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Commercialization of Accounting Profession: The Case of Non-audit Services

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ABSTRACT

Over the last decade, the accounting profession has witnessed the commercialisation of audit firms through offering of non-audit services (i.e. business consultancy services) to their audit client. Regulators and stakeholders have placed a great concern on the potential threat of commercialization of audit services on perceived auditor independence. This study reports the effects of the joint provision of audit and non-audit services (NAS) and the type of NAS on perceived auditor independence. The main findings suggest that auditor independence is perceived to be compromised when audit and NAS were jointly offered by audit firms. However, when there exist proper segregation of duties in audit firms that offer both services, the perception changed.

Keywords: Non-audit services (NAS), auditor independence, segregation of duties

INTRODUCTION

Evidence of audit failures documented worldwide have led to major criticism of the auditing professions' independence and exposed its implication on shareholders' and stakeholders' interests (Fearnley and Beattie, 2004; Ghosh and Moon, 2005; Krishnan, 2005). External auditors are expected not only be independent but more importantly must be seen to be independent when examining and attesting clients' financial statements (Fearnley and Beattie, 2004; Sori and Mohamad, 2009a, 2009b; Stevenson, 2002, p. 155)¹. Auditors are expected to decide on reporting strategies

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Any remaining errors or omissions rest solely with the author(s) of this paper.

¹ Fearnley and Beattie (2004) argued that independence in appearance is important because "independent behaviour (i.e. independence in fact) is unobservable" (p. 121).

without any influence from their clients' management (Chandler and Edwards, 1996; Cullinan, 2004).

The globalisation of the accounting profession and the subsequent increase in competitiveness and the need to survive has forced many auditing firms to diversify into non-audit services and has created 'the multidisciplinary nature of large audit firms' (Brierley and Gwilliam, 2003, p. 435). These multidisciplinary firms offer audit and non-audit services (NAS) to audit clients and has become a major concern on the potential auditor independence (Craswell, 1999; Muhamad Sori and Mohamad, 2007; Quick and Warming-Rasmussen, 2005) and substantial amount of empirical evidence has been documented in identifying the nature and extent of this threat in developed countries (e.g. Abbott *et al.* 2001; Beattie and Fearnley, 2002; Brandon *et al.*, 2004; Canning and Gwilliam, 1999; Chung and Kallapur, 2003; Ezzamel *et al.*, 2002; Fearnley and Beattie, 2004; Felix *et al.*, 2005; Frankel *et al.*, 2002; Jenkins and Krawczyk, 2001; Quick and Warming-Rasmussen, 2005; Raghunandan, 2003) and in less developed countries (e.g. Gul and Yap, 1984; Teoh and Lim, 1996). The evidence suggests that the joint provision of audit and NAS raise the risk of client retention due to economic incentives, and the tendency to compromise on auditing quality and independence (Beck *et al.*, 1988; DeAngelo, 1981; Frankel *et al.*, 2002; Simunic, 1984).

The main question that arises when auditors provide both audit and NAS is whether the auditors are able to conduct their audits impartially, without being concerned about losing or failing to gain additional services, and the subsequent economic implications for the audit firm (Lee, 1993, p. 103). In fact, the provision of NAS has the potential to create economic bonding from the significant amount of fees received from clients (Simunic, 1984; Beck *et al.* 1988). The economic bonding between audit firms and their clients would influence auditor independence. It may be that the level of client pressure would increase and auditor becomes less concerned with the quality of internal audits.

The main concern is the ability of auditors to objectively examine their clients' financial statements while at the same time receiving lucrative NAS fees from the same client. The joint provision of audit and NAS would create a potential conflict of interest either consciously or unconsciously, and audit client would feel closely associated with the auditor and expect them to compromise their independence at the behest of the management's requirement. Flint (1988) pointed out, "the auditors may become unduly sympathetic to a directorial or managerial attitude or interpretation of events, or the work may involve the creation of systems and information rather than assessing the adequacy of the systems and information which have been created by the directors or managers" (p. 81).

This paper examines the effects of the joint provision of audit and non-audit services and the provision of different types of non-audit services on perceived auditor independence from the perspective of senior managers of audit firms, loan officers and public listed companies in Malaysia. A good understanding on auditor

independence from this part of the world is important and perhaps will shed some light on the effect of globalization of auditing services on the independence of external auditors in the local audit market.

The paper is organised into five sections. The following section reviews the literature on joint provision of audit and non-audit services. Section three discusses the information collection and analysis procedures and the fourth section presents the findings. The conclusions and implications of the findings are summarized in the final section.

REVIEW OF LITERATURE

Research on the choice of NAS tends to focus on the selection of service providers, such as from the company's auditor or elsewhere, and if audit and NAS are jointly provided by the company's auditor, whether proper segregation of duties exists. Research findings on the association of joint provision of audit and NAS and auditor independence are inconclusive (Ashbaugh, 2004; Brandon *et al.*, 2004; Chung and Kallapur, 2003; DeFond *et al.*, 2002; Frankel *et al.*, 2002; Geiger and Rama, 2003; Kleinman *et al.*, 1998; Reynolds *et al.*, 2004).

The proponents of joint provision of audit and NAS contend that auditor independence would not be affected but would improve audit quality (Antle *et al.*, 1997). Hartley and Ross (1972) found that only 6% of their respondents believed that the provision of NAS posed a significant threat to independence. Firth (1980) showed that the provision of NAS was considered to be only a minor threat to auditor independence. In a study of financial disclosure of NAS, Glezen and Millar (1985) discovered that stockholders were unconcerned about the joint provision of audit and NAS adversely influencing auditor independence. Also, it was claimed that the auditor's knowledge of the client company would be improved by the provision of NAS, resulting in increased objectivity (knowledge spillover) and independence (Goldman and Barlev, 1974; Wallman 1996).

It was argued that the dependence of company management on the audit firm would be higher in cases where the auditors are providing NAS to their clients, and the client management would have an interest in not losing their auditor (Goldman and Barlev, 1974). In a study of the profiles of NAS purchased by US companies, Palmrose (1988) found that the majority of the sampled companies sourced NAS from their auditors rather than from other suppliers. These results indicate that the respondents were not concerned about the perceived negative impact to auditor independence. Gul (1989) studied the perceptions of bankers in New Zealand and found that the effect of provision of NAS was significantly and positively associated with auditor independence. Moizer (1997) pointed out that the greater the audit firm's economic interests, the greater will be client's dependence. Hussey (1999) reported that the majority of the UK finance directors that participated in his study suggested that joint provision of audit and NAS to audit clients should continue to be allowed.

In Malaysia, Gul and Yap (1984) reported that only a small number of the shareholders and auditors that participated in their study believed that NAS provision increased their confidence in auditor independence. Teoh and Lim (1996) found that the provision of NAS was ranked as the second most important factor that undermines auditor independence.

