assessment of the going concern status of the client (statement 8). This perception indicates the critical user's needs to have some information that facilitates the future predictions, while the academics view is that future predictions not necessary based on the audit report, but there would be other separated reports that could offer these information. On the overall level, there is insignificant difference between the auditors group and the overall non auditors group regarding this statement.

Similarly, the academic group disagree with the auditors and non-auditors groups regarding that in the future there should be an explicit statement in the audit report of the auditor's findings in relation to fraud or illegal acts (statement 9). The reason of this significant difference between academics and other groups is that they believe that there would be a separated report that shows these issues. But there is insignificant difference between the auditors and overall non auditors groups.

On the other hand, the auditors group disagree with the non-auditors groups about the indication of the extent of their examination of the chairman's statement either in the auditor's report or in a separate statement (statement 10). This significant difference between the auditors group and overall non-auditors groups results from the expanding of the responsibilities of the auditors by accepting the burden of auditing the chairman's statement, while for the users it is critical to them to be assured from this statement as it is the corner stone of the corporate governance of the company as it would be shown latter.

However, the auditors agree with the non-auditors that it should be useful for the auditor to indicate either in the audit report or in a separate statement, the extent of their examination of the director's report (statement 11), and the extent of their examination of the operating and financial review (statement 12). This auditors' agreement indicate that they believe that these reports need to be critically audited due to the existing conflict of interests between the directors and the other users. The overall result illustrates the significant difference between the auditors and overall non auditors groups due to the different levels of agreement between the different groups.

Moreover, auditors group disagreed with the non-auditors groups regarding the usefulness for the auditor to indicate either in the audit report or in a separate statement, the extent of their examination of any other information included in the annual report but outside the financial statements (statement 13). The reason of this significant difference is previously mentioned to justify the significant difference of statement 10, as the auditors were not willing to expand their responsibilities to include auditing of other additional information. In addition, it is clear that the users requested additional assurance statements beside the auditors report, indicating their additional needs for other information offered by the auditors rather than the stated ones in the audit report. Therefore, there is a significant difference between the auditors group and no auditors groups' perceptions towards this statement.

The auditors group and non-auditors groups agreed that the value of the audit would be enhanced if the auditor reported, either in the audit report or in a separate statement, in respect of each audit engagement the scope of their study of the client's internal control (statement 14), and in respect of each audit engagement the extent to which they relied on internal controls (statement 15). These results shows the importance of evaluating the internal control structure of the company, and that it could be disclosed separately from the audit report showing the in inclusive nature of the existing audit report form. The significance difference between the auditors and overall non auditors' perceptions results from the different degrees of agreements towards these statements.

It is agreed by the auditors group as well as the non-auditors groups that the value of the audit will be enhanced if the auditor reported, either in the audit report or in separate statement, in respect of each audit engagement the materiality level they used (statement 16). The materiality level shows the extent of the auditor's scope which indicates the differentiation between the material and immaterial errors discovered during the auditing inspection which is in turn reflected on the users' expectations towards the auditing process and reduces the auditing expectations gap. Therefore, there is insignificant difference between the auditors group's perception and the overall non auditors groups' perception towards this statement.

Moreover, explaining the most difficult issues arising in the audit and how they had been resolved (statement 17) is agreed by the auditors and non auditors to enhance the value of audit due to the degree of transparency associated with the auditing process leading to avoid having users' over expectations. However, there is significant difference between the auditors group and overall non auditors group due to the inconsistency of agreement among the diversified groups towards this issue.

Regarding corporate governance issues, there is significant difference between auditors group and overall non auditors' groups towards the inclusive of the audit report the corporate governance issues they are responsible for (statement 18). However, there is an agreement trend towards this issue. In addition, there is insignificant difference between auditors group and overall non auditors groups towards the usefulness of the directors' statement in respect of corporate governance (statement 19).

Table 7.6

The Role of Users' Education in Reducing the Auditing Expectations Gap

(Comparative Mean Response)

Statements	Mean Responses				
	Auditors	Academics	Investors	Bankers	Overall
1-The auditor's responsibility for the soundness of the internal control structure of the company.	1.84	3.21*#	1.35	3.07*#	2.51*#
2-The auditor's legal responsibility to the different users.	1.29	1.94*#	1.47	2.62*#	1.98*#
3-The auditor's responsibility for maintaining accounting records of the company.	1.13	2.58*#	1.26	2.00*#	1.94*#
4-The auditor's responsibility for detecting all fraud.	1.26	1.94*#	1.65*#	1.90*#	1.82*#
5-The auditor's responsibility for preventing all fraud.	3.06	4.18*#	1.79*#	2.55	2.84
6-The auditor's unbiased and objectivity.	1.23	2.70*#	1.62*#	1.86*#	2.06*#
7-The financial statements' true and fair view.	1.65	2.79*#	1.56	1.97	2.10*
8-The assurance that the financial statements contain no material misstatements.	1.40	3.42*#	1.65	2.00*#	2.36*#
9-The extent of audit work performed explained in the audit report.	1.71	2.42*#	1.79	1.52	1.93
10-The extent of assurance given by the auditor indicated in the audit report.	1.74	3.81*#	1.62	2.10*#	2.52*#
11-The auditor trustworthy.	1.77	2.15*	1.56	2.00*	1.90*

Statements	Mean Responses				
	Auditors	Academics	Investors	Bankers	Overall
12-The audited financial statements usefulness in monitoring the company's performance.	1.61	2.39*#	1.59*	2.48*#	2.14*#
13-The audited financial statements usefulness for decision making.	2.39	3.15*#	1.47#	2.31	2.30

1 strongly agree, 2 agree, 3 neutral, 4 disagree, and 5 strongly disagree.
*Significantly different from auditors at $p \leq 0.05$ (Mann-Whitney U test)
#Significantly different from auditors at $t \leq 0.05$ (t-test)

The results of table 7.6 show the role of educating the different users towards the responsibilities of the auditors in reducing the auditing expectations gap. The education process is an indicator that the auditor is more transparent to his clients which may leads to controlling the users' expectations regarding the auditors' responsibilities.

There is an agreement that users' education towards the auditor's responsibilities for the soundness of the internal control structure of the company (statement 1), to the different user's (statement 2), for maintaining accounting records of the company (statement 3), and for detecting all fraud (statement 4). However, there is significant difference between auditors group and non auditors groups concerning these issues indicating that although it is useful, it is not effective issues to reduce the auditing expectations gap.

There is insignificant difference between the auditors group and overall non auditors groups concerning the disagreement that educating users towards preventing all fraud (statement 5) would reduce the auditing expectations gap as the auditor actually is not responsible to prevent fraud so this expansion of the auditors responsibilities would raise the users' expectations and expand the auditing expectations gap instead of reducing it.

In contrast, there is agreement among the different auditors and non auditors groups regarding educating users towards the auditor's unbiased and objective opinion (statement 5), the financial statements trustiness and fairness (statement 7), and the assurance that the financial statements contain no material misstatements (statement 8). However, there is significant difference between the auditors group and the non auditors groups indicating that although the agreement of the auditors and non-auditors groups towards the usefulness of the awareness of these issues, it is not effectively reducing the auditing expectations gap.

However, there is insignificant difference between the auditors group and the overall non auditors groups regarding that educating the users towards the extent of audit work performance explained in the audit report (statement 9) would reduce the auditing expectations gap. That is due to the expansion of the users' awareness towards the scope of the audit work.

In addition, the auditors and non-auditors groups agree that educating users towards the extent of assurance given by the auditor and indicated in the audit report (statement 10), the auditor trustworthiness (statement 11), and the audited financial statement usefulness in monitoring the company's performance (statement 12) would reduce the auditing expectations gap. However, the auditors group's perception significantly different from the overall non-auditors' perceptions regarding these issues, which indicates the ineffectiveness of educating the users toward these issues would reduce the expectations gap.

The auditors and non auditors agree about educating users towards the usefulness of the audited financial statements for decision-making (statement 13). In addition, there is insignificant difference between auditors group and overall non-auditors group regarding this issue, indicating its effectiveness in reducing the auditing expectations gap.

