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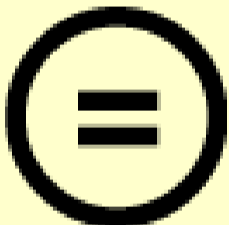
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**Communication through the Audit Report:
An Empirical Investigation of the Unqualified Audit Report in
Saudi Arabia**

by

Salem Abdullah Al Otaibi

**A thesis submitted in partial fulfilment of the requirements of
the Degree of Doctor of Philosophy**

**Business School
Loughborough University**

September 2003

Dedication

To my beloveds

Abdullah

Lama

&

Um Abdullah

Abstract

This study is an examination of communication through the unqualified audit report currently in use in Saudi Arabia and the usefulness of modifying the wording of such a document. In order to assess the views of members of the Saudi Organization for Certified Public Accountants (SOCPA) (auditors group), the Financial Directors of the Saudi Corporations (preparers group), and Saudi financial statement users (e.g., loan officers and financial analysts in the 10 Saudi commercial banks and institutions and private shareholders - users group) a questionnaire was distributed.

The identification of the underlying dimensions of the messages communicated by the unqualified audit report, part I of the questionnaire, resulted in the identification of five factors: (1) purpose of the audit, (2) auditor responsibilities, (3) financial statement reliability, (4) the entity future viability, and (5) the decision usefulness of financial statements. An expectation gap was found - particularly in relation to the responsibility factor. The purpose of an audit factor, however, suggested that the current standard audit report was a readable document which enhanced the credibility of the financial statements. Also, the current audit report appears to have been successful in clarifying the purpose of the audit. An audit expectation gap was seen to exist between auditor and non-audit groups concerning the extent of assurance given by auditors, the term 'present fairly' and the extent of audit work performed. In relation to the future viability factor, the results indicate that an audit expectation gap exists over the question of whether the unqualified audit report communicates management efficiency and whether the audited financial statements are useful in monitoring the performance of the entity.

Part II of the questionnaire related to the possible expansion of the contents of the audit report. This revealed significant differences in respondents' views regarding the expansion of the scope of auditors' opinion. Concerning the factor relating to the disclose of additional information about the internal controls and the auditor's assessment of the going concern status of the entity, the users, in contrast to the auditors, were of opinion that such disclosure would be useful in enhancing the value of the audit. In relation to the issue of the usefulness of adoption of the free form report factor, all three groups are in agreement that they are not interested in such a development.

These results present a challenge for the SOCPA, as they indicate that considerable potential value of the financial reporting process is being lost as a result of the expectation gap in Saudi Arabia. These results also support the call by previous studies worldwide for a change from a short-form audit report to the long-form audit report and the need to educate the users about the nature of audit and responsibilities and duties of auditors.

Acknowledgements

At the outset, I thank the Almighty 'ALLAH' for enabling me to complete this thesis.

A thesis needs a supervisor and I have one of the best. Special thanks to Dr Andrew Higson for being an excellent supervisor. His valuable critical and insightful comments and suggestions on initial drafts of each chapter of this thesis together with his overwhelming encouragement and support at all stages of my study were invaluable and much appreciated. I would also like to thank other members of my Supervisory Panel Meeting, namely Professor Barry Howcroft and Dr Laurie McAully, for being very helpful and supportive in the past three years. Their insightful advice, comments and suggestions have enriched the structure, content and quality of this thesis.

I wish to record my appreciation of the Umm Al-Qura University for granting me a scholarship to pursue my MSc and PhD studies. I would also like to record my gratitude to each individual participant in this study for the generous time they spent to complete the questionnaires and great enthusiasm shown during the conduct of the empirical work. I would like also, to thank my friend Mr Ahmed Al-Mutlaq. Many thanks also to my brothers Abdullaziz, Abdulmuhsen, Mohammed, Ahmed, and Bander Al-Otaibi and my sisters for their help and support.

Last, but not least, I would like to pay special tribute to the patience and support of my wife, and my children, Abdullah and Lama. Without them, not only would this work have been impossible, but also the inspiration underlying it would not have been allowed to flourish.

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Chapter One

Introduction to the thesis

1-1 Introduction and Motivation:

The need for the external audit may be seen as a response to the agency problem (Dunn, 1996). In Saudi Arabia, the Companies Act 1965 stipulates that every company (and the Act makes clear which companies are exempt and which are not by size or other specific criteria) is required to have its financial statements audited annually. This is often referred to as the statutory audit. Section 132 of the Act states that a company's financial statements are required to be laid before the company in its annual general meeting. The Act also requires the auditor of a company to provide a report to its members on the accounts presented at the annual general meeting. Thus, the auditor's report is a necessary attachment to any Saudi firm's published annual report. It is by the Act addressed to company shareholders and contains the auditor's opinion about whether the company's financial statements are fairly presented. It can thus enhance or weaken the credibility of the management's representations in their financial statements.

In 1985 the Saudi Arabian Ministry of Commerce financed a research project, the result of which were published in two volumes; the first was entitled "Accounting Objectives and Concepts", and the second, "Auditing Standards". These concepts and standards are similar to those issued by the American Institute of Certified Public Accountants (AICPA) (Aba-Alkhail, 2001; Al-

Motairy, 1999; Al-Rehaily, 1992). The "Auditing Standards" comprise seven standards, which can be outlined briefly as follows: adequate professional competence, auditor neutrality and independence, due professional care, auditing planning, documentation and control, auditing evidence, and *audit reports*. In October 1993 the Saudi Organisation of Chartered Public Accountant (SOCPA) Board of Directors gave their seal of approval to the two volumes which had been issued and approved by the Ministry of Commerce in 1985 (SOCPA's Board of Directors, Decision No. 3/2/4, October 1993).

The audit report standard, which was one of the seven auditing standards mentioned above, still remains ostensibly unaltered and can be said to have enjoyed a long period of existence. The effectiveness of communication in this report is the focus of this thesis. This focus will be based on the perceptions of members of the financial community namely: the auditors, the preparers of the financial statements (the auditees) and the users of these financial statements. This thesis presents the results of a questionnaire that directly addresses the existence of the audit expectation gap within the current audit report in use in Saudi Arabia. The thesis also examines the usefulness of arbitrary or codified additions to the report to be reported upon by the auditor to improve communication in such a document (the term 'communication' will be explored more fully in section 1-2).

The audit report is the main means of conveyance available to the auditor for communicating the results of the audit to groups external to the management of the company. In the audit report, the auditor has the opportunity to communicate his opinion, state the type of assurance he wishes to give, and

draw attention to additional information he feels is important with respect to those documents or areas of organizational performance which fall within the scope of his audit. If the meaning of the auditor's report is not clear then the value of the audit could, quite rightly, be questioned (Higson, 2003).

Around the world changes have been made to both the form and content of audit reports to tackle perceived misunderstanding of the message conveyed by audit report. In the US, for example, in 1988, the short report format used for forty years was replaced by a longer audit report as a part of attempts to close the audit expectation gap. The expanded audit report aimed to clarify the respective roles of auditors and managements in preparing the financial statements. Several countries have proposed and subsequently adopted expanded audit report wording in an attempt to tackle the audit expectation gap. In the UK, the Auditing Practice Board (APB) introduced in 1993 an expanded audit report. The purpose of expanding the audit report in the UK was to "set out in more details the work of auditors, as well as the auditors and directors' responsibilities, and thus help to tackle the audit expectation gap" (Higson, 2003, p.162). However, this report was revised in 2001. Hence the aim of audit report wording changes has been to improve the effectiveness of communication through the audit report.

The timeliness of this study lends to its importance. It comes a few years after the adoption of the auditing standards and also follows the creation of the Saudi Organization of Certified Public Accountants (SOCPA) in 1992. Furthermore, it comes shortly after the passing of a new foreign investment law in April 2000 (see Appendix A, p.286) in which audited financial

statements play a significant role in assuring local as well as foreign investors. There is also the establishment of the new Saudi stock market to take into consideration.

These are factors enough to justify this study, but there remain other important motivating circumstances for undertaking this study which include:

- The number of public and joint venture companies in Saudi Arabia has increased insignificantly over the years, partly as result of the government's policy in promoting free-market capitalism and encouraging the foreign investment into the country. As such, it is especially important for foreign partners and shareholders to gain an understanding of the meaning of the audit report currently in use to ensure their continued confidence in the local auditing profession and report audited by its members to help them (foreign business partners) in their investments decision-making.
- Saudi Arabia is one country whose auditing profession is the least researched and understood. This research intends to fill this academic gap by providing an insight into Saudi Arabia's auditing profession. Its results would help as well as provide the Saudi Organisation for Certified Public Accountants (SOCPA) when making recommendations and issuing standards on issues related to audit report by highlighting the concerns raised by the subjects who participated in this study regarding the existence of the audit expectation gap with the current audit report in use as well as to go beyond such a document.

The next section of this chapter develops a framework within which audit expectation gap issues can be examined while the final section describes the format of the thesis.

1-2 The Research Framework:

Over the last two decades, the western world has experienced a spate of corporate failures (the more recent ones being the Enron and WorldCom financial scandals of 2001). Audit failures have placed the audit expectation gap debate firmly on the agenda of the accounting profession, regulators and the public (Humphrey et al., 1993).

The audit expectation gap debate has consistently centred on a number of issues which fail to go away. According to (Humphrey, 1997, p. 13) these issues include: audit assurance; audit reporting; audit independence; and audit regulation and liability. If one accepts that communication is central to the function of accounting and auditing and meaning is critical to communication, then the study of meaning is central to the study of accounting and auditing. Leading from this, the study of *shared* meaning between users and producers of accounting and auditing information is central to the study of the effectiveness of accounting and auditing communication (Houghton, 1998, p.2).

Communication theory attaches central importance to the role of meaning in the communication process: communication involves the encoding and

decoding of messages, with a code being a shared system of meaning. If senders and receivers of messages have access to the same code, then meaning is generally shared and communication takes place with some resultant effect on the receiver. A code is "a system of meaning common to the members of a culture or sub-culture. It consists of both signs and rules or conventions that determine how and in what context these signs are used and how they can be combined to form more complex messages" (Fiske, 1990, p.19). Arguably, the audit report is a code belonging to the sub-culture of financially literate people. For instance, after the completion of the audit process, the auditor decides on the message he would like the report reader to receive. This message must be selected from, or encoded within, a limited number of choices of wordings. Primary transmission of the message is in the form of the printed auditor's report attached to the financial statements in the annual report of the auditee company. The reader receives the report and is presumed to read it. In reading the report, the user interprets and decodes the message in some way, resulting in some kind of judgment about the validity and reliability of the financial statements.

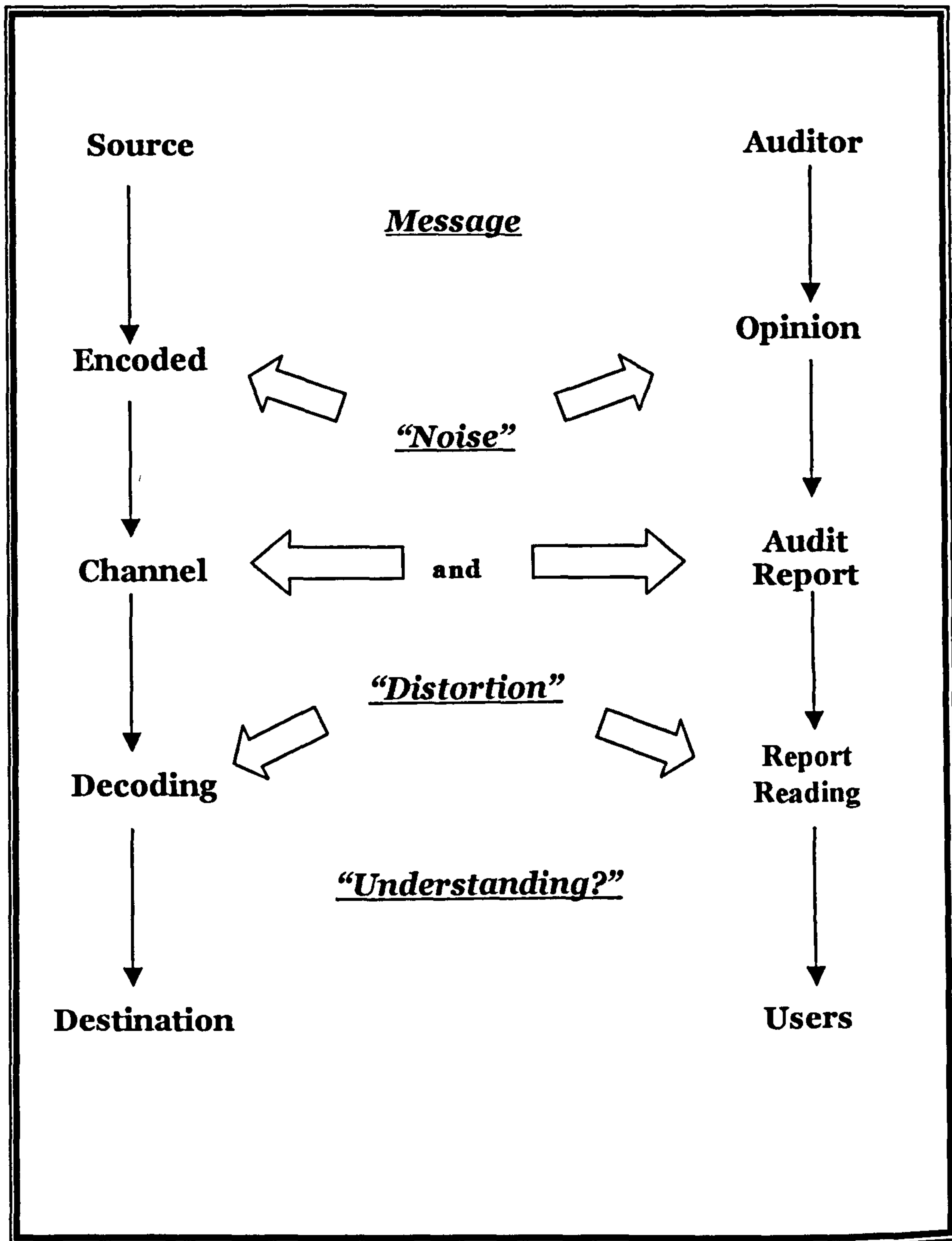
Despite the differing emphases and theoretical frames of reference employed by the different disciplinary approaches to communication, certain elements are regarded as fundamental to the process of communication. These are: a sender, a receiver, a channel, a message and an effect. For any communication to take place, a sender initiates a message, then encodes it (translates it into a signal, such as writing). The message is then sent (transmitted) through a channel or medium (such as a report) to a receiver who decodes the message. In decoding the message, the reader interprets it

in some way, with a consequent behavioural or affective response. The analysis to which this process has been subjected may be divided into two major schools of thought. These are: "process" and "semiotic" (for more details see Fiske, 1990).

Process-type models are largely derived from the basic linear model of Shannon and Weaver (1949). Higson (1991) illustrated such a model as applied to the audit reporting process as can be seen in **Figure 1.1**. The three elements identified are the message to be communicated, the channel or how the message should be communicated and the receiver (Higson, 1991). Central to the communication process is the identification of the message to be sent. Communication is effective if the message is understood by the receiver. However, noise and distortions are identified as hindrances to effective communication (Higson, 1991, p.21).

In relation to the audit report, the auditor is the source of the message. The channel of communication is the audit report and the receivers are the users of financial statements. The users of the financial statements can read the audit report but problems can arise in the transfer of the auditor's message due to noise and distortion (e.g. see Lucey, 1987).

Figure 1.1
The Communication Process*



* Source: Higson, 1991, p.21

Noise in audit report could relate to the technical phrases used, whilst distortion could be from the users interpretations of the words in the audit report. This problem could be traced to the fact that a given set of data can have different meanings to different users where the processes of thought and understanding are involved (Haried, 1973; Oliver, 1974).

To achieve effective communication there needs to be a clear message and an audit report should, therefore, aim to minimise noise and distortion. Effective communication is more than sending information; it is about understanding whether the message is received (Higson, 1991).

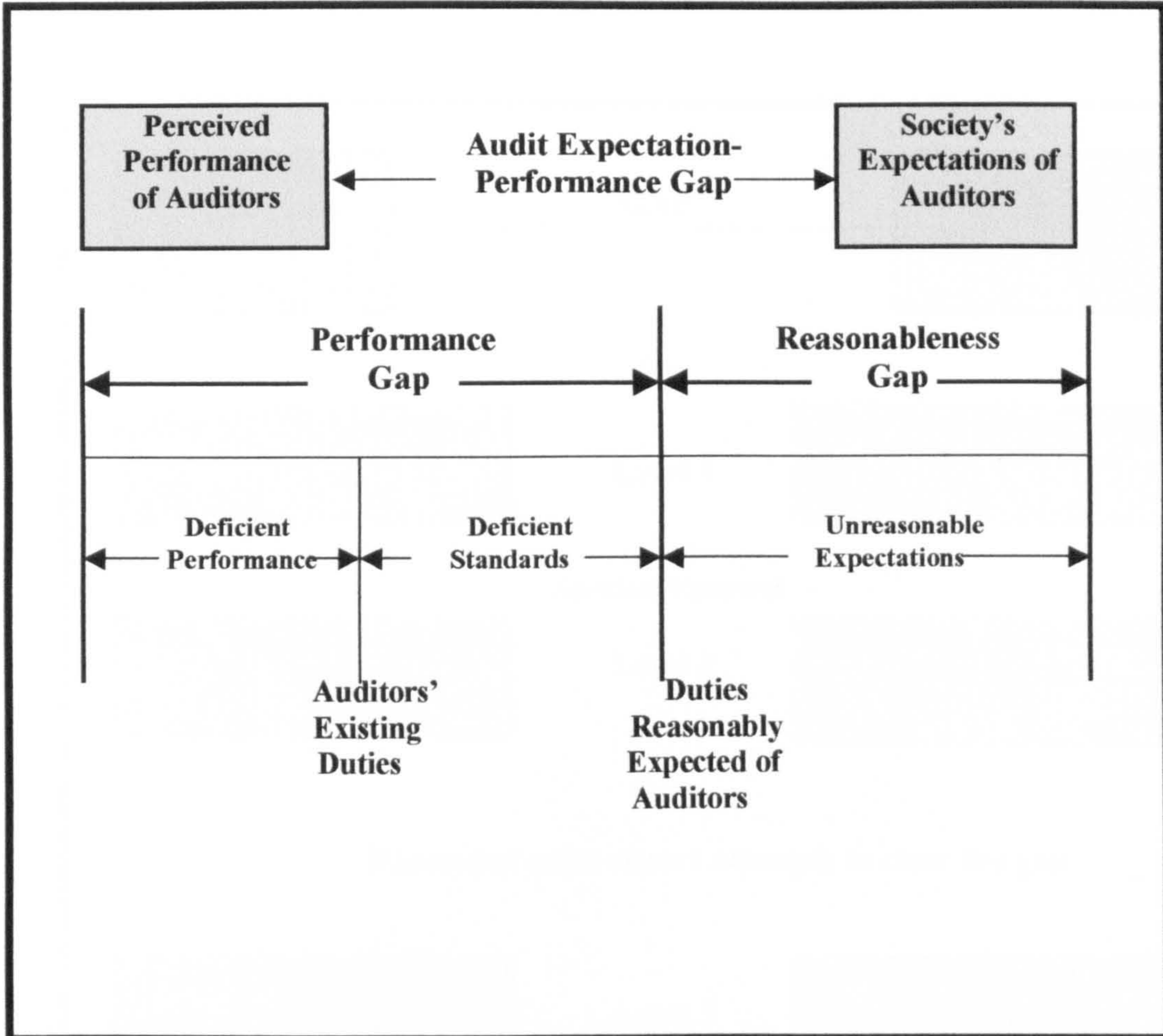
In relation to the audit expectation gap, such process-type models have been implicitly applied in the existing literature which typically identifies the audit expectation gap as a communication problem: the audit report is not worded adequately so as to convey the message intended by the auditor in respect of the auditee's financial statements. Although a useful starting point, such a model is partial and simplistic. The assumption is that the meaning encoded and the meaning decoded should be the same, unless there has been some noise and distortion (or encoding or decoding "error") in the communication process. However, it may be problematic whether a standard set of words can encapsulate the multitude of professional judgments and interpretations necessary in the conduct of an audit.

Previous studies of the audit expectation gap while not conducted within an explicit theoretical framework, may be viewed as based implicitly on a process-type model of communication. That is, the emphasis is on how best

to transmit the message to the receiver (e.g. by altering the wording of the audit report) and the receiver (generally through the process of "educating the public"). To develop a framework within which audit expectation gap with audit report issues can be examined to examine the effectiveness of communication on the audit report, it is useful to also consider two frameworks that were discussed in the literature. One of them was developed by Porter (1991, 1993) and the other by Harthley et al (1992).

Porter (1993) as seen in **Figure 1.2** believes that the expectation gap comprises two components: (1) the difference between the expectations of users and the reasonable standard of auditing which the auditing profession can be expected to deliver ("unreasonable expectations" or reasonableness gap); and (2) the difference between the standard of auditing services currently being delivered and a reasonable standard of auditing services ("inadequate performance" or performance gap). The inadequate performance component is comprised of: (i) the difference between the standard of auditing services currently being delivered and existing auditing standards; and (ii) the difference between existing standards and the reasonable expectations of the market place. Porter termed the first sub component "deficient performance" and the latter "deficient standards".

Figure 1.2
Structure of the Audit Expectation Gap*

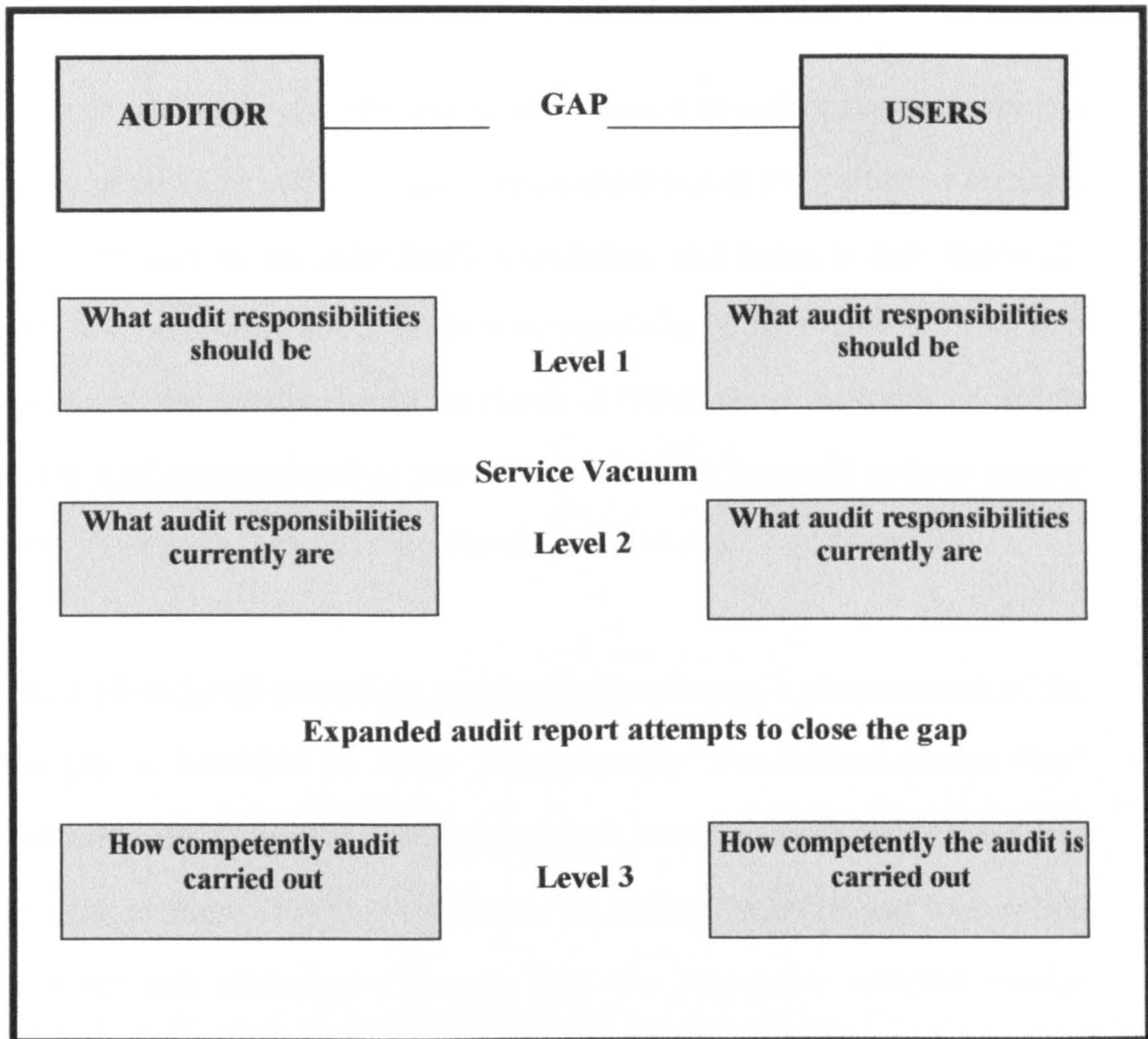


***Source: Porter (1993, p. 50)**

Hatherly et al. (1992, p.6) have adopted a slightly different focus when considering the components of the expectation gap. Hatherly et al (1992) indicate that the gap comprises the three levels depicted in **Figure 1.3** “(1) what the role, responsibilities and environment of the auditor ideally should be; (2) what the responsibilities currently are as determined by present

statute and interpretation; and (3) how these responsibilities are currently carried out.” (p.6)

Figure 1.3
Expectation Gap Basic Framework*



Source: Hatherly et al, 1992, p.8.

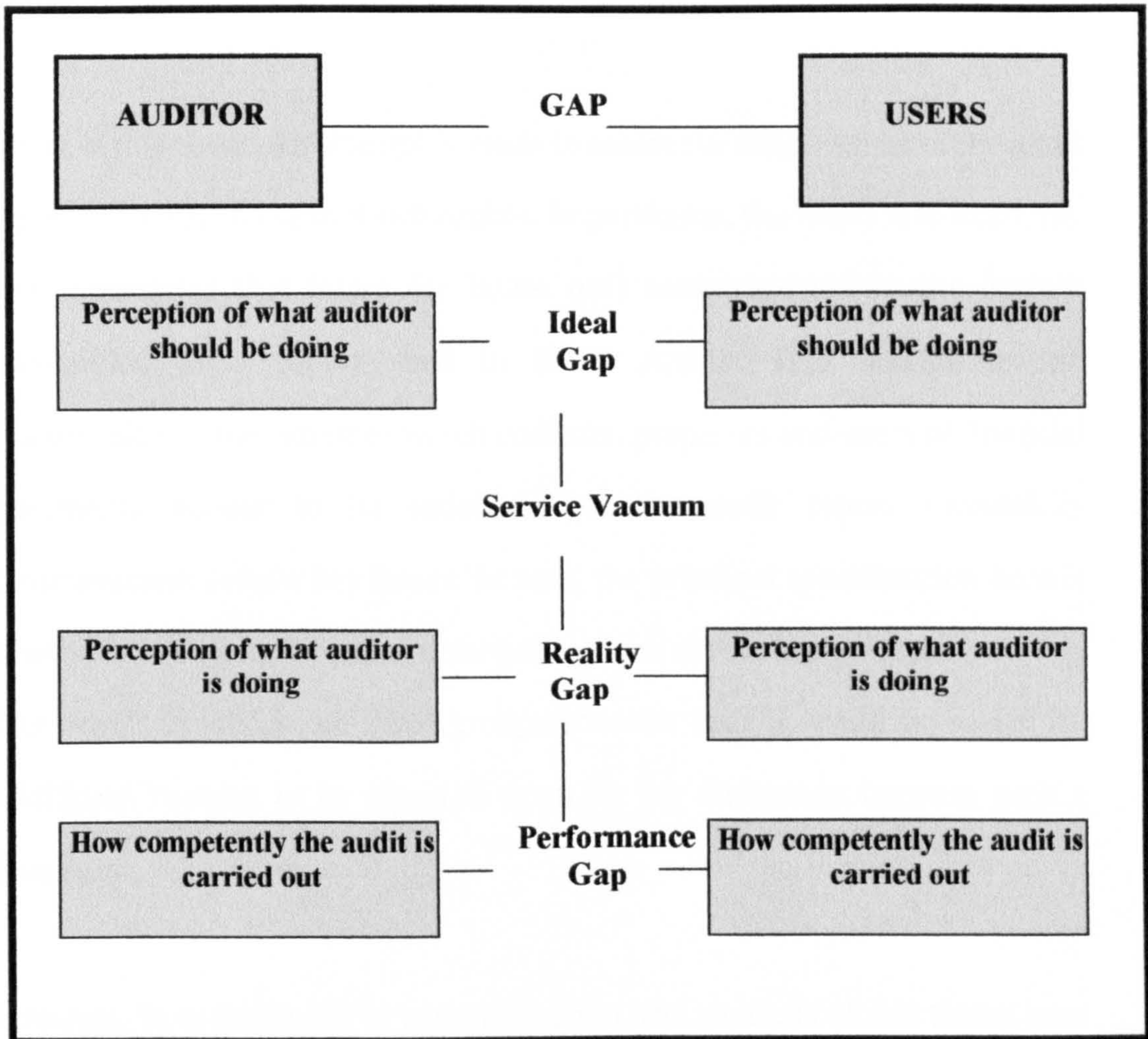
The first level concerns differences about what auditors’ duties and responsibilities should be (Ideal Gap). The second level reflects differences about the duties and responsibilities of the parties to an audit and the messages communicated throughout audit reports (Reality Gap). The

difference between Level 1 and Level 2 is a service vacuum, which represents a shortfall in current audit standards against expectations of auditors and financial report users. Both “unreasonable expectations” and “deficient standards” contribute to this service vacuum. The third level arises when auditors fail to exercise due professional care.

However, changing the wording of audit report to reflect more clearly the nature of an audit and the relative responsibilities of the parties to an audit should impact on an individual’s knowledge, and hence beliefs (Level 2), while not necessarily affecting the individual’s belief over what the auditor’s responsibilities ideally should be (Level 1) (Hatherly et al. 1992). Similarly educational programmers or promotions would be expected to have greater impact on beliefs (Level 2) than (Level 1) toward auditor responsibility.

This study is based around the communication theory; it concentrated on the first gap as identified by Porter (1993) namely “*The Reasonableness Gap*” and as the Hatherly et al. (1992) framework based on audit reports contains elements of Potter (1993) in their study on audit expectation gap framework. It is for this all-inclusive reason that the researcher adopted similar framework to that of Hatherly et al. (1992) framework as the basis for this study. Thus, the expectation gap here was concerned with gap two in **Figure 1.4**, namely the expectations gap between what auditors perceive they are doing and what users perceive auditors are doing based on an audit report.

Figure 1.4
The Expectation Gap Framework



1-3 The Focus of The Study:

An “audit expectation gap” was defined to exist when there are differences in beliefs between auditors and the public about the duties and responsibilities assumed by auditors, and the message(s) conveyed by audit reports (level 2, reality gap). An important step in addressing the expectation gap is identifying where differences in beliefs (Level 2) exist between auditors and financial report users. As evidence in Saudi is sparse and the main purpose of

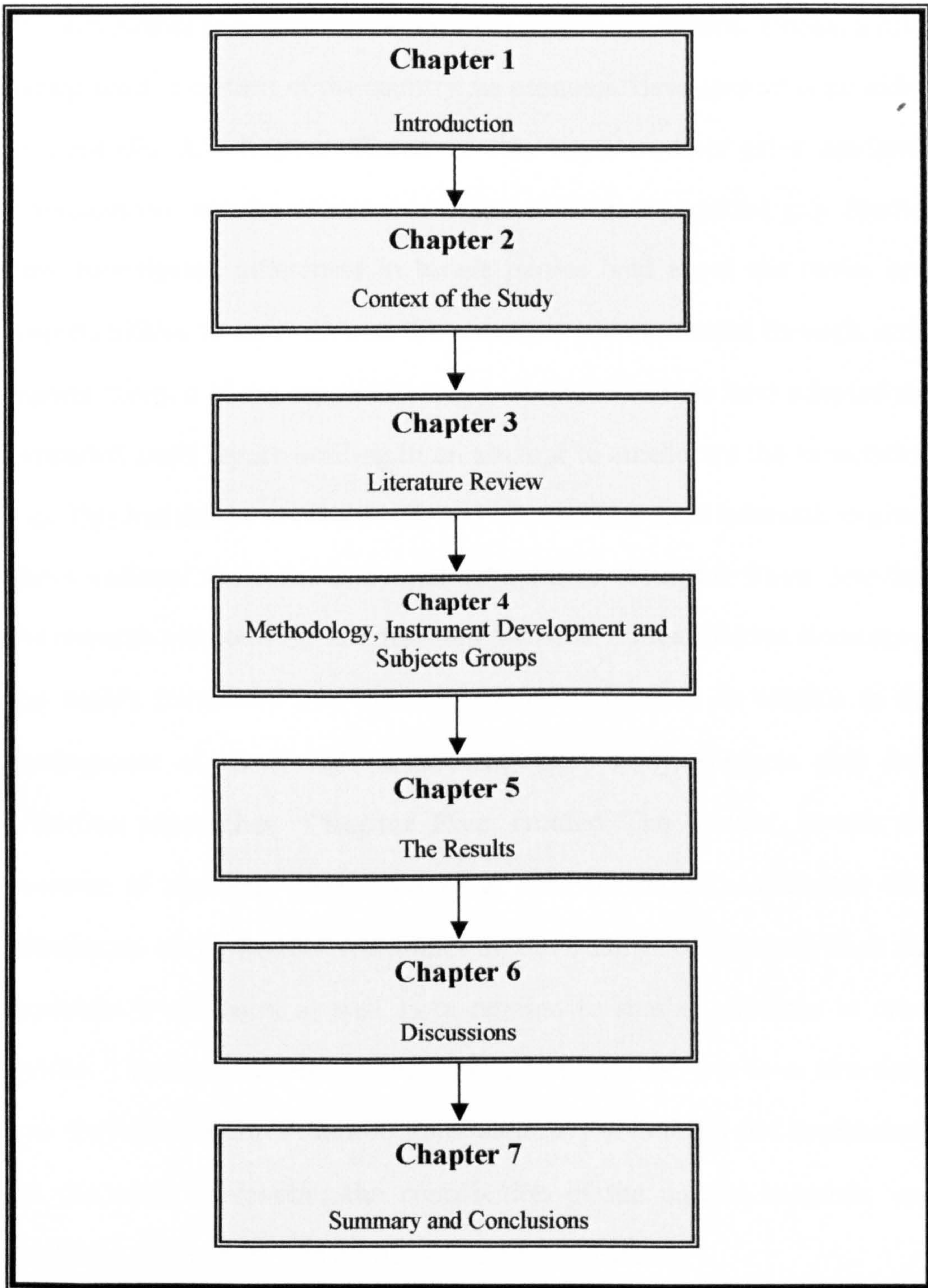
this thesis is to identify where differences in expectations and beliefs are concentrated, if indeed there is a pattern within the current unqualified audit report in use.

Thus, in this thesis, an attempt is made to assess the effectiveness of the audit report currently in use in Saudi Arabia. In particular, the thesis is to examine: The message(s) that is/are (or is/are not) communicated in the current unqualified audit report used in Saudi Arabia. This necessitates an examination of the extent to which auditors, preparers and users of financial statements appear to be satisfied that the audit report successfully communicates certain key issues. In turn, the principal consideration here is whether there are differences in the perceptions of the three groups.

The extent to which the three groups consider that it would be useful for additional matters to be reported upon by the auditor to improve such a document.

However, In order to aid in comprehension, the contents of this thesis have been structured into seven chapters as illustrated in **Figure 1.5**. **Chapter One** of this thesis is an introduction, and it pinpoints the research line that this study follows. Moreover, the objectives which governed the overall conduct of are outlined as well as the research framework and motivation of the research. **Chapter Two**, the context of the research, focuses on the framework for financial reporting and auditing in Saudi Arabia. Moreover,

Figure 1-5
Structure of the Thesis Chapters



aspects of the characteristics of audit firms and auditees operating in the business environment, and prominent aspects of the audit reporting system in Saudi Arabia (e.g. elements of the audit report) are tackled. Finally, a brief background to context of the country, its economic development is provided in appendix A. **Chapter Three** of this thesis reviews prior academic investigations into the existence and nature of an expectation gap. Studies have investigated differences in beliefs parties hold about the duties and responsibilities to an audit and the messages communicated through audit reports (Level 2 of the expectation gap). Several countries have adopted the expanded audit report wording in an attempt to ameliorate the expectation gap. This has also been considered, and some background information given about auditors' assurance and auditors' opinion. **Chapter Four** describes the research methodology and research methods, it identifies the elements of the study's framework and delineates steps undertaken in relation to the development of the study's instrument, pilot study, subjects, and data collection approaches. **Chapter Five**, entitled 'The Results', reveals the outcome of applying specific statistical tests to the data. **Chapter Six**, 'Discussion of the Results', elucidates on the findings of the study from the researcher's viewpoint as well as in relation to similar findings in other studies. **Chapter Seven**, 'Summary and Conclusions', has been structured into the following three main sections: summary of findings and implications for the audit profession; the contribution of the current research; and limitation of the study and avenues for future research.