The joint provision of audit and NAS would create ‘economies of scope’²; Arrunada (1999, p. 165) pointed out that joint provision of audit and NAS would reduce overall costs, raises the technical quality of auditing, enhance competition, and need not prejudice auditor independence or the quality of non-audit services, which would ultimately increase auditor independence (Goldman and Barlev, 1974; Wallman 1996). Based on the standard organisation analysis, Arrunada (1999, p. 169) showed that cost savings gained from the joint provision of audit and NAS will be transferred to customers as a decrease in price in both markets, and also that the provision of NAS would ‘result in an increase in client- and firm-specific assets’ (p. 168), where firm-specific assets would ‘always have a positive effect on independence’ (p. 168). This argument is supported by Grout *et al.* (1994), who argued that permitting auditors to perform joint services would reduce auditors’ dependence on a single client and encourage them to diversify as a consequence.

Opponents to the joint provision of audit and NAS claimed that auditors would not perform their audit services objectively and that joint provision would impair perceived independence (see, for example, Brandon *et al.*, 2004; Frankel *et al.*, 2002; Glezen and Miller, 1985; Jenkins and Krawczyk, 2001; Raghunandan, 2003) because ultimately they would be auditing their own work or acting as management (SEC, 2001), and management’s power over the auditor could be increased due to auditors’ reliance on fees received (Canning and Gwilliam, 1999). Thus, it may influence “their mental attitude, impartiality and objectivity, and independence of thought and action” (Flint, 1988, p. 82).

Provision of Non-Audit Services

The previous section documented inconclusive findings on the issue of impact of joint provision of audit and NAS on auditor independence. It is expected that public accounting firms should have the maximum discretion to develop and provide audit and NAS to their clients (Mikol and Standish, 1998). However, Mitchell *et al.* (1993) rejected this idea and believed that the joint provision of audit and NAS to audit clients would cause unfair competition due to the use of audit services to sell

² There are two types of economies of scope, namely ‘knowledge spillover’ and ‘contractual economies of scope’ (Arrunada, 1999, pp. 75-77). Knowledge spillover takes place when two different services involve elements of the same information set and/or the same professional qualifications. Contractual economies of scope happen due to the provision of professional services with associated high transactions costs because of informational asymmetry between client and supplier. Joint provision of services diminishes the cost of seeking a credible consultant and the cost of warranting contractual performance.

NAS, and suggested that auditors should be banned from offering both services to the same client. Similarly, Flint (1988) believed that auditors would have some form of predisposition towards a favourable assessment because the firm as a whole was involved in the creation, development or consultation of the NAS.

As an alternative to a total ban on provision of NAS to audit clients, Arrunada (1999) recommended the use of different divisions that are responsible for each series of services as a safeguard to maintain independence. These divisions are organized as profit centres within audit firms that have their own management and exert little if any influence over the audit partners' evaluation or compensation process. In fact, the idea is justifiable in the UK environment, where Lennox (1999) found a weakly positive significant association between audit qualifications and disclosed NAS and construed that the 'current UK policy may be justified in not banning NAS. This conclusion is strengthened if policy-makers take account of the economies of scope that may accrue from allowing the joint provision of audit and NAS' (p.250). Consistently, Hillison and Kennelley (1988) believed that the approach would enhance auditor independence, especially when appropriate safeguards are in place, such as 'Chinese walls' (Mikol and Standish, 1998, p. 546)³.

The potential threat to auditor independence is lessened when there is a separation of personnel performing NAS and audit services (Pany and Reckers, 1984). Similarly, Lowe *et al.* (1999), Lowe and Pany (1995) and Swanger and Chewning (2001) discovered significant positive associations between auditor independence and joint provision of NAS by staff separation (segregation of duties). Also, Canning and Gwilliam (1999) found that only a small percentage of their respondents expressed concern about the threat to independence when separate departments provide joint services. However, the option of separate workforces to perform audit and non-audit services is only possible if the audit firm has enough resources, and smaller firms may not have such an opportunity for specialisation. However, Quick and Warming-Rasmussen (2005) found that joint

³ Section 48 (2) (h) of the UK's Financial Services Act 1986 illustrates Chinese Walls as "procedures for restricting flows of information within a firm to ensure that information which is confidential to one department is not improperly communicated to any other department within the firm. They are widely used in the financial services sector to manage or avoid conflicts between the duties owed to different customers, or conflicts between the firm's interests and the duties owed to customers, which arise out of the different activities of the component parts of the firm on different sides of the wall". On the other hand, the Consultation Paper on Fiduciary Duties and Regulatory Rules the Law Commission (1992) (Law Com. No. 124) describes Chinese Walls as normally involving some combination of the following organisational arrangements: (i) the physical separation of the various departments in order to insulate them from each other; (ii) an educational programme, normally recurring, to emphasise the importance of not improperly or inadvertently divulging confidential information; (iii) strict and carefully defined procedures for dealing with a situation where it is felt that the wall should be crossed and the maintaining of proper records where this occurs; (iv) monitoring by compliance officers of the effectiveness of the wall; (v) disciplinary sanctions where there has been a breach of the wall (House of Lords, 1998).

provision of audit and NAS by staff from separate departments did not improve perceived independence.

Realising the obstacles faced by small firms, Mautz and Sharaf (1961, p. 230) suggested three alternatives: (i) forbid/prohibit small firms from performing auditing services on the conjecture that they cannot appropriately perform both on impartial basis and that auditing is much less likely to be a major source of revenue to small firms; (ii) require each small firm to select which of the two fields of specialisation it will take on; or (iii) permit small firms to take on work as they do at present, performing a variety of services for their clients. Due to lack of incentive for a stringent approach at that time, Mautz and Sharaf (1961) favoured the third course of action, because small firms rarely undertake audit duties for companies that have public interest and usually perform audits for small businesses at the request of bankers or creditors that have good knowledge about the credibility and reliability of local accounting practitioners. They further asserted that the drawback of segregation of duties for small firms is that it will 'make it more difficult to service their clients and others with no substantial offsetting benefits resulting from such restriction' (p. 230).

In Malaysia, Arens *et al.* (1999) revealed that Big Four firms audited more than 60% of listed companies and that a large majority of medium and small firms serve unlisted companies with a lack of public interest. However in developed markets, Mautz and Sharaf (1961, p. 230) suggested that 'as soon as a given client becomes of sufficient size that there is a substantial public interest in its audited financial statements, . . . a strict separation of auditing and other services should be effected, if not by a division within the accounting firm, then by employment of separate accountants for the two types of services' (p. 230).

Hillison and Kennelley (1988) had recommended three additional alternatives to a total prohibition of NAS provision to audit clients: (i) offer NAS to non-audit clients only; (ii) prohibit certain types of NAS; or (iii) permit all types of NAS with full disclosure requirements. They alleged that although prohibiting all NAS would produce the greatest positive impact on perceptions of auditor independence, it would be the most drastic action. They favoured permitting all types of NAS with full disclosure because it would create the least resistance from practitioners, avoid companies' rejection on disclosure, and it would possibly be effective in monitoring audit clients' acquisition of NAS. Although a conflict of interest might arise from the joint provision of audit and non-audit services to audit clients, it might be inappropriate to prohibit accounting firms from offering non-audit services if this issue is observed from the 'business efficiency' perspective (Chandler and Edwards, 1996, p.26). Fearnley and Beattie (2004) reviewed prior studies and concluded that there is no need for total prohibition of joint provision of audit and NAS, as the dilemma could be overcome by the following suggestion: "more transparency about how firms manage the conflicts of interest that NAS provision creates; whether audit partners are rewarded for earning NAS; and the nature of the NAS being provided" (p. 124). Additionally, audit committees should play

their role in approving the provision of NAS. Indeed, the Securities and Exchange Commission (SEC) in the US and Bursa Malaysian Berhad (BMB) in Malaysia have required public companies to disclose the joint provision of audit and NAS in their financial statements, where the disclosure would “shed light on the independence of public companies’ auditors” (SEC, 2000c).