Table 7.7

The Role of Standards Settings in Reducing the Auditing Expectations Gap

(Comparative Mean Response)

Statements	Mean Responses				
	Auditors	Academics	Investors	Bankers	Overall
1- Increasing regulation governing auditor appointment.	1.81	2.33#	1.29*#	1.31*#	1.66*
2- Increasing regulation governing provision of non-audit services.	2.23	2.52	1.18*#	1.90*#	1.85*#
3- Increasing regulation governing rotation of audit partner.	1.77	3.45*#	1.55	2.31*#	2.44*#
4- Increasing regulation governing rotation of audit firm.	1.61	2.52*#	1.44	2.07*#	2.00*#
5-Extending auditor responsibilities as regards fraud detection.	2.32	2.61	1.32*#	1.86*#	1.93*#
6-Extending auditor responsibilities as regards going concern certification.	1.81	2.58*#	1.32*#	1.38*#	1.77
7-Extending auditor responsibilities as regards wider stakeholders.	1.81	3.55*#	1.56*#	1.31*#	2.17
8- Assigning independent body responsible for monitoring of audit work.	4.39	2.55*#	1.35*#	2.66*#	2.16*#
9- Assigning independent body responsible for disciplining of auditors.	4.35	2.67*#	1.29*#	2.52*#	2.14*#
10- Joint and several liabilities of audit partners on its own provide assurance to the quality of auditors' work.	3.06	3.97*#	1.32*#	1.93*#	2.42*#
11- Liability of auditors should be restricted.	3.35	3.39	1.47*#	2.00*#	2.29*#

1 strongly agree, 2 agree, 3 neutral, 4 disagree, and 5 strongly disagree.
*Significantly different from auditors at $\rho \leq 0.05$ (Mann-Whitney U test)
#Significantly different from auditors at $t \leq 0.05$ (t-test)

Table 7.7 shows the role of setting standards towards the expansion of the auditors' responsibilities in reducing the auditing expectations gap. The table's result indicates the effectiveness of the different areas of standards that could be modified to expand the auditor's roles and responsibilities to reduce the existing auditing expectations gap.

There is an agreement among the auditors and non-auditors groups that increasing regulation governing auditor appointment (statement 1), provision of non-audit services (statement 2), rotation of audit partner (statement 3), and rotation of audit firm (statement 4) would reduce auditing expectations gap, as these issues are concerned by maintaining the auditor's independence. However, there is significant difference between the auditors group and the overall non-auditors groups regarding that the setting of standards governing these issues would reduce the auditing expectations gap.

In addition, auditors and non-auditors groups agreed that setting standards that extends auditors' responsibilities as regards fraud detection (statement 5) would contribute to the reduction of the auditing expectations gap. However, there is significant difference between the auditors group and non-auditors groups, indicating that although it is useful to settle such standards, it is not effective in reducing the auditing expectations gap.

Setting standards regarding extending auditors responsibilities as regards the going concern certificate (statement 6), and wider stakeholders (statement 7) have been agreed upon by the auditors and non-auditors groups. In addition, there is in significant difference between the auditors' group and overall non-auditors groups indicating that the wider range of stakeholders are interested in being offered more information by the auditor concerning the future, and the auditors accepting the need to offer this sort of information to wider range of users. In turn, this would meet the users' expectations and reduces the auditing expectations gap

Auditors group disagree with setting standards regarding assigning independent body responsible for monitoring of audit work (statement 8), and disciplining of auditors (statement 9), as they believe that this would affects their independence while performing their responsibilities. While there is an agreement among non-auditors groups towards setting standards that regulate these issues. Of course, the different perceptions results in significant difference between the auditors group and the non auditors groups regarding these statements.

Similarly, auditors group disagreed with setting standards concerned with providing assurance to the quality of auditors' work by joint and several liabilities of audit partners on its own (statement 10), and restricting the auditor's liabilities (statement 11), while the non auditors groups agreed on the issuance of such standards. These perceptions distortion result in the significant difference between the auditors group and non auditors group regarding that these standards would reduce auditing expectations gap.

Table 7.8

The Role of Voluntary Corporate Disclosure Auditing in Reducing the Auditing Expectations Gap

(Comparative Mean Response)

Statements	Mean Responses				
	Auditors	Academics	Investors	Bankers	Overall
1. General Disclosure					
1.1 Mission & vision.	3.97	1.27*#	1.29*#	1.24*#	1.27*#
1.2 Statement of corporate strategy.	2.32	1.49*#	1.56*#	1.34*#	1.47*#
1.3 Top management names / experience.	3.65	1.85*#	1.26*#	1.66*#	1.58*#
1.4 Majority of stockholders (composition of shareholdings).	2.06	1.64*#	1.32*#	1.59*#	1.51*#
1.5 Organization structure.	2.23	1.52*#	1.65#	1.41*#	1.53*#
1.6 Statement of corporate goals and objectives.	2.03	1.61	1.65	1.31*#	1.53#
1.7 Presentation of annual reports in Arabic & English.	2.50	1.24*#	1.74*#	1.55*#	1.51*#
2. Market Disclosure					
2.1 Industry size.	3.71	1.42*#	1.50*#	1.52*#	1.48*#
2.2 Product (s) information.	3.71	1.33*#	1.56*#	1.41*#	1.44*#
2.3 Customers' information.	3.68	1.69*#	1.35*#	1.41*#	1.48*#
2.4 Supplier information.	3.55	2.22*#	1.38*#	1.55*#	1.72*#
2.5 Market (s) information.	3.74	2.09*#	1.41*#	1.38*#	1.64*#
2.6 Market share.	2.32	1.82*#	1.82*#	1.41*#	1.70*#
2.7 Competitive environment.	2.26	1.67*#	2.03	1.69*#	1.80*#
2.8 Productivity capacity.	2.55	1.85*#	1.91*#	1.52*#	1.77*#
2.9 Productivity indicators.	2.35	1.91*#	1.76*#	1.55*#	1.75*#
2.10 Marketing networks.	3.35	1.91*#	2.09*#	1.69*#	1.91*#
2.11 Physical outputs.	3.84	2.06*#	1.82*#	1.86*#	1.92*#
3. Risk Management Disclosure					
3.1 Financial risk (interest rate, currency, credit & fin. Instruments).	1.48	1.39	2.03*#	1.72*#	1.72*
3.2 Political risk (international business).	1.55	1.48	1.91	1.28	1.57
3.3 Market risk (competition, market share).	1.68	1.45	1.79*	1.55	1.63*
3.4 Technology risk (rapid change)	1.68	1.44	1.88*	1.38	1.67*

Statements	Mean Responses				
	Auditors	Academics	Investors	Bankers	Overall
3.5 Environmental risk (laws & regulations).	1.68	1.55	1.82*	1.41	1.65
3.6 Weather risk (climate conditions).	1.77	2.18	2.09*	1.69	2.00*
3.7 Government regulation risk (control, regulation, taxation).	1.77	1.42*	1.97*	1.52	1.65
3.8 Seasonality risk (natural seasonal patterns).	1.48	1.81	1.79*	1.55*	1.78*
3.9 Operational risk (technical, accidents, human error & loss).	1.42	3.15*#	2.06*#	1.69*	2.40*
3.10 Cyclicality risk (natural cyclical trend).	1.26	1.88*#	2.03*#	1.86*#	1.86*#
3.11 Suppliers risk (Main Supplier).	1.29	1.79*#	1.71*#	1.72*#	1.73*#
3.12 Natural resources risk (reserves quality and quantity).	1.19	2.24*#	1.91*#	1.28*	1.98*#
4. Financial Disclosure					
4.1 Financial ratios & statistics.	1.26	1.61*#	1.88*#	1.86*#	1.63*#
4.2 Industry ratios.	1.23	1.33	2.00*#	1.79*#	1.67*#
4.3 Using charts, graphs, photos.	2.10	2.24	1.79*	2.03	1.65*#
4.4 Market Share price.	1.16	2.00*#	1.74#	1.86*#	2.00*#
4.5 Bank loans, mortgages and their uses.	1.90	2.15	1.71*	1.90	1.65*#
4.6 Information of capital structure.	1.65	1.42	1.91	1.90	1.78
4.7 Information of dividends policy.	2.06	1.82	1.85	2.00	2.40
4.8 Reasons and effects of acquisions / disposals on past results.	1.81	2.24*#	2.15#	1.90	1.86
4.9 Information of foreign sales.	1.77	2.85*#	2.21#	1.86	1.73
4.10 Financial information on quarterly basis.	1.42	1.82*#	1.97*#	1.55	1.98*#
4.11 Changes in inventory level.	1.65	2.00*#	1.47*	1.72	1.73
4.12 Dividends per share compared with previous years.	1.39	2.06*#	1.91#	1.86*#	1.95*#
5. Human Resources Disclosure					
5.1 Consultation with employees.	4.35	1.85*#	2.06#	1.45*#	1.80*#