1-4 Summary and Conclusion:

This introductory chapter presents the research line that this study follows and the objectives which governed the overall conduct of are outlined as well as the research framework and motivation of the research. The next chapter will provide information about the context of the research, namely Saudi Arabia, and focuses on the framework for financial reporting and auditing in that country.

Chapter Two

Background to the Research

2-1 Introduction:

The auditing profession in Saudi Arabia has developed into its modern form only since the passage of the 1991 Certified Public Accountants' Law (Al-Motairy, 1999). The Saudi Organisation for Certified Public Accountants (SOCPA) became the national organisation of accountants and auditors. Whereas this thesis is about investigation of the message(s) communicated in the audit report currently in use in Saudi Arabia and the usefulness of going beyond such a document, it would be helpful to familiarise the reader with the setting and environment of audit profession in the country where auditors operating their work (Appendix A gives a brief introduction to Saudi Arabia and its economy).

The Saudi auditing profession, in its both practising and regulatory divisions, has recently developed into a contemporary form. Auditing has been practiced in Saudi Arabia for about forty- eight years, since the establishment of the first audit firm in 1955 (Jadallah, 1972). The auditing profession in Saudi Arabia was recognised legally in 1965 by the Companies Act, which required companies to appoint auditors.

The background to the Saudi auditing profession given in this chapter will be organised in the following manner - four sections and conclusion will be

included. The first section is concerned with highlighting features of the Saudi auditing profession in its early stages of development prior issue of the Statutory Accountant Act in 1973. The second section is an explanation of the major efforts and progressive steps for such a development, leading to the third section where the current status of the profession becomes the principal focus (see Al-Motairy, 1999 for more details about the emergence of auditing in Saudi Arabia). These first three sections provide a description and, to some extent, analysis for the historical development and current status of the Saudi auditing profession. What then follows is a fourth section which describes the characteristics of audit firms and their clients, as well as delivering a brief assessment of the Saudi auditing market.

2-2 The Audit Profession in its Early Stage:

This section reviews the emergence of the Saudi auditing profession (1955 to 1974) and highlights attempts to regulate it in Saudi Arabia. The section is structured as follows: firstly, the appearance of professional auditing in Saudi Arabia is affirmed and reviewed; secondly, the 1965 Companies Regulation is presented; and thirdly, the emergence of the 1968 ministerial decision is described. Finally, the emergence of the first Public Accountants Regulation is presented.

Public accounting licensing activities started in Saudi Arabia in 1955, when the Ministry of Finance and National Economy issued CPA licences to the partners of Nawar, Saba and Co., the first recorded audit firm (Jadallah, 1972, p. 26). In 1957 licensing authority was transferred to the Ministry of

Commerce. By that date, a total of seven audit firms had already been licensed, four of which were Egyptian, two Lebanese and one local (Shinawi and Crum, 1971, p. 107). Up to this period licensing requirements of CPAs had not been clearly defined. Holding a CPA or Chartered Accountant's certificate, a BA in accounting or management, or even being an expert in accounting and auditing practices were the guidelines or criteria upon which licences to practice had been granted (for more details, see: Shinawi and Crum, 1971, p. 108). Ba-Eissa (1984) claimed that the late appearance of audit firms in Saudi Arabia was due to three key factors, namely: the country's short period of existence; its poor economic situation previous to the discovery of oil; and the country's lack of educated and skilled auditors (p. 302).

In the years before the passing of the 1965 Companies Act by the Ministry of Commerce, public corporations were rarely independently overseen. Audits were largely voluntary despite the need to comply with Al-Zakah (almsgiving) and Income Tax regulations, although companies increasingly engaged auditors to attest to their annual financial reports. A large proportion of audit work prior to the issuance of the Companies Act of 1965 was the balance sheet audit attesting to a company's collateral and liquidity to satisfy bankers who supplied most corporate financing, and, at times, for a company's own information record (Al-Rehaily, 1992). The role of audit was perceived as being primarily for the benefit of the management of the company, while shareholders and other interest groups were almost completely neglected.

The 1965 Companies Act provided regulations concerning the required annual financial statements of companies, the role of the external auditor in such statements and the relationship between the company and its external auditor (Articles 123 to 133). These issues are summarised below.

According to the Act, the board of directors of a company is required to prepare three financial statements, viz: balance sheet and profit and loss account at the end of the company's financial year. It was stipulated that these statements must be prepared on a consistent accounting basis and be audited by an external certified auditor. The appointment of an auditor must be made by the shareholders at their annual general meeting.

Being licensed to practice in Saudi Arabia, the selected auditor, according to the Act, must not be a partner, an employee, nor a relative to the fourth degree of any of the founders or directors of the company he audits. This guideline, however, does not strictly forbid the external auditor from providing management and consulting services to his audit client. Shinawi and Crum (1971), in this respect, state that: "Article 130 on independence is not strictly enforced, it could be interpreted to prevent the auditor from rendering management services to the company he audits. It was not believed that this had happened up to this time" (Shinawi and Crum, 1971, p. 105).

The appointed external auditor, according to the Act, is entitled to gain access to the balance sheet and profit and loss account of the company being audited at least 55 days before the shareholders' annual general meeting, as well as obtain any document or clarification he requires, at any time, from the board

of directors or shareholders during his auditing task. Any hindrance or difficulty the auditor encounters in gaining such access should, according to the Act, be reported to the company's board of directors.

Regarding the responsibilities of the auditor, according to the Act, he is held responsible for any damage to the company he has access to during his assignment, its shareholders or third party resulting from error, negligence or unauthorised disclosure of information. Furthermore, both the auditor and any member of the company he audits are subject to penalties and fines in the case of entering false information or concealing important material in financial statements (this could entail an imprisonment for a period of between three months and one year and/or a fine ranging from SR5,000 to SR20,000). Also managers or directors of the company under audit are subject to a fine (SR1,000 to SR5,000) if they attempt to impede the work of their external auditor.

In addition, the 1965 Companies Act has broadened the role of the auditor to include verifying and signing the subscription prospectus of any capital increase, the statement of shares issued to cover debts, and the report on capital reduction or changes in the method used to prepare the financial statements and in estimating assets and liabilities.

Finally, the auditor's report, according to the Act, should include his opinion on the financial statements of the company he has audited, stating in particular the extent to which such statements were prepared consistently using a set of accounting principles, their compliance with the companies'

rules and regulations in Saudi Arabia, and the extent to which they present fairly the company's financial position. The Act also requires the auditor to state in his report whether he was able to gain access to all the information and explanations he required during his auditing task. The auditor's report, as well as the inventory, balance sheet and profit and loss accounts of the company he has audited should, according to the Act, be published in a daily newspaper and distributed within the company's headquarters at least 15 days before the annual general meeting of the company.

In spite of the gradual increase in the number of audit firms, no attempt had been made, up to this stage of development, to develop accounting and auditing standards, codes of ethics nor to define the scope, function and objectives of accounting and auditing practices. None of these fundamentals principles were broached by the Companies Act of 1965. Neither did it lay down any guidelines on how these principles could be addressed in the future. The Act instead contains regulations that seem to be: "designed to achieve a legal objective, such as governing a specific relationship or implementing a public policy issue, rather than fulfilling a financial reporting objective" (Moustafa, 1985, p. 204).

The establishment of a professional body to organise and regulate the auditing profession had not yet been deemed necessary, at least not from the point of view of the Ministry of Commerce. As a result, most audit firms in this period have relied on international or other countries' professional standards and ethical codes of professional conduct (e.g. the USA, the UK and Egypt) (Ba-Eissa, 1984). On the other hand, management of companies

could choose from a variety of alternative practices and valuation methods, including costing, profit distribution, depreciation, and other matters without disclosure and could count on the support of their external auditors.

In the meantime, the number of firms licensed to practice as public accountants and auditors in Saudi Arabia gradually increased, from 20 firms in 1968 to a total of 51 firms by 1970 (Jadallah, 1972, p. 26-7). Among these were only 13 local firms run with the aid of foreign employees, mainly Egyptians, while the rest were international audit firms, originating mainly in Egypt, the Lebanon, Sudan, the UK and the USA. This diversity of origins, in turn, allowed or even encouraged a culture of diversity in accounting and auditing standards and in particular audit report wordings, which were often in worldwide usage among these firms.

In 1968 the Ministry of Commerce, aiming to improve the accounting and auditing profession in line with the economic growth the country was witnessing during the late 1960s and beginning of the 1970s, issued a proposal for the first Certified Public Accountants' Law (Ba-Eissa, 1984). The proposal was enacted in 1974 after being submitted to the Council of Ministers in 1969.

The 1974 CPA Law entailed the creation of the Higher Committee of Chartered Accountants, a body set up and supervised by the Ministry of Commerce to control the process of licensing certified accountants and auditors in line with the rules and regulations included in the CPA Law of 1974. This same Law, as well as reasserting the auditing related issues of the

1965 Companies Act, provided the general conditions and requirements for applications of certified public accountants' licences in Saudi Arabia. These included: the applicant's age (must be 21 years of age or over); nationality (must be a Saudi or foreigner licensed to practice in his native country); place of residence (must be resident in Saudi Arabia); registration categories and fees (SR300 for public accountants and SR500 for chartered accountants); qualifications (must hold a PhD or an MA in accounting with one year of training at a licensed audit firm, public or private sector organisation; or hold a BA in accounting or management with a Diploma in accounting or taxation, with three years training at a licensed audit firm or five years experience in a public or private sector organisation; or hold a BA in management with four years training in a licensed audit firm); personality (must be of respectable moral character); and experience (must not undertake audits for publicly owned enterprises before three years of being licensed). Thus, the eligibility of a potential auditor became clearer, although the Law lacked any practical guideline (e.g. written examination) upon which the practical competence of applicants could be assessed.

The organisation of the accounting and auditing profession in Saudi Arabia faced two substantial difficulties in the early stage of its historical development, difficulties which had far reaching implications for the way the profession panned out as it reached the beginning of the twenty first century. Firstly, the lack of an adequate accounting education system and training programme could only come to one thing: it was bound to lead to a shortage of qualified Saudi national accountants and auditors (Abdeen and Yavas, 1985). Secondly, the absence of an authorised professional organisation to

organise and regulate accounting and auditing practices (Shinawi and Crum, 1971) has led to a lack of a set of mandatory accounting and auditing principles, standards and codes of ethics. The ability to compare, judge or monitor professional conduct has thereby been impeded.

2-3 The Audit Profession Prior to Emergence of SOCPA:

Several voluntary attempts were made by various interest groups in the face of the dilemma discussed above, including audit firms, the Higher Committee of Chartered Accountants and the General Auditing Bureau. These were reflected in proposals soliciting the development of the auditing profession of Saudi Arabia submitted to the Ministry of Commerce during the second half of the 1970s. Supplementary, but separate efforts were being made elsewhere by academics, particularly members of the accounting department at the King Saud University in Riyadh. Considerable efforts were being made with the same aim in mind, and a certain achievement was heralded with the establishment of the Saudi Accounting Association (SAA) in 1981, an academic organisation under the auspices of the King Saud University (Al-Rehaily, 1992; Al-Motairy, 1999).

Before considering the current status of the Saudi auditing profession, it is worthwhile considering the project for 'the development of the accounting and auditing profession in Saudi Arabia', which the Ministry of Commerce launched at the beginning of the 1980s. This project resulted from increasing

calls by academics, professionals and private and public sector representatives for the need to develop accounting and auditing practices in line with the economic growth (Shinawi and Crum, 1971; Jadallah, 1972; Al-Kurdi, 1981; Hijazi, 1981; Al-Rashid, 1983). The demands stemmed from the substantial pressures which arose from the need to further control the growing number and size (the introduction of the big international audit firms, including Arthur Andersen, Price Waterhouse and Whinney Murray (Ernest and Young)) of audit firms and were also clearly motivated by a desire to as well as harmonies accounting and auditing practices.

In 1979 a proposal containing a research project prepared by Al-Rashid and Co. Certified Accountants and Auditors, a leading local audit firm, was submitted to the Ministry of Commerce for approval and financial support. The overall aim of the project was to develop a framework for organising and regulating the Saudi accounting and auditing profession that bore a greater relevance to the socio-economic and political environment of Saudi Arabia. The Ministry agreed to finance the project.

Three executive teams, each of which included local and international academics and experts, were set up to deal with the three distinct components of this project (see Aba-Alkhail, 2001, for more details). The first was concerned with issues relating to the internal organisation of the profession (licensing, training, monitoring, and issuing professional standards and codes of ethics). The second was concerned with developing a set of auditing standards, focusing on major issues relating to auditing procedures, such as the standard of the audit report. The third team was

concerned with selected issues of financial accounting, mainly defining the concepts and objectives of financial accounting in Saudi Arabia and the development of standards of presentation and general disclosure.

Two volumes entitled 'Objectives and Concepts of Accounting and Standard of General Presentation and Disclosure' (the Ministry of Commerce, 1985a) and 'Auditing Standards' (the Ministry of Commerce, 1985b) were approved by the Ministry of Commerce and became effective from November 1985, but only to be used as a formal guideline (Ministerial Decision No. 692). Other issues addressed in the original final draft of the Al-Rashid firm, particularly concerning the professional organisation, codes of professional ethics and monitoring rules were postponed. Importantly, this indicated that the accountancy profession in Saudi Arabia, up to this stage of development, was entirely in the hands of the government.

By the mid 1990s, the two volumes indicated above (the Ministry of Commerce, 1985a, 1985b) became mandatory and thus auditors were required to comply with the accounting and auditing guidelines introduced in 1985 by the Ministry of Commerce (Ministerial Decision No. 852). The first volume 'Objectives and Concepts of Accounting and Standard of General Presentation and Disclosure' which dealt with three issues. The first issue was financial accounting and objectives (Paragraphs 51-82), focusing on the significance of financial statements of profit-oriented enterprises to external decision making processes of various parties (e.g. investors, suppliers and creditors), clarifying the nature, objectives, and limits of the information which accounting financial statements provide, and increasing users'

awareness of the objectives of financial accounting and reporting. The second issue highlights the financial accounting concepts (Paragraphs 233-336). The focus here is on defining the fundamental elements of financial statements of profit-oriented enterprises and their required accounting treatments. The third, and final, major issue of the first volume presents the standard of general presentation and disclosure (Paragraphs 578-775). It is organised into four subsections to deal in turn with the following issues. First, general presentation of financial statements. Second, general disclosure of financial statements. The third and fourth subsections outline the general presentation and disclosure requirements for consolidated financial statements and for enterprises under formation. These however, the three issues, namely financial accounting and objectives, financial accounting concepts, and the standard of general presentation and disclosure, are very similar to the accounting principles issued by the American FASB (Naser and Nuseibeh, 2003).

The second volume (Auditing Standards, the Ministry of Commerce, 1985b) presents seven auditing standards as follows (see Aba- AlKhail, 2001 for more details about setting these standards). The first, the Standard of Sufficient Professional Competence (Paragraph 503), requires certified auditors to assess their own professional competence before undertaking auditing tasks as well as those competencies acquired by each individual of their teams in order to ensure that they are able to perform properly. The second, the Standard of Neutrality, Objectivity and Independence (Paragraph 1004), requires certified auditors, as well as those involved in their team, to be fully independent, objective and neutral when performing auditing tasks,

otherwise auditors must not give their professional opinions. The third, the Standard of Proper Professional Care (Paragraph 1503), requires auditors to put in proper efforts at all stages of their auditing assignments, to seek help from others if necessary and to implement accepted auditing standards, being aware of all circumstances, financial affairs, plans and the consequences of the usage of their final reports on the financial statements of their clients. The fourth, the Standard of Planning (Paragraphs 2009-2012), explains the issues that auditors should consider and observe while planning their auditing assignments (e.g. required auditing procedure, number of assistants, timing, extent of the auditing tasks, nature of clients and auditing regulations). The fifth, the Standard of Control and Documentation (Paragraphs 2518-2528), explains auditors' supervisory roles on their teams (e.g. organisation of the work among assistants, making each member of the team aware of the objectives and duties of the work being performed, comparing what has been done with the auditing plans and co-operating with other auditors involved with the same client) and, at the same time, they must maintain the required quality and style of the documentation of auditing processes (e.g. assessment of the client's internal control system and auditing plan and procedure). The sixth, the Standard of Auditing Contexts and Evidence (Paragraphs 3024-3044), explains the extent to which auditors are required to search for evidence in support of their final opinions on the financial statements of enterprises. It also highlights some important questions that have to be answered before such opinions are given (e.g. are all of the assets owned by the enterprise recorded on the balance sheet? Are the methods used to measure and disclose profits and losses in accordance with the companies' regulations and with generally accepted accounting

standards?). The seventh, and final auditing standard, the Standard of Reporting (Paragraphs 3539-3563), explains the characteristics of an audit report focusing mainly on its style, language and content. To provide a brief outline, the report should be introduced by stating the name of the party to which the report is addressed; followed by an explanation of the extent of the auditor's work and the financial statements covered. References to the accounting and auditing standards followed and the extent to which the auditor is confident of his work and opinion. Next come the auditor's opinion, this must state whether the financial statements as a whole were presented fairly, and whether such statements were prepared in accordance with the generally accepted accounting principles and standards, with the companies' regulations and with the internal policy of the enterprise. Finally, the audit report concludes by giving the auditor's name, certificate number, signature and date. Further, many issues regarding an audit report were not discussed, such as the responsibilities and procedures required in the case where an auditor, after having his report published, comes across new information causing him to realise that his opinion had been misleading. **Figure 2.1** shows the wording of this report.

Figure 2.1
The Wording of the Saudi Audit Report

Auditors' Report to the Annual General Meeting of Members of X company

Scope of audit:

We have audited the statements of financial position of X Company Limited as at xx and the related statements of income, retained earnings and source and applications of funds for the year ended. The financial statements are set out on page x to x. In accordance with article 123 of the Company Law, the overall responsibility for the preparation of the financial statements is that of the Company's management. We have obtained all information and explanations, which we considered necessary for our audit. We conducted our audits in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinion.

Unqualified opinion:

In our opinion, such financial statements taken as a whole:

- 1) Present fairly, in all material respects, the financial position of the Company as at xx and the results of its operations and its cash flows for the year then ended in conformity with generally accepted accounting principles; and,
- 2) Comply with the requirements of the Regulations for the Companies and the Company's Articles of Association with respect to preparation and presentation of financial statements.

Signature

License Number.....

Date.....

Source: the Ministry of Commerce, 1985b

To summarise, up to this stage of development the auditing profession in Saudi Arabia had been regulated by laws and acts, including the 1965 Companies Act and the 1974 Certified Public Accountants' Law, as well as the 1985 Accounting and Auditing Standards issued by the Ministry of

Commerce. In spite of the remarkable effort by the latter to reflect the Ministry of Commerce's project for the development of the Saudi auditing profession, the accounting and auditing standards issued remained incomplete since they were far from covering many of the most important issues (Al-Rehily, 1992).

The Saudi Organisation for Certified Public Accountants (SOCPA), a professional organisation for organising and regulating the auditing profession, was given permission by Royal Decree No. M/12 in November 1991 to come into existence (Al-Motairy, 1999). The establishment and subsequent recognition of SOCPA reflects a remarkable chain of event in the history of Saudi Arabia, since it became the first authorised quasi-independent professional institution in the country (Al-Motairy, 1999).

Importantly, during the same period audit firms were dominated by foreign professionals. There were neither clear mandatory structural and practical frameworks nor adequate control systems for these firms. Although the number and size of firms was growing gradually, the amount of contributions made by qualified Saudi national professionals remained small. Variation and, thereby, incompatibility in professional practices continued. At the same time financial statements of public sector organisations became more important tools for decision-making processes for various users.

These conditions emphasised the compelling need to reform the existing structure and components of the Saudi accounting and auditing profession. Coupled with the government policy of placing more responsibility in the

private sector came increased calls from academics, Saudi national professionals and members of the SAA to establish a professional body capable of organising and regulating accounting and auditing practices in the country.

The SAA, therefore, continued to play the significant role in the development of the profession, which it had started at the beginning of the 1980s. This function expanded during the second part of the 1980s to include the formation of various advisory committees to deal with four key accounting related issues (accounting standards, education and training, professional ethical codes and accountancy regulatory systems). Each committee consisted of members representing certified public accountants, academics and businessmen. These active bodies made several concerted attempts to establish accounting and auditing standards and professional ethical codes at the beginning of 1990. The role played by the SAA, especially during the late 1980s and at the beginning of the 1990s, has undoubtedly facilitated the emergence of the 1991 CPA Law and consequently the establishment of SOCPA. Even since the establishment of SOCPA, the SAA has continued to contribute towards the enhancement of accounting and auditing theory and practice in Saudi Arabia, through the organisation of academic conferences, providing training programmes and publishing academic textbooks and research (see Al-Motairy, 1999 for more details about the SAA activities and relation with SOCPA).

2-4 The Current Stage (1991 onward):

The auditing profession in Saudi Arabia has developed into its current form since the passage of the current CPA Law in November 1991 (Royal Decree No. M/12, 1991). This section describes the regulations included in the Law and also explores the Law's features and consequences.

The new 1991 CPA Law (Articles 1-38) and its Executive Calendar (Articles 1-15) (SOCPA, 1994a) deal with five major issues as follows. First, attention was turned to the establishment of the Saudi Organisation for Certified Public Accountants (SOCPA), a body supervised by the Ministry of Commerce and set-up to organise, regulate, monitor and develop the accountancy profession in Saudi Arabia (Articles 19-27). According to the Law, SOCPA is responsible for the following:

- Reviewing, developing and issuing accounting and auditing standards.
- Setting and organising professional fellowship examinations, which should include theoretical topics and practical skills as well as related regulations.
- Organising continuous training programmes.
- Undertaking research on accounting and auditing related issues.
- Publishing journals, books and bulletins on accounting and auditing related issues.
- Monitoring professional compliance with the Certified Accountants' Law and the issued accounting and auditing standards.
- Participating in local and international accounting and auditing conferences (SOCPA, 1994a, CPA Law 1991, Article 19, pp. 6-7).

The Law goes as far as to detail SOCPA's management structure and sets out the functions of a Board of Directors authorised to take decisions regarding SOCPA's responsibilities and objectives. An appointed SOCPA Secretary General and a deputy also have their responsibilities, rights and duties determined for them. The Board is chaired by the Minister of Commerce, with two voting voices, and includes 12 members, each with one voting voice, including the Deputy Minister of Commerce, the Deputy Minister of Finance and National Economy, the Vice President of the General Auditing Bureau, two academics, one representative of the Council of Chambers of Commerce and six Saudi certified public accountants elected for a period of three years at SOCPA's annual general meeting. Meetings of SOCPA's Board of Directors, according to the Law, shall be attended by the majority of members, including the Board's Chairman, and held on a regular basis, at least once every 90 days. Further, in terms of the organisation's funding, the Law indicated four resources, including: membership fees; government subsidies; gifts, donations and legacies accepted by the Board of Directors; and returns on the investment of SOCPA's funds and proceeds of the income from SOCPA's publications and services.

The second issue addressed by the 1991 CPA Law concerns the conditions of registration and registration procedure of certified public accountants (Articles 1-5). According to the Law, no person shall practice as a public accountant unless he is registered on the ad hoc registration list of public accountants at the Ministry of Commerce. Applicants to the list must be Saudi nationals, fully competent and of a good behaviour. An applicant must also hold a BA degree in accounting or its equivalent with three years full-

time training with an audit firm or a private or public sector organisation. This is reduced to two years if an applicant holds an MA and one year for a PhD in accounting or its equivalent. Finally, an applicant to the register must also be a fellowship member of SOCPA (having passed SOCPA's fellowship examination or, for those licensed before issuance of the Law, having subsequently attended SOCPA's compulsory seminars). Registration applications should thus include all documents for the above requirements as well as the registration fee (SR1,000). More details of the documents required for registration are provided in the Executive Calendar of the CPA Law of 1991 (e.g. conditions of the training period and SOCPA's fellowship certificate).

Applications, according to the Law, are submitted to a specialist committee, consisting of three members (chaired by an employee of the Ministry of Commerce, a Saudi legal consultant appointed by the Minister of Commerce and a Saudi certified public accountant nominated by SOCPA's Board of Directors for a period of not less than five years). This committee is authorised to accept or reject applications within 30 days of submission. Certifications to practice for five years as public accountants are provided to those accepted, after being numbered, dated and signed by the chairman of the committee. The information included on the ad hoc registration list is explained in more detail in the Executive Calendar of the 1991 Law (e.g. it includes names of individuals, or names of partners of firms, and dates and numbers of certificates).

The third issue addressed by the Law is certified public accountants' obligations (Articles 6-18). According to the Law, certified public accountants must be free physically to practice auditing and other professional practices; must give SOCPA all information required about themselves and their professional firms (e.g. they must regularly update information about their addresses, phone numbers, mailing addresses, number of branches, number of staff and expansions, and also, in the case of quitting, information must be supplied within 30 days); must sign audit reports for the auditing assignments carried out by their firms, in which they were physically involved or engaged in a supervisory capacity as partners (indicating the numbers and dates of their certificates); must place their certificates in obvious places at their professional firms, which should be titled with their names; must comply with SOCPA's accounting and auditing standards and ethical codes of professional conduct as well as attend SOCPA's compulsory seminars; must keep a record of their professional engagements (e.g. copies of their audit reports and audited financial statements) for a period of at least 10 years; must avoid auditing assignments for enterprises they have an interest in whether directly or indirectly and assignments for banks or publicly owned enterprises before five years of being licensed; must employ the required number of Saudi nationals in their professional firms; and, finally, certified public accountants are subject to penalties and compensations for any error or negligence they commit during the course of their professional work both for their clients or third parties.

Public accountants' obligations have been clarified further in the Executive Calendar of the 1991 CPA Law. For example, in terms of the nature of their

work, they are permitted to provide audits and management and financial consultations. They can also buy properties and shares or own any type of business organisation, apart from their professional firms, on condition that they do not engage in the management of such organisations and inform their clients, SOCPA and the Ministry of Commerce of such business activities. In terms of the limits of auditing practices, a certified public accountant must not carry out an audit for enterprises in which he is a partner, shareholder, member of the board of directors, relative to the fourth degree or partner of any of their founders or directors, nor enterprises that are similar in nature to those in which the auditor is a member of the board of directors. In terms of the required number of Saudi national employees, the Executive Calendar of the Law requires every audit firm to employ Saudi nationals to at least 20% of its employment capacity. Also, all registered public accountants, individuals or firms must provide SOCPA with all information it requires at any point in time, as well as on a regular basis, including names of their clients (and their number) and copies of financial statements audited by them.

The fourth issue addressed by the 1991 CPA Law is the type of penalties which certified public accountants are subject to if they do not comply with the regulations included in Law. For this, the Law entailed a committee of three members (chaired by the Deputy Minister of Commerce, and including a Saudi legal consultant and a member of SOCPA's Board of Directors) to be formed by the Minister of Commerce to investigate and question cases of disorder. The committee is authorised to penalise certified public accountants who do not comply with the regulations included in the 1991 CPA Law. The penalties vary according to the nature and degree of the

offence, being either: a caution, warning or temporary withdrawal from the ad hoc registration list for not more than six months; or a lifelong withdrawal from the list with the additional imposed cost of publishing such a decision in at least one local newspaper.

Finally, the Law of 1991 addresses some regulations in respect of several general issues, mostly relating to the consequences of the 1991 Law. Among these are the abandonment of the 1974 CPA Law and its amendments, and the expansion of the authority of the Minister of Commerce in that he can obtain any information he requires on certified professionals. Also, there are matters pertaining to the status of certified public accountants who obtained their licences before the enactment of the Law (licences granted to Saudi nationals are still valid; licences granted to foreigners whether individual or firms are also still valid provided that foreign certified professionals stay in the Kingdom for a period of at least nine months a year and comply with the Saudisation policy through engaging in partnerships with at least one qualified Saudi national as a 25% equity partner).

To summarise, the issuance of the new CPA Law is seen as a culmination of the efforts put into the development of a Saudi conceptual framework by the Ministry of Commerce, professionals and the SAA. Article 19 of the Law entails the establishment of a professional body (the SOCPA) responsible for and authorised to organise, regulate and promote the accountancy profession. Although this body operates under the supervision of the Ministry of Commerce, it signifies a remarkable movement in the nature of the Saudi accountancy regulatory system, from having been entirely governmental in

form to becoming a quasi self-regulatory system, since almost half of the total number of participants in SOCPA's Board of Directors are certified public accountants. The new CPA Law provides not only regulations concerning the internal regulation of the profession, conditions of registration, registration procedure, obligations and penalties of certified public accountants, but also the mechanisms that enable the implementation of such regulations.

By 1992, six technical committees had been formed within SOCPA, following initial meetings of its first Board of Directors (SOCPA, 1995a). Each committee involves representatives of various interests, including professionals, academics, private and public sector personnel and is responsible for the achievement of a specific objective. The first, the Accounting Standards Committee, has as its brief the development of a set of accounting standards. This Committee involves nine members, two of whom are drawn from the ranks of professionals, three academics, two private sector members and two members representing the public sector. The second, the Auditing Standards Committee, is responsible for the development of a set of auditing standards. It involves nine members, two of whom represent professionals, four academics, one private sector member and two members representing the public sector. The third, the Education and Training Committee, is obliged to work toward the development of accounting and auditing education and training programmes. This Committee involves eight members, four of whom represent professionals, two academics, one private sector member and one member representing the public sector. The fourth, the Examination Committee, is responsible for the development of SOCPA's fellowship examination programme. It involves

eight members, three of whom represent professionals, three academics, and two members representing the private sector. The fifth, the Professional Ethics Committee, is responsible for the development of a set of ethical codes of professional conduct, involving eight members, two of whom represent professionals, five academics, and one member representing the public sector. The sixth technical committee, the Quality Review Committee, is responsible for the development of SOCPA's quality review programme for audit firms. It involves eight members, four of whom represent professionals, three academics, and one member representing the private sector. For more details on the nature of work, responsibilities, structure, meetings and members' rights and obligations of the above committees. (see, SOCPA, 2001).

By May 2003, eight auditing standards had been approved by the Auditing Standards Committee of SOCPA that augmented to the seven auditing standards issued by the Ministry of Commerce in 1985. The issued standards had worked their way through all the checks and procedural balances as explained in the Executive Calendar of Accounting and Auditing Standard-Setting Procedure (SOCPA, 2001), and as discussed previously in this section. Importantly, there were no significant variations between the eight standards in their final effective drafts and the form they took in their initial drafts. The parties appointed by SOCPA to undertake projects for these standards ('the consultants') were either professional firms or individual certified public accountants.

The Auditing Standards Committee of SOCPA stated that where there are no Saudi standards issued, International Auditing Standards should be followed.

The following is a list of the fifteen issued Saudi auditing standards:

- Professional qualification.
- Integrity, objectivity and independence.
- Due professional care.
- Planning.
- Control and documentation.
- Evidences of auditing.
- Reporting (audit report).
- Auditing in computer environment.
- Study and assessment of internal control for the purpose of auditing financial statements.
- Special reporting.
- Interim reporting.
- Audit risk and materiality.
- Attestation standards.
- Audit sampling.
- Internal auditing for the purpose of auditing financial statements

The committee decided also to start issuing the following standards:

- Auditor's responsibility to detect and report errors or irregularities.
- Prospective financial reporting.
- Reports on processing information by service organizations.
- Analytical procedures.

- **Clients' representations.**

The committee also issued a number of professional opinions as follows:

- **Including in the auditor's report the phrase "Inventory was valued by management".**
- **That there should be a procedure outlining what the auditor is required to do if the management does not submit the financial statements to him.**
- **Inquiry about audit procedures to be carried out by auditor on auditing consolidated financial statements in case that other auditor has audited subsidiaries.**
- **Audit procedures concerning subsequent events.**
- **Tentative tests before the date of balance sheet.**
- **Communication between the predecessor auditor and the succeeding auditor.**
- **Audit procedures for inventorying.**
- **Actions to be taken by auditor when knowing, after issue of report, of procedure not done by him and that had to be done during the execution of the engagement.**
- **Information in documents attached to financial statements audited by the auditor.**
- **Detection of facts before issue of auditor's report, which became known to him only after issuance of audit report.**

To summarise, the auditing profession in Saudi Arabia, since the issuance of the 1991 CPA Law and the establishment of SOCPA, has witnessed remarkable changes. Fundamental changes have been reflected in the nature of the new regulatory system, moving from a governmental form to becoming closer to a professional self-regulatory form. Following this quite striking transition, basic requirements needed for the enhancement of the profession (e.g. accounting and auditing standards, ethical codes, quality review programmes and licensing rules) have been prepared by six specialised committees formed within SOCPA, and approved and enacted by SOCPA's Board of Directors during a relatively short period of time. In addition, during the same period SOCPA has organised accounting and auditing conferences and training programmes, undertaken and published research on existing accounting and auditing practices (e.g. SOCPA, 1996, 1997) on a regular basis.

In the face of such an extensive series of changes, the audit report standard, which was issued and approved by the Ministry of Commerce in 1985 (with the seven auditing standards) and approved in 1993 by SOCPA's Board of Directors, still remains ostensibly unaltered and can be said to have enjoyed a long period of existence. Understanding the message(s) communicated in this report and evaluating the need to go beyond it are the focus of this research. This focus will be based on the perceptions of members of the auditing profession namely: the auditors, the preparers of the financial statements (the auditees) and the users of these financial statements. Thus, the next section describes the characteristics of the audit profession and audit market in the Saudi Arabian business environment.

2-5 Characteristics of the Audit Market:

As seen earlier, the growth of the auditing profession in terms of audit firms, and the setting of auditing standards has come about largely as result of the increasing demand for auditing services. The following sub-sections describe the characteristics of audit markets in the Saudi business environment in terms of audit firms and auditees .

2-5-1 The Characteristics of Audit Firms

According to the list issued by SOCPA, by 2001 there were 103 audit firms licensed by the Ministry of Commerce and Industry. Since there is no stranded classification of audit firms, the researcher classified these firms as a large or small firm based on their international reputation as well as general perception among users and auditors in the country. The former includes Arthur Andersen¹ (AA), Deloitte Touche Tohmatsu International (Deloitte), PricewaterhouseCoopers (PwC), Whiney Murray (part of Ernst & Young)¹ (WM) and KPMG. The rest are therefore considered as small and local audit firms.

The number of licences and method of licensing have changed over the years, as seen in the previous sections. The number of licensed auditors increased from only three in the year 1957 to seventy as at the end of 1968 (Shinawi and Crum, 1971), and to 103 active firms with 209 partners by the end of 2001. Before the establishment of SOCPA in 1991, licensing requirements were less

¹ In 2002 after the Enron scandal, Arthur Andersen became part of Al-Twaimi and Co (Ernst & Young) in Saudi Arabia.