In a study of bank loan decisions, Firth (1981) discovered that smaller loans were granted for companies that showed joint provision of audit and NAS in their financial statements than companies that did not have such information. Jenkins and Krawczyk (2001) found that joint provision of audit and NAS had a positive impact on the perceptions of auditor independence, and also discovered that the disclosure of the amount of NAS and audit fees was preferred by investors. Similarly Raghunadan (2003) lent support to the SEC’s argument that disclosure of NAS fees could influence shareholders’ voting decisions, observing that shareholders did not consider that the provision of NAS would threaten auditor independence even if the companies purchased very large non-audit services from their auditors.

Schleifer and Shockley (1990) evidenced that the other two options to a total ban on NAS, as identified by Hillison and Kennelley (1988), would improve the perceived independence of auditors. Similarly, Gul and Yap (1984) found that the majority of Malaysian auditors, managers, bankers and shareholders agreed that disclosure of NAS fees would enhance perceived auditor independence. Also, Scheiner (1984) provided evidence that disclosure of NAS reduced the purchase of personnel services from the incumbent auditor. Consistently, Schleifer and Shockley (1990) found that over half of the Big Eight auditors and financial analysts and around a third of non-Big Eight CPAs and loan officers opposed the policy to ban auditors from providing joint audit and NAS. The majority of the Big Eight auditors and financial analysts believed that disclosure of NAS would not enhance auditor independence, while the majority of financial analysts, non-Big Eight CPAs and loan officers have conflicting views. Lee (1993, p. 109) stressed that perceived auditor independence would only improve if the joint provision of audit and NAS was either completely prohibited or publicly disclosed. However, Canning and Gwilliam (1999) found that the threat to auditor independence would be minimal when the provision of NAS was to non-audit clients only i.e. ban NAS to audit clients.

However, Flint (1988) disagreed with the suggestion that an alternative “organisational and constitutional structure” (p. 82) should be created for audit firms to provide joint audit and NAS, and argued that the potential conflict of interests would still exist. Sherer and Kent (1983, p. 27) maintained that ultimately, auditors would be examining their own work and asking for explanations from a member of the client’s staff in whose appointment process they had been involved (i.e. rendering human resource services), and argued that the joint provision of audit and NAS must be prohibited. Also, Flint (1988) argued that auditors might find themselves at a point where they had to decide whether to criticise or to take

exception to a situation where the firm had a direct interest in the outcome of the audit that conflicted with their role as consultants. Indeed, there would be an “economic bond or a legal bond – particularly a bond of joint responsibility and liability” (Flint, 1988, p. 83). He argued that the firm as a whole would receive ‘net benefit’ from the NAS work brought in by the audit division, and as a result the audit function would be unduly affected by “a general directorial or managerial point of view” (Flint, 1988, p. 83).

Types of NAS

The provision of selected types of NAS to audit client might threaten perceived auditor independence. To overcome this threat, the US regulators adopted prescriptive approach that outline nine types of non-audit services that inconsistent with auditor independence. These services are bookkeeping or other services related to the audit client’s accounting records or financial statements, financial information systems design and implementation, appraisal or valuation services or fairness opinions, actuarial services, internal audit services, management functions, human resources, broker-dealer services and legal services.

Most of the studies were conducted in the US and similar research in other parts of the world started in the last two decades. Titard (1971) investigates the impact on perceived auditor independence when auditor provides 33 specific categories of NAS to audit client and found that more than 20% of the respondents agreed that mergers and acquisitions, executive recruitment, policy determination, personnel appraisal and/or selection and executive and wage incentive plans services could threat auditor independence. However, only small percentage (i.e. 10% to 20%) of the respondents believed that the five services should be banned. Lavin (1976; 1977) found that the provision of accounting services and the maintenance of executive payroll (limited accounting services) would impair perceptions of auditor independence. Wide-ranging accounting services were considered by less than half of the respondents to threat independence. Goldman and Barlev (1974) argued that the provision of non-routine audit services could enhance auditor independence because the auditor’s value to and power over the client company increases. Pany and Reckers (1983) found that service type and magnitude of the services as highly significant factors to threat auditor independence, where less routine duty would give rise to higher self-review threat.

Pany and Reckers (1984) found no significant difference in perceptions of auditor independence when auditor provides executive recruiting, actuarial services, redesign of an accounting system, market feasibility studies, independent board of director recruiting, purchase acquisition assistance, and client employment of firm employees to audit client. In a study on the impact on auditor independence when auditor provides acquisition investigation, design of accounting systems, assistance with accounting decisions, and executive search and hiring of CEO, Bartlett

(1993) found that the provision of executive search threaten the perception of independence and assistance with accounting decisions enhance the perceptions of independence.

Lowe, Geiger and Pany (1999) discover that auditor independence would mostly safeguard when the company's CPA firm employ separate staff members to execute the internal auditing services. In a more recent study, Swanger and Chewning (2001) investigate the influence of five different internal audits outsourcing arrangements on perceived independence of 250 financial analysts and found that in the event of staff separation, perceptions are not adversely affected. Respondents did not comprehend a difference between partial and full outsourcing. Mauldin (2003) found that internal audit outsourcing and mergers and acquisition as a threat to auditor independence.

In the UK, Beattie et al. (1996) found that majority of NAS supplied by auditors is accounting services that facilitate listed companies to conform to the legal and regulatory requirements rather than management consultancy. They concluded that it would be beneficial to show the split or detail of NAS services offered in disclosure of financial statement. In German, Dykxhoorn and Sinning (1981) evidenced that more than half German auditors thought that auditor independence would be harmed when auditor provide extensive accounting services. However, three-third of German auditors viewed that the auditor's independence would not be harmed with more limited accounting service provision. Three services were identified to affect auditor independence namely extensive accounting services, limited accounting services and EDP provision. In Canada, Lindsay et al. (1987) investigate the effect three specific types of service namely preparation of accounts, executive search and accounting systems design. They found that accounting systems design was considered as the least threat to auditor independence and around a third of the respondents considered the other two services makes auditor dependent on client.

COLLECTION AND ANALYSIS OF INFORMATION

This study was conducted in two stages. The first stage involved the use of a postal questionnaire to seek information from auditors, loan officers and senior managers of public listed companies on the impact of joint provision of audit and non-audit services on auditor independence. The questionnaire was pilot-tested to increase the relevance and validity of the information sourced. The second stage entailed a series of interviews with senior managers of audit firms, banks and publicly listed companies to solicit more detailed information on the issue of interest. Auditors were selected because they are the main subjects of the issue of interest that provide certification and/or information credibility assessment to the stakeholders (Humphrey, 1997). Furthermore, Flint (1988, p. 76) pointed that the person to whom the audit reports is addressed and the person that are subjected to audit have a direct interest in the audit outcome. Gul (1991, p. 165) argued that bank

officers are relatively sophisticated financial statement users who could be expected to understand the importance of auditor independence. Finally, the manager is the agent of the principal, who conducts business on behalf of the principal and, hence, requires a monitoring mechanism (i.e. an auditor) to report on their performance (see Jensen and Meckling, 1976), and on this basis, senior managers' perceptions of auditor independence are valuable to this study.