Statements	Mean Responses				
	Auditors	Academics	Investors	Bankers	Overall
5.2 Employee share ownership.	1.84	3.06*#	1.97*	1.52	2.21*#
5.3 Employment data.	3.94	3.27*#	2.09*#	1.62*#	2.35*#
5.4 Pension commitment.	1.77	2.91*#	2.21	1.72	2.30*#
5.5 Employees health & safety.	1.65	3.28*#	1.79	1.72*	2.27*#
5.6 Average compensation of employees.	3.90	3.12*#	1.97*#	1.83*#	2.32*#
5.7 Percentage of foreign and national labour force.	4.06	3.24*#	1.68*#	1.62*#	2.20*#
5.8 Information of training and employee development.	3.68	3.24*#	2.21*#	1.86*#	2.46*#
5.9 Number of employees trained.	3.35	3.12	1.88*#	1.83*#	1.73*#
5.10 Amount spent on training.	3.52	2.03*#	1.79*#	1.62*#	1.95*#
6. Research & Development Disclosure					
6.1 Inputs: Product.	1.52	1.79	1.47*	1.93*#	1.80*#
6.2 Inputs: People.	3.94	2.24*	1.70#	1.66*#	2.21*#
6.3 Input: Infrastructure.	1.68	2.15*#	1.79*	1.62	2.35*#
6.4 Outputs: Actual achievements (Product development).	2.68	2.24*#	1.41#	1.59*#	2.30*#
6.5 Outputs: Actual achievements (Beyond Product development).	2.26	2.64	1.24*#	1.86*#	2.27
6.6 Outputs: Potential achievements.	3.00	2.33*#	1.38*#	1.69*#	2.32*#
6.7 Output: Product timing.	1.74	2.27*#	1.38*#	1.52	2.20*#
6.8 Future expenditures.	1.81	2.30*#	1.65	1.66	2.46*#
6.9 Financing Past, Present, and Future.	1.71	2.39*#	1.65	1.79	1.95
6.10 Accounting/ financing (Comparing prior years, competition, budget).	1.74	2.12*#	1.41*#	1.66	1.73
6.11 R&D ratios.	1.74	1.73	1.38*#	1.66	1.58
6.12 R&D as explanatory.	2.65	2.73	1.76*#	1.72*#	2.08*#
6.13 Explaining R&D changes.	3.06	2.48*#	1.53*#	1.76*#	1.93*#
7. Environmental, Social, and Ethical Disclosure					
7.1 Environmental reports.	1.94	2.21*	1.44*#	2.00	1.88
7.2 Value added statement.	2.03	1.70	1.38*#	2.03	1.69#
7.3 Social activities & contributions.	1.61	1.48	1.76	2.04*	1.75

Statements	Mean Responses				
	Auditors	Academics	Investors	Bankers	Overall
7.4 Environmental health safety.	1.77	2.03*	1.47	1.45*	1.66
7.5 Energy Information.	3.32	2.76*#	1.47*#	1.66*#	1.97*#
7.6 Community information.	3.35	2.18*#	1.59*#	1.52*#	1.77*#
7.7 Charitable donations information.	3.39	3.52	1.88*#	1.83*#	2.43*#
7.8 Using photocopy of awarded certificates.	1.77	3.27*#	1.79	1.90	2.33*#
7.9 Methods of provisions computation.	1.32	1.88*#	2.62*#	1.90*#	2.15*#
7.10 Employment of disabilities.	3.61	2.33*#	1.88*#	1.62*#	1.96*#
7.11 Ethical actions.	2.29	2.18	1.82*#	2.45	2.14
8. Corporate Governance Disclosure					
8.1 Major share ownership and voting rights.	1.26	1.61*#	1.82*#	1.41	1.63*#
8.2 List of board members.	3.23	1.82*#	1.71*#	1.97*#	1.82*#
8.3 Picture of chairperson and/or other members.	3.45	2.12*#	1.91*#	1.90*#	1.98*#
8.4 Board member qualifications.	3.42	3.12	1.88*#	1.83*#	2.29*#
8.5 Number of shares held by members of the board.	2.00	2.21	1.91	1.66	1.94
8.6 Remuneration policy for board members and key executives.	2.97	2.24*#	1.76*#	2.00*#	2.00*#
8.7 Audit committee members: names, addresses, experiences	3.84	3.12*#	1.68*#	2.10*#	2.30*#
8.8 Corporate governance codes, policies, implementation extent.	1.49	1.55	1.76	1.76	1.69

1 strongly agree, 2 agree, 3 neutral, 4 disagree, and 5 strongly disagree.
*Significantly different from auditors at $\rho \leq 0.05$ (Mann-Whitney U test)
#Significantly different from auditors at $t \leq 0.05$ (t-test)

Table 7.8 represents the proposed method for the reduction of the existence auditing expectations gap. The method is based on expanding the auditors' roles and responsibilities to include voluntary disclosure auditing, which satisfies the different stakeholders' expectations, represented by the non auditors groups, and in turn reduces the auditing expectations gap.

Regarding the general disclosure (statement 1), there is agreement among the non auditors groups that auditing general disclosure items would contribute to the reduction of the auditing expectations gap. On the other hand, auditors group disagreed that auditing of the company's mission and vision (statement 1.1), and the top management names and experiences (statement 1.3) would reduce the auditing expectations gap, while agreed that auditing the rest of general disclosure items would reduce the auditing expectations gap.

However, there is only insignificant difference between auditors group and overall non-auditors group regarding auditing the statement of corporate goals and objectives to reduce the auditing expectation gap, while there is significant difference between auditors group and overall non auditors groups concerning the rest of the general disclosure items.

In relation to the market disclosure (statement 2), auditors group agreed that auditing the market share (statement 2.6), competitive environment (statement 2.7), productivity capacity (statement 2.8), and productivity indicators (statement 2.9) information would reduce the auditing expectations gap. On the other hand, this group disagreed that auditing any of the remaining items would reduce the auditing expectations gap. The non-auditors groups agreed that auditing any of the market disclosure items would reduce the auditing expectations gap. However, there is significant difference between auditors group and overall non auditors group indicating that auditing the items of market disclosure items would not effectively reduce auditing expectations gap.

With respect to the risk management disclosure (statement 3), it was interesting observation that both auditors and non auditors groups agreed that auditing risk management disclosure would contribute to the reduction of the auditing expectations gap. However, there are insignificant differences between auditors group and overall non auditors groups regarding that auditing political (international) risk disclosure (statement 3.2), environmental risk disclosure (statement 3.5), and government regulation risk disclosure (statement 3.7) would effectively reduces the auditing expectations gap. While on the other hand, there are significant differences between auditors group and non auditors groups regarding the rest of the risk management disclosure items.

Similarly, regarding the voluntary financial disclosure, both auditors and non auditors groups agree that auditing voluntary financial disclosure items would reduce the auditing expectations gap. However, there are insignificant differences between auditors group and non auditors groups regarding auditing information of capital structure disclosure (statement 4.6), information of dividends policy disclosure (statement 4.7), reasons and effects of acquisions / disposals on pat results disclosure (statement 4.8), information of foreign sales (statement 4.9), and changes in inventory disclosure (statement 4.11) would effectively reduce auditing expectations gap. On the other hand, auditing of the other voluntary financial disclosure items would not contribute effectively to the reduction of auditing expectations gap.

Concerning human resources disclosure (statement 5), auditors group agreed that auditing only employee share ownership disclosure (statement 5.2), pension commitment disclosure (statement 5.4), and employees health and safety disclosure (statement 5.5) would reduce the auditing expectations gap. Other wise, none of the other human resources disclosure's auditing would reduce the expectations gap. While non-auditing groups agreed that auditing all the human resources disclosure items leads to the reduction of the auditing expectations gap. However, there is significant difference between auditors group and overall non auditors groups concerning the auditing of human resources disclosure, which indicates that the human resources disclosure auditing would not effectively reduce the expectations gap.

With respect to research and development disclosure (statement 6), auditors group agreed that auditing the items of this sort of disclosure would reduce that auditing expectations gap, except for the auditing of the inputs (people) disclosure (statement 6.2), output (potential achievement) disclosure (statement 6.6), and explaining the research and development changes disclosure (statement 6.13), they disagree upon that auditing of these items would reduce the auditing expectations gap. On the other hand, non-auditors groups agreed upon auditing the different items would reduce the expectations gap.

There is insignificant difference between the auditors' group and the non-auditors groups regarding the suggestion auditing outputs (actual achievements beyond product development) disclosure (statement 6.5), financing past, present and future disclosure (statement 6.9), accounting/financing (comparing prior years, competition, budget) disclosure (statement 6.10), and research and development ratios (statement 6.11) would contribute effectively to the reduction of the auditing expectations gap, while the other items would not.

Moreover, the non-auditors groups agreed that auditing of all the environmental, social, and ethical disclosure (statement 7) items would reduce the existing auditing expectations gap, while the auditors group disagreed that auditing of the energy information disclosure (statement 7.5), community information disclosure (statement 7.6), charitable donations information disclosure (statement 7.7), and employment of disabilities disclosure (statement 7.10) would reduce this gap.

There is insignificant difference between auditors group and overall non-auditors groups regarding the suggestion that auditing of the ethical reports (statement 7.1), value added statement (statement 7.2), social activities contributions disclosure (statement 7.3), environmental health and safety disclosure (statement 7.4), and ethical actions disclosure (statement 7.11) would effectively reduce this existing gap rather than the other environmental, social, and ethical items.

Finally, concerning corporate governance disclosure (statement 8), as usual non-auditors groups agreed that auditing these items would reduce the expectations gap, while the auditors' group agreed that auditing only the major share ownership and voting rights disclosure (statement 8.1), number of shares held by members of the board disclosure (statement 8.5), remuneration policy for board members and key executives (statement 8.6), and corporate governance codes, policies, implementation extent disclosure (statement 8.8) would reduce the existing gap.

Therefore, there is insignificant difference between auditors group and overall non auditors groups regarding the idea that auditing of the number of shares held by members of the board disclosure (statement 8.5) would reduce this auditing gap, while there are significant differences between the both groups regarding the other items.