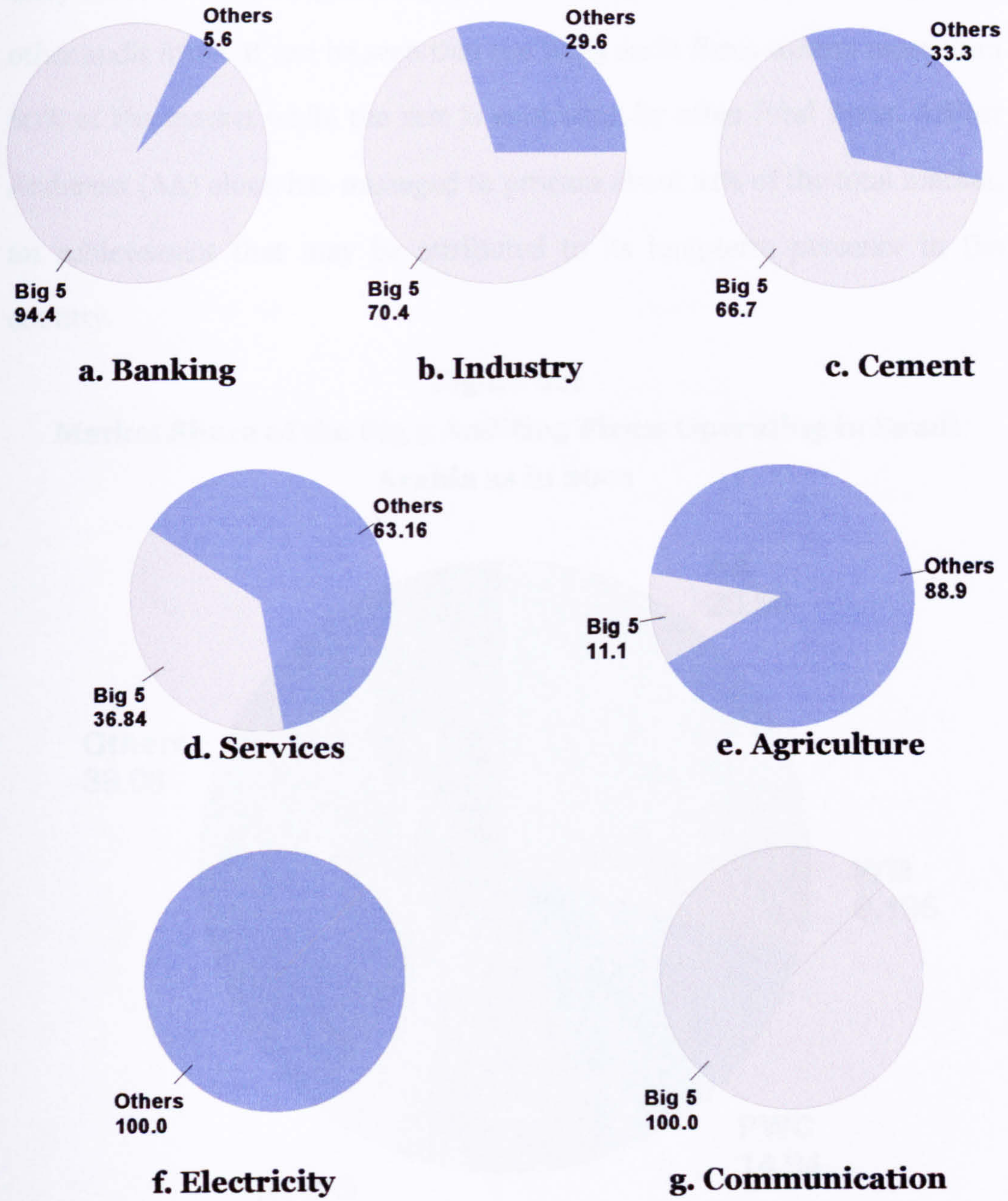
stringent as seen in section 2-2. For example, article six of the CPA Law of 1974 required that the auditor had merely to practice accounting and auditing work for three years on his own before he could be licensed to audit joint stock companies. In other words, a college degree, the passing of a professional exam as test of competence and practical training under more experienced accounting firms were not prerequisites for getting a licence to practice. This lax policy in licensing auditors subsequently lead to a reluctance on the part of leading users in the country such as the Saudi Arabian Monetary Agency (SAMA) to include and/or recommend such firms to audit financial institutions. These doubts have been in some way alleviated with the establishment of SOCPA, which as seen earlier, required auditors to have at least a university degree in accountancy and to sit for professional exams before being granted license to practice auditing in the country.

As can be seen in **Figure 2.2**, the Big 5 audit firms² have come to dominate the communication, banking, industry and cement sectors while the local audit firms are left to exercise their control over the electricity, agriculture and services sectors. It should be noticed here that the Big 5 domination the banking sector is due to choice auditors being imposed on others by parent banks and by the selection of auditors from SAMA's list of recommended audit firms. On the other hand, the electricity sectors have been audited by

² Following Arthur Andersen's disappearance it is now the Big 4.

Figure 2.2

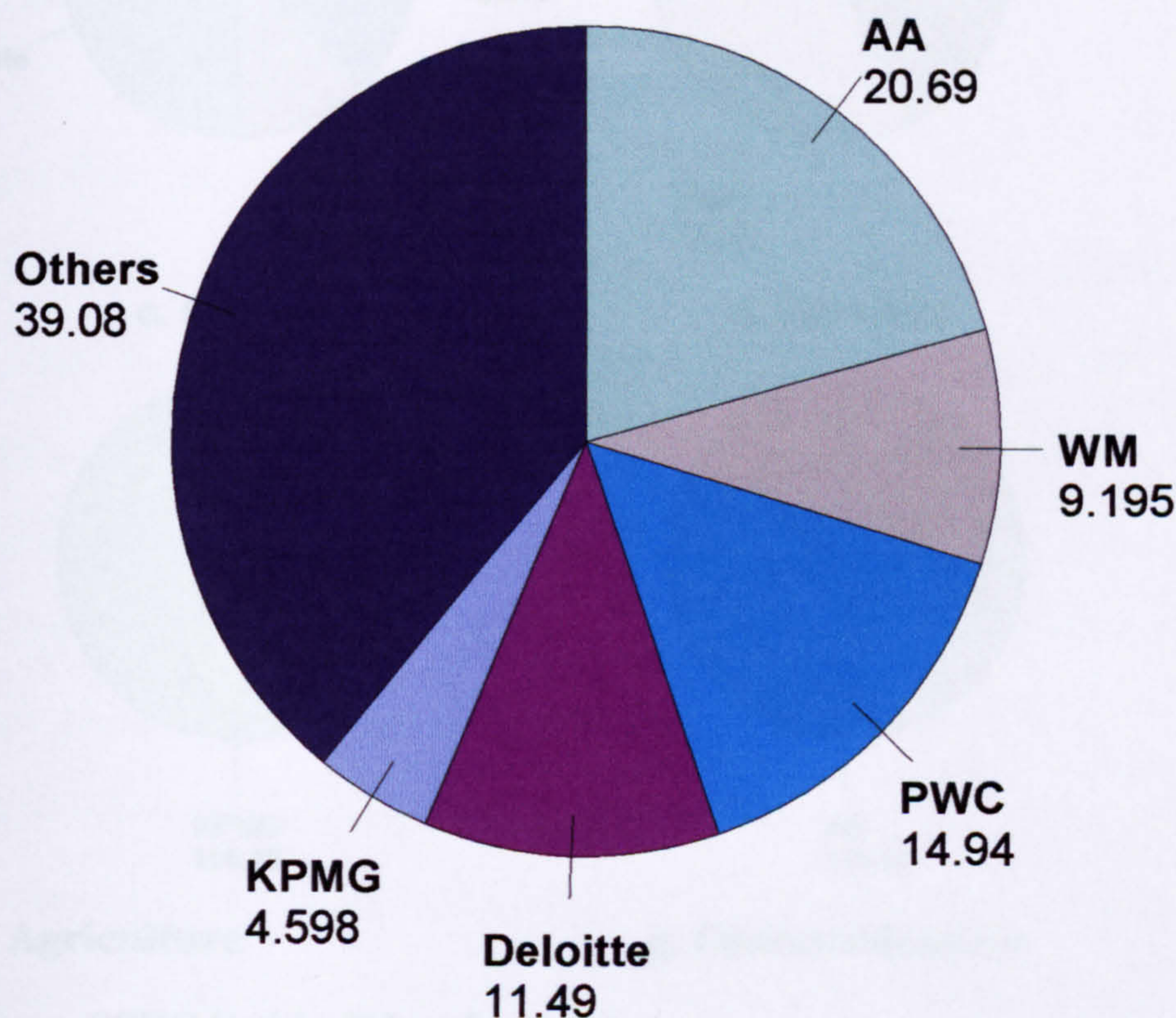
Type of Audit Firms Auditing Listed Companies by Sectors as in 2001



Source: SSRC Guide (March 2002)

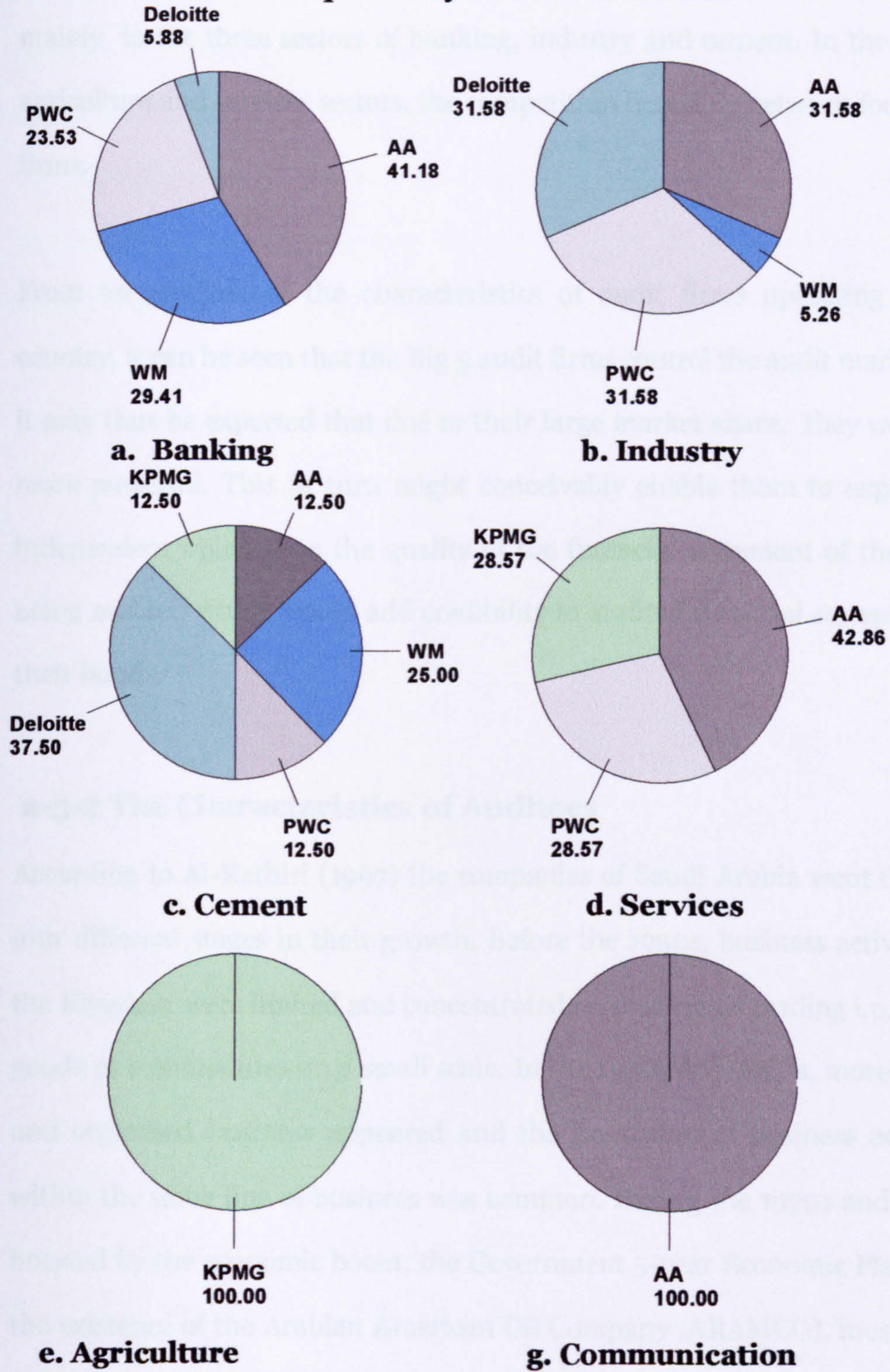
other local audit firms due to the fact that the government has the majority shares in this sector and does not foresee the need to have Big 5 audit firms to audit, as the General Auditing Bureau (GAB) would also have the means to carry out such audits. **Figure 2.3** presents the market share of the Big 5 and other audit firms. It can be seen that the Big 5 audit firms control more than 60% of the market while the rest is controlled by other local firms. Arthur Andersen (AA) alone has managed to procure about 21% of the total market, an achievement that may be attributed to its long-term presence in the country.

Figure 2.3
Market Share of the Big 5 Auditing Firms Operating in Saudi Arabia as in 2001



Source: SSRC Guide (March 2002)

Figure 2.4
Domination of the Big 5 Audit Firms Auditing Saudi Listed Companies by Sectors as in 2001



Source: SSRC Guide (March 2002)

Figure 2.4 shows the domination of various Big 5 audit firms by sector. It can be seen that there exists strong competition among the Big 5 firms mainly in the three sectors of banking, industry and cement. In the case of agriculture and services sectors, the competition is mainly between four audit firms.

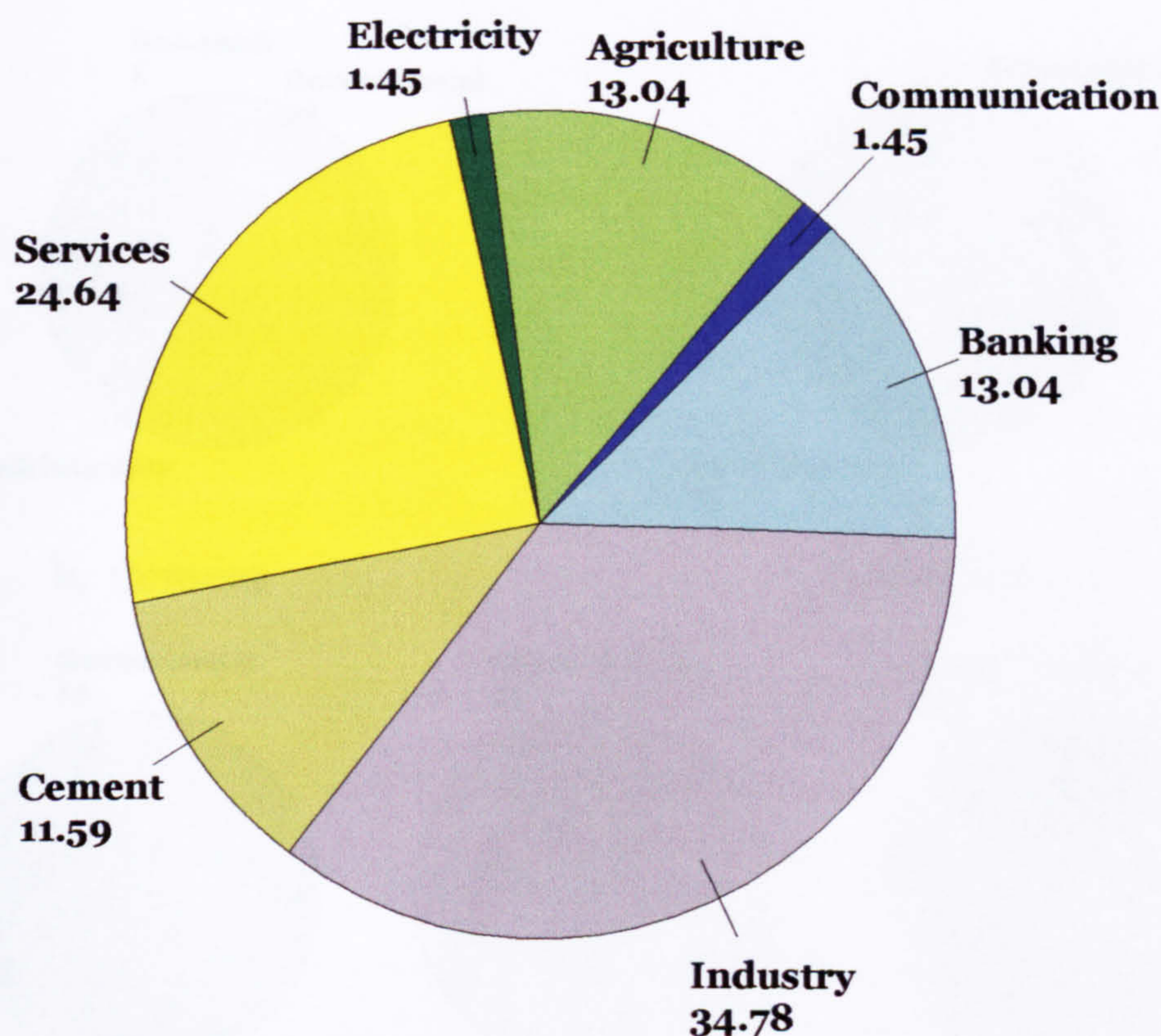
From an analysis of the characteristics of audit firms operating in the country, it can be seen that the Big 5 audit firms control the audit market and it may thus be expected that due to their large market share, they would be more powerful. This in turn might conceivably enable them to express an independent opinion on the quality of the financial statement of the entity being audited which would add credibility to audited financial statements at their hands.

2-5-2 The Characteristics of Auditees

According to Al-Kathiri (1997) the companies of Saudi Arabia went through four different stages in their growth. Before the 1950s, business activities in the Kingdom were limited and concentrated on traditional trading i.e, selling goods or commodities on a small scale. In the 1950s and 1960s, more formal and organised business appeared and the expansion of business activities within the same line of business was common. During the 1970s and 1980s, boosted by the economic boom, the Government 5-year Economic Plans and the existence of the Arabian American Oil Company (ARAMCO), most Saudi companies expanded horizontally from single business into multi-business. The 1990s was a period of concentration and consolidation.

There are 69 listed companies with shares actively traded. These 69 companies fall into one of the seven sectors: banking, industry, cement, services, agriculture electricity and communication. **Figure 2.5** shows that the majority (34.78%) of listed companies are in the industry sector, followed by those of the service sector (24.64%). There were equal numbers (13.04%) of listed companies in the banking and agricultural sectors with the least (1.45%) being the electricity company and the communication company.

Figure 2.5
The Percentage of Listed Companies by Sector

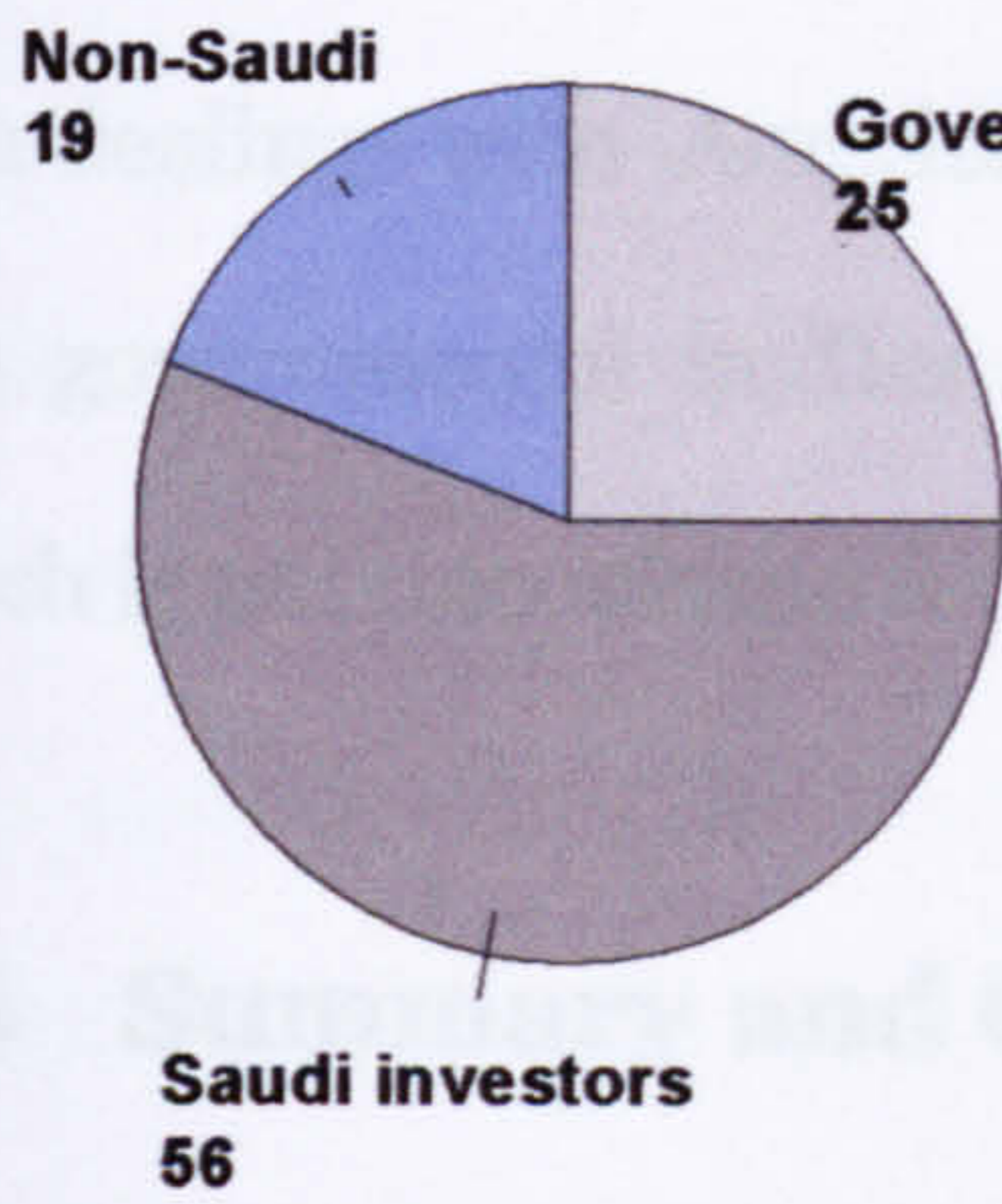


Source: SSRC Guide (March 2002)

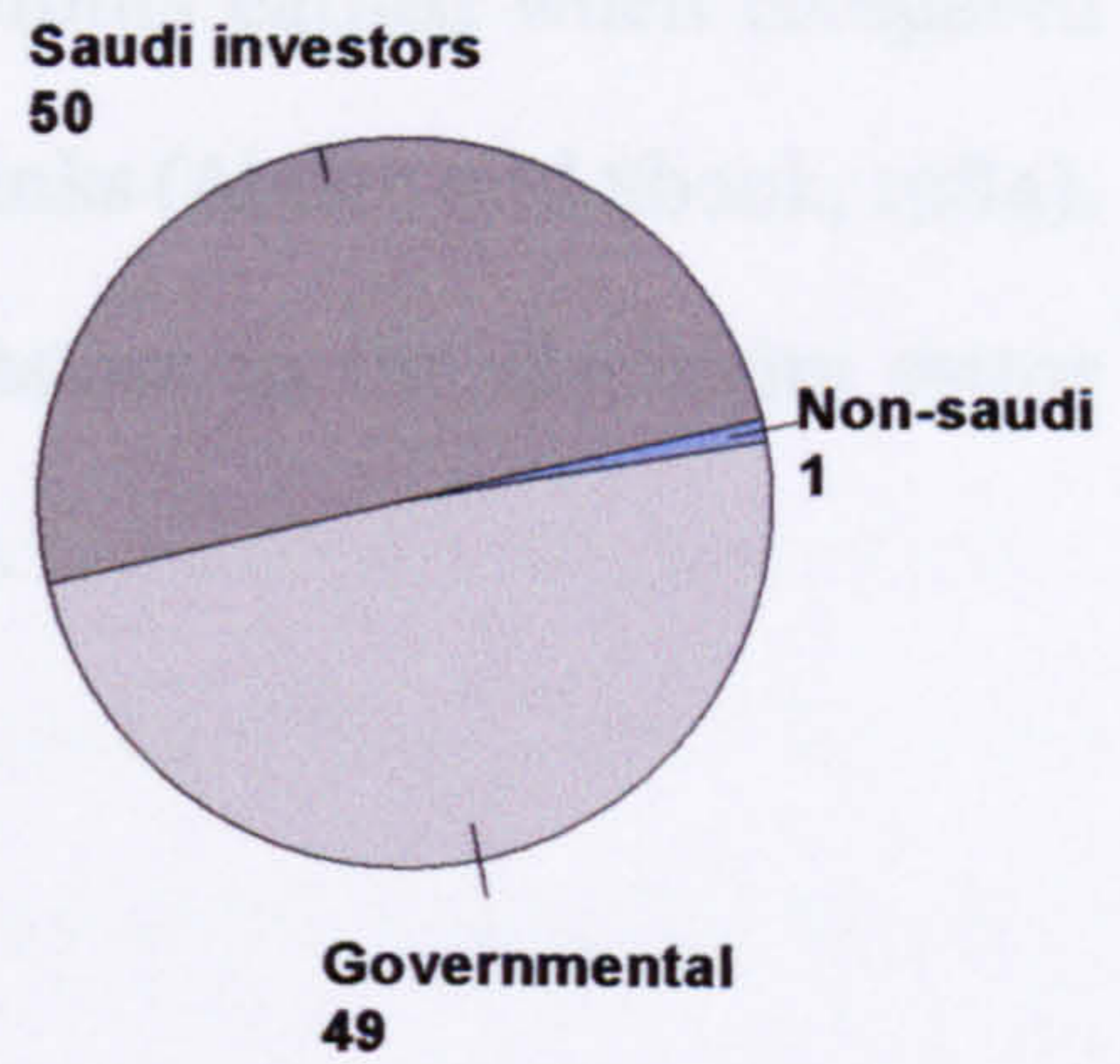
The heavy presence of listed companies in the spheres of industry and services is understandable as it is in keeping with the government's plan encouraging self-sufficiency, import substitution and the tapping of unused resources in the country.