The total questionnaires distributed and responded are reported in Table 1, where 31%, 44% and 36% of the questionnaires were returned from auditors, loan officers and senior managers of public listed companies respectively.⁴

An analysis was carried out of the designation of the respondents and details of the findings are tabulated in Table 2.⁵ The majority of the respondents held relatively senior positions in their respective organisations: 46% of the responding auditors were line managers, while 47% and 43% of the loan officer and corporate management groups were senior managers, the remainder being the first line of management and the chief executives of the respective organisations. The respondents were responsible for the auditing, accounting and finance function and their seniority indicates the validity of the information provided.

⁴ It is well recognised in the literature that responses to mail questionnaires are generally poor, and it is a common phenomenon to see return percentages as low as between 30 to 50% (Wallace and Mellor, 1988, p. 132). Indeed, the possibility of occurrence of non-response bias arises when some of the survey sample failed to return the questionnaire and the data may consequently turn out to be invalid. Hence, in order to ensure the reliability and validity of the data, an attempt to diagnose the presence of non-response bias is essential (see Bartlett and Chandler, 1997; Mallin and Ow-Yong, 1998). Based on the technique recommended by Oppenheim (1966) and Wallace and Mellor (1988), the first 20 questionnaires were compared with the last 20 questionnaires. The Mann-Whitney test was employed as a statistical tool to investigate the differences. It was found that there was no significant difference between the 20 early and 20 late responses, implying the absence of non-response bias.

⁵ Another source of bias in survey-type studies is self-selection bias (Eysenbach and Wyatt, 2002; Oppenheim, 1992; Whitehead, 1991). The bias might arise from the fact that "people are more likely to respond to a questionnaire if they see items which interest them" (Eysenbach and Wyatt, 2002) and "they may try to 'respond' extra-well" to the questions (Oppenheim, 1992, p.30). Indeed, self-selection bias is a result of a pre-existing interest factor, and it is more serious than the non-representative nature of the population due to the existence of many unknown factors (Eysenbach and Wyatt, 2002; Oppenheim, 1992). It may be that the people who responded to the questionnaires have dissimilar characteristics to those who did not reply. Although no specific approach to identify self-selection bias has been documented, this study employed two techniques. First, two groups of control and experimental respondents were developed (Oppenheim, 1992). The control group consisted of respondents with more than 10 years' experience, while the experimental group comprised of respondents with less than 10 years' experience. Using the Mann-Whitney test, responses from both groups of respondents from all three classifications (i.e. auditors, loan officers and senior managers of public listed companies) were examined, and it was found that the distribution of responses of the two groups in all respondent classifications was not significantly different, indicating that the effect of self-selection response bias was minimal or non-existent. Second, since this study employed both questionnaire and interview survey approaches, the results of interview survey tend to confirm the questionnaire survey in all variables examined. The consistency of responses in both approaches indicates minimal or non-existent self-selection response bias.

Table 1 Analysis of responses by respondent’s category

Category	Total questionnaires issued	Usable responses received pre-reminder	Usable responses received post-reminder 1	Usable responses received post-reminder 2	Total usable response	Total usable response rate
	Frequency	Frequency	Frequency	Frequency	Frequency	%
Audit Firms	300	25	30	38	93	31
Financial Institutions	200	32	28	27	87	44
Public Listed Companies	300	42	16	49	107	36
Total	800	99	74	114	287	36

Table 2 Profile of postal survey respondents analysed by category of employment

Auditors			Loan Officers			Senior Managers		
Status	Number	%	Status	Number	%	Status	Number	%
Audit Senior	38	41	Officer	34	39	Financial Accountant	36	34
Line Manager	43	46	Senior Manager	41	47	Senior Manager	46	43
Senior Manager	12	13	Chief Executive	12	14	Chief Executive	25	23
Total	93	100		87	100		107	100

From the prespective of work experience of respondents, information summarized in Table 3 shows that more than 80% of the respondents had more than 5 years’ experience in their respective functions. The length of service indicates respondents familiarity with their job functions and changes in the accounting and auditing profession.

Table 3 Analysis showing the period of employment of respondents participating in the interview survey

Level of Experience	Auditors		Loan Officers		Senior Manager of Public Listed Companies		Senior Manager of Regulatory Bodies	
	Number	%	Number	%	Number	%	Number	%
Under 5 years	1	8	1	6	0	0	2	29
Between 6 and 10 years	3	23	3	18	3	18	0	0
Between 11 and 15 years	5	38	5	29	6	35	4	57
Between 16 and 25 years	2	16	7	41	5	29	0	0
More than 25 years	2	15	1	6	3	18	1	14
Total	13	100	17	100	17	100	7	100

The interviews help to consolidate and clarify the information gathered from the questionnaire survey. A detailed analysis of the period of employment of the respondents participating in the interview stage is provided in Table 3.

Table 3 shows that vast majority of the interviewees had more than 5 years of experience. Hence, the opinions provided by interviewees are expected to be reliable.

FINDINGS

Mode of NAS Provision

Respondents were asked to provide their perceptions on six literature based (Arrunada (1999), Canning and Gwilliam (1999)) mode of provision of non-audit services; (i) provision of non audit services by audit engagement staff, (ii) provision of non audit services by staff from separate department, (iii) provision of non audit services by staff from different entities; (iv) audit firms are prohibited providing non-audit services to audit client; (v) audit firms are completely banned from providing non-audit services; and (vi) audit firms providing non-audit services with disclosure of such provision in client financial statements. Besides the above issues, respondents were asked for the reasons underlying for the support of or objection to the joint provision of audit and non-audit services to audit client.

Provision of NAS by Audit Personnel

It was found that 76% of the auditors, all of the loan officers and 91% of the senior managers of public listed companies agreed with the statement that the provision of NAS to audit clients by audit engagement staff threatens auditor independence (refer to Table 4). Although there is strong agreement from the auditors, this is less than that expressed by the loan officers and senior managers of public listed companies, and this reflects on the unwillingness of a minority of the auditor respondents to acknowledge any problems that the joint provision of audit and non-audit services by staff from the same department. The result is consistent with a study of Irish users of financial statements by Canning and Gwilliam (1999).

The interview survey revealed that the majority of the auditors (77%), loan officers (88%) and senior managers of public listed companies (82%) agreed that auditor independence would be threatened if the same personnel provides joint provision of audit and non-audit services. The interviewees were concerned with the ability of the auditors to behave independently and professionally and to resist management pressure due to their dependence on income from both services. The interviewees disclosed that auditors' financial dependence on the client would create a tendency to threaten auditor independence and would lead the auditors to think in the client's way.

The interviews also disclosed that auditors tend to succumb to client pressure when there is a lack of monitoring activities. In fact, some of the interviewees noted that auditor independence would be threatened if they were to gain more knowledge of various aspects of the client's business from their regular review of the business in audit and non-audit services. Thus, they would be familiar with the system's weaknesses and as a consequence expose to manipulation. The interviewees disclosed that there is a need for different people to independently scrutinise the audit and non-audit work.