7.4 SENSITIVITY ANALYSIS

To examine how sensitive the results, a t-test is applies over the previously examined data using the Mann-Whitney U non parametric test. The significant differences between the score means of the various respondents is measured using the t-test, as there is an existence of significant difference between the auditor and the non auditor group if the t value ≤ 0.05, otherwise the different between the two groups is not significant. The results of the t-test are compared to the results of the Mann-Whitney U non parametric test to examine the sensitivity of the results towards changing of the applied test.

It is observable from the previous analysis that the significant difference analysis using the t-test analysis do not differ significantly from the results of the Mann-Whitney U non-parametric test, specially on the overall level, which indicates that the results are non sensitive to change of the statistical test. This sensitivity analysis result confirms, and support, the results of the Mann-Whitney results, and evidence that this selected statistical test fits with the examined data.

7.5 CONCLUSION

It is shown from the previous discussion that there is an existing auditing expectations gap in Egypt, which is consistent with the previous study applied on Egypt (Dixon *et* *al.*, 2006). There is effectiveness variation between the different traditional methods of the auditing expectations gap reduction compared to the role of voluntary disclosure auditing in reducing this gap. The results indicate that although most of the solutions are useful in reducing such a gap, they are not effective, based on the significant difference between auditors group and overall non-auditors groups. The interesting point about the results is that auditing voluntary disclosure items score insignificant differences between the auditors group and non-auditors groups indicating that auditing this sort of disclosure would effectively reduce the auditing expectations gap. It is observed that these items focus on future aspects, environmental, social, and ethical perspectives of disclosure, in addition to the voluntary financial disclosure. Therefore, it is worth auditing these items in order to reduce the auditing expectations gap, as this auditing process would be accepted by both auditors and non auditors.

Therefore, the results and findings of this empirical analysis agree with the research hypothesis that the voluntary disclosure auditing is an effective method in reducing the existing auditing expectations gap in Egypt compares to the traditional methods, including audit report form, users' education, and standards settings. As a result, it is concluded that voluntary corporate disclosure auditing is an effective approach, in comparison to the traditional methods, to reduce the existing auditing expectations gap from one side, and improving the assurance quality of this sort of disclosure from the other side. Also, these results introduced a new field of auditing titled 'Auditing of Voluntary Disclosures'. This new area requires more efforts to initiate the appropriate guidelines and code of practice.

CHAPTER EIGHT

CONCLUSION

8.1 INTRODUCTION

The thesis is expected to contribute to auditing knowledge in different perspectives. First, the thesis provides a comprehensive view of the previous studies that have discussed the auditing expectations gap paradigm and the different recommended methods that are believed to contribute to the reduction of this existing gap in the developing as well as the developed countries. Second, the thesis reviews the different theories that could offer the scientific base for the proposed method of reducing this gap, and provided a conceptual framework showing the relationship between the auditing expectations gap and voluntary corporate disclosure auditing as a proposed method of reducing this existing gap. Third, the thesis provides an updated examination of the level of voluntary disclosure in Egypt during the most recent two years. In addition, the thesis investigates the determinants of voluntary disclosure, whether on the aggregated level of voluntary disclosure or for each category of this sort of disclosure.

Finally, the thesis examines recently the existence of the auditing expectations gap in Egypt. In addition, it investigates the usefulness and effectiveness of the traditional methods of reducing this existing gap compared to the voluntary disclosure auditing as a proposed method of auditing expectations gap reduction.

This chapter illustrates the relationship between the auditing expectation gap and the audited voluntary corporate disclosure by summarizing the results of the two empirical chapters. In addition, the chapter shows the suggested conceptual framework of this relationship in relation to the empirical analysis performed by the thesis.

The following sections of the chapter discuss the implications of the findings of the thesis, and the limitations and future research suggestions.

8.2 SUGESTED CONCEPTUAL MODEL

The suggested conceptual model provides a comprehensive view of the relationship between the voluntary corporate disclosure and the auditing expectations gap as shown in the following figure:

Figure 8.1

Suggested Conceptual Model

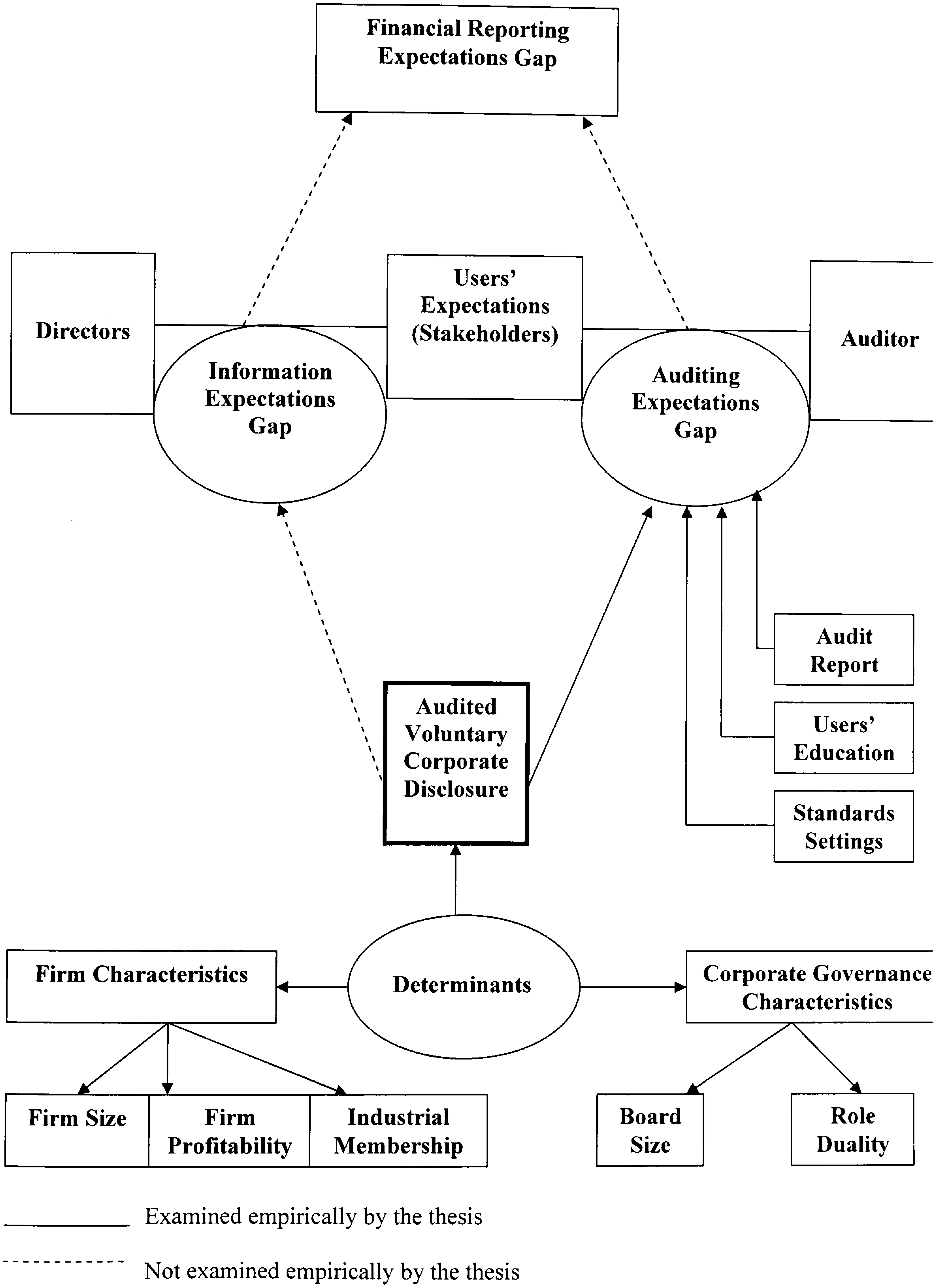


Figure 8.1 views the audited voluntary corporate disclosure as the focal point of the model. It is argued that audited voluntary disclosure is plying dual roles in reducing the information expectations gap (information asymmetry) between the directors and users, which is the traditional role of voluntary disclosure (Diamond and Verrecchia, 1991), from one side, and reducing the auditing expectations gap between auditors and users, which is the proposed role, from the other side.

It is clear that both gaps form the financial reporting expectations gap. Therefore, reducing any or both of the two gaps would contribute to the reduction of the reporting gap which in turn improves the financial reporting quality which satisfies the needs of the different stakeholders whom are the main incentive for any company based on the stakeholder–agency theory.

The information gap exists as a result of the certain items absence from being disclosed which fails to satisfy the stakeholders' expectations towards the firm's disclosure (Hooks *et al.* 2002). Voluntary disclosure reduces the information expectations gap (information asymmetry) as it provides stakeholders with relative confidence that the stock transactions occur at a fair price which increase stock liquidity (Diamond and Verrecchia, 1991; Kim and Verrecchia, 1994). In addition, voluntary disclosure reduces uncertainty and therefore reduces the information asymmetry gap and reduces the cost of external financing (Healey and Palepu, 1993, 2001).