Figure 2.6

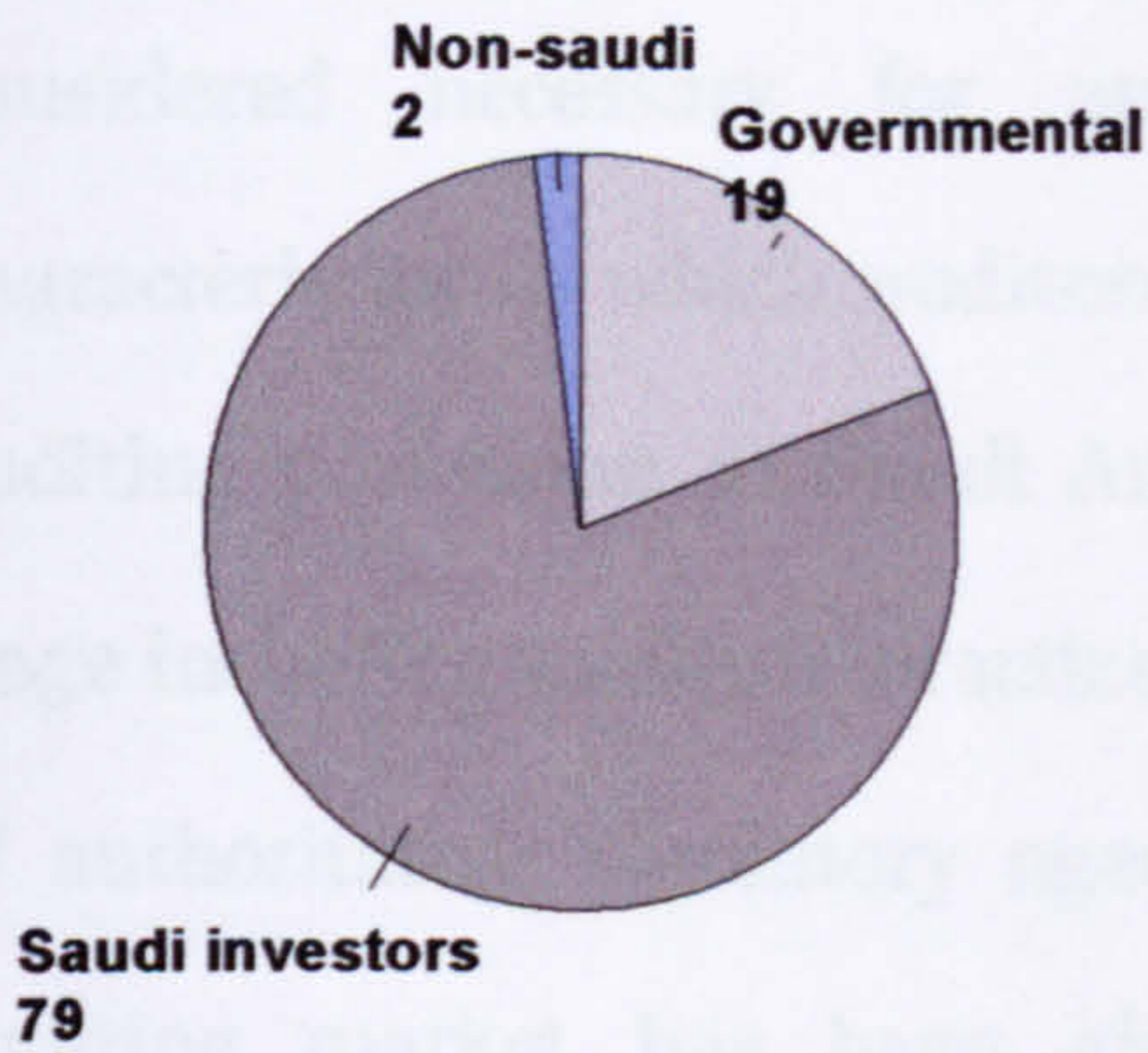
Type of Investors by Sector as in 2001



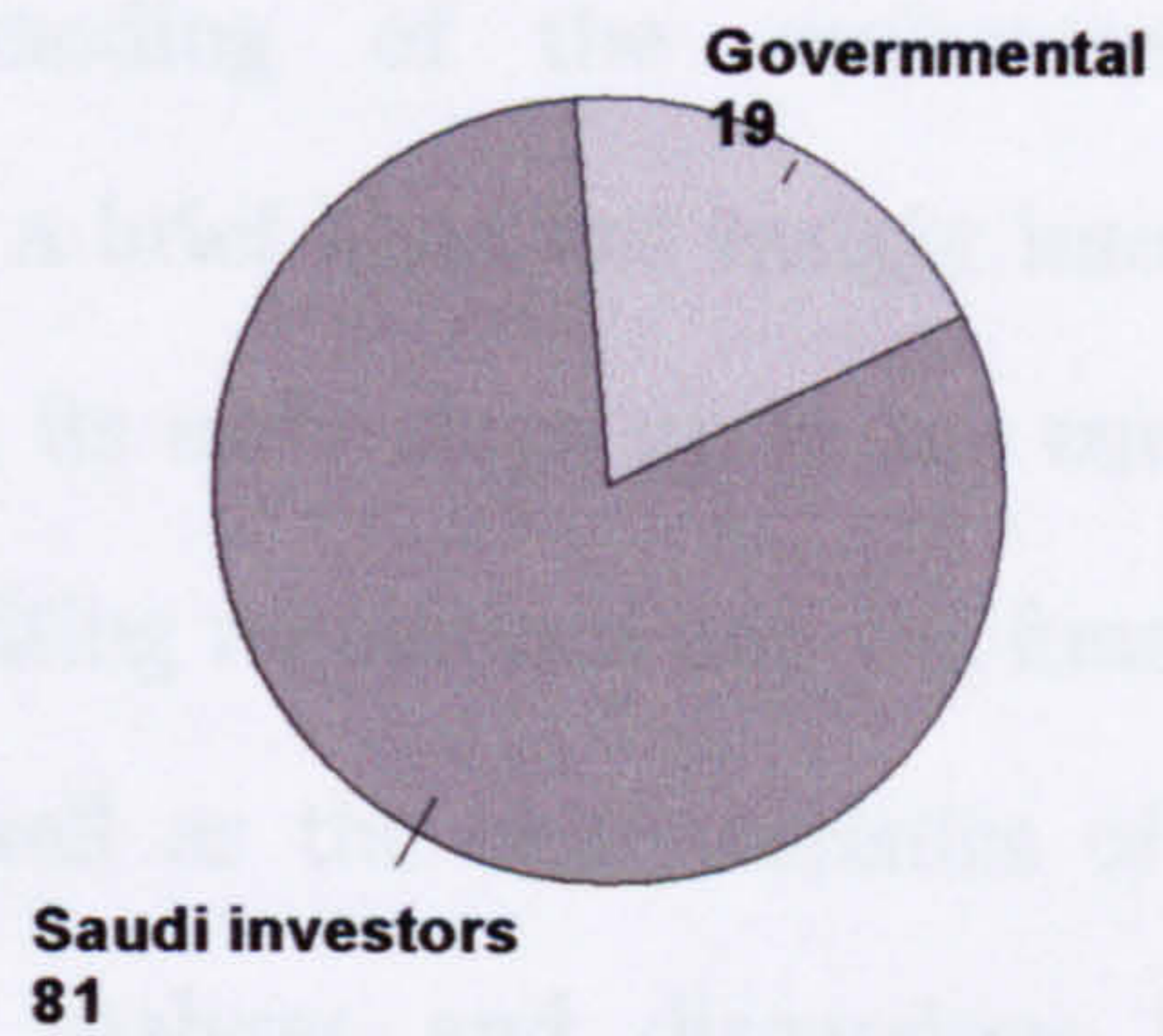
a. Banking



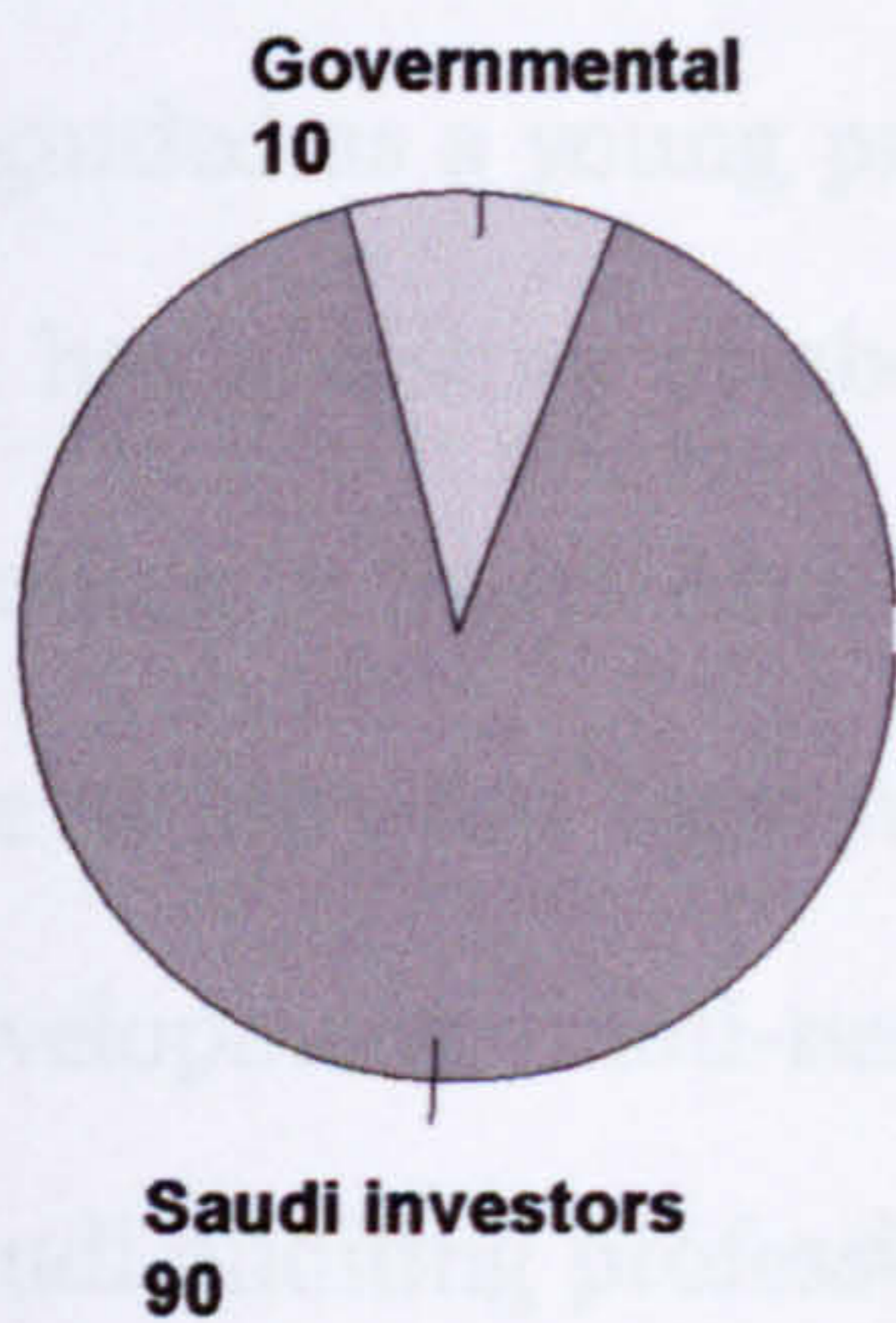
b. Industry



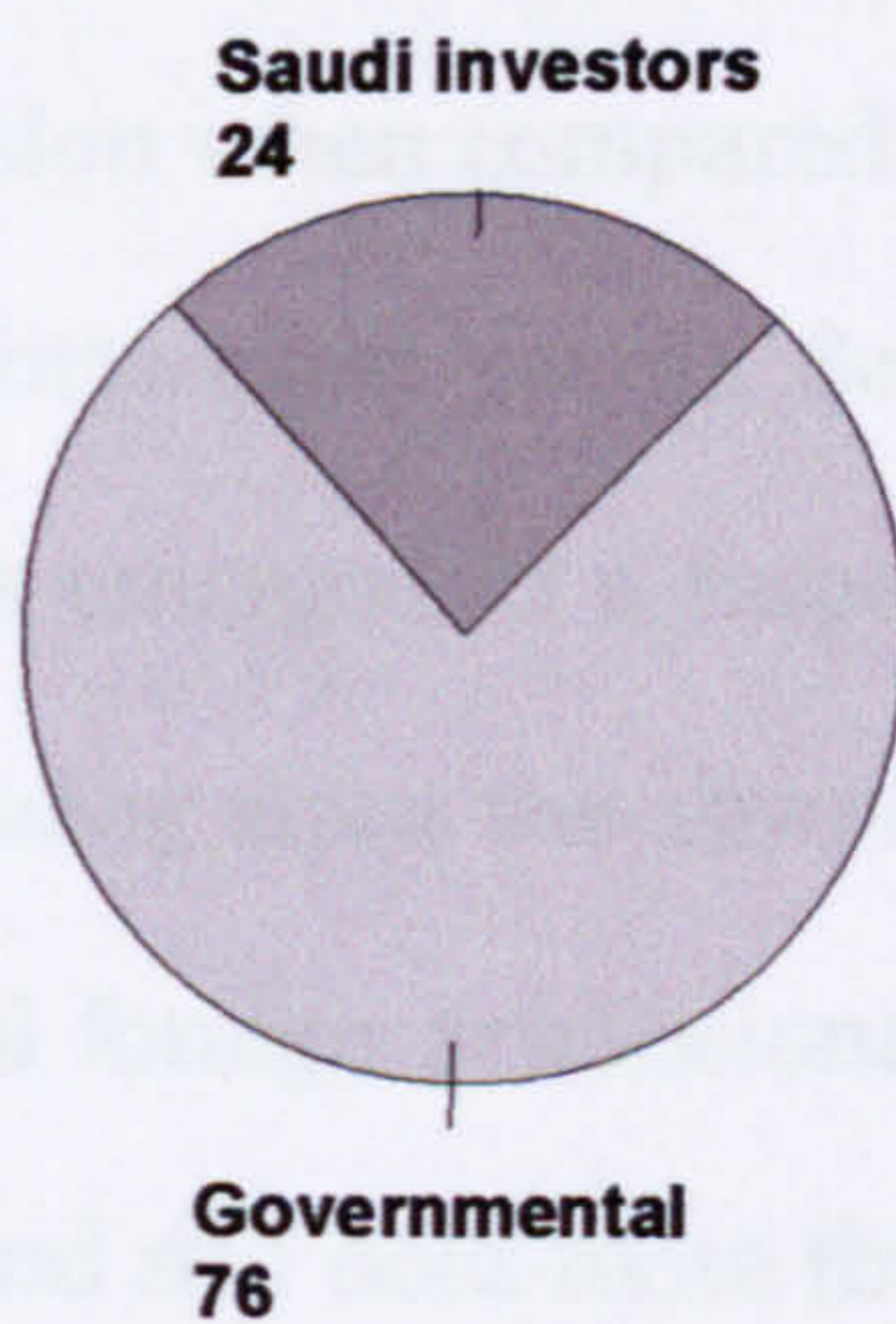
b. Cement



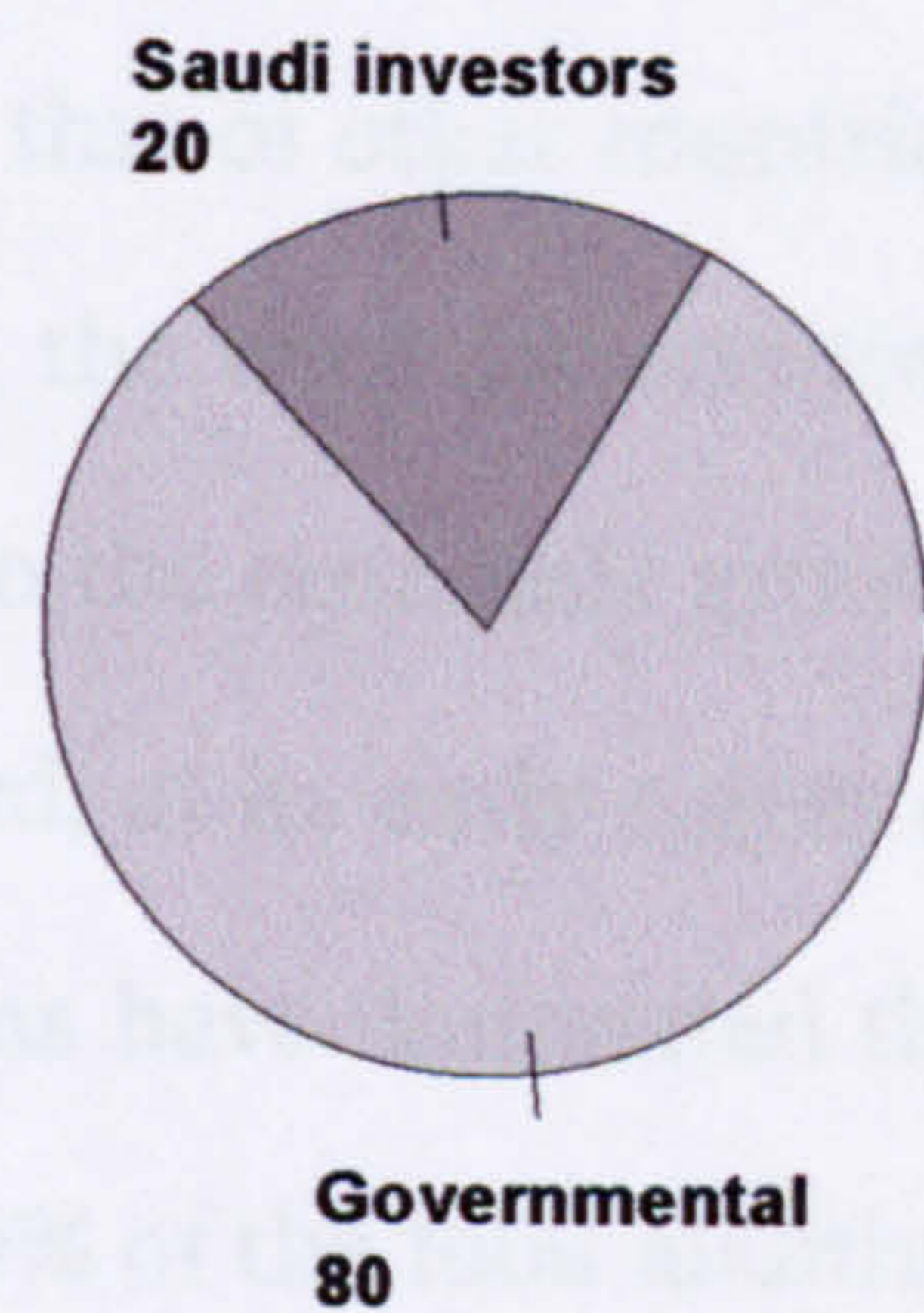
d. Services



e. Agricultural



f. Electricity



g. Communication

Source: Compiled from various sources

Figures 2.6 shows the different types of investors by sector. Foreign investors are largely involved in the banking sectors. This could be due to the low cost of deposits and consequently high profits earned when compared with dealings with American and European banks (Abden and Shook, 1984). The governmental bodies are the major investors in the electricity sector which is not uncommon for utilities companies.

2-6 Summary and Conclusion:

The context of research has been provided in this chapter. This background is considered necessary for an understanding of the environmental characteristics in which auditors operate. A brief historical insight into the auditing profession in Saudi Arabia from its early stage up to the current stage including auditing practices and auditing regulations and the function of authoritative regulatory agencies as well as the characteristics of the auditing market has been given. The analyses and discussions have highlighted a number of points. First, the profession in Saudi Arabia can be regarded as a young profession when compared with that of other countries (it has a history of about forty-eight years). Second, the need for auditing services in Saudi Arabia has emerged as a response to the economic growth the country has been witnessing since the 1970s. Third, at its early stages of development, multi-national foreign professional firms have dominated the Saudi auditing profession and still hold more than 60% of the total auditing market. Thereby, a diversity of employed accounting and auditing standards and procedures and professional ethical codes used worldwide has existed. Fourth, previous to the issuance of the 1991 CPA Law and the establishment

of SOCPA, the profession in Saudi Arabia had been regulated by some laws and acts, including the 1965 Companies Act and the 1974 CPA Law, as well as the 1985 accounting and auditing standards and guidelines issued by the Ministry of Commerce. In spite of the immense effort of the latter, reflecting the Ministry of Commerce's project for the development of the Saudi auditing profession, the issued standards and guidelines remained incomplete since they were far from covering most important issues. Fifth, the establishment of SOCPA is a noteworthy event in the history of the profession in Saudi Arabia, because it makes a fundamental change in the nature of the Saudi auditing profession's regulatory system, shifting control from under the auspices of being government. The supervisory framework of checks and balances now became a great deal closer to being professional and independent in form. Sixth, in relatively short period of time since the latest the reform, basic requirements needed for the promotion and the enhancement of the profession (e.g. auditing standards, ethical codes and licensing rules) have been prepared, approved and enacted by the Ministry of Commerce and SOCPA. Finally, it can be seen that, in the face of the series of auditing changes, the standard audit report form are in pressing need of scrutiny. Having enjoyed a long and fruitful period of existence (about 18 years) it now needs to be examined to ascertain whether there is a need to undertake immediate changes.

Thus, the focus of this thesis as stated earlier is about assessing the quality of the current audit report by addressing the existence of the audit expectation gap between auditors and users of the financial statements and the usefulness

of going beyond the current unqualified audit report currently in use by adding additional matters to be reported by auditors. Evidence of widespread concern that there is a gap between auditors' understanding of their function and the public expectations of the audit process is recognised worldwide. An "audit expectation gap" was defined to exist when there are differences in beliefs between auditors and the public about the duties and responsibilities assumed by auditors and the message(s) conveyed by the audit report. (Monroe and Woodliff, 1994). The following chapter is a review of literature and provides empirical evidence of the existence such a gap worldwide by reviewing academic investigations conducted worldwide.

Chapter Three

Literature Review

3-1 Introduction:

Since the 19th century there has been difference in opinions concerning the form of wording to be used in audit reports (Chandler and Edwards, 1996). Several changes have been made to both the form and content of audit reports to tackle perceived misunderstanding of the message conveyed by audit report. The expanded audit report served mainly to clarify the respective roles of auditors and managements in preparing the financial statements. However, it struggles to change the users' perceptions of auditing (Jaenicke and Wright, 1992). Several countries have proposed and subsequently adopted expanded audit report wording in an attempt to ameliorate the expectation gap (section 3-2 provides historical developmental summaries of the adoption such audit reports). According to Hatherly et al. (1992, p.11) such expansion "is not intended to help close either the service vacuum of performance gaps or differences between the auditor and user over what the auditor's responsibilities ideally should be (level 1 of expectation gap)".

A summary of the empirical research conducted on the ability of expanded audit reports to reduce the Level 2 gap is given consideration in section 3-5. Concern with and calls for changing the terminology used in the audit report dates back at least to the late 1960's when William Roth, the chairman of AICPA committee on Auditing Procedure, saw the label "present fairly" as widely misunderstood and claimed that the term "GAAP" was meaningless (for details see Previts and Merino, 1998). Ironically, the same labels that were

criticized in the 1960's are still being used in the current financial statements and there seems to be little intention on the part of the profession to change them (Boyd et al, 2001). Section 3-3 provides discussion about auditors' assurance, while section 3-4 provides discussion about the auditor's opinion. Before that the discussion is touched upon, however, to provide a summary of the historical development of long form audit report (the expanded audit report) and its adoption.

3-2 The Development of the Audit Report:

As mentioned above, several changes worldwide have been made to both the form and content of audit reports to tackle perceived misunderstanding of the message conveyed by audit report and to set out in more details the work of auditors, as well as the auditors and directors' responsibilities, and thus help to tackle the audit expectation gap by adopting a long form audit report. This section provides historical developmental summaries of the adoption of such audit reports. The section is organized as a narrative and is subdivided by the country to give the reader a clearer historical perspective.

The form of the audit reports used in Great Britain during the latter half of the nineteenth century provided the foundation for the early American and [world] audit report (Carey, 1969, p. 27). This report was primarily the result of statutory requirement of an audit (Pusker, 1970, p.14). **Figure 3.1** provided an example of the form of the British report that was mandated by the Company Act of 1862 (Pusker, 1970, p.14).

Figure 3.1
The Early British Audit Report 1862

In our opinion the balance sheet was a full and fair balance sheet, properly drawn up so as to exhibit a true and correct view of the state of the company's affairs as shown by the books of the company.

(Source, Pusker, 1970, p. 14).

In the US, until the early 1930s, auditors reported their audit findings in their own words to express their opinion on their client's financial statements. Wording such as 'correctly set forth', 'exhibit a true *and* correct view', 'accurately recorded conditions', and 'represent the true financial position' were used (Campbell and Michenzi, 1987). **Figure 3.2** shows examples of such reports.

Figure 3.2
Examples of Early US Audit Reports

Example 1

We have attended at Chicago, Illinois, and audited the accounts of the Company for the year ended June 30, 1907, and **certify** that the balance sheet, in our opinion, **correctly sets forth** the position of the Company as shown by the books of account.

(Source, Campbell and Michenzi 1987, p.36)

Example 2

We have audited the books and accounts of the ABC Company for the year ended December 31, 1915, and we certify that, in our opinion, the above balance sheet **sets forth** its position as at the termination of that year and that the company profit and loss account is correct.

(Source, Thomas et al, 1991, p.16)

However, these individually written audit reports frequently led to confusion on the part of the users since often no clear expression of the auditor's opinion was given. Also, comments on the accounting measurements and scope of the examination were, at times, combined (AICPA, 1978).

Along with the confusion brought on by the sometimes poor communicative ability of these unstandardized reports, Liggio (1974) attributed the 'expectations gap' to the profession's successful campaign in the 1930s to have the audit report raised to the status of a certificate, thus the use of the word 'certify' to imply a level of accuracy not in the financial statements. He wrote "one professional has suggested that the accounting profession in the 1930s attempted to have its word, its report, considered the equivalent of the designation of the Good Housekeeping Seal of Approval. In fact, it was considered by some to be sterling on silver" (pp.29-30).

During the 1920s the American Institute of Accountants (AIA) made several recommendations as to wording. For example, in a booklet prepared by the AIA and adopted by the Federal Reserve Board in 1918, "Approved Methods for the Reparation of the Balance Sheet Statements", the AIA recommended the use of 'certify' to describe the action of the auditor. In 1929, the booklet was revised and renamed, 'Verification of Financial Statements'. In it, the AIA recommended the use of 'examined' instead of audited to indicate that the auditor had not checked all the transactions in detail. The booklet also recommended the wordings illustrated in **Figure 3.3** for the audit report.

Figure 3.3

Wording of the Audit Report Proposed By the AIA 1929

We have examined the accounts of the ABC Company for the period from January 1 to December 31, 1929. We certify that the accompanying balance sheet and statement of profit and loss, in our opinion, set forth the financial condition of the company at December 31, 1929, and the results of operation for the period.

(Source, Campbell and Michenzi, 1987, p. 36).

The 1940s also brought changes to the audit report. According to Campbell and Michenzi (1987) joint discussions between the SEC and the AIA resulted in the issuance of SAS No. 5 in 1941. This standard added 'generally accepted auditing standards' to the scope paragraph. In 1948, SAS No. 24 standardized the scope statement to be read as shown in **Figure 3.4.**, the term 'in conformity with generally accepted accounting principles' has been added to the scope paragraph. This report remained essentially unchanged until 1988, except for terminology changes to reflect current usage (Campbell and Michenzi, 1987).

Figure 3.4

The Short-Form American's Audit Report (SAS 24)

Auditor's Report

We have examined the balance sheet of X Company as of 19XX, and the related statements of income and surplus for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of X company as of December 31, 19XX and the results of its operations and the changes in its financial position for the year then ended, in conformity with generally accepted accounting principles on a basis consistent with that of the previous year.

(Campbell and Michenzi, 1987)

However, the Cohen Commission (AICPA 1978) recognized that this standard form report in use in the US did not adequately convey the management's responsibility for either the financial statements or the importance of auditor judgment. It also succeeded in confusing readers' understanding by using ambiguous language such as 'tests of the accounting records', 'present fairly' and 'in conformity with generally accepted accounting principles'. The Commission argued that if the report was expanded to represent the specific circumstances of individual clients, it would become less standardized and 'the tendency for the report to become an unread symbol will be reduced' (AICPA 1978, p.75). The Cohen Commission in recommending an expanded report stressed the importance of stating the management's responsibility for the representation of the financial statements, the undertaking of an explanation of the audit procedures, and the similar importance of making direct references to client specific areas such as interim financial information, internal accounting controls and audit committees.

Despite the reservations expressed above, the recommendations of the Cohen Commission were in some way incorporated in the US Auditing Standard Board (ASB) issue of an exposure draft proposing seven changes to the wording of the existing report. These were:

- The word 'independent' should be added to the title.
- Assert that the financial statements are the representations of the management.

- State that an audit is intended to provide reasonable, but not absolute, assurances as to whether financial statements taken as a whole are free of material misstatements.
- Replace the word 'examined' with 'audited'.
- State in the scope paragraph that the application of generally accepted auditing standards requires judgment in determining the nature, timing, and extent of tests and other procedures and in evaluating the results of these procedures.
- Delete the word 'fairly'.
- Delete the reference to 'consistent' application of generally accepted accounting principles.

(Quoted from Dunn, 1996, p.96)

In 1987, following further ASB 'expectation gap' exposure drafts, an expanded report was again proposed. The ASB, in the light of criticisms in the early 1980s, stressed that the report was put forward as a result of the concerns of interested third parties such as stockholders, creditors and potential investors that audited financial information did not communicate sufficient information see **Figure 3.5**. Nair and Rittenberg (1987), as would be explained in section 3-5-1 of this chapter, studied users' perceptions of this report (and the similar version suggested by the Cohen Commission) and concluded that the additional descriptions of both auditors and management's responsibilities, and the education process of the ASB to improve communication by familiarizing users with various reports, were both effective. But they stressed that "there may be a finite limit on the number of gradations of audit reports that can be effectively communicated" (Nair and Rittenberg 1987, p.35). For

the major academics studies that examined the message(s) communicated through these reports and existence of audit expectation gap with these reports refer to subsection 3-5-1 of this chapter.

Figure 3.5
The Wording of the Post-1988 US Unqualified Audit Report
(SAS 58)

Independent Auditor's Report
<p>Date</p> <p>Board of Director and Shareholders,</p> <p>X Corporation</p>
<p>We have audited the accompanying balance sheet of X Company as of 31 December 19.., and the related statements of income, retained earnings, and cash flows for the year then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audit.</p>
<p>We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.</p>
<p>In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of X Company as of [at] 31 December 19.., and the results of its operations and its cash flows for the year then ended in conformity with generally accepted accounting principles.</p>
<p>A, B & C</p> <p>Certified Public Accountants.</p>

In the UK, the Auditing Practices Board (APB) issued a standard in May 1993, the Auditors' Reports on Financial Statements SAS 600 (see **Figure 3.7** for wording of this report). This standard is similar to the US standards SAS 58 in moving from a short form audit report to an expanded audit report (Manson and Zaman, 2001). See subsection 3-5-2 for major UK studies of audit expectation gap with the audit report.

Figure 3.6
The Short- Form British Audit Report

We have audited the financial statements on page... to ... in accordance with Auditing Standards.

In our opinion the financial statements, which have been prepared under the historical cost convention, give a true and fair view of the state of affairs of the company and the group at and of the profit and source and application of funds for the year then ended and comply with the Companies Act 1985

The standard covered many of the requirements that Hatherly and Skuse (1991) argued an audit report should cover. For instance:

- A title identifying the person or persons to whom the report is addressed.
- An introductory paragraph identifying the financial statements audited.
- Separate sections, appropriately headed, dealing with Respective responsibility of directors (or equivalent persons) and auditors.
- The basis of auditors' opinion.
- The auditors' opinion on financial statements.

Figure 3.7

The Wording of the UK Expanded Audit Report (SAS 600)

Auditors' Report to the Shareholders of XYZ PLC.

We have audited the financial statements on pages ... to ... which have been prepared under the historical cost convention and the accounting policies set out on page

Respective responsibilities of directors and auditors.

As described on page ... the company's directors are responsible for the preparation of financial statements. It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

Basis of opinion.

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion.

In our opinion the financial statements give a true and fair view of the state of the company's affairs as at 31 December 19.. and of its profit for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Registered auditors

Date

Address

- The manuscript or printed signature of auditors.
- The date of the auditors' report.

Quoted from Hatherly (1997, p.183).

This standard however, was revised in January 2001, the UK APB issued a Bulletin (2001/2), *'Revisions to the Wording of Auditors' Report on Financial statements and the Interim Review Report'*. The report format is presented in **Figure 3.8**. The changes in the report presentation that the Bulletin 2001/2 made rise from a desire to improve communication and understanding. Therefore the Bulletin is the latest example of an attempt to address the expectation gap between auditors and users of the financial statements (Chitty, 2001).

Also in January 2001, the UK APB issued a Bulletin (2001/1), on the *electronic publication of auditors' reports*, which addresses the situation where companies produce annual financial statements and the associated auditors' report on their website. Auditors should review the process of electronic publication, check that the contents of the electronic version are identical to the hard copy, and check that there is no distortion in overall presentation. If not satisfied, the auditor should refuse to give consent to the electronic release of their audit opinion. The wording of the auditors' report should be altered to refer to the financial statements by name rather than by page.

Figure 3.8

The Wording of Revised UK Audit Report

Independent Auditors' Report to Shareholders of XYZ Plc

We have audited the financial statements of (name of entity) for the year endedwhich comprise [state the primary financial statements such as Profit and Loss Account, the Balance Sheet, the Cash Flow Statement, the Statement of Total Recognized Gains and Losses] and the related notes. These financial statements have been prepared under the historical cost convention and the accounting policies set out therein.

Respective responsibilities of directors and auditors.

The directors' responsibilities for preparing the Annual Report and the financial statements in accordance with applicable law and United Kingdom Auditing Standard are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirement, United Kingdom Accounting Standards and the Listing Rules of the Financial Services Authority.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the [Companies Act 1985]. We also reported to you if, in our opinion, the Directors' Report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all information and explanation we require for our audit, or if information specified by the law or the Listing Rules regarding directors' remuneration and transaction with the company [and other members of the group] is not disclosed.

We review whether the Corporate Governance Statement reflects the company's compliance with the seven provision of the Combined Code specified for our review by the Listing Rules, and we report if it does not. We are not required to consider whether the board's statement on internal control cover all risks and controls, or form an opinion on the effectiveness of the [Company's] corporate governance procedures or its risk and control procedures.

We read other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. This other information comprises only [the Director Report, the Chairman Statement, the Operation and Financial Review and the Corporate Governance Statement]. We consider the implications for our report if we became aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Basis of opinion.

We conducted our audit in accordance with United Kingdom Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion.

In our opinion the financial statements give a true and fair view of the state of the company's affairs as at 31 December 19.. and of its profit for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

Registered auditors

Date.

Source: APB, 2001/2, p.5

In February 1982, the International Federation of Accountants (IFAC) issued an exposure draft on the auditor's report ISA 13 which was finally promulgated in October 1983. Motivated by the belief that "a measure of uniformity in the form and content of the auditor's report is desirable because it helps to promote the reader's understanding" (paragraph 3), the stated purpose of ISA 13 was "to provide guidance to auditors on the form and content of the auditor's report issued in connection with the independent audit of the financial statements of any entity" (paragraph 2). Since its issuance, ISA 13 has been revised twice (in 1989 and in 1993) to address issues related to the form of the audit report and to provide clarifications of the standard (IFAC, 1995).

The ISA 13 requires the auditor's report to include the following elements (paragraphs 3–13):

- **Title:** An appropriate title to help readers identify easily the report within an annual report.
- **Addressee:** The report should be appropriately addressed as required by the circumstances of the engagement and local regulation.
- The report should identify the financial statements that have been audited, including the name of the entity and the date and periods covered by the financial statements.
- The report should indicate the auditing standards or practices followed in conducting the audit. Unless otherwise stated, the auditing standards or practices are presumed to be those of the country indicated by the auditor's address.

- The report should clearly set forth the auditor's opinion on the presentation in the financial statements of the entity's financial position and the results of its operations.
- **Signature:** The report should be signed in the name of the audit firm, the personal name of the auditor, or both as appropriate.
- **Auditor's address:** The report should name a specific location, which is usually the city in which the auditor maintains his office.
- **Report date:** The report should be dated to inform the reader that the auditor has considered subsequent events about which he became aware up to that date.

An important feature of ISA 13 is that it requires the auditor to express an opinion on whether the financial statements give a true and fair view of the financial position of the entity. This requirement helps ensure that the information satisfies the need of the international users of financial statements (Gangolly et al, 2002). **Figure 3.9** shows the wording of the unqualified audit opinion.

It also discusses circumstances that may result in other than an unqualified opinion, which include limitation of scope, disagreement with management, and uncertainty. The appendices to the standard include suggested expressions for the different types of opinions. Although one can debate whether ISA 13 is the best standard to meet the needs of the international users of financial statements, it is the standard that IFAC member countries are expected to follow.

Figure 3.9

The Wording of the International Audit Report (IAS 13)

Addressee

Introductory Paragraph

We have audited the accompanying [indicate names of each financial statement] of the XYZ Company as of December 31, 19XX [indicate any other additional years necessary] for the year(s) then ended. These financial statements are the responsibility of [identify Borrower]. Our responsibility is to express an opinion on these financial statements based on our audit.

Scope Paragraph

We conducted our audit in accordance with International Standards on Auditing. Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Opinion Paragraph

In our opinion, the financial statements give a true and fair view of the financial position of the XYZ Company as of December 31, 19XX, and of the results of its operations and its cash flows for the year then ended in accordance with [indicate International Accounting Standards or relevant national standards].

[Name and Address of Audit Firm]

[Date - Completion Date of Audit]

Recently the International Federation of Accountants (IFAC) also, has published an exposure draft that proposes changes to its standard on audit reports. IFAC's International Auditing Practices Committee has recommended

a requirement that the auditor clearly states the financial reporting framework being used to prepare financial statements. The revisions to International Standard on Auditing (ISA) 700, *'The Auditor's Report on Financial Statements'*, which would become effective for audits of financial statements for periods ending on or after 30 September 2002, are intended to enable users to better understand the context under which the auditor's opinion is expressed¹.

Figure 3.10
The Wording of the International Audit Report (ISA 700)

"AUDITOR'S REPORT"

(APPROPRIATE ADDRESSEE)

We have audited the accompanying balance sheet of the ABC Company as of December 31, 20X1, and the related statements of income, and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with International Standards on Auditing (or refer to relevant national standards or practices). Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

¹ Viewed on IFAC's website on 19 Sep. 2001

In our opinion, the financial statements give a true and fair view of (or ‘present fairly, in all material respects,’) the financial position of the Company as of December 31, 20X1, and of the results of its operations and its cash flows for the year then ended in accordance with International Accounting Standards (or [title of financial reporting framework with reference to the country of origin]) (and comply with ...).

AUDITOR

Date

Address

In Australia, in July 1993, the Australian Auditing and Assurance Standards Board (AuASB) of the Australian Accounting Research Foundation (AARF) reacted to a demand for significant modifications to the language of the unqualified short form audit report (AUP 3) (Schelluch, 1996). Subsequently a long form audit report was embodied in codified standard AUS 702 in 1994, with the stated intention to “improve communications between auditors and financial report users in order to alleviate the misconception held by users about the function, role and responsibilities of the auditor, which were created in part by the short form audit report of the processor AUP 3” (Schelluch, 1996, p. 48). This standard is consistent with the American standard SAS 58. **Figure 3.10** shows the wording of this report. (sub-section 3-5-3 provides the studies of the Australian)

Figure 3.11
The Wording of the Australian Audit Report (AUS 702)

Independent audit report

To XYZ Limited

Scope

We have audited the financial statements of XYZ Limited for the half-year ended 31 December 19XX as set out on pages X to Y. The company's directors are responsible for the preparation and presentation of the financial statements and the information they contain. We have conducted an independent audit of these financial statements in order to express an opinion on them in order for the company to lodge the financial statements with the Australian Securities Commission.

Our audit has been conducted in accordance with Australian Auditing Standards to provide reasonable assurance as to whether the financial statements are free of material misstatement. Our procedures included examination, on a test basis, of evidence supporting the amounts and other disclosures in the financial statements, and the evaluation of accounting policies and significant accounting estimates. These procedures have been undertaken to form an opinion as to whether, in all material respects, the financial statements are presented fairly in accordance with Australian accounting standards and statutory requirements so as to present a view which is consistent with our understanding of the company's financial position, the results of its operations and its cash flows. The audit opinion expressed in this report has been formed on the above basis.

Audit Opinion

In our opinion, the financial statements of XYZ Limited are properly drawn up:

- (a)** so as to give a true and fair view of: (i) the company's state of affairs as at 31 December 19XX and its profit and cash flows for the half-year ended on that date; and (ii) the other matters required by Divisions 4, 4A and 4B of Part 3.6 of the Corporations Law to be dealt with in the financial statements;
- (b)** in accordance with the provisions of the Corporations Law; and
- (c)** in accordance with applicable Accounting Standards.

Date Firm

Address Partner

In June 2003, The Australian AuASB has issued a Guidance Note “Improving Communication between Auditors and Shareholders”. This according to Mr Bill Edge, Chairman of the AuASB, was because “There is demand for an alternative form of audit report by users of audited financial reports in the Australian marketplace. This Guidance Note represents a step towards improving the quality of communication between auditors and shareholders”. Mr Edge added: “The AuASB is committed to exploring improvements in audit reporting that provide users with a clearer, more understandable and more business-like summary of the auditor’s work. An enhanced audit report will enable a clearer communication of the linkage between that work and the opinion expressed in the audit report.”³

In December 2002 one of the Big 4 leading auditing firms “PricewaterhouseCoopers” has decided to amend the wording of its opinion by including the wording ‘We do not, in giving this opinion, accept or assume responsibility for any other person to whom this report is shown or in whose hands it may come save where expressly agreed by our prior consent in writing’. This was to limit liability from legal action by banks (Accountancy, 2002)⁴.

In March 2003 the “PricewaterhouseCoopers” started to work to close the expectation gap⁵. To announce their intentions, the firm's chairman, Dennis M. Nally, told 400 business executives at the Economic Club of Detroit that a high-quality audit is essential to delivering the level of assurance investors

³ Viewed at 3rd of August 2003 at <http://accountingeducation.com/news/news4266.html>

⁴ Viewed at 23rd of April 2003 at <http://www.accountancymag.co.uk/>

⁵ Viewed at 22nd of March 2003 at <http://www.smartpros.com/x37474.xml>

require. He stressed that PwC was working to reduce the "expectation gap" so that investors might better evaluate a company's true condition, and to so to restoration of investor confidence in the profession. "This is nothing less than what the investing public expects from us," Nally said. Among PwC's efforts and recommendations; come the following:

- The Sarbanes-Oxley corporate reform legislation requiring auditors to attest to management's internal controls should be extended beyond the finance function. It should provide a market overview, review of company strategy and value-creating activities, in addition to the finance function. The auditor should develop a viewpoint on the company's internal controls to manage its business risks and then share that view with the audit committee.
- The accounting profession needs to go beyond the recently released standard for detection of material fraud. Specifically, Nally said, accountants must expand the requirements to include audit procedures to detect "significant" fraud. Trained auditors are able to look at incentives and pressure to commit fraud, the opportunities to commit fraud through weak internal controls and where it might arise given the overall tone of the business regarding ethics and codes of conduct.
- The auditors should go beyond the traditional corporate reporting model to provide investors with more access to information that is subject to audit procedures and to enhance the transparency and completeness of disclosures. Nally cited that PwC has developed a framework that enables a company to report from three different perspectives: using global Generally Accepted Accounting Principles;

reporting based on industry standards; and reporting based on company-specific information.

- Auditors must go beyond traditional reporting and report to audit committees on those aspects of a company's operations that shed light on the overall health of the business, such as liquidity, cash flow, the quality of earnings and assets and the company's overall prospects for sustaining current operations.

To sum up, since the 1930s, there has been several attempted worldwide to better the communication between auditors and the users to bring the audit report users closer to those of auditors by altering the wording of the audit report. Hence the aim of audit report wording changes has been to affect beliefs about the duties and responsibilities of auditors and the messages conveyed by audit reports and to close the audit expectation gap. However, the long-form audit reports have been criticized for what Humphrey et al (1992) state that the response of the auditing profession to the audit expectation gap seems to give readers more information about auditing, rather than more information about the results of the audit. The profession has responded to such criticism by claiming that the misunderstanding have arisen primarily because of ineffective communication between auditors and users of the audit report (Manson and Zaman, 2001, p.116). Though some auditing commentators have suggested that the solution (closing the gap) is to reduce the length of the audit report (Mautz and Sharaf, 1961) and others that there should be no standardized method of reporting the auditor's opinion (Estes, 1982), The APB in the UK (1992) did propose the introduction of the free-form

report as a way of improving the communication between the auditor and the users. Percy (1997) has made similar calls, advocating “discursive” forms of reporting that explain in layman’s language what is reported and what kind of assurance is provided. Hatherly et al (1998) suggested that the process of communication via the report could be improved by auditors using ‘free-form’ reporting rather than standardized reporting. They conducted experimental study on the usefulness of a free-form report and they found it significantly changes the users’ perceptions of the audit process: enhancing the “value and credibility of the audit” (p.30). However, there have been no official attempts in the UK nor in the US to put such a reporting system into operational practice.

The long form report have also been criticized for what it does not include more information about auditors’ assurance in regards of fraud, going concern doubts and the effectiveness of the entity internal control. These issues however, is a debatable itself, the next section will provide a discussion of auditors’ assurance in regard to such issues.

3-3 Auditor Assurance:

An audit report on general-purpose financial statements expresses a positive and objective opinion, and provides a high but not absolute level of assurance about management representations. When expressing an audit opinion on general-purpose financial statements, the auditor provides a “reasonable” level of assurance, in recognition of the fact that it is not possible to achieve absolute

assurance due to the inherent limitations of an audit. These limitations include the need to apply judgment in determining the nature, timing and scope of tests, the use of sample testing, the persuasive rather than conclusive nature of much of the available evidence and the inherent limitations of the internal control structure (Gay et al, 1998).

A major concern with assurance is related to auditors' responsibility for the detection of fraud, which seems to be big as a debating point as it used to be in the 1890's (Chandler and Edwards, 1996). From the time of its emergence until the 1940's, the corporate audit function had the detection of fraud as its primary objective (for more details about development of auditing and assurance, see Higson, 2003, pp. 90-112). However, in the post-1940s era, detection of fraud was no longer a main audit objective (Porter, 1997). The profession sees the detection of fraud as the responsibility of management, with the emphasis instead being on whether the financial statements present true and fair view. Humphrey et al (1993) saw the profession as being behind this change rather than it being changes driven by activities in the business environment or users needs.

In recent years, the debates and concerns about the auditing function that usually emerge in the aftermath of financial scandals have led to changes in auditing standards (Vanasco, 1998). In the USA, the American Institute of Certified Public Accountants (AICPA) issued standard SAS 99 in 2002, '*Consideration of fraud in a financial statement audit*', the standard requires auditors to assess the risk of material misstatements in the financial statements due to fraud and consider that assessment when planning and

performing the audit. The International Federation of Accountants (IFAC) issued in 2001 an International standard on Auditing ISA 240, '*The Auditor's Responsibility to Consider Fraud and Error in an Audit of Financial Statement*', the standard is similar to the American SAS 99. The standard (with ISA 700, '*The Auditor's Report on Financial Statements*') required auditors to depart from an unqualified opinion by expressing a qualified (or, in more serious events, an adverse or disclaimer) opinion in the cases when material fraud is not properly reflected or corrected in the financial statement. In the UK, SAS 110, '*Fraud and Error*' is less demanding than both the American SAS 99 and the ISA 240. It required the auditor to plan, perform and evaluate audit work to have a reasonable expectation of detecting material fraud, but does not require formal fraud risk assessment or response by auditors to fraud risk when planning and performing an audit (Porter et al, 2003).

Calls have nevertheless been made for auditors to provide other forms of assurance (see European Commission, 1996; Humphrey, 1997; Percy, 1997). These include assessing and reporting on management performance, internal control (ICAS, 1993; APB, 1994) and going concern. Although professional bodies thought that it would be unreasonable to provide guarantees of no fraud, on occasions they have given some support to auditors reporting on the effectiveness of internal control in minimizing the possibility of fraud taking place (ICAS, 1993; APB, 1994). The American GAO (1996) argued, "auditor reporting on the effectiveness of internal control is fundamental in successfully addressing the public expectation gap for fraud" (p.10). While the accounting profession in the USA supports calls for reporting on internal control it has not linked this issue to fraud detection and the Securities and Exchange

Commission (SEC) has yet to support such calls (GAO, 1996). In the UK, the Turnbull Committee, which was set up by the ICAEW, finalized a consultation paper (ICAEW, 1999) proposing that the board of directors of listed companies carry out, at least once a year, a review of the company's internal control and report to the shareholders that they have conducted such a review. Even so, the consultation paper did not require the auditors to express an opinion on the effectiveness of the internal control.