Interestingly, the majority of the loan officers (80%) pointed out that they did not take into account the provision of non-audit services to audit client in their loan making decisions. A manager of the corporate loan division of a top bank noted:

In analysing the financial statement for loan processing, we actually do not look at this criterion. Perhaps it is good to know the way they operate. But, our knowledge is limited to the information disclosed by the company.

Only a small number of interviewees (i.e. 23% of the auditors; 12% of the loan officers; 18% of the senior managers of public listed companies) disagreed with the statement that joint provision of audit and non-audit services would threaten auditor independence and argued that auditors are professional enough to perform their duties independently without any bias. It may be the case that auditors are bound by their professional ethics and will not compromise their ethical standards for the sake of their business. The occurrence of misbehaviour among auditor was said to originate from a small and insignificant number of 'bogus' accountants. Indeed, the large majority of the auditors were said to adhere to the spirit of the rules and regulations on auditor independence.

Provision of NAS by Staff from Separate Department

As an alternative to joint provision of audit and NAS by audit personnel, it was suggested that the provision of these services should be performed by staff from separate departments. The majority of the auditors (51%), loan officers (42%) and senior managers of public listed companies (58%) disagreed with the statement that auditor independence would be threatened if the provision of NAS to audit clients were to be undertaken by staff from different departments within the same firm (Table 4), and this reflect the respondents' confidence in the safeguards of auditor independence by splitting the provision of audit and NAS into separate departments, which is consistent with Canning and Gwilliam (1999) and Pany and Reckers (1984). Indeed, the separation of personnel is one of the alternatives to a total ban on the joint provision of audit and NAS (Hillison and Kennelly, 1988).

Table 4 Analysis showing perceptions of the method of NAS provision

The independence of the auditor, for the purpose of audit, is reduced if NAS are	Auditors (N=93)				Loan Officers (N=87)				Senior Managers (N=107)				Significance
	Disagree %	No View %	Agree %	Mean	Disagree %	No View %	Agree %	Mean	Disagree %	No View %	Agree %	Mean	
	21	3	76	2.56	-	-	100	3.00	6	3	91	2.84	
Provided to audit clients by personnel involved in audit	51	15	34	1.83	42	20	38	1.95	58	11	31	1.73	
Provided to audit clients by a separate department within the audit firm	74	14	12	1.38	85	1	14	1.29	58	18	24	1.66	***
Provided to audit clients by a separate entity where the auditors have an interest	66	24	10	1.44	99	1	-	1.01	88	12	-	1.12	***
Provided to non-audit clients only	61	39	-	1.39	71	29	-	1.29	62	32	6	1.44	**
Not provided at all	40	60	-	1.60	30	54	16	1.86	42	40	18	1.76	*
Provided by the auditor to all clients but full disclosure is made in the client financial statements													

Note: ***, **, * indicates that the distribution of responses is significantly different at 1%, 5% and 10% level (using the Kruskal Wallis test). The responses were reported on a 5-point scale ranging from 1 (strongly disagree), through 2 (disagree), 3 (no view), 4 (agree) to 5 (strongly agree). For presentational purposes these 5 points have been collapsed into disagree (scored 1), no view (scored 2) and agree (scored 3) and the reported means are calculated on this collapsed scale. However, the significance tests are based on the full 5-point distribution of responses.

In the interview survey, the vast majority of the auditors (85%), loan officers (71%) and senior managers of public listed companies (59%) indicated that auditor independence would not be threatened if the provision of audit and non-audit services to audit client was performed by staff from different departments, which is consistent with the result of questionnaire survey. The interviews disclosed that this mode of NAS provision would allow segregation of duties in monitoring activities, widely known as the ‘Chinese Wall’ (Mikol and Standish, 1998). It was believed that different partners would handle the different departments, which would result in greater monitoring activities and mean that the audit division might not lose sight of the material issues. As a manager of a Big Four audit firm pointed out:

You may not detect the errors that you made yourself. By having different departments, at least someone else is looking into your work, rather than you performing both of the services.

In fact, some of the interviewees argued that auditors are still good candidates for provision of NAS to their audit clients, due to their understanding and knowledge of clients’ business operations, which would speed up the process and allow them to deliver better quality services. A chief executive of a merchant bank remarked:

I think it is good to have separate departments that perform the services rather than one person wearing two hats, but ultimately it goes back to the people, their professionalism and their characters.

Also, some of the interviewees indicated that this kind of arrangement would ease information exchange, which may not be achieved if NAS are provided by other firms. Perhaps, audit firms could effectively utilise their personnel who have a good understanding of the client’s business to speed up the process and subsequently produce a high quality financial statement.

However, a small minority of the interviewees disclosed that the provision of non-audit services by a separate department would threaten auditor independence. They were sceptical about the ability of audit firms to ensure total segregation of duties, and suggested that most audit firms would try to achieve economies of scale by allocating idle staff to any department within the same firm that required their services. Also, some of the interviewees expressed concern about the ability of auditors to act professionally and differentiate between friendship and responsibility to the general public. They indicated that partners in the same audit firm that perform audit and non-audit services are closely connected.

Provision of NAS by Staff from Separate Entity

As shown in Table 4, 74 percent of the auditors, 85 percent of the loan officers and 58 percent of the senior managers of public listed companies indicated that auditor independence would not be threatened when the provision of NAS to audit client is done by a separate entity where the auditors have an interest. Perhaps, the attitude demonstrated by the respondents in this issue indicates their support in the “Chinese Wall” concept that received much attention among Malaysian professionals recently. The increase in respondents support in this issue indicate the objective to segregate job functions between audit and NAS would be more attainable when exist separate entities to handle different responsibilities as compared to separation of department.

The interview survey indicated that as many as 92% of the auditors, 94% of the loan officers and 82% of the senior managers of public listed companies interviewed agreed that the provision of audit and non-audit services by separate entities would safeguard auditor independence. The interviews disclosed that this mode of provision of NAS would safeguard auditor independence due to the structure of audit and non-audit firms, which would ensure greater transparency of financial reporting (i.e. Chinese Wall). When different staff from different entities is handling the assignments, most of the interviewees indicated that each entity would act independently and perform ‘checks and balances’ on each other’s work. Therefore, the majority of the interviewees disclosed that it would act as a deterrent to auditors against compromising their independence.

Although the majority of the loan officers supported the notion that auditor independence would not be threatened if separate entities existed to perform these different services, it was discovered that most of the Malaysian bankers did not take into account the methods of provision of NAS to audit clients in their daily duties of loan processing as indicated in the above sub-section. The interviews indicated that Malaysian auditors were currently performing a good job and producing reliable financial statements. These loan officers may have come to hold this view due to a lack of disclosure of non-audit services in financial statements. Regarding the loan officer’s belief, a manager of a corporate loan department of a local bank revealed his experience in analysing corporate loan applications:

... as bankers, we don't take into account whether there is a segregation of duties between audit and other services. We accept the accounts as good, as long they are audited and there is a stamped, signed declaration by the auditor; that's good enough for us. It doesn't matter whether they provide non-audit services to the company.