Accordingly, voluntary disclosure is considered to be an effective solution for the reduction of the information gap. Therefore, increasing the level of voluntary corporate disclosure reduces the information expectations gap. This result indicates that the existence of low level of voluntary disclosure is considered to be a sign of the existence of the information expectations gap, which in turn contributes to the existence of the aggregated financial reporting expectations gap.

On the other hand, the stakeholders' reliance on the voluntarily provided information is increased when assurance is provided on this type of information (Coram, 2004). That is due to the increasing demand for audit of regulated and unregulated information providing assurance to stakeholders (Abdel-Khalik, 1993; Chow, 1982; Watts and Zimmerman, 1983). Therefore, the effectiveness of voluntary disclosure in reducing information expectations gap is restricted by auditing this sort of information, which introduces the role of assurance provision for this sort of disclosure by voluntary disclosure auditing.

Voluntary disclosure auditing is related to assuring that the voluntary provided information is fair and true and is provided for the benefit of the stakeholders in making right decisions based on complete and assured information, rather than for the sake of manipulating and directing these stakeholders to take specific decisions that are in the advantage of the firm on the expense of their interests.

The introduction of this auditing service means expanding the role of the auditors to include additional services besides the traditional services they are currently offering to their clients. As a result of this expansion of the auditors' responsibilities, the auditors will tend to meet the stakeholders (users) needs, and in turn meet their expectations and reduces their expectations gap towards the tasks and responsibilities performed by the auditors. There are different traditional methods employed to reduce this existing auditing expectations gap, including audit report form, users' education and standards settings. These methods need to be taken in consideration in comparison to the voluntary disclosure auditing as a proposed method to reduce this gap.

It is clear in the conceptual model that the audited voluntary corporate disclosure is performing two basic roles. First, role is reducing the information expectations gap from one side. Second, role is reducing the auditing expectations gap from the other side. The dual roles played by the audited voluntary disclosures require that this sort of disclosure is assured by means of auditing. The direct effect of the audited voluntary disclosure in reducing both gaps is on the reduction of the financial reporting expectations gap. Hence, the aggregated effect of auditing this sort of disclosure would contribute to the improvement of the quality of financial reports.

The common party between the two gaps of financial reporting is the stakeholders' expectations. Therefore, the research is based on the stakeholders-agency theory as a basic motive for the efforts made in order to reduce both gaps. Thus, the indicator of the effectiveness of the audited voluntary disclosures in reducing both gaps is measured by reaching the stakeholders' expectations through the directors, to reduce the information gap, from one side, and through the auditors, to reduce the auditing gap, from the other side.

However, voluntary corporate disclosure is considered to be dependent to great extent on two groups of determinants. First, group is firm characteristics determinants, including firm size, firm profitability and industrial membership. Second, group is corporate governance characteristics, including board size and role duality. These determinants justify the level of information voluntarily disclosed by the firm.

The conceptual framework draws attention towards the relationship between the audited voluntary corporate disclosure and the auditing expectations gap. This relationship is examined on two stages. First, examining the level of voluntary corporate disclosure in the annual reports of the Egyptian companies, and justifying this resulting level by the different determinants of this sort of disclosure. Second, investigating the usefulness and effectiveness of auditing this voluntary disclosure in reducing the auditing expectations gap compared to the other traditional methods.

8.3 RESULTS AND FINDINGS

The empirical study of the thesis is divided into two parts. First, the examination of the level and determinants of voluntary corporate disclosure in the most active listed Egyptian companies during years 2004-2005, and 2005-2006. Second, investigating the usefulness and effectiveness of voluntary disclosure auditing compared to the different traditional methods in reducing the auditing expectations gap.

The results and findings of the first empirical part of the thesis showed that the Egyptian companies are characterised by relatively low level of this sort of disclosure (22%). This result is based on a validated and adapted checklist check list that fits with the Egyptian context. The voluntary disclosure is categorized in to eight main categories; general disclosure, market disclosure, risk management disclosure, financial disclosure, human resources disclosure, research and development disclosure, environmental, social and ethical disclosure and corporate governance disclosure. The data is analysed using ordinary least square (OLS) cross sectional panel regression (fixed – effect) regression. Since the data is not normally distributed, a robust standard error is employed to overcome this problem. Panel (A) represents the voluntary disclosure of year 2004-2005, panel (B) represents the voluntary disclosure of year 2005-2006 and panel (C) represents the average voluntary disclosure of both panels (A) and (B). The descriptive statistics shows that the voluntary disclosure of the Egyptian companies is condensed in the market disclosure on the expense of the other categories of disclosure. The relationship of the voluntary disclosure and its determinants is examined on two different dimensions. First dimension is the examination of the relationship between the total voluntary disclosure and the disclosure determinants. Second is the examination the relationship between each voluntary disclosure category and the disclosure determinants.

A dummy variable is employed to differentiate between the two panels when applying the regression analysis at confidence levels of 99%, 95%, and 90%. The findings of the panel regressions showed that there is significant association between the total voluntary disclosure and the different firm characteristics. There is a positive significant association between total voluntary disclosure, firm size and firm profitability. This indicates that the bigger the size and the more profits performed by the firm, the higher the level of total voluntary disclosure. Moreover, there is negative significant association between total voluntary disclosure and industrial membership. This relationship indicates that the non manufacturing (services) firms got a higher level of voluntary disclosure than the manufacturing company. This is an expected result as the high scores of voluntary disclosures are achieved by the services firms in the telecommunications sector.

Consequently, there is an in significant association between total voluntary disclosure and corporate governance characteristics, including board size and role duality. This relationship is a result of the recently launched paradigm of corporate governance and this is also reflected in a level of corporate governance disclosure in the annual reports of 19% which is relatively low disclosure level.

On the voluntary disclosure categories level, the results of the association between each voluntary disclosure category and the disclosure determinants are mainly similar to those of the total voluntary disclosure association with the same determinants. It is noted that the majority of voluntary disclosure categories have the same relationships with voluntary disclosure determinants as the relationships on the total level of voluntary disclosure.

As a matter of confirming the previous results and findings, a sensitivity analysis is applied on the entire data using ordinary least squares (OLS) pooled regression using robust standard error. The results of the sensitivity analysis showed similar results to the panel data regression, indicating that the examined data is not sensitive to the change of the employed test. These findings showed that the results of the panel data regression are reliable, which is reflected on the strength of generalizing the sample results on the whole population of the Egyptian companies.

The results and findings of the second empirical part of the thesis are related to the investigation of the different methods of reducing the auditing expectations gap. As an introductory section of this part of the empirical analysis, the existence of the auditing expectations gap in Egypt is examined to confirm that this gap is still existing compared to the examined gap by Dixon *et al.* (2006). This part of analysis is different than Dixon *et al.* (2006) analysis as it includes the academics as a non auditor group beside the other included groups, investors, bankers and auditors. The results of this part indicate that there is an existing auditing expectations gap in Egypt. The thesis argues that voluntary disclosure auditing is an effective method in reducing auditing expectations gap compared to the different traditional methods. The thesis is considered to be the first to compare between the traditional methods in reducing the expectations gap from one side, and to compare between the traditional methods and the proposed method presented in voluntary disclosure auditing from the other side.

The results differentiated between the usefulness of the examined method in reducing the existing gap based on the agreement or disagreement that the examined statement is useful to reduce the auditing expectations gap, and the effectiveness of each method in reducing the gap based on the significance difference between the auditor group and non auditor groups. The insignificant difference between the auditor and non-auditor groups indicates that the examined statement is effective in reducing the existing gap. The effectiveness of the different statements reflects the effectiveness of the whole examined method.

This part of empirical study depends on the questionnaire tool to gather primary data from the Egyptian context. The questionnaire is designed based on the Likert 5 scale to measure the different perceptions of the examined sample. The questionnaire is composed of six different sections. The first section includes the demographic data of the respondents which reflects their accounting education and experience. The second section includes different statements measuring the existence of the auditing expectations gap in Egypt. The third section includes different statements measuring the significant differences between the different groups of respondents toward the effectiveness of the audit report form as method of reducing the existing gap. The fourth section shows the different responses of the respondents towards the effectiveness of educating the users about the task and responsibilities performed by the auditor in reducing the expectations gap. The fifth section illustrates the different perceptions of the respondents towards setting standards regarding expanding the roles and responsibilities performed by the auditor to reduce the expectations gap. The final section examines the effectiveness of voluntary disclosure auditing, which is the proposed method, to reduce the auditing expectations gap.

The questionnaire technique is characterised by having low response rate from the respondents. The current research shows a response rate of 31.75%, which an acceptable response rate compared to the relevant studies at the same area (Dixon *et al.* 2006; Manson and Zaman, 2000; Best, 1999; Dewing and Russel, 2002; Fadzly and Ahmad, 2004). A dummy variable is used to differentiate between the auditors and non auditors groups.

The results are derived using Mann–Whitney U non parametric test to investigate the significant difference between the perceptions of the different respondents. The entire results showed that there is an existing wide auditing expectations gap in Egypt between the auditors group and the non-auditors group which is consistent with the results of Dixon *et al.* (2006) applied on Egypt. The efforts achieved by the different methods of reducing this gap, whether the traditional or the proposed method, seems to be useful in reducing this gap. However, most of the traditional methods are not effective enough to reduce such a gap as there are various significance differences between the perceptions of the different groups regarding the effectiveness of these methods on reducing this gap.