3-4 Auditors Opinion:

In the UK the auditor's opinion is an expression as to whether the financial statements give a 'true and fair' view. The 'true and fair view' concept is one of two competing that have been subject to debate on their meaning, use and importance. The other is 'present fairly in conformity with generally accepted accounting principles'. While the former is closely identified with judgment and is used in the United Kingdom (UK), the European Union (EU), Australia, the latter is the standard for United States (US) financial reporting. Both terms have a long history in audit reporting. 'Present fairly in accordance with GAAP' first appeared in US financial reporting regulation in 1939 (McEnroe and Martens, 1998) and 'true and fair view' in the UK Companies Act 1947 (Parker and Nobes, 1994) (see Higson, 2003, for more details about development of 'true and fair'). The International Accounting Standards Committee's (IASB) latest version of International Accounting Standard-1 (IAS-1), operational for periods beginning on or after 1 July 1998, adopts both concepts. It requires fair presentation and disclosure of compliance with IAS and a limited 'true and fair

view' override if compliance is misleading (IAS-1, 1998). Saudi Arabia has tended to follow the US example.

The phrase 'true and fair' in an audit report however, refers to financial statements as a whole, and whether each individual figure is judged to be true and fair depends on the materiality measure adopted by the auditor. It has been argued that a balance sheet based on historic cost values cannot be true and fair, as it shows a set of values which "does not as a general rule purport to show the net worth of an undertaking at any particular date" (AICPA 1978, p.73). To ascertain which true and fair view should be considered, it must be decided which objectives of reporting are being fulfilled, and at which user groups the reports are aimed. Morris (1973) believes that a true and fair view is not compatible with financial statements using historical cost measurement, as any judgment regarding a true and fair view is inextricably linked to an assumed purpose for the financial statements.

An unqualified audit report is required to show that the financial statements give a true and fair view of the Company's affairs at a given point in time. Higson (1991) and Higson and Blake (1993), in examining the communication value of the audit report, tested the value of the true and fair statement in the light of "the message the auditor is trying to communicate, the way it should be communicated, and whether it is understood?" (Higson 1991, p.16). Higson (1991), as will be discussed in sub-section 3-5-2, held twenty-five unstructured interviews with technical partners of accountancy firms between December 1990 and May 1991, and in the process analyzed the responses to, and understanding of, 'true and fair'. Surprisingly more than half of those

questioned expressed reservations about the appropriateness of the phrase, typically feeling that “if auditors can’t define what is meant, how can we expect the public to understand?” (Higson 1991, p.16). Much concern was expressed at the apparent ambiguity between the accepted meaning of the words separately and the technical implication of the phrase. ‘True’ was recognized as the real problem word as it all too often suggests accuracy or correctness, terminology that an auditor is all too keen to avoid. Typically the response of those in favour of retaining true and fair was that there was nothing better with which to replace it. Higson and Blake (1993, p. 114) claimed that this dislike was due mainly to the ‘spurious precision implied by word ‘true’ and the ambiguity of the formula. Lastly, one of the interviewees raised the issue as to whether users of audit reports appreciated the subtlety between ‘a true and fair view’ and ‘the true and fair view’.

Edey (1971) proposed replacing ‘true and fair’ with ‘properly compiled’ or ‘presents a fair view, while Hatherly and Skuse (1991) recommended the term ‘a fair view’. In the US, the audit report as mentioned above includes the term ‘present fairly’ and although the Cohen Commission identified even this statement as misleading (AICPA 1978, p. 74) and recommended that it should be removed from the auditor’s opinion, it has subsequently been retained in the expanded US report and has contributed to the audit expectation gap (Boyd et al, 2001). Boyd et al (2001) stated that “As long as users and auditors continue to have different understandings of the real meaning of ‘present fairly’, according to Generally Accepted Accounting Principles, the gap will remain”.

McEnroe and Martens (1998) surveyed UK and US individual shareholders to determine how they interpreted 'present fairly in conformity with GAAP' and 'give a true and fair view' and their preference for either phrase. They found that both groups preferred 'true and fair view' but the preference of UK investors for 'true and fair view' was more marked than that of the US investors, a result that perhaps conforms to expectations, given the US reporting rules. There was also evidence that when the language for the standard unqualified audit report is prescribed investors in both countries tended to be indifferent to the exact phraseology.

However, the interpretation of such phrases is very much determined by other information in the audit report. A report, that on the one hand clearly states the limitations of the work and assurances of the auditor but on the other reinforces accuracy and correctness (in the form of 'true and fair' and "present fairly") will inevitably lead to a situation where there exist increased misunderstandings of the auditor's role and responsibilities and widen the audit reporting gap. The next section is providing an empirical evidence of existence of such misunderstanding.

3-5 Evidence of the Existence of the Expectation Gap:

This section reviews the major empirical academic investigations conducted in relation to the existence expectation gap vis-à-vis the audit report. These essential studies are related to level 2 of the expectation gap according to the simple conceptual framework developed in Chapter One. This section is

organized as a narrative and is subdivided by the country to give the reader a clearer historical perspective. Libby (1979) was the first to investigate the messages communicated by audit reports. Subsection 3-5-1 of this section reviews Libby's work and the other work of Americans, directly addressing whether there are differences in beliefs between auditors and the public about the duties and responsibilities of auditors and the messages conveyed by audit reports (level 2). The discussion then goes on to review the UK studies in subsection 5-3-2. The Australian studies are the focus of attention in subsection 5-3-3. The last subsection is a review of the study conducted by Best et al (2001) in Singapore. Reader can clearly see that there is no direct Saudi evidence on either level 1 or Level 2 of the expectation framework.

3-5-1 The American Studies

In the US, Libby (1979) pointed out that the audit report was a pivotal form of communication between the auditor and those who see her/his work. He also brought to the fore the fact that the message intended by different audit reports had been the basis of little systematic study. He split the impact of the audit report on user decisions into three components "the accuracy of the user's perception of the auditor's intended message; the impact of the perceived message on the user's decisions and the resulting impact from the decision outcome" (Libby, 1979, p.100).

Libby investigated differences in perception between bankers and auditors using a geometric distance model. Thirty audit partners, from "Big 8" firms, and 28 commercial loan officers, from five large banks, participated in the

experiment. The bankers were mainly of vice-presidents and above, with most having an MBA from a prestigious institution. Subjects were asked to rate the similarity of the message intended by ten different types of audit reports issued for a fictitious firm with a "Big 8" auditor. Subjects were presented with pairs of the audit reports and asked to rate their similarity on a nine-point scale. Subjects were also asked to provide a numerical rating on thirteen adjectival phrases rating scales for each of the ten audit reports. The phrases chosen had been suggested in the professional literature as descriptive of the messages intended to be conveyed in audit reports.

Libby constructed a model of perception, based upon the relative similarity ratings, using multidimensional scaling. His two-dimensional solution showed highly similar perceptions between the two groups. He then proceeded to identify the two perceptual dimensions using the responses to the adjective rating scales. There were high correlations between the ratings on the scales for both groups, which also indicated similar perception. Libby identified the first dimension as being primarily related to the need for further information to estimate the riskiness of a loan prospect. The second dimension, while being less clear, appeared to relate to the source of the limitation on the scope of the audit and the auditor's ability to make a judgment because of that scope limitation. Libby concluded that his finding no large difference in perception implied fears of miscommunication between auditors and more sophisticated users were perhaps unjustified. However, Libby suggested that extending this generalization even to lower levels of sophisticated users would be precarious since the subjects had been chosen specifically for their sophistication in the evolution of financial statements. Furthermore, the findings were limited to the

messages intended to be conveyed by reports issued by “Big 8” accounting firms. Debriefing of the bankers revealed that virtually all “were of the opinion that the quality of audit work performed by different public accounting firms and the resulting meaning of their opinion vary among firms, particularly outside this group of large firms.” (p.119).

Bailey *et al* (1983) investigated differences in the perceived messages between existing audit reports and those proposed by the Auditing Standards Board (AICPA, 1980). These perceived differences were measured in terms of qualities or attributes that the Auditing Standards Board exposure draft implied audit reports should possess. They also studied differences in the messages as they were perceived by two groups of readers having different levels of audit report knowledge: recent accounting graduates, and fourth-year accounting students who had not yet taken an auditing course.

Similar to Libby (1979), Bailey *et al.* asked each subject to rate the relative similarity of pairs of audit reports on a nine point scale anchored by the terms ‘least’ and ‘most similar’. Each subject received ten different audit reports and was required to rate the similarity of all 45 combinations. Subjects were also asked to rate each of the ten reports on twelve attributes. Eight of the attributes were derived from the Auditing Standards Board’s proposal and four were taken from Libby’s (1979) study. Each attribute had a nine-point rating scale with appropriate adjective anchor points. Finally, each subject was asked to perform similarity ratings for the 66 possible pairs of the twelve attributes.

Twenty-seven recent accounting graduates, who had undertaken the CPA exam, received audit reports worded according to the proposal. The second group, consisting of 44 fourth year accounting students who had completed advanced accounting but not yet taken auditing, was split in two. Half received the ten proposed audit reports and the other half the existing reports. The alternate wording was treated as a between subject variable, as Bailey *et al.* believed that if subjects were exposed to two alternate wordings for the same report the experiment would become transparent and induce significant demand effects.

The report and attributes similarity data were analyzed using multidimensional scaling and the adjective scales were analyzed using MANOVA and ANOVA. The results, across the two statistical methods, indicated no relative difference in report meanings within each set of reports. However, while the MDS results indicated no difference in perception between his two knowledge groups, the MANOVA results indicated there was a difference. To resolve this issue and the question of whether there was absolute difference in the perceived messages between the existing and the proposed reports a further experiment was undertaken. Twenty-four accountants and thirty-eight advanced accounting students participated in a within-subjects design. Each subject was exposed to both existing and proposed wordings, but never for the same report. Both the MDS and MANOVA analyses indicated an absolute difference in perception due to the wording and a difference in perception due to reader knowledge.

Bailey *et al.* concluded that their results indicated that the proposed wording changes produced an absolute but not relative difference in perceptions. The subjects' perceptions of the responsibility for financial statements was shifted away from the auditors and towards management by the wording changes. They therefore considered that the proposed wording would achieve its goal. Second, they found that the more knowledgeable reader placed more responsibility on management and less on the auditor, than less knowledgeable readers. They suggested that such evidence supported the proposition that educational programs could educate people about the intended message of audit reports.

Nair and Rittenberg (1987) extended Libby's (1979) research by including "non- Big 8" auditors and bankers from smaller banks. Their study involved forty bankers and forty CPAs drawn to provide a cross-section of large and small organizations. Twenty of the CPAs came from "Big 8" offices and twenty from small local firms. Nineteen participants from the banking industry came from "large" banks while twenty came from "small" banks. The subjects were chosen by senior personnel in the organizations to fit the desired criteria. They completed Nair and Rittenberg's research instrument in a laboratory setting. Subjects were presented with background data on a hypothetical manufacturer, information which indicated the auditor was from either a "Big 8" office or a small local CPA firm, and nine different types of reports. Five of the reports were traditional audit reports, two were review reports, one a compilation and the ninth was a reworded unqualified report.

Subjects were asked to perform two tasks. First, all possible pairings of the nine reports were rated according to their similarity on a nine point scale. Repeat pairs included to test reliability provided reasonable assurance of the consistency of the participants' responses. The pairings were presented in two different random orderings. However, Nair and Rittenberg found that order made no difference in the assessment of the reports. Second, they were presented with sixteen adjectival phrases and asked to indicate (on a 0 to 9 scale) the extent to which each phrase was applicable to the financial statement for each of the nine reports. Six of the phrases were adapted from Libby (1979) and the authors generated the remaining ten. The adjectival phrases dealt with auditor responsibilities and the reliability/usefulness of the financial statements.

Multidimensional scaling (MDS) was used to analyze the similarity ratings. Their model revealed two dimensions for both the CPAs and the bankers, which they labelled "work performed" and "assurances communicated". They then factor analysed the responses to the adjectival phrases to see whether the factors were similar to the MDS dimensions. Two factors labeled "reliability" and "auditor responsibility" were identified for both the CPAs and bankers. The two groups' factor structures were similar except that bankers appeared to associate reliability with the extent of CPA involvement.

Chi-square tests, on the adjectival phrases, revealed no significant differences in responses between whether that hypothetical auditor was from a "Big 8" or local firm, so the responses for both CPAs and bankers were combined and tested for differences using the Mann Whitney *U* Test. The overall analysis

indicated substantial agreement between the bankers and the CPAs on the messages communicated by the different types of reports. Consistent with the hypothesized expectation gap, bankers placed more responsibility on the auditor for the correctness of the financial statements than did the CPAs. This difference, however, was not significant for the alternatively worded report.

Tests revealed similar understanding between the "Big 8" and local CPAs regarding the audit reports. However, there were significant differences regarding the compilations and reviews with the local CPAs perceiving these reports to be more reliable and useful than did the "Big 8" auditors. Similarly, the greatest differences between the "small" bankers and the local CPAs related to differing assessments of compilations and reviews, with the CPAs seeing such reports as more reliable and useful.

The Nair and Rittenberg study showed substantial differences between auditors and bankers concerning the messages communicated in compilation and review reports (i.e., those reports not resulting from an audit). They also reported a difference in perception of the message communicated about auditor responsibility and that this difference was diminished by the modified wording. They drew the following implications: firstly, additional descriptions of procedures performed and degree of responsibility assumed might be useful in improving the consistency of messages communicated in audit reports; secondly, that there may be a limit on the number of gradations of audit reports; and thirdly, that the education process could improve communication by familiarizing users with various audit reports. Limitations of the Nair and Rittenberg study include the non-randomness of the sample, the fact all

subjects came from a limited geographic area and the difficulty in distinguishing between the sophistication levels of the bankers. Furthermore, their scales appear to have been developed in an *ad hoc* manner with little attempt to develop an instrument that validly and reliably measures beliefs about the messages conveyed by audit reports.

Kelly and Mohrweis (1989) investigated the impact of SAS No.58 on bankers and investors perceptions' of the auditor's role in financial statement reporting. They pointed out that the changes in audit report wording made by SAS 58 were intended to improve the understandability of audit reports and not to change the inherent relationship between management and auditor in the financial reporting process.

Three research questions were addressed. First: What message is the audit report wording of SAS 58 communicating that is different to the existing wording?' Second: Has the wording been improved enough or are additional revisions necessary? And third: 'Does the new report communicate a different level of auditor responsibility?'

They utilized only the unqualified opinion. Subjects were asked to read either the old or new report and then respond to eight statements on a seven point scale (strongly agree /strongly disagree) the statements, which were pre-tested on colleagues, were mainly based on the Exposure Draft Package (AICPA, 1987). The statements were designed to see if understandability was increased.

Fifty banker and fifty investors (MBA students) participated in the study. Since auditors did not participate in the study no direct evidence of an expectation gap is provided. However, Kelly and Mohrweis were able to examine whether perceptions differed between groups. Initially half, of each group received either the old or new report and the eight statements. After the questionnaires were completed and returned, each participant was given the opposite report and asked to indicate if the report wording of SAS 58 implied that a different level of auditor responsibility was assumed.

For both user groups, those with the new reports agreed more strongly: that the financial statements were the responsibility of management; that the purpose of the audit was clearly communicated; and that the audit procedures were clearly delineated. Both groups were undecided about the auditor's responsibility for the detection and correction of material errors. In the second stage, the bankers (but not investors) perceived the new reports to be conveying a lower level of auditor responsibility than did the old reports.

The limitations of the Kelly and Mohrweis study include: the very limited (small) size of the sample employed; all subjects were from a limited geographical area; there were only two different groups; and all subjects received only the unqualified report. To reiterate, since auditors were not included as subjects, the study says nothing about the existence of an expectation gap. Nevertheless, their study adds evidence to the proposition that wording changes on audit reports have the ability to impact on the beliefs of financial statements users.

Miller *et al.* (1993) investigated the effect of the wording changes in SAS 58 on bank loan officers' perceptions of the messages communicated through audit reports. Their study differed from that of Kelly and Mohrweis (1989) in three main aspects. First, they used a national, rather than local sample of bankers. Second, perceptions of the information communicated by both qualified and unqualified reports was the objects of study; and third, they compared the views of both large and small lenders.

They used a context-free instrument where bankers were asked to respond to questions on a 100-point scale. Each subject received only one report followed by eighteen questions. The overall response rate was 22% and comparison of first and second mailing responses indicated no-response bias to be insignificant. In the first phase of their survey, 120 bankers were sent the unqualified new opinion and 120 the unqualified old opinion. Two forms of the questionnaire were used and there appeared to be no order affects. In the second phase of the survey, four groups of 200 bankers were sent one of two types of qualified report containing either old or new wording. The reports were made up of a qualification due to scope limitation (unable to observe talking of inventories) and a GAAP departure (inventories valued at selling price, not cost). The average responses provided by the bankers in the first phase were marked on the second phase questionnaire to provide a benchmark against which to judge the qualified reports.

The responses to the eighteen questions were grouped into six categories and averaged for each subject. Use of Cronbach's alpha test indicated that variables

were internally consistent and that such an averaging should result in reliable measures. The six categories were:

- The reliability of the financial statements (four questions).
- The responsibilities of the auditor (two questions).
- The responsibilities of management (two questions).
- Auditor communications (four questions).
- The extent of testing and the scope of the audit (four questions).
- The auditors' responsibility for the detection of fraud (two questions).

Overall the new report improved certain aspects of the audit report's ability to communicate between auditors and financial statement users. The loan officers perceived the new report wording as implying that management had more responsibility for the accuracy of the financial statements. However, only for the GAAP qualification were auditors seen as having reduced responsibility. The new wording resulted in the scope qualification being perceived as both more understandable and more reliable.

Millier *et al.* thought their results were encouraging and that the wording changes had been successful in addressing many of the concerns expressed by the auditing profession. However, as with Kelly and Mohrweis (1989), no direct evidence of an expectation gap or the ability of expanded form audit reports to ameliorate that gap is provided.

Mohrweis (1995) investigated a concern voiced by respondents to the ASB's 1980 Exposure Draft and researchers: the changes to the audit report may give

the perception of reduced auditor's responsibility (Dillard and Jensen, 1981; Kelly and Mohrweis, 1989). Specifically, Mohrweis investigated whether the post-1988 standard audit report had produced a "cynical" effect among users concerning the level of assurance auditors provide. The author surveyed Big-6 auditors, commercial lenders and financial analysts concerning their perceptions of the assurance level communicated by the auditor when issuing the unqualified and unmodified audit reports. Inferences concerning assurance levels were measured for both errors and irregularities, using percentage answers ranging from 0 to 100 percent.

Mohrweis found no significant difference between auditors and bankers with respect to the assurance communicated in the audit report concerning irregularities ($p = 0.927$); however, a significant difference did exist between the two professions concerning the assurance provided for errors, with the bankers being more cynical than the auditors ($p = 0.015$). Analysis of differences between auditors and financial analysts had similar results. That is, no significant difference existed between auditors and financial analysts concerning the level of assurance provided by auditors with respect to irregularities ($p = .638$), but marginal support was found for the hypothesis that a difference existed between the auditors' and financial analysts' perception of the level of assurance provided with regard to errors ($p = .089$). Again, the analysis found that the financial analysts were more cynical than the auditors. Mohrweis also found that all three of the professional groups differentiated between the assurance provided for errors and the assurance provided for irregularities.

McEnroe and Martens' (2001) study surveys auditors and individual investors in US to obtain their perceptions of the extent to which an expectation gap existed in 1999, over a decade after the release of the expectation gap SASs, and after SAS No. 82 (AICPA 1997). This study extends previous American research by directly comparing the perceptions of audit partners (auditors) and investors (users), and by investigating the wording of the audit opinion and certain dimensions of the attest function. The auditors' population is a random sample of 500 audit partners with a response rate of 23.4 percent (117). The population of users sample is also of 500 investors from the American Association of Individual Investors, a total of 147, resulting in a 29.4 percent response rate.

The researchers tested the reliability of the instrument by computing the statistic 'coefficient alpha' for these same questions for all the respondents. This test examines the average correlations among the items on the research instrument to measure the "internal consistency" of the research instrument. They computed alpha of 0.86.

The study presented that the majorities of both the auditors and the investors agree that Present Fairly GAAP (PFGAAP) means presented in conformity with GAAP, and also present in a no misleading way, for example, a majority of investors (52.6%) believe that 'fairly' in PFGAAP adds to the presentation of the financial statements in conformity with GAAP by requiring that such presentation be no misleading. Even larger majorities of both groups agree that the signal of an unqualified opinion is more important than any specific terminology contained in the report expressing that opinion.

They found that the auditors and investors tend to agree about the meaning and importance of the specific terminology used in an unqualified opinion, while they (auditors and investors) do not agree about what an auditor should do or judge before issuing an unqualified opinion. The results indicate the existence of an expectation gap along several dimensions. The researchers conclude that users do not want auditors to issue an unqualified opinion unless:

- Every item of importance to investors and creditors has been reported or disclosed.
- Auditors have been "public watchdogs".
- The internal controls are effective.
- The financial statements are free of misstatements resulting from management fraud.
- The financial statements are free of misstatements intended to hide employee fraud.
- The firm has not engaged in illegal operations.

McEnroe and Martens (2001) stated "Because this research was conducted in 1999, over a decade after the release of the expectation gap SASs, and after SAS No. 82's (AICPA 1997) attempts to clarify the auditor's responsibility to detect fraud, it is evident that the pronouncements designed to reduce the expectation gap are not effective in the areas pointed out by the respondents to this survey".

McEnroe and Martens (2001) proposed two appropriate actions to reduce expectations:

- A possible solution is to include, as an SEC mandated part of the annual report, a uniform explanation developed by the ASB as to what the attest function is designed to accomplish, as well as a condensed summary of the authoritative guidance regarding auditors' responsibilities. This explanation could serve as a brief overview, similar to our discussion of the auditors' responsibilities in this paper. This narrative might be a page or two in length and could be positioned immediately following the audit opinion.
- Another possible course of action is to have the auditor provide a similar explanation at the annual shareholders' meeting and entertain questions regarding the nature and scope of the audit. Measures such as these could educate the public and reduce the expectation gap or minimize its importance.

3-5-2 The UK Studies

Holt and Moizer (1990) conducted a survey designed to test the differences in the inferred meaning of audit report wording on thirteen decremental dimensions of the unqualified audit report and various types of qualified audit reports used in the United Kingdom (UK). These dimensions included the reliability and usefulness of financial statements, compliance with company law and accepted accounting practice, inclusions of distortion, omission, role of the auditor, appropriateness of controls, viability of firm, and appropriateness of directors' actions.

They used a Likert scale to measure the subjects' agreement or disagreement with the given statements concerning the dimensions studied. A Wilcoxon Matched-Pairs Signed-Ranks test was used to test for significant differences among the subjects' responses. Those surveyed included audit firm senior partners, those classed as accountants and stockbrokers and employees of insurance companies, investment trusts, pension funds and banks. This last group of subjects were classed as users. The average response rate was 36.5%

The researchers found that while both the accountants and users were able to distinguish one type of report from another, users inferred fewer differences in the meaning of the audit report wording in the qualified reports than did the accountants. Additionally, Holt and Moizer's study suggests that substantial areas of disagreement exist concerning both the meaning of the unqualified audit report and the interpretation of the qualification used by auditors. Interestingly, the users were much more sceptical than the accountants about the results reported in the unqualified report. However, for the qualified reports, the direction of the differences varied, with the accountants at times being more sceptical than the users and vice versa. In summary, the Holt and Moizer study suggested that, in the UK at least, an expectations gap still exists concerning what the auditor has actually accomplished in the audit and the meaning of those accomplishments. However, it must be noted that at the time of the study, the changes made to the audit report in the United States had not been made to UK's standard audit report.

The objective of Higson's (1991) study was to identify the message which the external auditor was trying to communicate in an unqualified audit report. He

used Communication Theory as the theoretical framework from within which the audit report was examined. Higson's study differs from previous work in that "it attempts to establish the auditor's message, not by asking auditors to interpret the wording of a given audit report, but rather to state what they were trying to say at the end of an audit" (p.3).

The study concentrated on the first part of the communication process, i.e. the message. The research methodology adopted was essentially qualitative in nature. The study was conducted by means of a series of semi-structured interviews. Twenty-five semi-structured interviews were conducted with senior practitioners- predominantly audit technical partners of the "top thirty" accountancy firms in the U.K. Higson wrote that "there was some consensus that the audit report was not implying that the financial statements were free from bias. Auditors were not saying that the data in the financial statements had been 'verified', but appeared to view their role as being to examine the reasonableness of management's justifications for their representations" (p.20). The interviews have highlighted major reservations regarding the phrase 'a true and fair view'.

King and Higson (1994) investigated the message(s) communicated through the unqualified audit report. Specifically, King and Higson's study sought to discover:

- Whether there existed differences of understanding and expectations within the selected group.
- The extent to which this group was satisfied with the phrase 'true and fair'.

- The extent to which respondents supported certain possible changes to the wording of standard unqualified audit report.

King and Higson (1994) differed from that of Higson (1991) in two main aspects. First, they used a questionnaire survey, rather than unstructured interviews. Second, perceptions of the preparers of financial statements was the objects of their study. A total of 195 questionnaires were sent to the finance directors and company secretaries in the UK East Midlands Companies. They used a five point Likert scale to measure the subjects' agreement or disagreement with the given statements concerning the dimensions studied. The average response rate was 35%.

The findings of King and Higson (1994) showed differences and misconceptions in the respondents' degree of understanding of the message communicated by an unqualified audit report. There was also a variety of views as the efficacy of the phrase 'true and fair' and suggestions for alternative words, and on the inclusion of statements on directors' responsibilities and subjective nature of the financial statements. Interestingly, they found that there were some strong reactions from the respondents to the inclusion of the word 'Independence' in the heading of the audit report. Almost half the responses being neutral and disagreement by around 22% in total to include such a word.

King and Higson (1994) concluded that their findings indicated that 'the clearly differences of understanding amongst this group of preparers of financial statements is evidence of an expectation gap' (p.8). They suggested a number

of potential areas for further works, including a detailed comparison of their findings with the views of auditors and users of the financial statements.

The primary research question addressed in Hatherly *et al.* (1991, 1992) was whether a UK derivative of SAS 58 had the power, compared to the current short form report, to help the reasonably intelligent reader to better understand the nature of an audit and the auditor's role.

One hundred and forty part-time MBA students were divided into two groups. The students were chosen as surrogates for reasonably intelligent audit report reader with business experience but no formal audit training or education.

A questionnaire was designed to elicit subjects' perceptions of the audit and the underlying financial reports and the audit. Eighteen statements were derived from a detailed analysis of prior empirical research: Libby (1979), Bailey *et al.* (1983), Nair and Rittenberg (1987), and Lee (1986). The respondents were given a director's report and a set of financial statements on a seven-point scale (strongly agree/ strongly disagree). Half of the subjects received the old short form audit report while the other half received a report based on SAS 58 but modified to make it compatible with the UK company auditing environment.

Hatherly *et al.* used a modified *t* test, which did not rely on equal variances, to test for differences between those receiving the old and the modified reports (Mann-Whitney *U* tests produced identical results). Seven of the 18 scales provided significantly different scores at the 5% level.

Five of the seven significant differences related to dimensions directly addressed by the expanded report. The subjects considered that the expanded report more clearly communicated the purpose of the audit. Furthermore, it heightened perceptions that: the auditor was unbiased and objective, the audit opinion related to the financial statements as a whole; management representations were not relied up without corroborating evidence; and that the auditor used judgment. Surprisingly the question of who was responsible for the financial statement did not produce a statistically significant difference between the groups with the modified and old reports. However, the absolute level of the scores suggested to Hatherly *et al.* that all subjects already appreciated that the financial statements were management's responsibility (a level of awareness, they suggested, that may not be present in other user groups).

Of interest were the two significant differences in perceptions on dimensions not directly addressed by the modified wording. In particular, the expanded report heightened the perception that the auditor was satisfied with the financial statements and that the company was free of fraud. Significantly different at the 10% level was the statement that the audit enhanced the credibility of the financial statements. Hatherly *et al.* termed this heightened perception on dimensions not explicitly addressed by the expanded wording a "halo" effect. They point out that such an effect will not be beneficial if it takes the expectations of the reader far beyond what the auditor considers the position to be. They suggest that further wording changes might be necessary to address these dimensions directly and so to dampen down such expectations.

Hatherly *et al.*'s results provide clear evidence of the ability of an expanded report to change reader perceptions of auditing and the auditor's role. As they acknowledge, what is not examined in their research is whether the expanded audit report moves readers' perceptions closer to the perceptions of professional auditors. That is: Modified wording has the capacity to change reader perceptions, but what effect does it have on auditors? Is there a difference between auditors and users using old reports and is this lessened by utilising expanded audit reports? These questions are directly addressed in Innes *et al* (1997).

In a related study, Innes *et al* (1997) compared the perceptions of Scottish chartered accountants with that of the MBA students and found that the expanded audit report, compared to the short form report, brought users' perceptions, to some extent, closer into alignment with those of auditors. They also found, however, that along a number of different dimensions users' perceptions were still significantly different from those of auditors. This can be interpreted as indicating that whilst the expanded audit report might reduce the expectation gap it is unlikely to eliminate it. Interestingly, they also found that the expanded audit report seemed to increase users' perceptions of the usefulness of financial statements. In particular, they found that the expanded audit seemed to increase users' perceptions that the financial statements were free from fraud. Innes *et al* (1997) concluded by stating that they considered 'the expanded audit report to have a useful but limited impact on the expectation gap and to give a patchy performance in term of moving users' perception towards those of auditors' (p. 714).

The objectives of Manson and Zaman (2001) are similar to those of this study, in that it was conducted to determine: (i) the extent to which the three groups (surveyed, auditors, preparers and users) appear to be satisfied that the expanded audit report (The UK SAS 600) successfully communicates certain key issues; (ii) the extent to which the three groups consider that it would be useful for additional matters, including corporate governance, to be reported upon by the auditor; and (iii) whether there are any differences in the perceptions of the three groups.

The researchers used a questionnaire survey, which was sent to a number of individuals from the three groups: auditors, preparers and users. Their questionnaire was structured such that it required a response on a seven-point Likert scale and was designed to determine respondents' views in respect of certain key issues relating to the change in wording of the expanded audit report. The questionnaire included, as an appendix, a sample auditors' report taken from SAS 600 to which respondents were referred. The researchers used *T test* to determine if there existed differences in belief between the three groups.

Contrary to the previous UK studies (e.g. Hatherly et al, 1991, 1992 and Innes, 1997), the researchers did not try to make a comparison of views of respondents on both the old (short-form) and the new auditing standard (the expanded form). They discounted this approach for two reasons. First, the new audit report had been in existence for six years at the time of the study and they doubted whether respondents would be able to cast their mind back to the time when the previous audit report had been in use (and therefore considered

that any responses might be unreliable). Second, the objective was to determine what respondents thought about the wording used in SAS 600, rather than to make a comparison with the previous audit report standard, and to identify areas where the scope of the audit report could be expanded.

A total of 1000 questionnaires were distributed to the study sample, with response rate of 33%. 400 questionnaires were sent out to the auditor sample which was selected from audit partners in big 5, top 40 (excluding big 5) and other firms. The response rate 41%. 400 questionnaires were distributed to the sample of finance directors (preparers group) with a 30% response rate. The user group sample comprised investment analysts and corporate bankers. The researchers gave reasons for disregarding the shareholder group by explaining that it was difficult to identify a suitable source from which to select an appropriate sample.

Manson and Zaman (2001) found that the UK expanded audit report SAS 600 has been successful in clarifying the purpose of the audit and respective responsibilities of auditors and directors. In other respects, (for example, conveying the auditors' responsibility in relation to fraud) the expanded audit report has been less successful. It is also apparent that auditors remain reluctant to go substantively beyond their present commitment to expressing an opinion on the financial statements. The researchers argued that the audit report is of limited value to users and that it needs to be extended to include information about the results of the audit. They concluded that the challenge for the Auditing Practices Board is to move forward towards providing more information to users about the findings of the audit.

3-5-3 Australian studies

Gay and Schelluch (1993) used a modified and extended form of the instrument used in the Kelly and Mohrweis (1989) study described earlier. They investigated whether the audit report wording changes advocated in the revised AUP3 (AARF, 1993a) increased user's understanding of the role of the auditor, the nature of the audit process and the financial reporting process. They noted that the revised wording did not alter the auditor's responsibilities: rather it attempted to make explicit that which was implicit in the old short form audit report. Their objective was to examine to what extent the revised AUP3 minimized the expectation gap. However, similar to the above studies, auditors were not included as part of the research design. Thus, they do not provide direct evidence on the nature and extent of any expectation gap.

Their research instrument was completed by subjects in a context free-frame of reference. The subjects' were 60 bankers and 120 MBA students. The MBA students were evenly divided into 60 shareholders (investors) and those with no investment experience (non-investors). The subjects in each group were asked to read an unqualified audit report and respond to nine questions, on a seven point scale, based on their understanding of the report. Half of each group of subjects received an audit report using the old wording while the other half received wording in accordance with the revised AUP3.

Tests of difference between those receiving the old and new reports revealed several differences significant at the 5% level. All three groups believed that the new report more clearly explained audit procedure. The investors and bankers believed the purposes of the audit were more clearly communicated in the new

report than the old report. The investors were the only group to perceive that the new report suggested the related financial reports were more accurate. Significant differences, at the 10% level, were reported for the questions dealing with the directors' responsibilities for material errors and the audit report clearly communicating the basis of the auditor's opinion.

Thus, the Gay and Schelluch study was very similar to the US and UK studies reviewed earlier in this section. The studies showed that the wording used in audit reports could impact on readers' perceptions of the role and responsibilities of auditors and directors in relation to the financial reporting process.

Monroe and Woodliff (1993) investigated the impact of education on beliefs about messages conveyed in audit reports. In a study involving undergraduate students, it was found that education significantly affected the students' beliefs and that there was an expectation gap. Monroe and Woodliff (1994) addressed the issue in Australia by conducting a study with auditors, accountants, creditors, directors, shareholders and students. Results confirmed that there was in fact an expectation gap between auditors and the various user groups about the auditors' responsibility for financial statement presentation and fraud, the level of assurance provided and the predictive value of the financial statements. The researchers found that the change to a long-form report (under the revised Australian AUP 3) had significant impact on beliefs and lessened the gap in some areas. However, some new differences in beliefs between auditors and user groups emerged.

Schelluch (1996) developed a semantic differential instrument to measure the messages communicated through audit reports (level 2) with the long form audit report Au 700 in Australia. This followed the steps outlined in Malhotra (1981), Holt and Moizer (1990), and Monroe and Woodliff (1993, 1994).

He extended previous research by examining perceptions of auditors, company secretaries and shareholders (both preparers and users) rather than concentrating on relatively sophisticated/specialised user groups such as bank loan officers and financial analysts, or shareholder surrogates. The research instrument was administered in a context-free frame of reference, to ensure that results were not affected by quarterly versus annual financial reporting considerations.

The researcher used principal components analysis (PCA) with varimax rotation, which was performed to identify the underlying dimensions of the messages communicated by the reports, resulted in three stable factors, (1) Responsibility, (2) Reliability, (3) Decision Usefulness.

Schelluch's (1996) study provides evidence that the expectation gap continued to exist in Australia after the introduction of the long-form audit report in relation to financial statement reliability. This finding appears to indicate continued difficulties being experienced by users in understanding audited financial statements. The study also appeared to indicate that users were generally unhappy with the role played by the auditing profession particularly with respect to auditor independence and the level of value (i.e. credibility) added to the financial statements from the auditing process. Schelluch (1996)

found that the expectation gap detected in prior Australian research studies (e.g. Schelluch et al, 1993; Monroe and Woodliff, 1993, 1994) dealing with auditor responsibilities appeared to be reduced over time with the introduction of the long-form audit report. Differences in beliefs between auditors and users (company secretaries and shareholders) appeared to be reduced in areas specifically addressed in the wording of the expanded report.

Gay et al (1998) expanded Schelluch (1996) by focusing on messages communicated by review reports and audit reports in order to provide an indication of users' understanding of these reports, as well as their ability to distinguish between messages conveyed by the two types of reports. The study shows how audit and review report messages affect perceptions of users, auditors and preparers in relation to auditor/management responsibilities, financial statement reliability and the decision usefulness of financial statements. To date, little direct evidence of comparative differences in perceptions of audit/review report messages between practising auditors, corporate secretaries and shareholders has been available.

Two versions of the final research instrument were administered. One version contained a negative assurance review report on interim financial statements, while the second version contained a positive assurance audit report, followed by the words "This review/audit report indicates to me that..." and each of the selected bipolar adjectival statements, separated by a seven point scale. While the selected statements and their related factors are identical to those of Schelluch, (1996) the first phrase was treated as the "1" end of the scale and the

second phrase was treated as the "7" end of the scale. In addition, demographic details of subjects were also sought in the final instrument.