In addition, the interviews disclosed that the separation of entities is an effective way to minimise the auditor independence dilemma because audit partners in the

different entities do not have any direct interests, either financial or personal, that would cause them to compromise their objectivity. A manager of a Big Four firm noted:

They do not directly share the same pool of revenue and profit. Thus, each of them will protect their interest and professionalism and will conduct their business objectively.

A small minority of the interviewees who were opposed to the suggestion to separate the entities contended that staff from different entities that undertake audit and non-audit services still belong to the same organisation and will ultimately report to the same group of partners. Their concern was focused on the willingness of partners within the same firm to expose the weaknesses, mistakes and wrongdoings of their colleague to the regulators or the public, hence, damaging the firm's reputation. A chief internal auditor of a public listed company pointed out:

All of them will report to the same partner, unless they have formalised some internal controls that are transparent to outsiders, which most of them claim that they have done; sure, they can say they have separate systems, they have separate reporting lines. However, who checks all these claims? Nobody checks the auditors. I don't know who audits their accounts, or what the accounts look like. Right now the disclosure of work is only on the clients' annual reports, not on their part. So when it comes to monitoring their independence, how do you do that?

Furthermore, the interviews revealed that users of financial statements might be misled by the different names under which both services were performed, when in actual fact the same person was running the firms.

Provision of NAS to Non-Audit Client and Total Prohibition

The majority of the respondents disagreed with the statement that auditor independence would be reduced if auditors were only allowed to provide non-audit services to non-audit clients. Although there is strong disagreement with the statement from the auditors (66%) and senior managers of public listed companies (88%), this is less than that expressed by the loan officers (99%), as shown in Table 4, and this might reflect the confidence of the loan officers in the safeguard to auditor independence created from the prohibition of provision of NAS to audit clients. This result is consistent with Canning and Gwilliam (1999). Teoh and Lim (1996) in Malaysia suggested that there is a need to restrict the provision of consulting services to non-audit clients. The result might be a sign of the need for auditors to concentrate on their main function, to provide assurance as to the truth and fairness of clients' accounts, and not involve themselves in providing non-audit

services to audit clients. In addition, the responses shown by the majority of the respondents might reflect their belief that auditors should concentrate on providing one kind of service to their clients, either audit or non-audit services, as this would reduce the risk of conflict of interest (Canning and Gwilliam, 1999).

Opponents to the joint provision of audit and NAS have pointed out that auditors should be banned from providing NAS (e.g. Flint, 1988; Sherer and Kent, 1983). It was observed that the majority of the respondents disagreed with the statement that auditor independence would be reduced if auditors were prohibited from providing non-audit services. Although there is strong disagreement from the auditors (61%) and senior managers of public listed companies (62%), this is less than that expressed by the loan officers (71%), as shown in Table 4, and this might reflect the loan officers' concern with the potential drawbacks associated with the joint provision of audit and NAS to audit clients.

When the interviewees were asked about the issue of limiting the provision of NAS to non-audit clients or completely prohibiting auditors from providing NAS, all of them agreed that both approaches would safeguard auditor independence, which is consistent with the questionnaire survey findings. Discussing the potential improvement to auditor independence, a director of a merchant bank remarked:

I think the scope would be less, if you ask me about impairment. I don't see total elimination, I see less, the reason being because I think the business world today is based on networking and contacts, so it is more likely that the audit firm might actually introduce whatever tax consultant, financial consultant, at the end of the day I mean we hate to say this, but there might be a certain kick back, there might be certain other benefits derived somehow, somewhere.

However, the interviews disclosed that the prohibition would be too stringent for local accounting profession, where there are other possible alternatives to overcome auditor independence issues. They indicated that the Malaysian accounting profession would severely resist this suggestion, due to the fact that fees from NAS could compliment their low incomes from audit fees, and pointed out that there is lack of financial services experts in Malaysian capital market to replace those audit firms. A chief of an internal audit department of a public listed company remarked:

If you look at the accounting firms, there are not many of them out there. We hate to lose some of the good work done by the KPMG or PriceWaterHouse or Ernst and Young and others. They are good consultants and also good at auditing statutory accounts. If you prohibit the business altogether, you'll lose that expertise and talent. Why would we go and shoot ourselves in the foot?

Therefore, the majority of the interviewees felt that these suggestions were not the best solutions to the problem faced by the profession.

Joint Provision of Audit and NAS with Full Disclosure in Client's Financial Statement

As shown in Table 4, a sizeable percentage of the auditors (40%), loan officers (30%) and senior managers (42%) disagreed with the statement that auditor independence would be reduced if full disclosure on NAS were to be made in the clients' financial statements, and this might reflect the confidence of the respondents in the potential benefits that disclosure on NAS might bring.

When interviewees were asked about what impact full disclosure in the client's financial statement of the provision of NAS by auditors to audit clients would have on auditor independence, about half of the auditors (54%), loan officers (53%) senior managers of public listed companies (53%) and senior managers of regulatory bodies (59%) agreed that this approach would safeguard auditor independence, which is consistent with the questionnaire survey findings.

The interviews disclosed that such disclosure could inform shareholders and regulators about auditors' involvement in clients' companies, and would trigger them to ask questions about the auditors' relationship with management. The interviews indicated that such disclosure would allow shareholders and the general public to assess the amount of money paid to the auditor and ask questions if they were not comfortable with the figures. A partner of a medium size audit firm noted:

It will create awareness among the public, shareholders and stakeholders. It also triggers them to ask question in the AGM, like 'Who is the auditor and consultant, and how will the management ensure there is a split of independency between the two?' If we don't have such disclosure, it is not fair to the public, who have a lack of knowledge on the operation side.

Some of the interviewees disclosed that many Malaysian investors did not care about accounting disclosure in financial statements, and were more concerned about the company's profits and payment of dividends. It was argued that a majority of small investors would not pay much attention to this type of disclosure. A financial controller of a second board company described her experience as follows:

I have attended so many AGMs, and none of the shareholders ask questions. They are not really interested in what the company does, and as long as the company pays dividend, they'll keep quiet. They don't really try to understand the business of the company. We don't have people that stand up and ask questions like 'why we are paying so much for consultancy?'

This argument was further supported by a vice president of a listed company, who added:

I supposed it also depends on the type of shareholders that we have. In general, Malaysian shareholders are still not aware of their rights, and do not question this issue during the AGM. If the majority of shares are controlled either by a single entity or a family, the minority shareholders may not ask the company or director questions.

The interviews disclosed that Malaysian regulators should require the disclosure to include further details that outline the type of non-audit services provided, together with the amount of fees paid for the services and not only the total amount, as practiced currently.

Analysis of Mode of NAS Provision

An attempt was made to identify whether there exist significant differences in perceptions on mode of NAS provision using non-parametric tests (i.e. Friedman two-way ANOVA). As shown in Table 5, the respondent's perceptions on the mode of NAS provision are significantly different, where the NAS provision by audit personnel was found as the most threat to auditor independence in all groups (i.e. auditors, loan officers, senior managers of public listed companies and overall).