Regarding the auditing of voluntary disclosure as a proposed method to reduce the auditing expectations gap, the categories used in the questionnaire are similar to the disclosure categories measured in the checklist examining the level of these disclosure categories. It is found that auditing the items focusing on future aspects, environmental, social and ethical perspectives of disclosure, in addition to the voluntary financial disclosure, would contribute to the reduction of the auditing expectations gap.

By this conclusion, the previously mentioned perspectives of voluntary disclosure need to be audited as to contribute to the reduction of the auditing expectations gap. Therefore, as a prerequisite for this method of reduction is to increase these categories of audited voluntary disclosure to satisfy the stakeholders' needs and desires. With respect to the disclosure level of these categories, it is clear that these categories are disclosed in a limited level.

The research and development disclosure is restricted to 21% over the years 2004-2005 and 2005-2006 representing 11.50% of the total voluntary disclosure of

Egyptian companies. Consequently, this indicates un-satisfaction of stakeholders towards the auditing of this sort of disclosure and its level.

Similarly, the environmental, social, and ethical disclosure's level is limited to 16% over the examined years 2004-2005 and 2005-2006, which represents 8.96% of the total voluntary disclosure of Egyptian companies. Therefore, stakeholders request to audit this sort of disclosure which satisfies their needs. However, to do so requires first expanding the disclosure level of this category of disclosure to perform a satisfactory audit process for the diversified stakeholders.

Financial voluntary disclosure scores a relatively higher disclosure level than the previously mentioned categories of 26% which represents 14.93% of the total voluntary disclosure of Egyptian companies during 2004-2005 and 2005-2006. However, this category of disclosure presents an acceptable level in comparison to the other categories, and this illustrates the stakeholders' concern about the financial figures especially in developing countries.

Finally, stakeholders were the main motive of the results and findings of the thesis, as their satisfaction is reflected to a great extent on the performance and survival of the company. However, satisfying diversified stakeholders with conflicting interests is not an easy mission. Therefore, the company needs to avoid being biased to any of the different stakeholders which is reflected on the selection of the examined sample to present the whole population in a fair way, which in turn strengthen the reliability and the generalization power of the results and findings of the entire thesis.

8.4 IMPLICATIONS FOR MANAGEMENT

The results and findings of the thesis draw a great attention towards an existing problem that is facing management regarding the stakeholders' expectations and satisfaction in respect to the quality of the provided information and its reliability. The thesis emphasized that there is a joint responsibility of management and auditors towards the existence of the auditing expectations gap. The management is responsible for the level of information of disclosure provided to the stakeholders, while the auditor is responsible for the provided information assurance. However, the auditor's responsibilities are restricted to the provided information by the management. Therefore, the thesis refers the problem of auditing expectations gap to the management in the first instance.

The management would benefit from the implications of this thesis, as it illustrates the link between the information voluntarily disclosed by the management, and the auditor's performance and responsibilities resulting in the existence of the auditing expectations gap. It is shown from the results and findings that the auditing expectations gap is effectively reduced by voluntary disclosure auditing in comparison to the other traditional methods, including audit report form, user's education, and standards settings, specifically research and development, environmental, social, and ethical, and financial disclosures.

Therefore, management can satisfy its stakeholders and contribute to the reduction of auditing expectations gap by focusing on increasing the level of voluntary disclosure. However, it may be not feasible to raise the voluntary disclosure of the different categories at the same time. Therefore, it would be worth it to begin increasing the level of research and development, environmental, social, and ethical and, financial disclosures. Doing so, would induce auditors to audit increasingly categories of disclosure. The thesis provided management with the first step of improving the quality of information by raising the disclosure level of specific categories of disclosure rather than increasing the whole categories of disclosure. The thesis takes into consideration the resources and capabilities limitations which supports the applicability power rather than being just theoretical framework.

Regarding the auditors, the management needs to assign qualified auditors who are willing to satisfy their clients, to achieve a competitive advantage, or at least maintain their competitive edge, by providing this sort of service of voluntary disclosure auditing. Since this sort of disclosure has not got any standards, as it is voluntary, therefore, it needs a diversified and qualified auditing team that can perform this sort of auditing. The auditing team is composed of diversified backgrounds and educational disciplines, which again needs some attention by the management to assign the suitable team.

Voluntary disclosure auditing is considered to be a recent area that needs a great amount of development in the future, as this type of auditing solves different problems regarding the stakeholders' satisfaction towards the level of information voluntarily disclosed by the management from one side, and expanding the auditor's roles and responsibilities to audit this type of information which is in turn reduces the auditing expectations gap. Therefore, it could be concluded that the audited voluntary disclosure is playing dual roles. First, increasing the level of voluntarily disclosed information avoids the existence of the information asymmetry problem between stakeholders and management. Second, expanding the roles and responsibilities of the auditors to include auditing this sort of information reduces auditing expectations gap.

8.5 LIMITATIONS AND FUTURE RESEARCH

There are some limitations that need to be taken in consideration when assessing the thesis' results and findings. The thesis is applied to the Egyptian context without comparison to any developed or even developing country. The research is considered to be specified to the Egyptian context for different reasons. First, it is indicated in the second chapter of the thesis that the Egyptian economy is considered to be a unique situation that passed over a great deal of reform programs which shaped its business culture leading to the limitation of the derived results to other contexts. Second, the objective ontological position and the positive epistemology of the research shown in the research methodology chapter which are driven from the research theoretical framework limits the generalization of the results only to the examined context using this sort of philosophical approach. Third, the adaptation of the research instruments, checklist and questionnaire, to fit with this unique Egyptian context limits the results of the thesis to the Egyptian culture using the tailored research instruments.

Regarding the first part of the empirical study, it includes only the 50 most active companies without expanding the sample to include other countries. At the same time, the results are based on only two years. Therefore, the sample could be expanded to include more companies and over a longer period of time.

The results and findings are based on the simplest form of content analysis (0/1) which may affect the significance of the analyzed data. Therefore, the same study could be applied using more detailed type of content analysis, number of pages, number of sentences, and number of words. Moreover, the thesis analyzed the data using Ordinary Least Squares (OLS) regression with robust standard error for cross sectional panel data, and employed a sensitivity analysis using pooled Ordinary Least Squares (OLS) regression with robust standard error. The data analysis could be extended to be analyzed using TOBIT and LOGIT analysis.

Regarding the second empirical part of the thesis, it depends on the questionnaire technique in gathering the required data, which is characterised by a degree of bias and subjectivity as it is a common limitation for the different studies carried on this type of research (Dixon *et al.* 2006; Manson and Zaman, 2000; Best, 1999; Dewing and Russel, 2002; Fadzly and Ahmad, 2004).

In addition to this, the sample size could be extended either to include more respondents of each of the examined groups, or to include other groups of respondents. Moreover, the data is analyzed using Mann-Whitney U non-parametric test to investigate the significant differences between the auditors group from one side and the non auditors groups from the other side. The research could be extended using Kruskal-Wallis test to examine the significant differences in between the non auditors groups.

Furthermore, the thesis examined the existence of auditing expectations gap and the different methods of reducing this existing gap in Egypt as a developing country. The research may be extended to compare the expectations gap in Egypt with the expectations gap in other developed or developing country and compare the effective methods in reducing the gap in both countries in the form of a comparative study.

8.6 CONCLUSION

The previous discussion explained in a comprehensive fashion the overview of the whole thesis. This thesis is considered to be unique for the following reasons. First, it is examining the voluntary corporate disclosure with one of the most detailed checklist in this area of research. Second, the checklist categorized the voluntary disclosure in to eight categories of disclosure, general disclosure, market disclosure, risk management disclosure, human resources disclosure, financial disclosure, research and development disclosure, environmental, social, and ethical disclosure, and corporate governance disclosure, and examined the determinants of voluntary disclosure not just for the total voluntary disclosure, but for every single category over the examined period of time. Third, the thesis examined its effectiveness compared to the traditional methods of reducing the expectations gap in a unique comparative form between the different methods. Fourth, the thesis is introducing a recent area of auditing, voluntary disclosure auditing, which acts as an effective method in reducing auditing expectations gap compared to the other traditional methods.

The chapter also showed how the management can obtain benefit from the implications of the entire thesis. In addition, this chapter illustrated the limitations and future research that could be done to overcome the limitations of this research.

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APPENDIX

Durham
University

عزيزي / عزيزتي

ارجو من سيادتكم الإلتفات لتلك الدراسة التي تهدف إلي إختبار وجود فجوة توقعات المراجعة في مصر و الحلول المختلفة لتخفيض تلك الفجوة. الدراسة تستخدم اسلوب قائمة الإستقصاء لتجميع بيانات حول وجهات النظر المختلفة لفئات العينة عن تلك المشكلة.

قائمة الإستقصاء تم تصميمها لتختبر وجهة نظرك حول مشكلة فجوة توقعات المراجعة و الحلول الفعالة لتلك المشكلة. إستجابتك ستساهم في الوصول للحل الفعال لتلك المشكلة بما يتلائم مع المجتمع المصري.