Gay et al's (1998) study has provided direct evidence about the beliefs of auditors, company secretaries and shareholders of messages conveyed by review reports and audit reports. Beliefs were assessed with respect to Responsibilities, Reliability and Decision Usefulness of financial information. With respect to Responsibility, the results indicate that company secretaries and shareholders placed greater responsibility on management for the maintenance of internal controls and accounting records than did the auditors. However, shareholders placed less responsibility on the auditor in a review engagement when compared to an audit. Both shareholders and company secretaries were more sceptical about auditor's objectivity and independence in both audits and reviews, than were auditors.

The researchers reported that significant gaps in expectations persist for all three dimensions analysed. Shareholders and, to a lesser extent, company secretaries place considerable responsibility on management and are more sceptical of auditor objectivity, financial statement reliability and decision usefulness. Doubts as to the assurance levels and work performed persist. They concluded that 'the expanded report now required for reviews and audits may have eliminated some expectation gaps revealed in prior studies based on short form audit/review reports. However, it has not prevented additional gaps occurring in relation to financial report reliability and the level of assurance provided, and has failed to alleviate the scepticism of shareholders and preparers'.

3-5-4 Other studies

Best et al (2001) reports a study conducted in 1996 of the audit expectation gap in Singapore. Their aims were to measure the level and nature of expectation gap in Singapore in the 1990s. The research method adopted is a replication of the study of Schelluch (1996). The questionnaire used in this study is identical to that of Schelluch (1996) consisting of two sections. The first section collected demographic data. The second section contained 16 semantic differential belief statements. These belief statements measured three factors:

- 1- Responsibility;
- 2- Reliability; and
- 3- Decision usefulness.

A total of 300 subjects were selected randomly and evenly split into 100 subjects from each of the three groups - auditors, bankers and investors. The subject group 'investors' included the general public (30), financial analysts (35) and brokers (35). These parties were grouped together as proxies for investors. Best et al. (2001) do make the assumption that the majority of the general public in Singapore are shareholders since the Singapore Government issues shares in direct proportion to the citizen's balances in their Central Provident Fund. It is an arguable criticism of their supposition to raise the question: 'What proportion of the total general public who received the shares from the government actually retain them and thus continue to be shareholders?'

Best et al (2001) found that users in general perceived that an audit cannot provide absolute assurance that financial statements contain no material

misstatements. They also found out that the users agreed that the extent of assurances on audit work was clearly given. Users were aware of the assurances given and the possibility that material misstatement might still occur in the audited financial statements. In addition, users placed responsibilities on the auditor for the maintenance of accounting records. To a lesser extent, Best et al. (2001) found out that expectation gap also existed concerning the auditor's responsibility for the soundness of internal controls. Best et al (2001) results found evidence of a wide audit expectation gap in Singapore in the areas of auditor responsibility for fraud prevention and detection, maintenance of accounting records, freedom of the entity from fraud, and auditor judgment in the selection of audit procedures. They conclude that their results "strongly support the adoption of the long-form audit report in Singapore if Singaporean professionals are serious about reducing the expectation gap and improving decision-making by financial statement users".

3-6 Summary and Conclusion:

This chapter started by reviewing the proposal development and adoption of the expanded audit report, followed by a review of literature on audit assurance and the audit report. Discussion then moved on to review the empirical academic investigations into the existence of an expectation gap within the audit report. The literature was classified according to the three level expectation gap framework developed in Chapter One. The first level concerns differences in beliefs about what auditors 'duties and responsibilities should be'. The second level reflects differences in beliefs about the duties and responsibilities of the parties to an audit and the messages communicated

through audit reports, while the third level arises when auditors fail to exercise due professional care. The first and third level do not concern themselves with beliefs about the message conveyed in the audit report, but merely with individual auditor performance and beliefs about what auditor should do. They are thus beyond the scope of this thesis.

The level 2 (ideal) studies took as their starting point a review of the American studies, for example Libby (1979). He found that auditors and bankers had similar beliefs about what the responsibilities of auditors were. Other US studies (Nair and Rittenberg (1987) and Robertson (1988) also used subjects who could be expected to be reasonably sophisticated with respect to the meaning and interpretation of financial statements and audit reports (bankers and financial analysts) and reached similar conclusions. Bailey et al. (1983) found that more knowledgeable users placed less responsibility on auditors than less knowledgeable users. Nair and Rittenberg (1987), Kelly and Mohrweis (1989), Miller et al (1993), reported that an expanded audit report changed users' perceptions about the relative responsibilities of management and auditors and that users found expanded audit reports more useful and understandable than the previous short form audit reports. However, McEnroe and Martens (2001) found that the expectation gap still existed in the US in 1999.

In the UK Holt and Moizer (1990) reported differences in perceptions of the meaning of audit reports between accountants and sophisticated users. Higson (1991) found that over 50% of the sample had reservations of some kind regarding 'true and fair view'. King and Higson (1994) showed differences and

misconceptions in the respondents' degree of understanding of the message communicated by an unqualified audit report. Hatherly et al. (1991,1992) found that changing the wording of the standard short form auditor's report in the UK resulted in different perceptions of the meaning of audit reports. What is not examined in their research is whether an expanded audit report moves readers' perceptions closer to the perceptions of professional auditors. In other words, modified wording has the capacity to change reader perceptions, but what affect does it have on auditors? Further to this, is there a difference between auditors and users using old reports and is this dissimilarity lessened by utilising expanded audit reports ? However, such concern has been addressed by Innes et al, 1997.

The majority of researchers (and the professional literature) have suggested that an approach that could potentially ameliorate the expectation gap would be to better educate the public as to the role and limitations of an audit. The auditor's report is deemed to be important in reducing the expectation gap. The research of Manson and Zaman (2001) on UK SAS 600 suggested that the provision of more information concerning the findings of the audit in the audit report would add more value and be able to meet the expectations of the users.

Since there is no evidence of differences in beliefs between auditors and users in Saudi Arabia about the duties and responsibilities assumed by auditors and the messages conveyed by audit reports. This thesis addresses this shortfall. The next chapter details the methodology of the study and development of the research instrument as well as giving some information about the subjects of this study and their demographical background.

Chapter Four

Methodology

4-1 Introduction:

Chapter Three provided evidence of widespread concerns that there is a gap between auditors' understanding of their function and the public expectations of the audit process. An "audit expectation gap" was defined to exist when there are differences in beliefs between auditors and the public about the duties and responsibilities assumed by auditors and the message(s) conveyed by the audit report (Monroe and Woodliff, 1994).

A three level framework for the expectation gap was developed in Chapter One. The first level concerns differences in attitudes about what auditors' duties and responsibilities should be. The second level reflects differences in beliefs about duties and responsibilities of auditors and the message(s) communicated through the audit report, while the third level arises when auditors fail to exercise due professional care.

The aim of this research was to investigate any differences between audit report preparers (the auditors group) and the beliefs (the preparers and users of financial statements) as to their beliefs about what messages are currently being conveyed via the unqualified audit report as well as opinions on the usefulness of modifying the wording in such a document by adding some additional matters to be reported upon by auditors to improve

communication in such a document (Level 2 of the expectation gap). Therefore, a research instrument was needed that measured such objectives.

Thus, the remainder of this chapter is organised as follows: first, section 4-2 will describe the research design. Next, section 4-3 will provide the rationales and justifications of the reasons why a survey instrument (questionnaire) was chosen as the research method. Sections 4-4 and 4-5 aimed at describing the development of the research instrument as well as the pilot study. Sections 4-6 and 4-7 of this chapter relates to the distribution of the research instrument and sections 4-8 and 4-9 provide some factual information on the subject groups as well as data analysis techniques.

4-2 The Research Design:

Previous empirical research, as seen in chapter three used two main strategies to investigate the usefulness of the audit report and the existence of an audit expectation gap. These are survey research and experimental laboratory research. Since the aim of this research was an investigation of the existence of the expectation gap within the current unqualified audit report in use in Saudi Arabia, it was thought that experimental laboratory techniques would be unsuitable to such tasks, lacking the necessary external validity. A better appreciation of the gap could be explored by accessing the subjects' response to the concepts in general rather than their response to artificial situations or tasks. For these reasons, this research used a survey design using cross-sectional survey methodology. Moreover, this research is descriptive in the sense that Best (1970, p.113) indicated when he said that

descriptive study is concerned with “conditions or relationships that exist, practices that prevail, beliefs, points of views; or attitudes that are held, processes that are going on, effects that are being felt; or trends that are developing”.

Additionally, this study is policy-oriented in that it intends to provide policymakers with specific recommendations, based on empirical evidence, in relation to the existence of an audit expectation gap in Saudi Arabia and the usefulness of going beyond such a document (Majchrzak, 1984). Nisbet (1997, p.212), in an attempt to define policy-oriented research suggested: “researchers undertake systematic procedures, such as surveys, to enable policymakers to base their decisions on evidence rather than on prejudice or guesswork”.

The term ‘survey’ implies, as suggested by Borg and Gall (1996, p.289) “collecting data from participants in a sample about their characteristics, experiences, and opinions in order to generalize the findings to a population that the sample is intended to represent”. Moser and Kalton (1971), on the other hand, indicate that the purpose of conducting surveys is to describe a social phenomenon and/or to explain relationships between a number of variables.

4-3 Choice of Self-Completion Questionnaire as the Research Instrument:

The self-completion questionnaire which is sometimes referred to as a self-administration questionnaire (Bryman, 2001) was chosen as the research method for collecting data. Using such a questionnaire as the method for collecting data gives respondents more time to consider their answers. Furthermore, Mason and Bramble (1979, p. 301) has stated that it has the merit of increasing the generality of data and ensuring a greater level of veracity in the respondents' answers. Other advantages of this method include the following (Bryman, 2001, p.129; Oppenheim, 2000, p.102; Nachmias and Nachmias, 1996, p. 225).

- It is cheaper than the technique of the interview.
- It covers a large number of samples.
- It guarantees respondent anonymity.
- Each respondent will receive and be exposed to the same questions and instructions.
- It avoids bias by interviewer.
- It is a quicker way of getting the questionnaire to the respondents.

The questionnaire survey, however, has its limitations (Bryman, 2001, p.129; Oppenheim, 2000, p.102; Nachmias and Nachmias, 1996, p. 225). The first limitation of the questionnaire survey is related to the fact that one cannot be sure who has completed the questionnaire. A further disadvantage is the possibility of a low response rate, particularly when respondents have no special interest in the subject of the questionnaire. This problem was

attended to and minimised in this research by directing the questionnaire to individuals who were assumed to have an interest in the subject (see section 4-7). The success of this strategy is reflected in the relatively good response rate obtained. Another disadvantage of the questionnaire survey is associated with the questionnaire format which carries the danger of restricting the quality and the depth of the information provided. The questionnaire also provides no opportunity to clarify questions or to overcome any unwillingness to answer particular question. These two limitations were tackled by adopting various processes in the questionnaire design stage, process which included the review of the initial questionnaire by experienced academic staff and by conducting the pilot study (see section 4-5).

4-4 Development of the Research Instrument:

A key objective of this thesis was the development of a reliable and valid research instrument (questionnaire) with which to achieve the research objectives. It was especially important for a study to be conducted in Saudi Arabia where the collection of such data is new and where no such data collection instrument exists. As a result, the researcher sees the development of reliable and valid instrument measures the research objectives to be an important task for his study. To achieve such a task, the researcher had to undertake a number of processes conducive to the development and validation of such an instrument. These processes are as follows: -

- Choice of a scaling procedure to measure beliefs about the meaning in the audit report;
- Identifying the frame of reference;

- Identifying conceptual dimensions under which the researcher can generate a number of scales or variables;
- Generating scales or items under each of the identified conceptual dimensions;
- Collecting data from a pilot study to purify the developed instrument, using the Cronbach alpha approach (Cronbach, 1951);
- Collecting data required by this study, via the research instrument; and
- Evaluating the reliability, dimensionality, and validity of the scales tackled by the current research.

4-4-1 Choice of a Scaling Procedure

A number of methods have been advanced to measure beliefs (Burton, 2000; Oppenheim, 2000). While these methods all used the questionnaire technique, they differ in the way the scales are constructed and used. An overview of the study topic that featured in the literature review in the previous chapter, (section 3-5) in relation to their research instruments, shows that the first type of these studies used the Likert Scales (e.g., Holt and Moizer, 1990; Hatherly et al, 1991, 1992, 1998; King and Higson, 1994; Innes et al 1997; Manson and Zaman, 2001 and McEnroe and Martens 2001) and the second type from amongst the studies used semantic differential scales (e.g. Houghton and Messier 1990; Monroe and Woodliff, 1993, 1994; Schelluch, 1996; Gay et al, 1998 and Best et al 2001). The question which arises here is closely related: Which scales procedure should be used for this study taking in consideration the context of the research (Saudi Arabia)?.

Osgood *et al.* (1957) developed an instrument to investigate the underlying structure of words. The technique, the semantic differential, has been successfully adopted to measure belief (Houghton and Messier 1991; Monroe and Woodliff, 1994; Schelluch, 1996). This measurement tool is a pairing of bipolar adjectives (e.g., good-bad) interspersed by several spaces. Subjects are given a concept along with several pairs of bipolar adjectives and are instructed to tick space between the adjectives that best describe the concept in relation to that set of graduated antonyms.

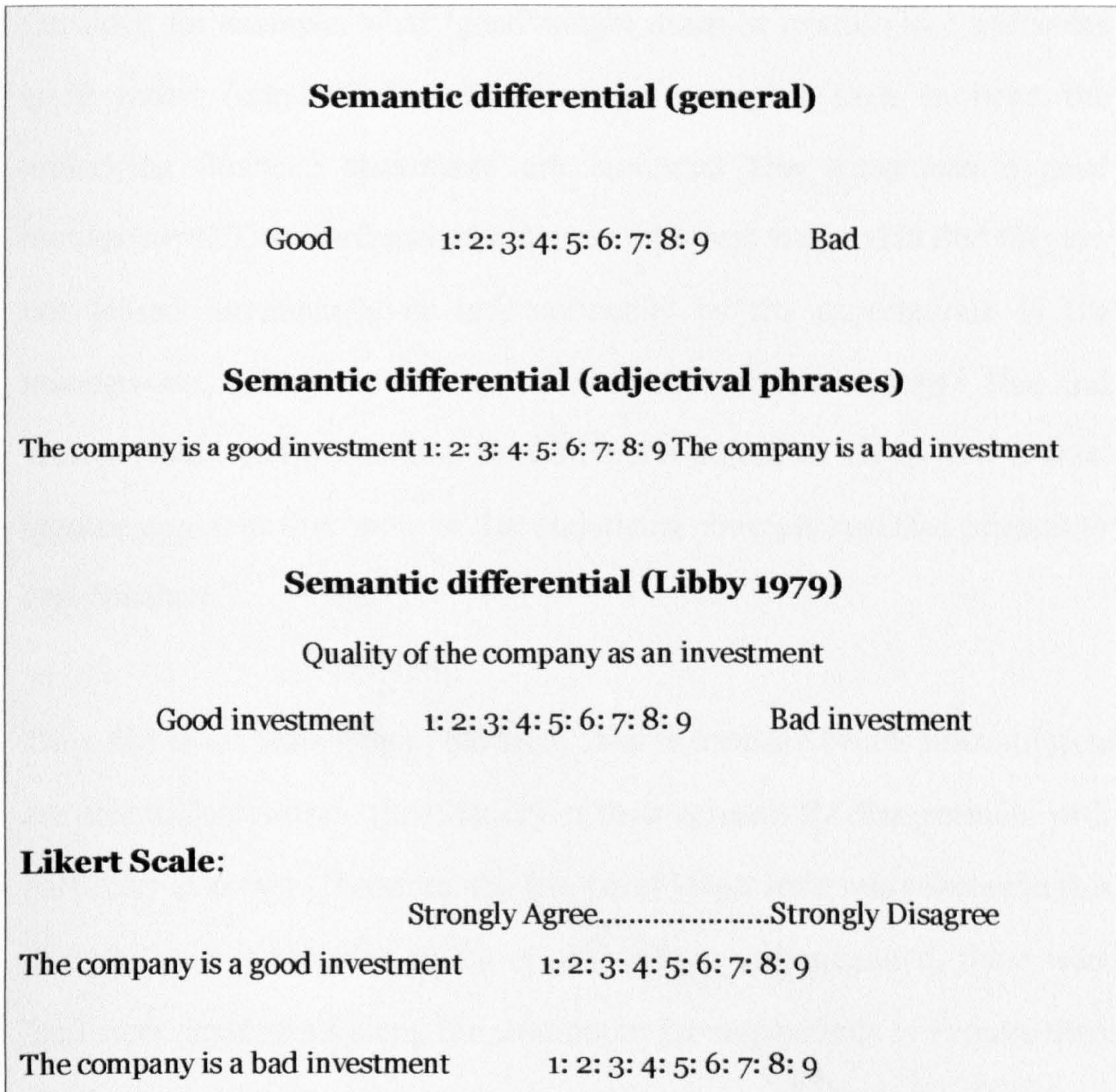
The semantic differential has achieved widespread acceptance and, as revealed in Chapter Three, has been used in most of the studies into the measurement of meaning in auditing. Houghton and Messier (1991), for example examined the impact of wording changes on the meaning of standard form audit reports. They used Osgood *et al.*'s semantic differential methodology adopted for accounting by Haried (1972,1973) and enhanced by Houghton (1987a, 1987b, 1988, 1998).

The semantic differential approach has also been used to measure perceptions about the messages communicated through audit reports. Both Libby (1979) and Bailey *et al.* (1983) incorporated semantic differential scales in their investigations. In these studies, subjects were asked to rate different audit reports on a variety of attributes. Adjectival phrases were used as the anchor points in contrast to the more general semantic differential which utilises adjectives. The attributes had numerical rating scales such as "poor investment/ good investment" (Libby) and "do not present fairly/ present fairly"(Bailey *et al.*).

Figure 4.1 demonstrates the difference between the general semantic differential scale using bipolar adjectives, a semantic differential utilising bipolar adjectival phrases and the approach taken by Libby and Bailey *et al.*, the attribute being investigated is the quality of the company as a good investment. The semantic differential presents bipolar adjectives/adjectival phrases, and subjects are required to mark the scale at the point that best describes the concept in relation to that set of antonyms. As explained in the next section the general adjective scale “good/ bad” does not relate to the concept (investment quality) being investigated and was unsuitable for the study. Libby presented the attribute and then required a response on a rating scale labelled with adjectival phrases. As can be seen, the two different approaches utilising adjectival phrases are very similar.

These semantic differential scales are similar to the Likert type scales used in the majority of the other studies reviewed (e.g., Holt and Moizer ,1990; Hatherly et al 1991,1992; Gay and Schelluch, 1993; and Innes et al ,1997; Manson and Zaman, 2001). For Likert type scales, subjects are asked to read a statement and respond with degrees of agreement or disagreement. Thus, intensity of beliefs are captured on a numerical rating scales anchored (usually) by strongly agree/ strongly disagrees. The modified semantic differentials of Libby and Bailey *et al.* could be separated into one (or two) Likert type scales. Use of a Likert scale to determine subjects’ beliefs about the quality of the company as a good investment is also shown in **Figure 4.1**.

Figure: 4.1
Alternative questionnaire scales (quality of the company as a good investment)



Any of the bottom three approaches illustrated in the **Figure 4.1** should elicit the same response with respect to beliefs concerning investment quality of the entity communicated through a particular audit report. Although, as Menezes and Elbert (1979) indicated, the results of Likert and semantic differential scaling did not produce materially different conclusions (quoted from Holt and Moizer ,1990).

On the other hand, in Osgood et al's approach there comes the use of bipolar adjectives to elicit responses to concepts. However, adjectival pairings such as "good- bad" have no clear meaning in relation to certain concepts. Consider, for example, what "good" might mean in relation to a particular audit report (unqualified audit report as example). Does it mean the underlying financial statements are accurate? The entity has a good management? That the financial statement numbers are good in that they are not biased intentionally or unintentionally by the expectations of the management, or any one of a myriad of other possible meanings? Holt and Moizer (1990, p.113) intended to use bipolar adjectival scales "but it soon became apparent that some of the underlying concepts required phrases to describe them".

Thus, the Likert scale type would seem ideal to measure beliefs since subjects are able to demonstrate the intensity of their agreement/ disagreement with particular assertion. Therefore, the five-point Likert scale was selected in this study because it provides, as Co *et al* (1998, p. 92) suggested, there were "sufficient alternatives along the continuum for respondents to express their opinion".

4-4-2 Frame of Reference

To measure the message(s) communicated in the audit report, it is necessary to provide the subject with an audit report. Both Bailey et al (1982) and Estes (1982) point out that it is hard to separate the information in the audit report from the information presented in the financial statement and footnotes. To isolate the effects of information conveyed in the audit report from the rest of

information, they suggested either comparing reaction to unaudited and audited financial statements or obtaining reaction to information sets consisting of identical financial statements accompanied by different audit reports. The focus of this study however, is on the message communicated by the unqualified audit reports, not the influence of audit reports in decision-making. An alternative suggestion of using financial statements is to present the audit reports in a context free frame of reference where subjects are not provided with any information about the client or the auditor.

The most obvious problem with including financial statements is that the information in the reports may influence the response when what are at issue are the messages communicated in the audit report. A question could arise as to whether the message was being sent by the financial statements (by management of the company) or the audit opinion (auditors). Furthermore, to be realistic the instrument would become very long, thus reducing the likelihood of completion. The only study to utilise such an approach appears to be that of Robertson (1988) whose response rate after second mailing was only 17.6%.

An alternative to a full set of financial statements is to provide a description of the type of the company being audited. This approach was adopted by Libby (1979), Bailey et al. (1983) and Nair and Rittenberg (1987). For Nair and Rittenberge, the provision of such information was necessary, given their interest in other forms of communication like compilations, reviews and the identity of the auditors. Yet again, however, the possibility of influencing the responses is introduced.

Other studies have adopted a context free-frame of reference. Miller et al (1993) for example, point out that audit opinion should convey a basic underlying message regardless of specific financial statements attached. Studies such as this thesis, which investigate the message(s) communicated in audit report as well as added additional matter to such a document, have invariably used free form of context framework. For example, both Kelly and Mohrweis (1989) and Gay and Schelluch (1993) assert that such an approach is necessary to minimise confounding effects and potential biasing of results. It was therefore decided to adopt a context free frame of reference.

Thus, the research instrument of this thesis contained a copy of unqualified audit report in use in Saudi Arabia. A similar approach although, was successfully adopted by Schelluch (1996), Manson and Zaman (2001), and Best et al (2001). A copy of the audit report was illustrated in Chapter Two and also, provided with the research instrument in Appendix D.

4-4-3 Scales Development

This subsection is an attempt to achieve an accurate identification of the conceptual dimensions under which one can generate a number of scales or variables. The subsequent task is to generate scales or items under each of these identified dimensions.

4-4-3-1 Message scales (statements):

The review of the professional and academic literature in Chapter Three resulted in twenty-eight main scales that measured the message(s) that may (or may not) be perceived to be communicated in the audit report. These

twenty eight scales were developed from the work of Higson (1991), King and Higson (1994), Monroe and Woodliff (1993, 1994), Schelluch (1996), Gay et al (1998) Hatherly *et al* (1991, 1992, 1998) and Innes et al (1997). The justification for use of such existing scales or attributes is because, as seen in Chapter Two and, as Al-Rehaily (1992) points out, an analysis of auditing standards in Saudi Arabia has revealed that they are similar to those of the UK and the US. To establish the point further, according to Aba-Alkhail (2001) the recent survey about policy-making in Saudi Arabia carried out by the Accounting Journal (January 1999, p. 11) shows that there is no major difference between national (Saudi) accounting and auditing standards and US standards.

However, as has been shown in Chapter Three, Hatherly *et al* (1991, 1992) have undertaken detailed analysis of those attributes incorporated into other studies that measured the message communicated in the audit report (e.g. Libby, 1979; Bailey et al, 1983; Nair and Rittenberge, 1987; Robertson, 1988; and Holt and Moizer, 1990). Hatherly et al (1991; 1992) also looked at theoretical studies as Mautz and Sharaf (1961) and Lee (1986). Their analysis concluded that the attributes could be categorised as belonging to 18 dimensions. Hatherly et al (1991, 1992), however, did not cover dimensions (scales) such as fraud and error, which are included in this study. Based on these works, the following are the statements that are covered by this thesis to investigate the message(s) that are intended or not intended to be communicated through the audit report. Each of these scales (statements) have appeared in the literature at least two or three times.

Table 4-1**List of the conceptualised message(s) dimensions and their associated scales**

Dimension	Question
A: Nature of auditor's work and his responsibilities	
Verifying the financial statements.	The auditor has verified the data in the financial statements.
Detecting fraud	The auditor is responsible for detecting all fraud.
Prevention of fraud	The auditor is responsible for preventing fraud.
Internal control	The auditor is responsible for soundness of the internal control structure of the entity.
Proper accounting records	The auditor is responsible for maintaining accounting records
Conflict between management/ auditors	The auditor agrees with accounting policies used in the financial statement.
Management/ auditor responsibility (producing financial statements)	The auditor is responsible for producing the financial statements.
Auditor's judgment	The auditor exercises judgment in selection of audit procedures
Extent of audit work	The extent of audit work performed is clearly communicated.
Extent of assurance	The extent of assurance given by auditor is clearly indicated.
Auditor's integrity, independence	The auditor is unbiased and objective.
B: Reliability of the financial statements	
Error freedom	The financial statements are free from error.
Fraud freedom	The financial statements are free from fraud
Bias freedom	The financial statements are free from bias.
Present fairly	The financial statements are presented fairly.

Material Misstatements	Users can have absolute assurance that the financial statements contain no material misstatements.
Decision usefulness	The audited financial statements are useful for making decision.
Performance monitoring	The audited financial statements are useful for monitoring the performance of the entity.
Credibility	The inclusion of an audit report enhances the credibility of the financial statements.
Specific versus whole	The audit report is attached to the financial statement as a whole and not to any specific items or group of items.
Satisfaction	The auditor is satisfied with the financial statements.
C: Efficiency of the entity management	
Management of the entity	The entity is well managed.
Entity efficiency.	The entity is run efficiently.
Investment/ disinvestments	The entity is a good investment.
Illegal acts	The entity is free from illegal acts.
Riskiness/ viability of the entity.	The entity is a going concern
D: General	
Purpose of audit	The purpose of the audit is clearly communicated in the audit report.
Readability	The audit report is readable.

4-4-3-2 Extension of audit report scales (statements):

Hatherly (1997, p.192) mentioned that developments in audit reporting would be necessary in respect of reporting on internal control and information included in the annual report but outside the financial

statements. He also discussed the adoption of free form reporting as a possible interrelated development for the future of traditional reporting functions in the financial statements. Manson and Zaman (2001) is the only study which addressed issues similar to that of this study. Their study, however, did not cover issues such as this adoption of the free form report and audit of graphs which have been covered by this study. Sixteen proposals or statements have been proposed as 'useful' to be reported by auditors as shown in **Table 4-2**.

Table 4-2
List of the conceptualised development dimensions and their associated scales

Dimension	Question
A: General	
	The information conveyed in the current audit report meets user needs.
	The auditor should give more information in the audit report.
B: Going concern and fraud or illegal acts:	
Going Concern	In future, there should be an explicit statement in the audit report of the auditors' assessment of going concern status of the client.
Fraud and illegal acts	In future, there should be an explicit statement in the audit report of the auditors' findings in relation to fraud or illegal acts
C: Non-financial information in annual report:	
The Chairman's Statement	How strongly do you agree that it would be useful for auditors to indicate in the audit report the extent of their examination of The

	Chairman's Statement?
The Director's Report	How strongly do you agree that it would be useful for auditors to indicate in the audit report the extent of their examination of The Director's Report?
Other information included in the annual report but outside the financial statements.	How strongly do you agree that it would be useful for auditors to indicate in the audit report the extent of their examination of any other information included in the annual report but outside the financial statements?
D: Internal control and materiality	
The scope of auditors' study of the client's internal controls.	How strongly do you agree that the value of audit would be enhanced if the auditors reported in the audit report the scope of their study of the client's internal controls?
The extent to which auditors relied on the internal controls.	How strongly do you agree that the value of audit would be enhanced if the auditors reported in the audit report, The extent to which they relied on the internal controls?
The materiality level that auditors used.	How strongly do you agree that the value of audit would be enhanced if the auditors reported in the audit report the materiality level they used?
E: Issues arising during the audit	
Issues arising during the audit	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
F: Free form report	
Usefulness of the free form report to convey more information to users of the	The non-standard wording report form would increase the amount of information conveyed to the users of the financial statements.

financial statements	
Usefulness of the free form report to increase the user's of the financial statements ability to evaluate the audited entity's exposure to risk.	The non-standard wording report form would increase the user's ability to evaluate the audited entity's exposure to risk.
Usefulness of the free form report to increase the user's of the financial statements understanding of auditor's role.	The non-standard wording report form would increase the user's understanding of the role of the auditor.
G: Graphs	
Use of Graphs	The use of graphs in an audit report make it more understandable.
Expansion the auditor's Role to audit graphs	The auditor's role should be expanded to include auditing the graphs.

Having developed conceptualised dimensions and their associated scales for the research instrument, the next step, as stated earlier, was to collect data from a pilot study to ensure that the wording of the 28 scales that measure the message(s) that may (or may not) be communicated in the audit report as well as the 16 scales (statements) that are proposed to be useful when reported upon by auditors, was clear to the participants and to gauge the internal consistency of the instrument using the Cronbach alpha approach (Cronbach, 1951).

Details on the pilot study will be presented in Section 4-5 below. Thus, as we can see in **Tables 4-5 and 4-6**, each item in the research instrument was

measured by using a five-point Likert scale (1 = strongly disagree, 2 = disagree, 3 = neutral, 4 = agree, and 5 = strongly agree).

The 28 scales that measure the messages shown in **Table 4-5** were listed, as can be seen, in random order, before being forwarded to the members of the pilot study. The 16 scales (statements) that are proposed to be useful if reported by auditors are listed in **Table 4-6**.

4-5 The Pilot Study: Translating, Pre-testing and Administering the Pilot Instrument:

The importance of the pre-testing of mail survey is very well recognised in the literature. The pre-testing and pilot study are conducted prior to the final distribution of the questionnaire to the target population. The processes are used to refine the instrument design and to identify errors in the research instrument that may only be apparent to the population concerned (Nachmias and Nachmias, 1996; Mulhern and Rae, 1998; Oppenheim, 2000; Bryman, 2001). At the beginning of March 2002, the researcher started to translate the research instrument into Arabic, as it is the official and predominant language in Saudi Arabia. Then the final draft of the translated questionnaire was given to some members of the faculty of the Arabic and English languages departments in the Colleges of Arabic Language and Social science at Umm Al-Qura University in Saudi Arabia. After corrections were made the research instrument was then ready for pilot testing.

The pilot study was undertaken in two phases, the first one was conducted when the researcher had the opportunity to attend the Ninth National Conference for Development Accounting in Saudi Arabia, which was hosted by the University of King Saud at Riyadh from Tuesday 2nd to Wednesday 3rd of April 2002. At this conference, both the original instrument and the Arabic version were passed to some accounting and auditing professors to have them review and judge them. The researcher had explained the objectives of the study to them and had asked them to comment on the validity of the questionnaire as well as to check for accuracy of the translation and simplicity of the questions. Generally speaking, there were no major criticisms or comments about the pilot questionnaire except for some minor recommendations concerning the layout. This added confidence that the questions were quite appropriate.

Having developed and pre-tested the research instrument, the next step was to collect data from a pilot study to ensure that the wording of the instrument was clear to the real samples and to measure the reliability of the instrument by gauging the internal consistency of the instrument using the most common statistical measure of internal consistency which is the Cronbach alpha (Bryman, 2001; Bryman and Cromer, 2001; Huck and Cormier, 1996).

4-5-1 Administrations of the Questionnaires for the Pilot Study:

A total of 50 questionnaires were distributed to the sample of the pilot study (20 questionnaire to the Auditors group , 20 questionnaire to the users group and 10 questionnaires to the preparers group) because of the time limit, these

50 questionnaires were distributed by drop-off and pick-up methods. For the users sample the researcher had the opportunity to attend the meeting of the general assembly of one of the largest corporations in the agricultural sector in Saudi Arabia namely, the National Agricultural Development Co. (NADC). This meeting was held at Riyadh Chamber of Commerce and Industry. There were about 60 people and the researcher was able to distribute 20 questionnaires. The respondents were given stamped, self-addressed envelopes to return the questionnaires or fax them to the fax number provided. Only seven questionnaires were returned, five of which were given to the researcher directly after the meeting and two were posted or faxed to the researcher. For the auditors, sample the researcher had distributed twenty questionnaires to the partners of some of the big firms in Saudi Arabia and a total of sixteen questionnaires were completed and returned back. For the preparers sample, ten questionnaires were distributed. Five of them were handed direct to the financial directors or their nominees of some Saudi corporations chosen by the researcher (those are NADC, The Saudi British Bank, Makkah Real-estate Co., Saudi Ceramic Co. and the National Gypsum Co.). The remaining five questionnaires were faxed to the financial directors of some of Saudi corporations directly after a telephone arrangement (those are Tabuk Agricultural Development Co., Jizan Agricultural Development Co., Bisha Agricultural development Co, Hail Agricultural Development Co., and Taibah Real-estate). The researcher received just two questionnaires of such faxed questionnaires. Thus, the total response rate of the financial directors is six questionnaires.

After two weeks, (by 23 of April 2002) and as a result of a daily follow up, the researcher was able to collect 29 of the 50 questionnaires which had been distributed to the members of the pilot study. (See table 4-7 for the response rate of the pilot study).

4-5-2 Reliability of the Research Instrument:

Reliability refers to the consistency of a measure of a concept (Bryman, 2001, p. 70). There are a least two different meaning of the term. These are:

- a) **Stability:** this entails asking whether a measure is stable over time, so that we can be confident that the results relating to the measure for a sample of respondents do not fluctuate (Bryman, 2001, p.70). This means that, if we administer a measure to a group and then re-administer it, there will be little variation over time in the results obtained. The most obvious way of testing the stability of a measure is the '*test-retest*' method. This involves administrating the research instrument on one occasion and then re-administrating it to the same sample on another occasion. Giving the large number of issues covered in the research instrument used in this research however, and its length, the researcher found it is difficult or 'impossible' to ask several questions about every dimension covered by the research instrument. In addition, applying a test-retest method to the results was very difficult since the research instrument is very long (44 statements or dimensions) made it inappropriate to ask the respondent to fill in the same questionnaire again. Also, the most problem of using this approach to evaluate the instrument reliability is that respondent answer to the administration instrument influence how they reply at

the re- administration instrument (Bryman, 2001, p.70). This means that respondent may using their memory rather than re-answering the questions, and the difficulty of interpreting different answers to the same question by the same respondent.

b) Internal Reliability: internal consistency methods of measuring reliability, such as the spilt-halves method and the Cronbach's Alpha method, can be used with the questionnaire where an issue is measured by more than one question (Bryman, 2001). This technique uses repeated measurements (of the parts of the questionnaire) to assess the relationship between these various parts. "To the extent that these parts "hung tighter" and measure the same thing, the full instrument is said to possess high internal consistency reliability" (Huck and Cormier, 1996). Cronbach's alpha takes a value between zero to one where one indicate perfect correlation between parts of the instrument. While there is no test of significance for the alpha, the literature suggests .70 as an acceptable level (Huck and Cormier, 1996). This however, does not perfectly applies to the questionnaire in this study, where questions don not measure precisely the same thing (e.g. respondent might agree on some of the message and disagree on others and yet still be reliable).

However, the researcher made the assumption that the questions in each section of the research instrument related to the same factor, for example the 28 statements that measuring the message communicated in the unqualified audit report are related to each other in some way which here is the message.

These relations between variables can be measured however, by assessing the factorial reliability or dimensionality of the variables which cannot be assessed here due to the small sample of the respondents (29 respondents out of 50 questionnaires distributed)

Table 4.3
The amount of the overall alpha for each part of the research instrument

Instrument parts	Subjects	Alpha
I	The belief about the message(s) that may (or may not) be communicated in the unqualified audit report.	0.84
II	The belief about the usefulness of adding some matters to be reported upon by auditors.	0.93

Thus, the reliability has been measured by applying the Cronbach's Alpha test to each section of the instrument. **Table 4-3** reports the amounts of the Cronbach alpha for each part of the questionnaire; a similar approach has been adopted by McEnrone and Martens (2001) who obtained an alpha amount of 0.86 by computing the alpha test for the same questions for all the respondents.