Table 5 Impact of method of provision of Non-audit Services (NAS) on perceived auditor independence

The independence of the auditor, for the purpose of audit, is reduced if NAS are	Mean Rank of the Friedman Two-Way Anova			
	Overall* n=287	Auditor N=93	Loan Officer n=87	Manager n=107
provided to audit clients by personnel involved in audit	5.35	5.04	5.66	5.37
provided to audit clients by a separate department within the audit firm	3.65	3.71	3.87	3.41
provided to audit clients by a separate entity where the auditors have an interest	2.94	2.83	2.58	3.31
provided to non-audit clients only	2.51	3.02	2.17	2.34
not provided at all	2.90	2.87	2.80	3.01
provided by the auditor to all clients but full disclosure is made in the client financial statements	3.66	3.53	3.91	3.56

* $\chi^2=561.326$, $p<0.0001$

Note: The higher the mean rank, the more the respondents agreed with the statements.

In Table 6, matched pairs of mode of NAS provision was made with the aim to identify whether significant differences exist in perceptions of auditor independence. Using the Wilcoxon matched pairs signed ranks tests; each methods of NAS provision were compared. For example, the NAS provision by audit personnel was exclusively compared with the other five mode of NAS provision (i.e. separate department, separate entity, non-audit clients only, not provided at all, and full disclosure). Based on the Wilcoxon matched pairs signed ranks tests, the provision of NAS to audit clients by audit personnel was found as the most threat to auditor independence.

Table 6 Comparison of method of provision of Non-audit Services (NAS) and its impact to perceived auditor independence

Wilcoxon Matched-Pairs Signed Ranks Tests				
Method of Provision of NAS	- Ranks MR (Cases)	+ Ranks MR (Cases)	Ties (Cases)	Test Results
B & A	106.44 (185)	114.24 (29)	(73)	$z = -9.740$; $p < 0.0001^*$
C & A	105.50 (210)	0.00 (0)	(77)	$z = -13.5869$; $p < 0.0001^*$
D & A	142.89 (248)	18.00 (19)	(20)	$z = -15.1920$; $p < 0.0001^*$
E & A	127.63 (251)	47.50 (2)	(34)	$z = -14.2475$; $p < 0.0001^*$
F & A	117.84 (225)	73.50 (7)	(55)	$z = -13.2041$; $p < 0.0001^*$
C & B	93.25 (120)	85.0 (60)	(107)	$z = -14.548$; $p < 0.0001^*$
D & B	73.39 (133)	79.75 (14)	(140)	$z = -8.644$; $p < 0.0001^*$
E & B	94.66 (116)	53.13 (48)	(123)	$z = -7.163$; $p < 0.0001^*$
F & B	116.11 (93)	79.23 (100)	(94)	$z = -1.917$; $p < 0.0001^*$
D & C	54.57 (66)	28.50 (27)	(194)	$z = -5.6235$; $p < 0.0001^*$
E & C	85.45 (66)	54.88 (72)	(149)	$z = -1.8991$; $p = 0.0575^*$
F & C	95.50 (29)	67.38 (116)	(142)	$z = -5.4307$; $p < 0.0001^*$
E & D	54.00 (31)	56.78 (80)	(176)	$z = -4.7802$; $p < 0.0001^*$
F & D	106.70 (28)	94.16 (163)	(96)	$z = -8.6361$; $p < 0.0001^*$
F & E	69.50 (41)	85.57 (121)	(125)	$z = -6.8213$; $p < 0.0001^*$

A: NAS provided by audit personnel; B: NAS provided by a separate department; C: NAS provided by a separate entity; D: NAS provided to non-audit clients only; E: NAS not provided at all; F: NAS provided but full disclosure.

* Two tailed probability; MR=Mean Rank

-Ranks: Respondents agreed less that independence would be threatened if the first rather than the second method of NAS provision were adopted.

+ Ranks: Respondents agreed more that independence would be threatened if the first rather than the second method of NAS provision were adopted.

Type of NAS

This section examines the impact on auditor independence based on different types of NAS to audit client. The main focus is to identify the different kinds of NAS potentially affect auditor independence in different ways or perhaps some of the

NAS may not give any impact at all. As shown in Table 7, Fifteen (15) types of non-audit services were examined.

As reported in Table 7, the mean distribution of the overall sample indicate that the provision of accounting/bookkeeping, internal audit, asset valuations, financial information system design and treasury management services as the top 5 services that may affect auditor independence if those services are provided by auditor to audit client.⁶ On the other hand, the overall respondents consider the stock exchange circulars, secretarial, due diligence, management training and human resources services would not undermine auditor independence.

This result suggested that recurring services like accounting/bookkeeping and internal audit, and non-recurring services such as asset valuations, financial information design and treasury management services were considered as a threat to auditor independence, which is not consistent with Beck, Frecka et al. (1988a) and Parkash and Venable (1993) findings. They posited that recurring services provide continuous rents to the auditor that can result in a perception of impaired independence, and conversely, bonding effects of non-recurring services would be minimal to non-existent. This clear dividing line between the effect of recurring and non-recurring was not supported in this study.

Responses from auditors show that only 3 NAS were considered as a threat to auditor independence namely accounting/bookkeeping, internal audit services and management functions. However, loan officers did not consider management functions services could undermine auditor independence; instead they believe that asset valuation, financial information systems design and implementation, treasury management services, corporate finance services, and accountant's report and review on profit forecast for Initial Public Offering Company as a threat to auditor independence. Consistent with loan officers, the managers are more stringent in their evaluation of type of NAS by adding additional services that may threaten auditor independence namely tax planning and compliance services, management functions and secretarial services. The variability of responses among the respondents' groups is clearly evident, where 14 out of 15 NAS were significantly different among the respondent's group implying that exist inconsistent opinion. Moreover, 13 of the 14 NAS are significant at 1% level (using the Kruskal Wallis test).

Majority of the loan officers (94 percent) and managers (82 percent) interviewed agree with the suggestion to adopt the rule to ban the provision of selected type of NAS to audit client as provided by the Sarbanes Oxley Act and the US's SEC rule, where they believe that this kind of prohibition would enhance auditor independence. Only 5 of the auditors agreed with the suggestion. Most of the interviewees that agreed with the suggestion reckon that the prohibition should be on selective basis. Majority of the interviewees reckoned that any adoption or

⁶ Mean distribution greater than 2.00 indicate that the respective NAS will undermine auditor independence if it is provided by auditor to audit client, while mean distribution lower than 2.00 indicate that the respective NAS will not undermine auditor independence.