في النهاية اود ان اشكرك علي إستجابتك لقائمة الإستقصاء و التي تعتبر حجر الزاوية لنتائج الدراسة.

شكرا جزيلا لإهتمامك و وقتك

الباحث

القسم الأول

البيانات الديموغرافية

برجاء ضع علامة (√) امام الإجابة التي تتناسب مع بياناتك الشخصية:

1- هل لديك مؤهل محاسبي ؟

نعم (   )   لا (   )

2- هل لديك خبرة محاسبية ؟

نعم (   )   لا (   )

3- إذا كانت إجابتك بنعم , كم عدد سنوات الخبرة ؟

2- 5 سنوات (   )   5 – 10 سنوات (   )   أكثر من 10 سنوات (   )

4- ما هو موقعك الحالي ؟

مراجع (   )   موظف ببنك (   )   مستثمر (   )   أكاديمي (   )

5- كم عدد السنوات التي قضيتها في موقعك الحالي

2- 5 سنوات (   )   5 – 10 سنوات (   )   أكثر من 10 سنوات (   )

6- هل ترغب في الحصول علي نسخة من نتائج تحليل البيانات ؟

نعم (   )   لا (   )

7- إذا كانت إجابتك بنعم , من فضلك كتابة بريدك الإليكتروني.

(   )

القسم الثاني

إختبار وجود فجوة توقعات المراجعة

وضح إلي اي مدي توافق او تعترض علي الفقرات الأتية:

الفقرات	أوافق بشدة	أوافق	محايد	أعترض	أعترض بشدة
1- الأدارة مسؤلة عن إعداد القوائم المالية للشركة.	1	2	3	4	5
2- المراجع مسؤل عن هيكل الرقابة الداخلية للشركة.	1	2	3	4	5
3- المراجع مسؤل قانونيا تجاه حاملي الأسهم فقط .	1	2	3	4	5
4- المراجع مسؤل عن الحفاظ علي دفاتر الشركة.	1	2	3	4	5
5- المراجع مسؤل عن إكتشاف التلاعب.	1	2	3	4	5
6- الإدارة يجب ان تتحمل المسؤلية في حالة إفلاس الشركة نتيجة للتلاعب.	1	2	3	4	5
7- المراجع مسؤل عن منع التلاعب.	1	2	3	4	5
8- المراجع غير متحيز و موضوعي.	1	2	3	4	5
9- القوائم المالية توفر صورة حقيقية و عادلة.	1	2	3	4	5
10- المستخدمين لديهم ثقة مطلقة في ان القوائم المالية لا تضمن اي اخطاء جوهرية.	1	2	3	4	5
11- الشركة خالية من اي تلاعب.	1	2	3	4	5
12- المهام التي يتم إنجازها من قبل المراجع محددة بصورة واضحة في تقرير المراجعة.	1	2	3	4	5
13- مدي الثقة التي يوفرها المراجع محددة بصورة واضحة في تقرير المراجعة.	1	2	3	4	5
14- المراجع موثوق به.	1	2	3	4	5
15- القوائم المالية التي تم مراجعتها تعتبر مفيدة لمراقبة اداء الشركة.	1	2	3	4	5
16- القوائم المالية التي تم مراجعتها تعتبر مفيدة لإتخاذ القرارات.	1	2	3	4	5
17- الشركة يتم إدارتها بشكل جيد.	1	2	3	4	5

القسم الثالث

دور شكل تقرير المراجعة في تخفيض فجوة توقعات المراجعة

وضح إلي اي مدي توافق او تعترض علي الفقرات الآتية في ضوء تخفيض فجوة توقعات المراجعة:

الفقرات	أوافق بشدة	أوافق	محايد	أعترض	أعترض بشدة
1- وجود تقرير مراجعة يدعم الثقة في القوائم المالية.	1	2	3	4	5
2- الغرض من عملية المراجعة يظهر بوضوح في تقرير المراجعة.	1	2	3	4	5
3- تقرير المراجعة يعتبر وثيقة مقروئة.	1	2	3	4	5
4- تقرير المراجعة يلخص بوضوح مدي و طبيعة الدلائل التي تم تجميعها لتكوين رأي المراجع.	1	2	3	4	5
5- تقرير المراجعة يظهر بوضوح دور الحكم الشخصي في تكوين رأي المراجع.	1	2	3	4	5
6- مسؤلية المراجع تجاه التلاعب تظهر بوضوح في تقرير المراجعة.	1	2	3	4	5
7- مسؤلية المراجع تجاه الافعال الغيرقانونية للعميل تظهر بوضوح في تقرير المراجعة.	1	2	3	4	5
8- مستقبلا يجب ان يشمل تقرير المراجعة تقييم المراجع لقابلية العميل للإستمرار.	1	2	3	4	5
9- مستقبلا يجب ان يشمل تقرير المراجعة التلاعبات و الأفعال الغير قانونية التي تم إكتشافها بواسطة المراجع.	1	2	3	4	5
10- من المفيد للمراجع ان يظهر في تقرير المراجعة او في تقرير منفصل مدي فحص تقرير المدير العام.	1	2	3	4	5
11- من الفيد للمراجع ان يظهر في تقرير المراجعة او في تقرير منفصل مدي فحص تقرير مجلس الإدارة.	1	2	3	4	5
12- من الفيد للمراجع ان يظهر في تقرير المراجعة او في تقرير منفصل مدي فحص البيانات المالية و التشغيلية.	1	2	3	4	5
13- من الفيد للمراجع ان يظهر في تقرير المراجعة او في تقرير منفصل مدي فحص اي معلومات في التقرير السنوي و لكن خارج القوائم المالية.	1	2	3	4	5

14- ترتفع قيمة المراجعة إذا قام المراجع – سواء في تقرير المراجعة او في تقرير منفصل – بتوضيح مجال دراسة نظام الرقابة الداخلية للعميل.	1	2	3	4	5
15- ترتفع قيمة المراجعة إذا قام المراجع – سواء في تقرير المراجعة او في تقرير منفصل – بتوضيح مدي إعتماده علي نظام الرقابة الداخلية.	1	2	3	4	5
16- ترتفع قيمة المراجعة إذا قام المراجع – سواء في تقرير المراجعة او في تقرير منفصل – بتوضيح مستوي الجوهرية المستخدم.	1	2	3	4	5
17- ترتفع قيمة المراجعة إذا قام المراجع بتوضيح الصعوبات التي واجهته خلال عملية المراجعة و كيفية التغلب عليها.	1	2	3	4	5
18- يجب علي المراجع ان يشمل في تقريره عناصر حوكمة الشركة المسؤل عنها.	1	2	3	4	5
19- تقرير المدير العام فيما يخص حوكمة الشركة يعتبر مفيدا.	1	2	3	4	5

القسم الرابع

دور تعلم المستخدمين في تخفيض فجوة توقعات المراجعة

وضح إلي اي مدي توافق او تعترض علي ان تعلم المستخدمين للعناصر الأتية سوف يؤدي إلي تخفيض فجوة توقعات المراجعة:

الفقرات	أوافق بشدة	أوافق	محايد	أعترض	أعترض بشدة
1- مسئولية المراجع عن هيكل نظام الرقابة الداخلية للشركة.	1	2	3	4	5
2- مسئولية المراجع القانونية تجاه المستخدمين المتعددين.	1	2	3	4	5
3- مسئولية المراجع عن تدقيق الدفاتر المحاسبية للشركة.	1	2	3	4	5
4- مسئولية المراجع عن إكتشاف التلاعب.	1	2	3	4	5
5- مسئولية المراجع عن منع التلاعب.	1	2	3	4	5
6- عدم تحيز و موضوعية المراجع.	1	2	3	4	5
7- صدق و عدالة القوائم المالية.	1	2	3	4	5
8- مدي الثقة في ان القوائم المالية تضمن أخطاء غير جوهرية.	1	2	3	4	5
9- مدي مهام المراجعة التي تم إنجازها و تم توضيحها في تقرير المراجعة.	1	2	3	4	5
10- مدي الثقة التي يوفرها المراجع و تم توضيحها في تقرير المراجعة.	1	2	3	4	5
11- مصداقية المراجع.	1	2	3	4	5
12- مدي الإستفادة من القوائم المالية التي مراجعتها في متابعة اداء الشركة.	1	2	3	4	5
13- مدي الإستفادة من القوائم المالية التي تم مراجعتها في إتخاذ القرارات.	1	2	3	4	5

القسم الخامس

دور وضع المعايير في تخفيض فجوة توقعات المراجعة

وضح إلي اي مدي توافق او تعترض علي ان وضع المعايير الأتية المتعلقة بزيادة دور و مسؤلية المراجع سيؤدي إلي تخفيض فجوة توقعات المراجعة:

الفقرات	أوافق بشدة	أوافق	محايد	أعترض	أعترض بشدة
1- زيادة المبادئ التي تحكم تعيين المراجع.	1	2	3	4	5
2- زيادة المبادئ التي تحكم تقديم خدمات اخري غير المراجعة.	1	2	3	4	5
3- زيادة المبادئ التي تحكم تغيير عملاء المراجع.	1	2	3	4	5
4- زيادة المبادئ التي تحكم تغيير شركة المراجعة.	1	2	3	4	5
5- زيادة مسؤلية المراجع تجاه إكتشاف التلاعب.	1	2	3	4	5
6- زيادة مسؤلية المراجع تجاه تقرير القابلية للإستمرار.	1	2	3	4	5
7- زيادة مسؤلية المراجع تجاه مجال اوسع من اصحاب المصلحة.	1	2	3	4	5
8- تعيين جهة مستقلة مسؤلة عن متابعة عمل المراجع.	1	2	3	4	5
9- تعيين جهة مستقلة مسؤلة عن تقييم المراجع.	1	2	3	4	5
10- الإلتزامات المتعددة و المشتركة علي عملاء المراجع توفر الثقة في جودة عمل المراجع.	1	2	3	4	5
11- إلتزامات المراجع يجب ان تكون مقيدة.	1	2	3	4	5

القسم السادس

دور مراجعة الإفصاح الإختياري في تخفيض فجوة توقعات المراجعة

وضح إلي اي مدي توافق او تعترض علي ان زيادة دور و مسؤلية المراجع ليتضمن مراجعة عناصر الإفصاح الإختياري الأتية سيؤدي إلي تخفيض فجوة توقعات المراجعة:

الفقرات	أوافق بشدة	أوافق	محايد	أعترض	أعترض بشدة
1- الإفصاح العام	1	2	3	4	5
1-1 الرؤية و الرسالة.	1	2	3	4	5
2-1 إستراتيجية المنظمة.	1	2	3	4	5
3-1 أسماء و خبرات أعضاء الإدارة العليا.	1	2	3	4	5
4-1 أغلبية حاملي الأسهم (تركيبة حاملي الأسهم).	1	2	3	4	5
5-1 الهيكل التنظيمي.	1	2	3	4	5
6-1 غرض و أهداف المنظمة.	1	2	3	4	5
7-1 نشر التقارير السنوية باللغة العربية و اللغة الإنجليزية.	1	2	3	4	5
2- إفصاح السوق	1	2	3	4	5
1-2 حجم الصناعة.	1	2	3	4	5
2-2 معلومات عن المنتجات.	1	2	3	4	5
3-2 معلومات عن العملاء.	1	2	3	4	5
4-2 معلومات عن الموردين.	1	2	3	4	5
5-2 معلومات عن الأسواق.	1	2	3	4	5
6-2 الحصة السوقية.	1	2	3	4	5
7-2 البيئة التنافسية.	1	2	3	4	5
8-2 الطاقة الإنتاجية.	1	2	3	4	5
9-2 المؤشرات الإنتاجية.	1	2	3	4	5
10-2 الشبكات التسويقية.	1	2	3	4	5
11-2 المخرجات المادية.	1	2	3	4	5
3- إفصاح إدارة المخاطر	1	2	3	4	5
1-3 المخاطر المالية (سعر الفائدة, سعر الصرف, الأدوات المالية و الإئتمانية).	1	2	3	4	5
2-3 المخاطر السياسية (الأعمال الدولية).	1	2	3	4	5
3-3 مخاطر السوق (المنافسة, الحصة السوقية).	1	2	3	4	5

3-4 المخاطر التكنولوجية (التغيرات السريعة).	1	2	3	4	5
3-5 المخاطر البيئية (المبادئ و القوانين).	1	2	3	4	5
3-6 المخاطر الجوية (الأحوال الجوية).	1	2	3	4	5
3-7 مخاطر القوانين الحكومية (الرقابة, القوانين, الضرائب).	1	2	3	4	5
3-8 المخاطر الموسمية (خصائص المواسم الطبيعية).	1	2	3	4	5
3-9 المخاطر التشغيلية (النواحي الفنية, الحوادث, الأخطاء و الخسائر البشرية).	1	2	3	4	5
3-10 المخاطر الدائرية (إتجاهات الدورات الطبيعية).	1	2	3	4	5
3-11 مخاطر الموردين (المورد الرئيسي).	1	2	3	4	5
3-12 مخاطر الموارد الطبيعية (الحفاظ علي الكمية و الجودة).	1	2	3	4	5
4- الإفصاح المالي	1	2	3	4	5
4-1 النسب و الإحصائيات المالية.	1	2	3	4	5
4-2 نسب الصناعة.	1	2	3	4	5
4-3 إستخدام الصورو الرسوم البيانية و التوضيحية.	1	2	3	4	5
4-4 السعر السوقي للسهم.	1	2	3	4	5
4-5 القروض البنكية و التمويل الإئتماني و إستخدماته.	1	2	3	4	5
4-6 معلومات عن الهيكل الرأسمالي.	1	2	3	4	5
4-7 معلومات عن سياسة التوزيعات.	1	2	3	4	5
4-8 أسباب و أثار الإستحواذ و التنازل علي النتائج الماضية.	1	2	3	4	5
4-9 معلومات عن المبيعات الأجنبية.	1	2	3	4	5
4-10 المعلومات المالية الربع سنوية.	1	2	3	4	5
4-11 التغيرات في مستوي المخزون.	1	2	3	4	5
4-12 توزيعات السهم مقارنة بالسنوات السابقة.	1	2	3	4	5
5- إفصاح الموارد البشرية	1	2	3	4	5
5- 1إستشارة العاملين.	1	2	3	4	5
5-2 حصة العاملين في الملكية.	1	2	3	4	5
5-3 معلومات عن العاملين.	1	2	3	4	5
5-4 انظمة المعاشات.	1	2	3	4	5
5-5 صحة و أمان العاملين.	1	2	3	4	5
5-6 متوسط حوافز العاملين.	1	2	3	4	5

5-7 نسبة العمالة الأجنبية للعمالة المحلية.	1	2	3	4	5
5-8 معلومات عن تنمية و تدريب العاملين.	1	2	3	4	5
5-9 عدد العمالة المدربة.	1	2	3	4	5
5-10 قيمة ما تم إنفاقه علي التدريب.	1	2	3	4	5
6- إفصاح البحوث و التطوير	1	2	3	4	5
6-1 المدخلات: المنتجات.	1	2	3	4	5
6-2 المدخلات: الأفراد.	1	2	3	4	5
6-3 المدخلات: البنية الأساسية.	1	2	3	4	5
6-4 المخرجات: الإنجازات الفعلية (تنمية المنتجات).	1	2	3	4	5
6-5 المخرجات: الإنجازات الفعلية (بأستثناء تنمية المنتجات).	1	2	3	4	5
6-6 الخرجات: الإنجازات المستهدفة.	1	2	3	4	5
6-7 المخرجات: توقيت المنتجات.	1	2	3	4	5
6-8 النفقات المستقبلية.	1	2	3	4	5
6-9 التمويل في الماضي, الحاضر, و المستقبل.	1	2	3	4	5
6-10 المحاسبة / التمويل (مقارنة بالسنوات السابقة, المنافسين, الموازنة).	1	2	3	4	5
6-11 نسب البحوث و التطوير.	1	2	3	4	5
6-12 تفاصيل البحوث و التطوير.	1	2	3	4	5
6-13 تفسير التغيرات في البحوث و التطوير.	1	2	3	4	5
7- الإفصاح البيني, الإجتماعي, و الأخلاقي	1	2	3	4	5
7-1 التقارير البيئية.	1	2	3	4	5
7-2 قائمة القيمة المضافة.	1	2	3	4	5
7-3 الأنشطة و المساهمات الإجتماعية.	1	2	3	4	5
7-4 صحة و أمان البيئة.	1	2	3	4	5
7-5 معلومات عن الطاقة.	1	2	3	4	5
7-6 معلومت عن المجتمع.	1	2	3	4	5
7-7 معلومات عن التبرعات.	1	2	3	4	5
7-8 الشهادات الممنوحة.	1	2	3	4	5
7-9 أساليب أحتساب المخصصات.	1	2	3	4	5
7-10 توظيف ذوي الإحتياجات الخاصة.	1	2	3	4	5
7-11 الأفعال الأخلاقية.	1	2	3	4	5
8- إفصاح حوكمة الشركات	1	2	3	4	5

8-1 ملكية الأغلبية و حقوق التصويت.	1	2	3	4	5
8-2 قائمة أعضاء مجلس الإدارة.	1	2	3	4	5
8-3 صورة رئيس مجلس الإدارة و أعضاء اخرين.	1	2	3	4	5
8-4 مؤهلات اعضاء مجلس الإدارة.	1	2	3	4	5
8-5 عدد الأسهم المملوكة بواسطة اعضاء مجلس الإدارة.	1	2	3	4	5
8-6 سياسة حوافز أعضاء مجلس الإدارة و الأعضاء المنتدبين.	1	2	3	4	5
8-7 اعضاء لجنة المراجعة: الأسماء, العناوين, الخبرات.	1	2	3	4	5
8-8 سياسات و ممارسات حوكمة الشركات.	1	2	3	4	5