As can be seen from the table, it shows a relatively high amount of internal consistency. The overall alpha for each part of the questionnaire comfortably

exceeds the rule of thumb cut-off of 0.70, at 0.84 and 0.93. This is an indication that the instrument is reliable (Huck and Cormier, 1996). The researcher believes that this was the best possible method for assessing the reliability and the results of the reliability results are satisfactory. Having ensured that our instrument was reliable, we had to forward our final version of this data collection tool to the subject members of this study for the purpose of collecting the study data.

4-6 The Final Research Instrument:

The final research instrument (questionnaire) layout included a front page and the questions. The front page included cover letter and guidelines for completion of the questionnaire. The cover letter included the name of the researcher and an appreciation of help and an assurance of the confidentiality of responses. The guidelines for completion of the questionnaire showed the number of sections, and informed the subjects that we were interested in their belief and that there is no correct or incorrect response. They were instructed to indicate the extent of their agreement or disagreement with each of the instrument statements in terms of intensity of their feeling, by ticking the box of the scale that best characterised their beliefs.

The questionnaire was divided into two sections as shown in **Table 4-4**. The second section (B) included two parts and the first section (A) contained the demographics. The second section of the final research instrument comprised two parts as mentioned earlier. The first (Part I) was designed to measure beliefs about the message conveyed in the unqualified audit report (Level 2 of

the audit expectation gap) while Part II dealt with belief (agreement) about the usefulness of add additional matters to be reported upon by auditors.

Table 4-4
Subjects covered in the questionnaire

Section	Part	Subjects
A	A	Demographics Data
B	I	The belief about the message(s) that may (or may not) communicated in the unqualified audit report.
	II	The belief about the usefulness of adding some matters to be reported upon by auditors.

One version of the research instrument was used for each of the three subject groups participant in this study. The instruction to part I informed the subjects that we were interested in their belief about the message conveyed in the unqualified audit report attached as explained in the covering letter. They were instructed to read it carefully and then to indicate the extent of their agreement or disagreement with each of the 28 statements in terms of intensity of their feeling, by ticking the box of the scale that best characterised their beliefs. As can be seen from the **table 4-5** as an internal validity check, some statements were positive and others negative in form.

Table 4-5**The 28 statements that measuring the message (s) that conveyed
in the unqualified audit report**

No	Statement	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
1	The auditor has verified the data in the financial statements.					
2	The financial statements are free from fraud.					
3	The entity is a good investment.					
4	The entity is run efficiently.					
5	The financial statements are free from bias.					
6	The entity is a going concern.					
7	The financial statements are free from error.					
8	The auditor is satisfied with the financial statements.					
9	The auditor is responsible for detecting all fraud.					
10	The auditor is responsible for the soundness of the internal control structure of the entity.					
11	The auditor is responsible for maintaining accounting records.					
12	The auditor is not responsible for producing the financial statements.					
13	The auditor is not responsible for preventing fraud.					
14	The auditor is unbiased and objective.					
15	The auditor does not exercise judgment in the selection of auditor					

	procedures.					
16	Users can have absolute assurance that the financial statements are free from material misstatements.					
17	The auditor does not agree with the accounting policies used in the financial statements.					
18	The extent of assurance given by the auditor is clearly indicated.					
19	The financial statements presented fairly.					
20	The entity is free from illegal acts.					
21	The extent of audit work performed is clearly communicated.					
22	The audited financial statements are not useful in monitoring the performance of the entity.					
23	The audited financial statements are not useful for making decisions.					
24	The entity is well managed.					
25	The audit report attaches to the financial statements as a whole and not to any specific items or groups of items.					
26	The inclusion of an audit report enhances the credibility of the financial statements.					
27	The purpose of the audit is clearly communicated in the audit report.					
28	The audit report is readable.					

Part II of the research instrument was designed to measure beliefs (agreements) about the usefulness of adding some matters to be reported

upon by auditors. The instructions that accompanied this part stressed that here the concern was with belief about what an auditor might usefully report. Subjects were asked to read carefully a series of statements about some matters that would be useful if reported upon by auditors and offer their opinion by ticking the box on a five point Likert scale that best characterised the extent of their agreement/ disagreement with each statement. **Table 4-6** contains the Part II statements and the scales.

Table 4-6

The 16 statements that would be useful if reported by the auditor

No	Statement	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
1	The information conveyed in the current audit report meet user's needs.					
2	The auditor should give more information in the audit report.					
3	In future, there should be an explicit statement in the audit report of the auditor's assessment of going concern status of the client.					
4	In future, there should be an explicit statement in the audit report of the auditor's findings in relation to fraud or illegal acts.					
5	It would be useful for the auditor to indicate in the audit report the extent of their examination of:					
	a) The Chairman's Statement.					
	b) The Director's Report.					

	c) Any other information included in the annual report but outside the financial statements.					
6	The value of the audit would be enhanced if the auditor reported in the audit report in respect of each audit engagement:					
	a) The scope of their study of the client's internal controls.					
	b) The extent to which they relied on the internal controls.					
	c) The materiality level they used.					
7	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.					
8	The non-standard wording report form would increase the amount of information conveyed to the users of the financial statements.					
9	The non-standard wording report form would increase the user's ability to evaluate the audited company's exposure to risk.					
10	The non-standard wording report form would increase the user's understanding of the role of the auditor.					
11	The use of graphs in an audit report makes it more understandable.					
12	The auditor's role should be					

	expanded to include auditing the graphs.					
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4-7 Subjects Selection and Instrument Administration:

An audit report communicates the result of an audit to financial statement users. A number of financial statements users have been identified by various authoritative sources. The Saudi Financial Accounting Standards (1985) identified four user groups who accessed financial accounting information: current and expected investors; current and expected long term creditors; short term creditors and suppliers; and customers and employees.

The various empirical studies reviewed in Chapter Three used at least one type of user group in their expectation gap studies. Most studies included either auditors or accountants as representing audit report preparers. The expectation gap literatures typically refer to differences in beliefs between the users of the financial statements and the auditors. However, the empirical literatures have focused on the financial statement users such as analysts and bankers (Libby, 1979; Nair and Rittenberge, 1987; Kelly and Morwies, 1989; Miller et al, 1990; Holt and Moizer, 1990; Humphrey et al, 1993; Gay and Schelluch, 1993; Monroe and Woodliff, 1993, 1994; Schelluch, 1996; and Best et al, 2001). Some of the studies used other groups such as stockbrokers, financial directors, investment analysts, etc., to represent sophisticated users (e.g. Holt and Moizer, 1990; Humphrey et al, 1993; and Porter, 1993). While MBA students have been used as representatives of financial statements users as both investors and non- investors (Bailey et al, 1983; Kelly and

Mohrweis 1989; Hatherly et al, 1991, 1998; Gay and Schelluch, 1993 and Innes et al, 1997).

Similar to the approach taken by Manson and Zaman (2001), and considering the Saudi Arabian profession, this study included subjects from groups associated with preparation and use of audited financial statements, namely auditors, and preparers of the financial statements and the users of the financial statements. Thus, the aim of this section is to provide a summary which delineates the subject samples and an outline of the rationales for choosing them. The manner in which the questionnaires were to be distributed will be also addressed.

The researcher started his work by contacting and arranging an informal meeting with the General Secretary of the Saudi Organisation For Certified Public Accountants (SOCPA) Mr Yussof Al-Mubarak on Wed 15 of May 2002. The aim of this meeting was to collect primary data about the SOCPA and to determine the population of auditors. However, the outcome of the meeting was unforeseen boon to the research in that the SOCPA, thankfully, agreed to photocopy and distribute the questionnaires to their members. Also it was agreed that no follow up letters would be sent to non-respondents.

The target subjects' population, as mentioned above, included three groups involved in financial reporting:

- **The auditors group:** As seen in sub-section 2-5-1 in Chapter Two, according to the list issued by SOCPA, by 2001 there were 103 active audit firms with 209 partners. However, as mentioned previously, the questionnaires were distributed to the sample of auditors by the Saudi Organisation for Certified Accountants (SOCPA). In all 90, questionnaires were distributed to the sample of auditors at the General Meetings of SOCPA, meeting called to discuss a project for a new audit standard. These meetings were held at the three principal business centres of the Kingdom of Saudi Arabia - Al Khobar/Dammam, Jeddah and Riyadh. (Riyadh on Saturday 18-5-02, Jeddah on Sunday 19-5-02, and Dammam on Tuesday 21-5-02). The questionnaires were distributed together with a draft of the project to those in attendance. At the end of the discussion the General Secretary of the SOCPA introduced the researcher to those in attendance and gave him the opportunity to present his project. The General Secretary then called for the compliance of the attendees in completing and returning the questionnaires directly to the researcher by hand, by post or by fax. Those attending the meeting were auditors partners who are ultimately responsible for the audit report and more likely to have the necessary experience to reliably complete the questionnaire. However, some of those present mentioned that they had already completed the questionnaire when it was released in the form of the pilot study and they expressed their desire not to have to complete it

again. A total of 34 questionnaires were finally received from this group.

- **The preparers** (represented by financial directors of all the Saudi companies listed on the Saudi Stock Exchange). There are 68 registered public limited companies in Saudi Arabia that are listed in the Saudi Stock Exchange. The rationale for selecting this sample is based on the fact that these companies are required to comply with the GAAP and the financial directors or their nominees have the practical responsibility for the preparation of company financial statements. Thus, excluding non-listed companies ensured that the research would directly applicable to all respondents. The questionnaires were mailed to the group in this sample throughout the month of May 2002 excluding the ten companies that had participated in the pilot study. The addresses and telephone numbers of these companies have been obtained from the Guide to Saudi Corporations that was issued by the Saudi Share Registration Company (SSRC) in 2001. Preliminary work was done prior to the sending any questionnaire, in that the researcher made telephone calls to the financial directors of these companies. The aim here was to ensure that the addresses and fax numbers were correct as well as to ask them about their preferences for receiving the questionnaire either by fax or post. The mail was sent out on Saturday 11th May 2002. It consisted of a covering letter, a four page questionnaire and pre-stamped returned envelope. By the end of the first week, the percentage of returned instruments was not encouraging, so the researcher decided to undertaking the initiative of

making follow up telephone calls to those who had not returned their questionnaires. These follow up telephone calls were made in the second week of the data collection period. After two weeks and as a result of the unexpected low response rate from this mail survey, and because, as ascertained by Al-Ansari (1995, p.122), “postal services in Saudi Arabia are not reliable”, the researcher decided to re-distribute the questionnaires to this group by drop-off and pick-up method. Since almost all of these companies are located in the two major cities of Saudi Arabia (Riyadh and Jeddah), the researcher visited them personally. Companies that are located outside those two cities were contacted by telephone and the questionnaire was re-faxed to them if they stated that they wanted new ones. At the end of these efforts, the researcher was able to collect 23 questionnaires out of the 58 questionnaires distributed.

- **The users** (represented by individual investors (shareholders); financial analysts; credit managers and institutional investors)). The sample of this group was determined using the non-probability sampling techniques (Bryman, 2001; Oppenham, 2000; Zikmund, 2000). Due to the fact that, there was no way of knowing population and addresses of the individuals in this group, the distribution and collection of the questionnaires for the group were made in person. Every type of the respondent groups was visited at the place where they were expected to be working or residing. In these visits, the researcher always carried a good quantity of questionnaires in both Arabic and English and stamped, self-addressed envelopes.

Explanations of the process of distributing and collecting the questionnaires as well as rationale for the choice of such a group or individual can be summarised as follow:

❖ **The individual investors (shareholders):** shareholders form one of the major groups that will make use of audited financial statements. Currently, there are about one and a half million shareholders (1,395,577) holding an estimated 1.7 billion shares in the 68 companies listed on the stock exchange (as at the end of March 2001 (SSRC, 2001)). The shareholders in Saudi Arabia are restricted to only the Saudi nationals and citizens of the Gulf Cooperation Countries (GCC). The interests of this group of users in the audit report is based on the premise of wanting to maximise their wealth which could be adversely affected or inhibited due to information asymmetry arising from agency problems. The main places where one is able to find the individual investors are the central shares trading units within every commercial bank in Saudi Arabia. The researcher paid at least two visits to each one of these central shares trading units operated by the ten Saudi commercial banks. One visit was for the morning session of these rooms and the other for the evening session room in both the major cities of Saudi Arabia (Riyadh and Jeddah). Every room operates for two hours in each session. The researcher was, once again, aided most graciously when staff in the Operation Officer's room, thankfully, agreed that they could act as a point of distribution and collection for the completed questionnaires. The researcher also had the opportunity to attend the general assembly of two listed

corporations in Saudi Arabia, namely, the Food Products Co. and the National Gas Co. (both were being held at Riyadh Chamber). The share registries of these two companies offered yet more help in distributing and collecting the questionnaires from and to those shareholders who made contacts with the registrar. Finally, the researcher contacted a number of active investors who were known through other investors, bank officers, or friends. These efforts enabled the researcher to distribute sixty questionnaires to individual investors/shareholders who stated that they used and read companies' annual reports as well as the audit report when making their investment decision. In the process of distribution, more than seventy people stated that they did not use the annual reports in their investments decision for buying and selling shares. Most of them invest according to the direction of the prices in the market or according to advice from peers or friends. Therefore, they were excluded from participating in the survey. In the end, the researcher was able to collect thirty-five questionnaires.

- ❖ ***The financial analysts:*** There is no official record showing the actual number of this group in either operating or occupation in their qualifications. However, they known to work for or within banks. The researcher was able to distribute twenty questionnaires to the leading officers of financial analyses departments of the ten Saudi Commercial Banks and received back eight of them.
- ❖ ***Credit managers:*** The credit managers in the ten Saudi commercial bank constitute another group of users of the audited financial statements. These statements are used to help them in

assessing the ability of borrowers to repay their loans as well as service their interest charges. They therefore have to depend on the auditors to a large extent to provide them with credible and reliable information that will help them in their lending decision. All of these ten banks were contacted personally and the researcher was able to distribute 20 questionnaires and receive 13 of them.

❖ ***Institutional investors:*** There are nine equity funds operated by ten Saudi commercial banks. These equity funds play the role of the institutional investors in Saudi Arabia. However, these equity funds have just an 8% share of the total market (Riyadh Chamber, 1998). The researcher was able to distribute 20 questionnaires and received back four of them.

4-7-1 The Overall Response Rate

As the pilot study questionnaire included all the questions which were in the main survey, the responses from the pilot study were considered to be part of the overall responses and were included in the analysis. Therefore, 318 questionnaires were distributed for the pilot and main study and 146 questionnaires were returned. This gives a satisfactory overall response rate of 45.9 %. The highest response rate was from among users (47.8%) followed by auditors (45.4%) and lastly financial directors (preparers) (42.6%). **Table 4-7** indicates the number of responses received, in terms of sample concerned, and the percentage response rate.

As Jackson and Furnham (2000, p.78) suggested, “there is no universally acceptable response rate since it depends upon so many other factors” and

that “a response rate of less than 35 percent might be considered unacceptable”. The response rates presented in **Table 4.7** above are exceeding such a limit.

Table 4-7
The questionnaire distribution and response rate

The study	Pilot Study			Main Study			Total		
	Number issued	Number returns	% Of Returns	Number issued	Number returns	% Of Returns	Number issued	Number returns	% Of Returns
Auditor	20	16	80 %	90	34	37.8%	110	50	45.4%
Financial Directors	10	6	60%	58	23	39.6%	68	29	42.6%
Users	20	7	35 %	120	60	50%	140	67	47.8%
Total	50	29	58%	268	117	43.6%	318	146	45.9%

Previous studies with a similar population to that of this study however, for example, Manson and Zaman (2001) have achieved an over all response rate of 33%. Best et al (2001), in their study, achieved 32.3% out of 300 questionnaires distributed and Innes et al (1997), achieved 51%.

After discussion with his supervisor, the researcher then considered that the response rate of 45.9% was acceptable, bearing in mind the disadvantages of this kind of survey. Studies that have come to use this type of survey in Saudi Arabia have obtained similar response rates or less. One example of such as studies is that of At-Twaijri and Woodworth’s (1996), who wished to evaluate corporate mentoring in Saudi Arabia. They reported an overall response rate

of 36 percents and happened to comment that, “a response rate of 36 percent is considered excellent for surveys of this type in Saudi Arabia” (At-Twajiri and Woodworth, 1996, p.26).

4-8 Data Analysis Techniques:

In order to achieve the research objectives, a number of statistical techniques were applied to the data through the use of the Statistical Package for the Social Sciences (SPSS, version 10). These are:

4-8-1 Descriptive Statistical Analyses

Frequency tables, measures of central tendency (e.g. mean) and measures of dispersion (e.g. standard deviation) have been used to describe the result for each part of the questionnaire. The measures of central tendency are concerned with the location of the area where most of the data points are concentrated. The measures of dispersion are concerned with showing how different data-points are spread in the possible range. In this research the perception of the three groups about different statements regarding the message conveyed by the audit report can be detected by calculating the mean of the three groups. By calculating the standard deviation around the arithmetic mean, on the other hand the degree of dispersion can be detected.

4-8-2 Inferential Statistical Analysis

The purpose of conducting an Inferential Statistical Analysis (ISA) is to explain the extent to which our data can reflect the population characteristics out of which they were withdrawn. Thus, both parametric or non-parametric tests could be conducted. In our research, the objective of the statistical analysis is to test whether there exist statistically significant differences among the three groups. The selection of statistical test to be applied to the data (parametric or non-parametric tests) depends on many conditions (Bryman and Cramer, 2001; Dancey and Reidy, 2002; Pallant, 2001; Kinnear and Gay, 2001; Huck and Cormier 1996). According to Bryman (2001) some writers have argued that it is only appropriate to use parametric tests when the data fulfil the following three conditions:

- The level of scale of measurement is an equal interval or ratio scaling, i.e. more than ordinal.
- The distribution of the population is normal; and
- The variance of both variables is equal or homogenous.

In our research, the number of participant groups is three groups. The groups are independent of each other, and, their perceptions were measured on an ordinal scale. Parametric tests are based on the assumption that we know certain characteristics of the population from which the sample is drawn, while non-parametric tests (or distribution-free tests) are not (Bryman and Cramer, 2001). For this situation, since there are more than two independent groups in this research, the appropriate non-parametric statistical test to be applied to the data is called the Kruskal-Wallis One-Way Analysis of Variance

by Rank (KWA) commonly called Kruskal-Wallis H test. This statistical technique is designed to test whether the different independent samples under consideration come from the same or identical populations (Siegal and Castellan, 1988, p.206). The rejection of the null hypothesis means that there is a significant difference between, at least, one pair of the groups considered in the test. This test however, cannot determine which pair, or pair of groups have contributed the significant differences. To do that, a post hoc analysis would have to be performed in each pair of groups. One of these post hoc analyses is the LSD, Tukey-HSD and Scheffe test. It distinguishes multiple differences, comparing the differences in means between each group and produces the same type of pair-wise result as Chi-square T tests for significant differences between two groups (Zikmund, 2000). However, to do this (the chosen post hoc) test we should use ANOVA, a multidimensional statistical tool that enable comparative analysis between more than two groups. According to Bryman and Cramer (2001) some people have argued that the parametric tests should only be used on interval/ ratio data. Others, have reasoned that such a restricting is unnecessary and suggested that parametric tests can also be used with ordinal variable since tests apply to numbers and not to what those number signify (Lord 1953, quoted from Bryman and Cramer 2001; p. 117). In this view of controversy, it may be interesting to see whether the use of the parametric test ANOVA on an ordinal data gives very dissimilar results to that of Kruskal-Wallis. Identical results of the two statistical tests indicate that the data collected by this study is normally distributed. This will give us the right to use the parametric ANOVA instead of the non-parametric test, Kruskal-Wallis. This is because, as suggested by Siegel and Castellan (1988), the non-parametric test is about

95 per cent as powerful as the parametric test. This means that the ANOVA test requires 5 per cent fewer subjects than the Kruskal-Wallis test to reject the null hypothesis when it is false (Bryman and Cramer, 2001).

4-9 General Descriptive Analyses of the Subjects:

In the first section of the research instrument subjects were asked to respond to specific questions concerning their length of experience in the present occupation, their formal accounting education, and their accounting experience. **Tables 4-8**, and **4-9** below show the result of analysing these demographic data.

Table 4-8
The respondents' length of time at the present occupation

Group	Categories in years				Total
	1-5	6-10	11-15	15+	
Users	13 (19.4%)	24 (35.8%)	14 (20.9%)	16 (23.9%)	67 (100%)
Preparers	9 (31%)	11 (37.9%)	3 (10.3%)	6 (20.7%)	29 (100%)
Auditors	9 (18%)	10 (20%)	13 (26%)	18 (36%)	50 (100%)
Total	31 (21.2)	45 (30.8)	30 (20.5)	40 (27.5)	146 (100%)

Table 4-8 indicates that occupational experience was quite widespread. For example, the highest percentage of respondents (approximately 31%) were in the six-to-ten year range, with the remaining 69% falling into the over-15 year range (27.5%), the 1-5 year range (21.2%) and the 11-15 year range (20.5%). The majority of the auditors' sample is located in the over-15 years' category with 36%, whereas the majority of preparers' and users' samples are in the 6-10 years range category, showing approximately 38% and 36% respectively.

Table 4-9
The respondents' formal accounting education

Group	Accounting Degree					Total
	None	Diploma	Bachelors	Masters	Doctorate	
Users	30 (44.8%)	2 (3.0%)	27 (40.9%)	6 (9.1%)	1 (1.5%)	67 (100%)
Preparers	0	1 (3.4%)	26 (89.7%)	2 (6.9%)	0	29 (100%)
Auditors	0	0	44 (88%)	5 (10%)	1 (2%)	50 (100%)
Total	30 (20.5%)	3 (2.1%)	97 (66.9%)	13 (19%)	2 (1.4%)	146 (100%)

Table 4-9 shows the distributions of accounting educational qualifications while **Table 4-10** displays the accounting experience of the respondent. These levels of qualifications and experience appear to indicate that the respondent groups are well informed about the use of financial statements and the auditing process per se and thus any measure of difference as

evidence to assess if there is an existing expectations gap should be considered to be stronger and more reliable than if the respondents were largely inexperienced.

Table 4-10
The respondents' accounting experience

Group	Accounting Experience					Total
	None	1-5	6-10	11-15	15+	
Users	31 (47.7%)	8 (12.3%)	11 (16.9%)	3 (4.6%)	12 (18.5%)	65 (100%)
Preparers	0	2 (7.1%)	4 (14.3%)	11 (39.3%)	11 (39.3%)	28 (100%)
Auditors	0	3 (6.1%)	11 (22.4%)	10 (20.4%)	25 (51.0%)	49 (100%)
Total	31 (21.8%)	13 (9.2%)	26 (18.3%)	24 (16.9%)	48 (33.8%)	142 (100%)

To sum up, the results we have achieved from analysing the frequency and percentage distribution of the respondents' demographic data indicate that the auditors were characterised by more than 15 years of accounting and auditing experience, with a Bachelor's degree or higher in accounting. The preparers' group characteristics revealed that 80% of them have at least 15 years accounting experience with a Bachelor's degree in accounting.

Thus, since we ensured that the respondents in this study had considerable years of experience in their areas of expertise as well as having a good level of accounting experience combined with a good level of accounting education, this should enable them to provide experienced judgements on the issues in

the survey. It will be interesting now to see whether such respondents' backgrounds will have a significant impact on their perceptions towards messages that are (or are not) communicated in the unqualified audit report as well as proving useful for further issues to be reported by the auditor to improve communication in such a document. These will be presented in the next chapter.

4-10 Summary and Conclusion:

For the purpose of achieving our research objectives, the above chapter described the elements of the research methodology, instrumentation, subject groups, data collection, response rate, and the statistical tests applied to the data.

The key aim of this chapter was to develop a reliable and valid research instrument which would enable the researcher to assess the differences in the perceptions (beliefs) of the subject groups towards the message(s) communicated in the audit report and to assess their agreements (beliefs) toward added some additional matters that would be useful to be reported upon by auditors to improve communication in such a document.

Having developed the research instrument, the researcher then conducted a pilot study as the first step toward validation of the instrument. The results achieved from the pilot study indicated that the research instrument was reliable. Thus, the researcher forwarded the final version of the research instrument to subject groups.

Responses provided by the subjects participant to the 28 statements (scales) of the instrument that were used to measure the message communicated in the audit report as well as the 16 statements that set out to measure the usefulness matters to be adding to the unqualified audit report, were factor analysed to reduce them into underlying dimensions. The results that arose from factor analysis of these 44 items are revealed in the next chapter, Chapter Five: the Results. Thus, the next chapter will present the result achieved by this study.

5-1 Introduction:

The results achieved from conducting this study are presented in this chapter, and attempt to achieve the research objectives raised in this study. Chapter Six, the next chapter, we will discuss these results identified by the current study. The results in this chapter however, are presented in five sections as follows:

- Section One displays the results achieved from an analysis of the average ratings of respondents towards the message(s) that may or (may not) communicated in the unqualified audit report (analysing part I of the research instrument).
- Section Two set out the results achieved from analysing the average ratings of respondents' perceptions upon introducing additional material that could usefully be reported on by auditors (analysing part II of the research instrument).
- Section Three presents the results gained from analysing the dimensionality of the 28 statements concerning the message communicated in the unqualified audit report as well as the results realised from analysing the dimensionality of the 16 statements having the additional material that it would also be useful upon which to report.

- Section Four represents a disclosure of the results that come from analysing the differences in the perceptions of the three groups towards the 'messages' factors.
- Section Five displays the results attained from analysing the differences in the perceptions of the three groups towards the 'usefulness' factors.

5-2 The Results Achieved from Analysing The Average ratings of The Respondents Towards The Message(s) That are (or are not) Communicated in The Unqualified Audit Report:

In this section, we will see how the three groups that participated in the current study expressed their beliefs on the level of agreement to each of the 28 scales (statements) developed for this study concerning the message communicated in the unqualified audit report. Or, to put it another way, the researcher will set down in terms of average ratings the results achieved from analysing the 146 useable questionnaires received as they present themselves across the three groups (Users, Preparers and Auditors).

Table 5-1 below displays the average ratings of the perceptions of the respondents towards each of the 28 statements concerning the messages that are communicated in the unqualified audit report.

Table 5-1

Average ratings of participants towards the 28 items concerning the message(s) communicated in the unqualified audit report

The statements	Groups			F-test
	Users	Preparers	Auditors	
1- The auditor has verified the data in the financial statements.	4.0 (0.98)	4.1 (0.76)	4.3 (0.93)	1.02
2- The financial statements are free from fraud.	2.9 (1.2)	3.1 (1.5)	2.2 (1.0)	6.13**
3- The entity is a good investment.	3.5 (1.0)	3.7 (0.99)	3.6 (1.0)	0.52
4- The entity is run efficiently.	3.3 (1.1)	3.3 (1.1)	2.5 (0.98)	7.98***
5- The financial statements are free from bias.	4.1 (0.93)	4.4 (0.74)	4.5 (0.50)	5.75**
6- The entity is a going concern.	3.9 (1.1)	3.9 (1.2)	4.2 (0.73)	2.02
7- The financial statements are free from errors.	3.4 (1.1)	3.4 (1.1)	3.0 (1.2)	2.17
8- The auditor is satisfied with the financial statements.	3.7 (1.1)	3.4 (1.1)	3.4 (1.2)	1.01
9- The auditor is responsible for detecting all fraud.	3.0 (1.4)	2.2 (1.1)	1.4 (0.50)	29.00***
10- The auditor is responsible for the soundness of the internal control structure of the entity.	3.2 (1.3)	2.9 (1.3)	1.9 (0.89)	17.55***
11- The auditor is responsible for maintaining accounting records.	2.9 (1.3)	1.6 (0.61)	1.5 (0.50)	32.75***
12- The auditor is responsible for producing the financial statements.	2.3 (1.2)	1.5 (0.51)	1.4 (0.50)	11.52***

13 -The auditor is responsible for preventing fraud.	3.1 (1.3)	2.5 (1.3)	1.8 (0.90)	17.43***
14 -The auditor is unbiased and objective.	4.1 (0.92)	4.3 (0.70)	4.6 (0.70)	5.84**
15 -The auditor exercises judgment in the selection of audit procedures.	2.6 (1.1)	4.1 (0.56)	4.4 (0.49)	68.9***
16 -Users can have absolute assurance that the financial statements are free from material misstatements.	3.6 (1.1)	3.8 (1.1)	3.7 (1.1)	0.055
17 -The auditor agrees with the accounting polices used in the financial statements.	3.7 (1.1)	3.9 (1.0)	4.0 (1.0)	1.69
18 -The extent of assurance given by the auditor is clearly indicated.	3.8 (0.99)	4.1 (0.96)	4.2 (0.78)	3.09*
19 -The financial statements are presented fairly.	3.9 (0.96)	3.4 (0.80)	4.4 (0.70)	4.54*
20 -The entity is free from illegal acts.	2.8 (1.1)	2.9 (1.3)	2.2 (1.1)	5.30**
21 -The extent of the audit work performed is clearly communicated.	3.6 (1.0)	3.9 (1.1)	3.5 (1.2)	0.37
22 -The audited financial statements are useful in monitoring the performance of the entity.	3.8 (0.80)	3.7 (0.88)	3.5 (1.1)	1.20
23 -The audited financial statements are useful for making decisions.	3.8 (0.85)	3.7 (1.1)	4.0 (0.81)	0.87

24 -The entity is well managed.	3.3 (0.95)	3.4 (1.0)	2.7 (0.99)	6.87***
25 -The audit report attaches to the financial statements as a whole and not to any specific item or groups of items.	4.0 (0.85)	4.2 (0.78)	4.5 (0.54)	6.25**
26 -The inclusion of an audit report enhances the credibility of the financial statements.	4.3 (0.83)	4.3 (0.80)	4.6 (0.76)	1.72
27 -The purpose of the audit is clearly communicated in the audit report.	3.9 (0.96)	4.2 (0.66)	4.3 (0.84)	2.34
28 -The audit report is readable.	4.0 (0.61)	4.1 (0.62)	4.2 (0.91)	0.86
* P < 0.05 ** P < 0.01 *** P < 0.001.				
NOTE: Scores of ratings: 1 = strongly disagree, 2 = disagree, 3 = neutral, 4 = agree, 5 = strongly agree. (Standard deviations are shown in brackets).				

To examine whether differences observed in the mean score ratings are statistically significant, a one-way analysis of variance was conducted (The result of Kruskal-Wallis test is provided in **appendix E**). The results indicate, as was seen in **Table 5-1**, that the differences between the mean score ratings for 15 out of the 28 scales (statements) set out to that are measure the message(s) that are (or are not) communicated in the unqualified audit report are statistically significant. These 15 items are as follows:

- The financial statements are free from fraud.
- Efficiency of the entity.

- Bias in the financial statements.
- Auditor's responsibility regarding fraud detected.
- Auditor's responsibility regarding internal control.
- Auditor's responsibility regarding the maintenance of accounting records.
- Auditor's responsibility regarding the production of financial statements.
- Auditor's responsibility regarding fraud prevention.
- Auditor's integrity.
- Auditor's judgement.
- Auditor's assurance.
- The financial statements presented fairly.
- Freedom of entity from illegal acts .
- The entity well managed.
- Specific versus whole.

Having these statistically significant results attributed to more than two groups now involves conducting post-hoc multiple comparison analyses as a necessary consequence, using specific statistical tests such as the least-significant difference (LSD) test or the Tukey-HSD test or Scheffe test, to show which means differ from which others.

The least-significant difference (LSD) test was selected as the preferred post-hoc multiple comparison test. The following two reasons justify such a decision (Howitt and Cramer, 2000): -

- It is the most-recommended post hoc procedure for different sample sizes; and
- It guarantees that the probability of making at least one Type I error will not exceed 0.05.

As a matter of fact, Carmer and Swanson (1973) suggested that the LSD is the most powerful of the common post-hoc multiple-comparison tests. Thus the LSD was chosen and to find which group(s) caused such statistically significant results see **appendix E** for the result of the post hoc test LSD. As stated previously discussion will be presented in the next chapter.

5-3 The Results Achieved From Analysing The Average Rating of Respondents Towards the 16 Scales That Would be Useful to be Reported by Auditors:

Table 5-2 below displays the average ratings of respondents towards each of the sixteen statements concerning the usefulness for added additional matters to be reported upon by auditors. To examine whether differences observed in the mean score ratings are statistically significant, a one-way analysis of variance was conducted . The results indicate, as we can see in **Table 5-2**, that the differences between the mean score ratings for 14 out of

the 16 items are statistically significant. Two items are statistically insignificant, these being: -

- Usefulness of the free form report to increase the amount of information conveyed to the users of the financial statements, and;
- Usefulness of the free form report to increase the user's understanding of the role of the auditor.

Table 5-2
Average ratings of participants towards the 16 items that might be useful to be reported upon by auditors

The statements	Groups			F-test
	Users	Preparers	Auditors	
1- The information conveyed in the current audit report meet the user's needs.	3.2 (0.92)	3.5 (1.1)	3.8 (0.87)	6.32**
2- The auditor should give more information in the audit report.	3.8 (1.0)	3.5 (1.1)	2.8 (0.98)	5.69***
3- In future, there should be an explicit statement in the audit report of the auditor's assessment of the 'going concern' status of the client.	4.0 (1.0)	3.8 (1.2)	2.7 (1.1)	20.44***
4- In future, there should be an explicit statement in the audit report of the auditor's findings in relation to fraud or illegal acts.	3.7 (1.2)	3.5 (1.3)	2.4 (1.0)	17.30***

5- It would be useful for auditors to indicate either in the audit report or in a separate statement, the extent of their examination of:				
5a- The Chairman's Statement	3.4 (1.1)	2.5 (0.99)	2.4 (0.96)	14.11***
5b- The Director's Report	3.5 (1.1)	2.6 (0.98)	2.5 (1.0)	14.77***
5c- Any other information included in the annual report but outside the financial statements	3.4 (1.1)	2.5 (1.0)	2.3 (0.92)	17.12***
6- 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:-				
6a- The scope of their study of the client's internal controls	3.8 (1.0)	4.0 (1.0)	3.3 (1.1)	5.38**
6b- The extent to which they relied on the internal controls	3.9 (1.0)	4.1 (0.90)	3.4 (1.0)	5.53**
6c- The materiality level they used	3.5 (1.0)	3.8 (0.87)	3.0 (1.0)	5.11**
7- 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.	3.4 (1.3)	3.2 (1.2)	2.4 (1.3)	10.03***

8- The non-standard wording report form would increase the amount of information conveyed to the users of the financial statements.	3.2 (1.1)	3.1 (1.0)	2.9 (1.1)	0.83
9- The non-standard wording report form would increase the user's ability to evaluate the audited company's exposure to risk.	3.3 (1.2)	3.3 (0.94)	2.6 (1.1)	7.21**
10- The non-standard wording report form would increase the user's understanding of the role of the auditor.	3.3 (0.92)	3.0 (1.1)	2.9 (1.1)	2.80
11- The use of graphs in an audit report make it more understandable.	3.5 (1.2)	3.2 (1.1)	2.5 (1.1)	10.27***
12- The auditor's role should be expanded to include auditing the graphs.	3.3 (1.2)	2.9 (1.1)	2.3 (1.0)	9.95***
* P < .05 ** P < .01 *** P < .001.				
NOTE: Scores of ratings: 1 = strongly disagree, 2 = disagree, 3 = neutral, 4 = agree, 5 = strongly agree. (Standard deviations are shown in brackets).				

While the twenty- eight scales (statements) concerning the message(s) that are (or are not) communicated in the current audit report used in Saudi Arabia as well as the sixteen statements or proposals to improve such a document seem to be useful for comprehending the views shared by the respondents, interpreting them simultaneously would be cumbersome. Thus,

these statements were factor analysed in order to transform them into a reduced number of underlying factors. The results of conducting factor analysis are presented in the following section, Section Three.

5-4 Dimensionality of The Instrument Scales:

As stated earlier, while these items or statements are useful for comprehending the respondents' views, interpreting and describing these variables simultaneously is cumbersome (Co et al., 1998).

In order to facilitate their understanding and interpretation, there was a need to reduce these items to a small number of derived factors. To achieve that, we needed to explore the dimensionality of research instrument statements or proposals, treated as two sets, using an appropriate factor analysis technique.

It is acknowledged that the use of factor analysis, whilst a valid, objective and reliable method, is mainly taxonomic. This result is an in-depth analysis of the underlying factors selected, rather than an exploration of a number of diverse issues (Gay et al, 1998).

The research instrument was as seen in Chapter Four originally designed to measure two main issues relevant to the unqualified audit report in use in Saudi Arabia. They are as follows: 1) an assessment of the message(s) that are (or are not) communicated by the unqualified report in order to provide an

indication of whether there is an audit expectation gap existing in such a document. 2) an assessment of the agreement of the users, auditors and preparers with respect to adding specific issues useful from their points of view. The factor analysis techniques that would be chosen will be applied to scales (statements) relevant to each of these issues rather than to all the statements in the instrument as a whole, since they are not a measurement of the same thing.