Table 7 Analysis showing perceptions of the effect of type of NAS provided by auditors to their audit clients to auditor independence

The following types of NAS provided by auditors to audit clients may threaten auditor independence:	Auditors (N=93)				Loan Officers (N=87)				Senior Managers (N=107)				Overall	
	Disagree %	NoView %	Agree %	Mean	Disagree %	NoView %	Agree %	Mean	Disagree %	NoView %	Agree %	Mean	Rank	Sig.
Accounting/bookkeeping	11	2	87	2.76	-	100	3.00	17	2	81	2.64	2.80	1	
Corporate finance services	21	67	12	1.92	28	48	2.21	20	9	71	2.50	2.21	6	***
Due diligence (e.g. acquisitions)	88	12	-	1.12	61	31	1.70	71	2	27	1.55	1.46	13	***
Financial information systems design and implementation (IT)	42	21	37	1.96	14	78	2.64	12	1	87	2.75	2.45	4	***
Accountant's report and review on profit forecast for Initial Public Offering (IPO) company	58	25	17	1.59	41	57	2.15	25	17	58	2.33	2.02	8	
Human resources/personnel services	71	29	-	1.29	46	27	1.82	33	23	44	2.11	1.74	10	***
Internal audit services	23	1	76	2.53	-	7	2.93	4	2	94	2.91	2.79	2	***
Legal services	35	52	13	1.78	41	43	1.75	69	23	8	1.39	1.64	11	***
Management functions (act temporarily or permanently as a director/officer)	24	42	34	2.10	27	51	2.22	30	20	50	2.20	2.08	7	***
Management training services	74	26	-	1.26	57	29	1.56	37	20	43	2.06	1.63	12	***
Secretarial services	87	2	11	1.24	76	11	1.37	65	20	15	1.50	1.37	14	***
Stock exchange circulars	76	22	2	1.25	75	24	1.26	78	14	8	1.29	1.27	15	
Tax planning and compliance services	70	15	15	1.45	54	31	1.77	13	12	75	2.62	1.95	9	
Treasury management services	56	30	14	1.58	21	26	2.32	6	12	82	2.77	2.22	5	***
Asset valuations or appraisal services or fairness opinion	50	11	39	1.89	8	90	2.82	10	4	86	2.78	2.50	3	***

Note: ***, ** indicates that the distribution of responses between Auditors, Loan Officers and Senior Managers is significantly different at the 1% and 5% level respectively (using the Kruskal Wallis test). The responses were reported on a 5-point scale ranging from 1 (strongly disagree), through 2 (disagree), 3 (no view), 4 (agree) to 5 (strongly agree). For presentational purposes these 5 points have been collapsed into disagree (scored 1), no view (scored 2) and agree (scored 3) and the reported means are calculated on this collapsed scale. However, the significance tests are based on the full 5-point distribution of responses.

enactment of law should be tailored to the local business environment. Perhaps, the lawmaker should seriously examine the impact of the suggested regulation to different type of companies like companies with high/low ownership concentration. This unique nature of Malaysian capital market is crucial to be considered before any new law being implemented.

Some of the loan officers believe that regulators should ban the auditor from providing merger, acquisition and due diligence services, while they believe that the provision of tax, recruitment and review of profit forecast services would not undermine auditor independence. However, the managers interviewed showed a different attitude, which is well summarised by a chief internal audit of a main board companies:

Perhaps, the provision of due diligence should not be a problem, while book keeping or anything to do with system improvement should be restricted. In one hand, they perform the services to satisfy their client expectation, and on the other hand, they going to audit it, and surely they won't criticise their own work. However, the provision of due diligence is more like exercising their professional judgement. I supposed anything to do with the company itself should not be provided by the company's auditor.

The information gathered from the questionnaires and interviews indicate that the majority of the participants consider the provision of NAS that involves financial services is inconsistent with auditor independence and should be banned. Moreover, consistent with loan officers and managers, a big four's audit manager felt that more efforts are needed to educate client and auditor should be in place:

I don't disagree to the suggestion to prohibit auditor from providing non-audit service to their client, but the most important is that we have to educate both the client and the audit firm. If the client knows that consultancy job would create future problem, I believed they will award the job to the other firms and audit firm got no choice.

Sixty-two percent of the auditors interviewed disagree on the suggestion to adopt the rule to prohibit auditor providing selected type of non-audit services to their audit client. They believe that Malaysian auditors are aware on their ethical and professional standards, which would deter them from committing irregular practices or any wrongdoings. A partner of a medium size audit firms noted:

...the law will make no different ... we don't always try to help client to do nonsense. We still professional but we guide them to do the right thing, not so much just because I got few consultancy job with the client, then I'll guide them to do the wrong thing.

CONCLUSION

This study investigates the perceptions of Malaysian auditors, loan officers and senior managers of public listed companies on the effect of joint provision of audit and non-audit services on auditor independence. The majority of the respondents agreed that the provision of NAS to audit clients by the audit engagement team would threaten independence. Perhaps, this might indicate the respondents' concern about the ability of auditors to independently act as a watchdog to assure the truth and fairness of clients' accounts, and at the same time to perform their NAS duties to advise and consult with the client. The main concern indicated by the interviewees was with the ability of the auditors to behave independently due to their dependence on income from both services. Also, there would be a lack of 'checks and balances' if both duties were to be performed by the same person. The Friedman two-way ANOVA and Wilcoxon matched pairs signed ranks tests indicate that the joint provision of audit and NAS to audit clients by audit staff as the most threat to auditor independence.

On the other hand, the majority of the respondents agreed that auditor independence would not be threatened if the provision of audit and NAS were to be provided by staff from a separate department and entity. The result indicates that the respondents had faith in the segregation of duties or 'Chinese Wall' offered by these approaches. Though the departments and entities are under the same ultimate control or belong to the same firm, the level of communication between both parties is minimal, because each of them is responsible for the operation of their own department/entity. Consistently, the interviews indicated that auditor independence would not be threatened if staff from separate departments or entities were to provide audit and NAS. It was mentioned that these modes of provision of NAS would allow segregation of duties, which would result in greater monitoring activities. Despite the consistent view among the respondents, it was pointed out that the loan officers did not consider the method of provision of NAS as an important issue in their daily duties of loan processing because they believed that the auditors were currently doing a good job and producing reliable financial statements.

In addition, the majority of the respondents indicated their agreement that the threat to auditor independence would be less if the provision of audit and NAS were limited to non-audit clients or if it was completely prohibited for auditors to provide joint services, consistent with the interview survey findings. However, these approaches are indicated to be too stringent and would be severely resisted by the profession because income from NAS complements the low income derived from audit services for some audit firms. The results suggest that auditors should concentrate on one type of service: either auditing or NAS. Through concentrating on audit or non-audit services, the risk of conflict of interest could be reduced or eliminated. Finally, the majority of the respondents agreed that auditor independence would be safeguarded if auditors were to provide full disclosure in client accounts following the provision of NAS. In interview survey, it was revealed

that such disclosure could inform shareholders and regulators about the auditor's relationship with the company, while some of the interviewees contended that the Malaysian investors did not care about accounting disclosure because they were more concerned about the company's profits and payment of dividends. The result might suggest that the users become aware of the level of relationship between auditors and clients' management, and could question both parties on any issues about which they need further clarification during the annual general meeting.

The majority of interviewees support the suggestion to ban selected type of NAS to be provided by auditor their audit client. On average, the respondents consider the provision of accounting/bookkeeping, internal audit, asset valuations, financial information system design and treasury management service is not consistent with auditor independence. Finally, it is found that auditors are protective to the criticisms on their profession, which is consistent with Teoh and Lim (1995) findings. While the other group of respondents' applied a more rigid critics and suggestions on the perceptions of auditor independence.

Based on the findings in this study, it is recommended that the best alternative to prohibiting audit firms from providing NAS is a proper segregation of duties between staff that perform audit services and NAS. This segregation of duties should be in the form of separate departments or entities, where different partners and team provide the two services. Audit partners should not be involved, directly or indirectly, in the provision of NAS or even in the marketing of these services. In order to monitor this practice, each audit firm and its NAS arm should lodge its organisation profile, which should clearly state the identities of the audit team and the NAS team, with the MIA.

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