A number of factor analysis techniques, such as 'principal components', 'principal factor analysis', and 'maximum likelihood', are easily accessible via computer software packages, such as SPSS, when a researcher needs to simplify into underlying dimensions a number of correlated variables (see Dancey and Reidy, 2002; Bryman and Cramer, 2001; Pallant, 2001; Thompson and Daniel 1996, for the differences between these techniques). The researcher should, however, justify the factor analysis technique he chooses in constructing the underlying dimensions from a large number of variables (Thompson and Daniel, 1996).

The Principal Component Analysis (PCA) as the method of extraction, with Varimax as the method of rotation, was chosen as the means to reduce the 28 and 16 items into underlying factors (Dancey and Reidy, 2002; Bryman and Cramer, 2001; Pallant, 2001; Gorsuch, 1983; Kline 1997; Gay et al , 1998; Schelluch, 1996). Furthermore, Al-Amri (2003) suggests the following justifications for the use of the PCA:

- The PCA technique enhances the researcher's understanding of the structure of the large number of correlated variables;
- Components extracted by the PCA technique are real factors because they are derived directly from the correlation matrix;
- The factor loadings identified by the PCA technique are not only the correlation of the variable with the factor, showing the extent to which a variable contributes to each factor, but also the beta (β) weights for predicting the relationship between the variables and the component to which they belong; and
- The PCA is an effective technique in establishing the factorial validity of a scale under development.

Moreover, Tabachnick and Fidell (1996, p.664) suggested, "PCA is the solution of choice for the researcher who is primarily interested in reducing a large number of variables to a smaller number of components".

Thus, the principal components analysis technique with an orthogonal rotation (Varimax) and the Kaiser rule of "eigenvalue greater than 1" was initially performed to identify the underlying dimensions of the messages communicated by the unqualified report as well as the underlying dimensions of the additional material that it would be useful for the auditors to report (Schelluch, 1996; Gay et al, 1998; Morgan and Halpern 1999).

However, the results to be maintained by this study, as a result of running the PCA on the instrument statements, have to meet the following three criteria

- For an item to be considered designative of a factor, it has to have a loading factor of 0.45 or more;
- Item-total correlations need to exceed 0.40; and
- Any extracted factor has to have a minimum of three items meeting the first two criteria, stated above.

These criteria were stipulated because the results which meet them enhance item-total correlations and scale reliability. Both are important issues in relation to the quality of extracted factors (King and Daniel, 1996).

5-4-1 The results achieved from conducting the PCA on the 28 statements concerning the message(s) communicated by the unqualified audit report

5-4-1 -1 Assessing the data and extracting the factors:

As the first step in reducing the 28 items into underlying dimensions, we need to assess the suitability of the data for factor analysis. This involves conducting a correlation matrix and seeing that there are many coefficient of 0.30 and above, and calculating the Kaiser-Meyer-Olkin Measure of Sampling Adequacy (KMO) and Bartlett's Test of Sphericity. The second step involves determining how many underlying factors there are in the set of variables (Dancey and Reidy, 2002; Bryman and Cramer, 2001; Pallant, 2001; Kinnear and Gay, 2001).

However, it should be noticed here that, as Bryman and Cramer (2001) stated, the reliability of factors emerging from a factor analysis depends on the size of the sample. The interesting point is that according to Bryman and Cramer (2001) there is no consensus on what size should be. In lieu of this, the agreement is that there should be more participants than variables (Bryman and Cramer, 2001, p.263). Gorsuch (1983) has proposed an absolute minimum of five participants per variable and no fewer than 100 individual per analysis. In this study the sample is 146 individuals and the variables are 28 which exceed this criteria and this indicates that the data in this section is appropriate for factor analysis.

As suggested by Pallant (2001) before conducting factor analysis it is nevertheless important to formally evaluate its appropriateness by assessing the KMO measure of sampling adequacy and the Bartlett's Test of Sphericity (i.e. to see if items are sufficiently correlated and factor analysis is worth doing or not). The KMO is an index for comparing the magnitudes of observed correlation coefficients to magnitudes of partial correlation coefficients (Dancey and Reidy, 2002; Bryman and Cramer, 2001; Pallant, 2001; Kinnear and Gay, 2001). A small value of KMO means that factor analysis of variables might not be appropriate, because correlation between pairs of variables cannot be explained by other variables. Kaiser (1974) characterises a KMO value in the 0.90's as marvellous, in the 0.80's as meritorious, in the 0.70's as middling, in the 0.60's as mediocre, in the 0.50's as miserable and below 0.50 as unacceptable. In this study the Correlation Matrix as well as the value of KMO and significance of the Bartlett's test of

Sphericity indicate that the data in this section is appropriate for factor analysis. In our study however, the KMO value is 0.759, this indicates a “middling” adequacy according to the Kaiser (1974) scale, and hence is very appropriate for use in further factor analysis. In addition, the Bartlett’s Test of Sphericity indicates that correlations among the 28 items are statistically significant (at .001).

To determine how many factors are to be extracted from the 28 items the researcher adhered to the following criteria (Dancey and Reidy, 2002; Bryman and Cramer, 2001; Pallant, 2001; Kinnear and Gay, 2001 Norusis, 1997):

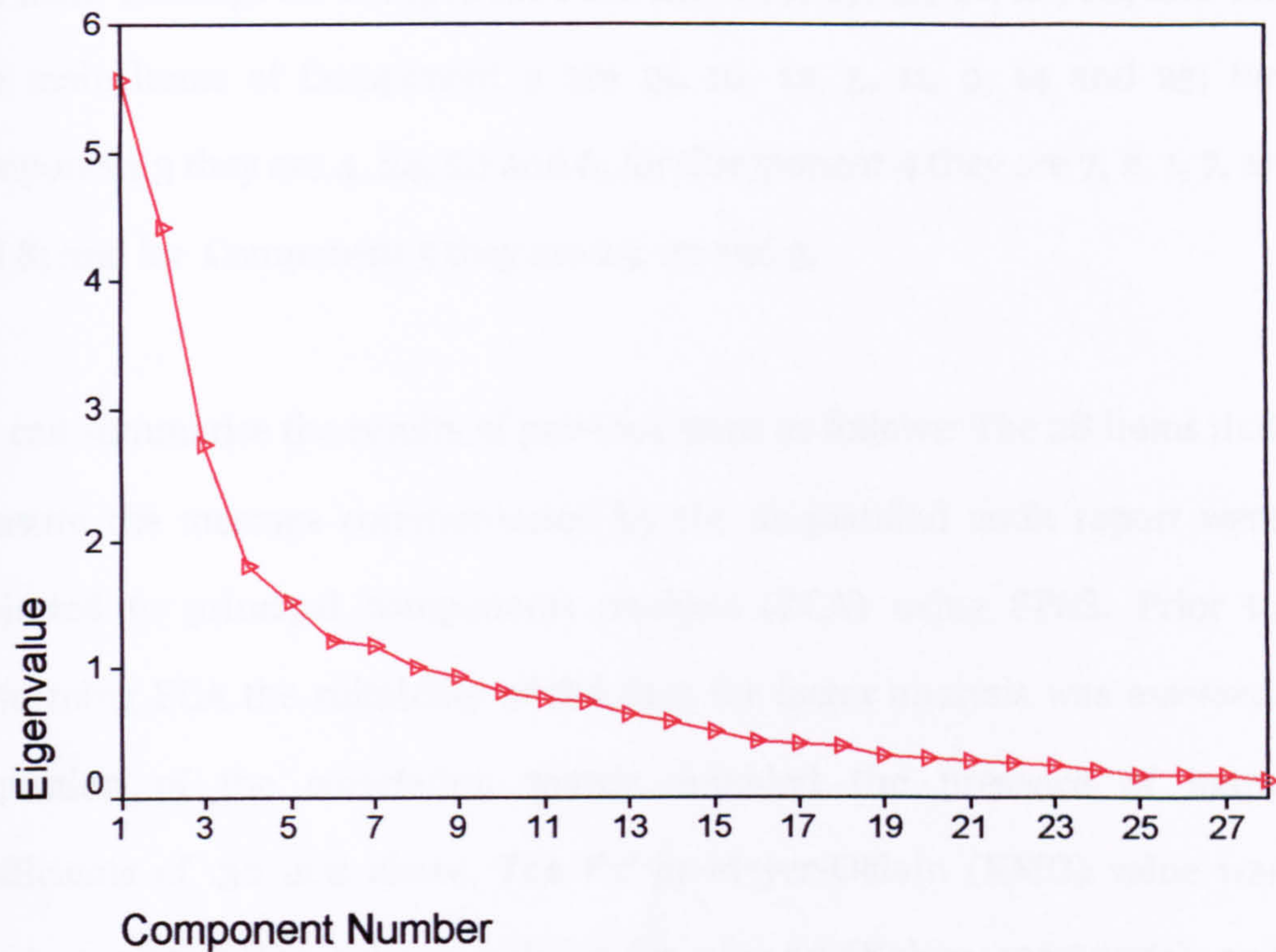
- The factors to be retained (kept) should have an eigenvalue of 1.00.
- The scree plot should be used to aid in determining of the number of factors.
- One should look at how much variance the factors account for and keeping as more variance as possible.

Dancey and Reidy, 2002 noted that “a good researcher needs to take everything into consideration in coming to a decision on how many factors to retain” (p.424). Thus, we need to look into the total variance explained as well as the scree plot. A scree plot however, is a plot of eigenvalues against the number of factors, in order of extraction. The shape of the plot is used to determine the number of factors. Typically, the plot has a distinct break between the steep slope of factors with large eigenvalues and a gradual trailing off associated with the rest of the factors. This gradual trailing off is

referred to as the “scree” (Pallant, 2001; Kinnear and Gay, 2001). Empirical evidence indicates that the point at which the scree begins denotes the true number of factors (Churchill, 1995). The Kaiser suggests eight factors and the component matrix shows the loadings of each of the items on the eight components that have an eigenvalue of more than 1. It is clear from analysing the component matrix that most of the items load quite strongly (above .4) on the first 5 components. Very few items load on components 6, 7 and 8. When viewed in isolation, the scree plot made it clearly that the number of factors that should be kept were less than eight.

While can be seen that the curve begins to flatten out at the sixth factor and becomes still more flat at the seventh factor, which indicates that there are five or six factors present, this the researcher decided to keep five factors. This was working on the principle that the purpose of factors analysis is to reduce the number of factor. It was a decision that was also taking in consideration of the three criteria described above. These are the factors which will be used for further investigation.

Figure 5.1 Scree Plot Graph



5-4-1-2 Factor Rotations:

Our study will use those five components which have been extracted. We now need to rotate these factors to determine factor loadings for the factor items. There are a number of different rotation techniques (Dancey and Reidy, 2002; Bryman and Cramer, 2001; Pallant, 2001; Kinnear and Gay, 2001). One of them is Varimax rotation, in which an orthogonal approach (which assumes that the factors are not related) is demonstrated (Pallant,2001).

In the total variance, we should note that there are now only five components. In the rotated Component Matrix (see **Table 5-3**), we can see

the loadings of each of the 28 variables on the five factors that were extracted. The main loadings on Component 1 are items 27, 19, 18, 21, 28, 26, and 16. The main items of Component 2 are 13, 10, 12, 5, 11, 9, 14 and 25; for Component 3 they are 4, 24, 20 and 6, for Component 4 they are 7, 2, 1, 7, 17 and 8; and for Component 5 they are 23, 22 and 3.

We can summarise the results of previous steps as follows: The 28 items that measure the message communicated by the unqualified audit report were subjected to principal components analysis (PCA) using SPSS. Prior to performing PCA the suitability of the data for factor analysis was assessed. Inspection of the correlation matrix revealed the presence of many coefficients of .30 and above. The Kaiser-Meyer-Oklain (KMO) value was 0.759, exceeding the recommended value of 0.60 (Kaiser, 1960,1974), and the Bartlett's Test of Sphericity (Bartlett, 1954) reached statistical significance at .01, supporting the factorability of the correlation matrix.

Principal components analysis revealed the presence of 8 dimensions with eigenvalues exceeding 1, explaining 20.1%, 16.6%, 8.7%, 6.5%, 4.9%, 4.1%, 3.9%, and 3.7% of the variance respectively. Using Catells's (1966) scree test, it was decided to retain five dimensions for further investigation (see the previous section and the scree plot). To aid in interpretation of these five components, Varimax rotation was performed. The 5-factor solution explained a total of 56.7% of the variance, with component 1 contributing 14.1%, component 2 contributing 12.4%, component 3 contributing 12.2%, component 4 contributing 10.2%, and component 5 contributing 7.9%.

These five extracted factors, which met the study criteria, were labeled as follows:

- Factor I – Purpose of the Audit.
- Factor II – Auditor’s Responsibilities.
- Factor III – Assurance of future viability.
- Factor IV - Reliability of the financial statement.
- Factor V – Usefulness of Decision-making.

What we need to do now is to explore the extent to which these five factors are reliable by using Cronbach's alpha approach (Cronbach, 1951).

Table 5-3 below displays item-total correlation, the alpha reliability for each of the constructed factors. These results suggest that the five factors measuring the message communicated by the unqualified audit report are reliable (Cronbach, 1951).

To sum up, looking at the results achieved from applying the PCA as the method of extraction, with Varimax as the method of rotation on the 28 statements concerning the message communicated in the unqualified audit report, as well as the alpha coefficients of factors, we can confirm that we have valid and reliable factors.

Table 5-3

Factor structure of the 28 Scales that measure the message commemorated in the unqualified audit report, as well as the corrected item-total correlation, the alpha reliability

Factors	Number of the statement	Corrected item-total correlation	Factor loading	Alpha
Purpose of Audit	27	0.74	0.850	0.81
	19	0.74	0.790	
	18	0.66	0.751	
	21	0.50	0.651	
	28	0.48	0.651	
	26	0.53	0.633	
	16*	0.38	0.445	
Auditors Responsibility	13	0.59	0.739	0.80
	10	0.68	0.682	
	12	0.49	0.665	
	5*	(-0.22)**	0.593	
	11	0.55	0.547	
	9	0.61	0.516	
	14*	(-0.12)**	0.462	
	25*	(-0.25)**	0.418	
	*These items have been deleted because they did not meet the study criteria			
Assurance of Future Viability	4	0.69	0.846	0.78
	24	0.63	0.798	
	20	0.59	0.643	
	6	0.45	0.615	
Reliability of	7	0.62	0.732	0.69
	2	0.51	0.619	

Audited Financial Statements	1	0.34	0.506	
	15*	(-0.22)**	0.501	
	17*	(-0.21)**	0.460	
	8*	0.43	0.379	
	*These items have been deleted because they did not meet the study criteria			
Decision Making	23	0.60	0.836	0.79
	22	0.50	0.797	
	3	0.30	0.490	
Alpha for the 28 items = 0.82.				
** An item with a low (or even negative) correlation coefficient would indicate that it was not eliciting responses consistent with the instrument (or section of the instrument) as a whole, (Black, 1999, p.280), so it should be deleted to determine the underlying reliability.				

5-4-2 The results achieved from conducting the PCA on the 16 Items of additional material that it would be useful for auditors to report on:

The sixteen scales (statements) that were proposed for measuring the usefulness of additional material that auditors might report on were subjected to principal components analysis (PCA) using SPSS. Prior to performing PCA the suitability of data for factor analysis was assessed. Inspection of the correlation matrix revealed the presence of many coefficients of 0.30 and above. The Kaiser-Meyer-Oklain (KMO) value was 0.890. This indicates a “marvellous” adequacy according to the Kaiser (1974) scale, exceeding the recommended value of .60 (Kaiser, 1970,1974) and hence is very appropriate for use in further factor analysis. Furthermore, the

Bartlett's Test of Sphericity (Bartlett, 1954) reached statistical significance at 0.01, supporting the factorability of the correlation matrix.

Principal components analysis revealed the presence of four components with eigenvalues exceeding 1, explaining 49.41%, 11.5%, 7.9%, and 6.4% of the variance respectively. Using Catell's (1966) scree test, and considering the criteria of this study to determine the number of factors that should be kept (described in the previous section) it was decided to retain three components for further investigation.

To aid in interpretation of these three components, Varimax rotation was performed. The 3-factor solution explained a total of 68.57% of the variance, with the contribution of Component 1 as 28.5%, Component 2 as 22.3%, and Component 3 as 17.7%.

These three extracted factors, which met the study criteria, were labelled as follows:

- Factor I – Expansion of the scope of the auditors' opinion.
- Factor II – Expanded Audit Report.
- Factor III – Free Form Report.

Cronbach's alpha approach was used to explore the extent to which the three factors are reliable.

Table 5-4 below displays item-total correlation, the alpha reliability for each of the constructed factors. These results suggest that the scale, as well as each of the three factors, have high reliability (Cronbach, 1951).

To sum up once more, in view of the results achieved from applying the PCA as the method of extraction, with Varimax as the method of rotation on the 16 items, and with the alpha coefficients of extracted factors, it can be confirmed that we have valid and reliable factors.

Table 5-4
Factor structure of 16, corrected item-total correlation, the alpha reliability

Factors	Number of the statement	Corrected item-total correlation	Factor loading	Alpha
The expansion of the scope of auditor opinion	5a	0.82	0.910	0.91
	5b	0.81	0.889	
	5c	0.74	0.858	
	11	0.75	0.686	
	12	0.68	0.611	
	2	0.64	0.554	
	4	0.66	0.550	
	1*	(0.38)	0.407	
*This item would have to be deleted because it did not meet the study criteria				
Expanded Audit Report	6a	0.84	0.876	0.87
	6b	0.84	0.872	
	6c	0.68	0.793	

	3	0.59	0.571	
Free Form Report	8	0.68	0.824	0.83
	10	0.64	0.793	
	9	0.77	0.767	
	7	0.58	0.493	
Alpha for the 15 items = 0.93				

Now that we have developed valid and reliable factors, we need to find out whether the perceptions of the three groups (users, preparers and auditors) are significant in respect to the five factors of the message that are (or are not) communicated in the audit report currently used in Saudi Arabia as well as the usefulness of the 'additional matters' factors. The next step was to calculate factor scores for each respondent as well as for each factor. Further details on how the factors' scores were developed are presented in the following section.

5-4-3 Factor Scores

In the previous section, 5-4, and its subsections, 5-4-1 and 5-4-2, eight valid and reliable factors were extracted from conducting factor analysis, namely PCA, on the instrument's variables (the 28 statements of the message and the 16 statements of the additional matters). The labelling of each of these factors, which were extracted from the factor loadings, has been addressed as well.

There are several sophisticated techniques for calculating factor scores based on the use of factor score coefficients. They are:

- The Regression Method.
- The Bartlett Method.
- The Anderson-Rubin Method.

Having used the principal components analysis, with an orthogonal rotation (meaning that the created factors are uncorrelated) based on the Varimax criterion, to reduce the instrument's items into underlying dimensions, 'the Anderson-Rubin method' was used to produce factor scores that are uncorrelated to each other (Kline, 1997).

Two other scaling methods can be used to produce factor scores. They are 'the regression method' and 'the Bartlett method'. Neither of these two scaling methods lead to orthogonal or uncorrelated scales (Field, 2000). The Anderson-Rubin method, which is a modification of the Bartlett method, is, as suggested by Tabachnick and Fidell (1996), best employed when uncorrelated scores are required.

Because the current research is interested in constructing uncorrelated factor scores, the Anderson-Rubin method was used for calculating the required factor scores.

Now that we have identified factor scores for each of the 146 subjects, namely the total number of useable questionnaires, as well as for each of the eight

factors, extracted from conducting PCA on the internment statements or items, we can use these factor scores rather than the original data in conducting any further analysis. (Foster, 2001; Field, 2000).

5-5 The Results Achieved from Analysing The Perceptions of Respondents Towards The Factors Concerning The Message(s) Communicated in The Unqualified Audit Report:

The results of this section were achieved from analysing the differences in the mean scores of the three groups in relation to the five factors related to the message(s) communicated in the current audit report.

The research question to be answered here is whether there are differences in mean scores of the three groups concerning the auditors' message(s) communicated in the current audit report used in Saudi Arabia. Stated differently, we want to find out if there is an audit expectations gap existing in Saudi Arabia with regard to the current audit report, pertaining to the purpose of the audit, the auditors' responsibilities, assurance of future viability, the reliability of the audited financial statements, and the usefulness of these financial statements in decision making.

To answer such a question, we need to decide the fate of our null hypothesis claim that differences in the mean scores of the perceptions of the three

groups used in this study are statistically insignificant. Thus, if we achieve statistically-significant results, meaning rejection of this null hypothesis, we can then say that there is an existing audit expectations gap.

5-5-1 Purpose of Audit Factor

Tables 5-5 and **5-6** present the results achieved from analysing the differences in the mean score ratings of the groups' perceptions relevant to that of the audit purpose factor. **Table 5-5** presents the descriptive statistics in terms of the number of cases, mean, standard deviation, standard error, lower and upper bounds of the 95% confidence interval, and the minimum and maximum scores, expressed by the groups.

Table 5-5
Descriptive statistics: the perceptions of the groups relevant to the purpose of an audit

Groups	N	Mean	Standard Deviation	Standard Error	95 % Confidence Interval for Mean		Min	Max
					Lower	Upper		
Users	67	3.89	0.65	0.007	3.73	4.05	1.86	4.86
Preparers	29	4.06	0.64	0.11	3.82	4.31	1.86	5.00
Auditors	50	4.14	0.62	0.005	3.96	4.12	2.29	5.00

Inspection of the table indicates that there are differences in the mean score ratings. To see whether these differences are statistically significant, we need

to use the one-way analysis of variance test. The results achieved from applying this test (Table 5-6) support our null hypothesis claim that differences in the mean score ratings (of the three groups' perceptions that the purpose of an audit is clearly communicated in the current audit report) are statistically insignificant.

Table 5-6
One-way analysis of variance comparing beliefs of the three groups relevant to the audit purpose

Source	Df	Sum of Squares	Mean Squares	F	Sig.
Between Groups	2	3.036	1.518	1.53	.220
Within Groups	143	141.96	0.993		
Total	145	145.00			

We conclude, therefore, that there is no audit expectation gap in existence in Saudi Arabia within the unqualified audit report currently in use.

5-5-2 Auditors' Responsibility Factor

Tables 5-7 and **5-8** present the results achieved from analysing the differences in the mean score ratings of the three groups' perceptions towards the 'auditors' responsibility' factor.

Table 5-7 presents the descriptive statistics in terms of the number of cases, mean, standard deviation, standard error, lower and upper bounds of the 95% confidence interval, and the minimum and maximum score ratings.

Table 5-7
Descriptive statistics: auditors' responsibility factors

Group	N	Mean	Standard Deviation	Standard Error	95 % Confidence Interval for Mean		Min	Max
					Lower	Upper		
Users	67	2.92	0.90	0.11	2.70	3.14	1.00	5.00
Preparers	29	2.47	0.91	0.17	2.12	2.82	1.00	4.20
Auditors	50	1.69	0.59	0.008	1.52	1.86	1.00	3.80

To resolve the research null hypothesis, we need to reach a statistical conclusion towards differences in the mean score ratings.

The results of applying the one-way analysis of variance test to our data (**Table 5-8**) did not support our null hypothesis claim that the differences in the mean score ratings of the perceptions of the three groups towards the auditors' responsibility are statistically insignificant. Thus, we conclude that an audit expectations gap does exist in relation to auditors' responsibility. These results therefore entail action in undertaking the necessary corrective intervention to enhance the clarity of the message related to the auditors'

responsibilities in a way which leads to the elimination of such significant differences.

Having these statistically significant results attributed to more than two groups now involves conducting post-hoc multiple comparison analyses as a necessary consequence. Thus the LSD test was applied and the results indicated that there were statistically significant differences ($p \leq 0.05$) in the mean score ratings of the following groups:

- Auditors, with the lowest mean score ratings (1.69), differed significantly from users, who had the highest mean score ratings (2.92).
- Auditors, with the lowest mean score ratings, differed significantly from preparers, who had the second lowest mean score ratings (2.47).
- Users, with the lowest mean score ratings, differed significantly from preparers, who had the second lowest mean score ratings.

The results indicate that auditors believe they have little responsibility for the tasks that are represented by this factor, while users and preparers appeared to place significant responsibility on auditors for these tasks. This would appear to be an area exhibiting an audit expectations gap in Saudi Arabia.

Table 5-8

One-way analysis of variance comparing belief of three groups towards auditors' responsibility factor

Source	df	Sum of Squares	Mean Squares	F	Sig.
Between Groups	2	42.22	21.11	29.37	0.001
Within Groups	143	102.78	0.71		
Total	145	145.00			

5-5-3 Assurance of Future Viability Factor

Tables 5-9 and **5-10** present the results achieved from analysing the differences in the mean score ratings of the perceptions of the three groups relevant to the 'assurance of future viability' factor.

Table 5-9

Descriptive statistics: assurance of future viability factor

Group	N	Mean	Std. Deviation	Std. Error	95 % Confidence Interval for Mean		Min	Max
					Lower	Upper		
Users	67	3.31	0.83	0.102	3.11	3.52	1.00	4.75
Preparers	29	3.37	1.00	0.186	2.98	3.75	1.00	4.75
Auditors	50	2.92	0.65	0.009	2.73	3.10	1.75	4.67

Table 5-9 presents the descriptive statistics in terms of the number of cases, mean, standard deviation, standard error, lower and upper bounds of the 95% confidence interval, and the minimum and maximum scores.

To reach a definite conclusion in relation to the null hypothesis which claims that differences in the mean score ratings (of the perceptions of the three groups that the unqualified audit report communicates the future viability of the entity) are statistically insignificant, we need to apply the one-way analysis of variance test to the data. The results presented in **Table 5-10** below do not support our null hypothesis.

Table 5-10
One-way analysis of variance comparing attitudes of the three groups relevant to assurance of future viability

Source	df	Sum of Squares	Mean Squares	F	Sig.
Between Groups	2	6.06	3.031	3.11	.047
Within Groups	143	138.94	0.972		
Total	145	145.00			

Use of the LSD test to identify which mean score ratings are responsible for these statistically significant results indicated that, among the three groups, auditors, with the lowest mean score, differed significantly from preparers, with the highest mean score, and also differed from that of users ($p \leq 0.05$).

Thus, we could conclude that there is an audit expectation gap exist in Saudi Arabia within the current audit report in use in the country in relation to assurance of future viability factor. It is interesting that of the three groups the auditors had the lowest mean score, being significantly different from the mean score of the preparers group. This can be interpreted as indicating that the auditors believe that the audit report wording may be improved to more successfully outline their responsibility in relation to assurance of the entity as a going concern.

5-5-4 Reliability of the Financial Statements Factor

Table 5-11 and **Table 5-12** present the results achieved from analysing the differences in the mean score ratings of the three groups' perceptions towards the 'reliability of financial statements' factor. **Table 5-11** presents the descriptive statistics in terms of the number of cases, mean, standard deviation, standard error, lower and upper bounds of the 95% confidence interval, and the minimum and maximum scores.

Table 5-11

Descriptive statistics: the reliability of financial statements factors

Group	N	Mean	Std. Deviation	Std. Error	95 % Confidence Interval for Mean		Min	Max
					Lower	Upper		
Users	67	3.51	0.84	0.103	3.30	3.71	1.50	5.00
Preparers	29	3.50	0.80	0.149	3.19	3.80	1.50	5.00
Auditors	50	3.22	0.72	0.102	3.01	3.42	1.75	5.00

The results from applying the one-way analysis of variance test to our data (**Table 5-12**) support our null hypothesis, which claims that the differences in the mean score ratings of the perceptions of the three groups towards the ‘reliability of the audited financial statements’ factor are statistically insignificant. Thus we conclude that the unqualified audit report clearly communicates the neutrality of the audited financial statements. In other words, there is no existing expectation gap regarding the reliability of the audited financial statements. It is noticeable here that the auditors’ group had the lowest mean score among the three groups. This may possibly signify that auditors think the words used in the audit report are not explicit enough to denote the reliability of the audited financial statements.

Table 5-12

One-way analysis of variance comparing the perceptions (beliefs) of the three groups towards the reliability of the audited financial statements factor

Source	df	Sum of Squares	Mean Squares	F	Sig.
Between Groups	2	3.55	18.08	1.795	0.170
Within Groups	143	141.45	15.88		
Total	145	145.00			

5-5-5 Usefulness of Decision-Making Factor

Tables 5-13 and **5-14** present the results achieved from analysing the differences in the mean score ratings of the three groups' perceptions (beliefs) towards the usefulness of the audited financial statements with regard to the usefulness of decision making factor.

Table 5-13 presents the descriptive statistics in terms of the number of cases, mean, standard deviation, standard error, lower and upper bounds of the 95% confidence interval, and the minimum and maximum scores, expressed by the groups.

Table 5-13
Descriptive statistics: decision-making factor

Group	N	Mean	Std. Deviation	Std. Error	95 % Confidence Interval for Mean		Min	Max
					Lower	Upper		
Users	67	3.72	.699	0.008	3.54	3.88	1.33	5.00
Preparers	29	3.71	.738	0.137	3.43	3.99	2.33	5.00
Auditors	50	3.65	.827	0.117	3.41	3.88	1.00	4.67

To see whether the differences in the mean score ratings are statistically significant we need to apply the one-way analysis of variance test to our data. The results we achieved from applying such a test to our data (**Table 5-14**) indicate that our research null hypothesis was supported. Thus, we conclude

that there is no expectations gap existing in this area simply because we were unable to establish a statistical significance between auditors and the two other groups under analysis.

Table 5-14
One-way analysis of variance comparing perceptions of the three groups towards the decision making factor

Source	Df	Sum of Squares	Mean Squares	F	Sig.
Between Groups	2	0.77	0.383	0.380	0.684
Within Groups	143	144.23	1.009		
Total	145	145.00			

5-6 The Results Achieved from Analysing The Perceptions of Respondents Towards The Factors Concerning The Usefulness of Adding Additional Matters to be Reported by Auditors:

The results in this section were achieved by analysing the differences in the mean scores of the three groups in relation to the three factors related to the usefulness of additional material that would be useful to be reported upon by auditors to improve the communication in the current audit report.

The research question to be answered here is to find out if there are differences in the mean scores of the three groups concerning the usefulness of additional material that could be added by auditors to improve communication in the current audit report. Stated differently, we want to find out if the groups are in agreement about the usefulness of expanding the scope of the auditors' opinion, expanding the audit report and using a free form report to improve communication in the audit report.

To answer such a question, we need to decide the fate of our null hypothesis claim that differences in the mean scores of the perceptions of the three groups used in this study are statistically insignificant. Thus, if we achieve statistically significant results, meaning rejection of this null hypothesis, we can then say that the groups are not in agreement about the usefulness of adding these issues.

5-6-1 Expansion of the Scope of the Auditors' Opinion Factor

Tables 5-15 and **5-16** present the results achieved from analysing the differences in the mean score ratings of the three groups' perceptions towards the 'expansion of the scope of auditors' opinions' factor.

Table 5-15 presents the descriptive statistics in terms of the number of cases, mean, standard deviation, standard error, lower and upper bounds of the 95% confidence interval, and the minimum and maximum scores.

The result shows that the groups were mildly in favour of the auditors expanding their opinion scope (3.04). However, it is obvious that the mean score ratings are different. For example, the users seem to be slightly in favour of expanding the scope of auditors' opinions to include more information to be given. In contrast, the auditors' groups were slightly against such an expansion.

Table 5-15
Descriptive statistics: the expansion of the scope of auditors' opinions factor

Groups	N	Mean	Standard Deviation	Standard Error	95 % Confidence Interval for Mean		Min	Max
					Lower	Upper		
Users	67	3.50	0.975	0.119	3.26	3.74	1.71	5.00
Preparers	29	2.95	0.802	0.148	2.64	3.25	1.86	4.86
Auditors	50	2.47	0.640	0.009	2.29	2.65	1.29	4.57
All Groups	146	3.04	0.952	0.007	2.88	3.19	1.29	5.00

Having identified differences in the mean score ratings we need to conduct an analysis to see whether such differences are statistically significant. We need to apply the one-way analysis of variance test to the data. The results from running such a test (**Table 5-16**) do not support our null hypothesis that differences in the mean scores of the perceptions of the three groups are statistically insignificant.

Table 5-16

One-way analysis of variance comparing attitudes of the three groups towards the expansion of the scope of auditors' opinions factor

Source	Df	Sum of Squares	Mean Squares	F	Sig.
Between Groups	2	32.35	16.174	20.531	0.001
Within Groups	143	112.65	0.788		
Total	145	145.00			

The issue that now needs resolving is which groups' mean score ratings caused our results to be significant. Thus the LSD post-hoc procedure was applied and the results indicated that there were statistically significant differences ($p \leq 0.001$) in the mean score ratings of the following groups:

- Users, with the highest mean score (3.5), differed significantly from the mean scores of auditors, with the lowest mean score (2.47).
- Users also differed significantly from the mean score of preparers.

Thus we can conclude that the three groups are not in agreement about the usefulness of expanding the scope of the auditors' opinions.

5-6-2 Expanded Audit Report Factor

Table 5-17 and **table 5-18** present the results achieved from analysing the differences in the mean score ratings of the three groups' participations towards the 'expansion of the audit report factor'. **Table 5-17** presents the descriptive statistics in terms of the number of cases, mean, standard deviation, standard error, lower and upper bounds of the 95% confidence interval, and the minimum and maximum scores.

Table 5-17
Descriptive statistics: The expanded audit report factor

Groups	N	Mean	Standard Deviation	Standard Error	95 % Confidence Interval for Mean		Min	Max
					Lower	Upper		
Users	67	3.79	0.867	0.105	3.58	4.00	1.75	5.00
Preparers	29	3.90	0.833	0.154	3.58	4.22	2.00	5.00
Auditors	50	3.04	0.980	0.138	2.76	3.32	1.00	4.75
All group	146	3.55	0.970	0.008	3.40	3.71	1.00	5.00

The results we achieved from applying the one-way analysis of variance test (**Table 5-18**) do not support such a claim. Thus, we reject the null hypothesis and conclude that the groups are not in agreement as to the usefulness of expanding the audit report as a way to improve communication in the audit report.

Table 5-18

One-way analysis of variance comparing attitudes of the three groups towards expanded audit report factor

Source	df	Sum of Squares	Mean Squares	F	Sig.
Between Groups	2	13.81	6.903	7.524	0.001
Within Groups	143	131.19	0.917		
Total	145	145.00			

The results of our LSD post-hoc test indicate that there were statistically significant differences ($p \leq 0.05$) in the mean score ratings of the following groups:

- The mean score of auditors differed significantly from those of the preparers, with higher mean scores.
- The mean score of users, the second highest, differed significantly from that of auditors.
- The users' mean score differed significantly from that of preparers.

The results indicate that the users and preparers groups are in favour of expanding the unqualified audit report whereas the auditors group are unwilling to support such an expansion.

5-6-3 Free Form Report Factor

Table 5-19 and **table 5-20** present the results of analysis of the differences in the mean score ratings of the three groups' perceptions of the usefulness of the 'free form report' factor.

Table 5-19 presents the descriptive statistics in terms of the number of cases, mean, standard deviation, standard error, lower and upper bounds of the 95% confidence interval, and the minimum and maximum scores.

Table 5-19
Descriptive statistics: the usefulness of free form report factor

Groups	N	Mean	Std. Deviation	Std. Error	95 % Confidence Interval for Mean		Min	Max
					Lower	Upper		
Users	67	3.31	0.938	0.114	3.07	3.53	1.25	5.00
Preparers	29	3.18	0.831	0.154	2.86	3.49	1.25	5.00
Auditors	50	2.70	0.889	0.125	2.44	2.95	1.00	4.75
All groups	146	3.07	0.936	0.007	2.92	3.22	1.00	5.00

The result indicates that the groups were mildly in favour of the auditors' expanding their opinion scope (3.07). However, it is obvious that the mean score ratings are different. Our null hypothesis, which claims that the differences in the perceptions of the three groups towards the usefulness of

adoption of the 'free form report' factor are statistically insignificant needed to be tested, so we applied the one-way analysis of variance test to our data.

The results we achieved from applying the one-way analysis of variance test (**Table 5-20**) support our null hypothesis claim that such differences are statistically insignificant.

Table 5-20
One-way analysis of variance comparing belief of the three groups towards the free form report factor

Source	df	Sum of Squares	Mean Squares	F	Sig.
Between Groups	2	1.71	0.855	0.853	0.428
Within Groups	143	143.29	1.002		
Total	145	145.00			

The lack of statistically significant differences between the groups might be due to the possibility that the users' group found the free form report somewhat ambiguous, as to how it should be interpreted, or perhaps it was that they disliked its format, which has elsewhere been found to increase the users' perceptions of the usefulness and rigour of the audit process (Hatherly et al., 1998).

5-7 Summary and Conclusion:

In this chapter, we analysed the data, using parametric and non-parametric statistical tests to find whether an audit expectation gap existed vis-à-vis the current audit report used in Saudi Arabia. This was done by seeing if it were possible to establish statistically significant differences between the three groups participant in this study (Auditors, preparers and users of financial statements).

Thus, the one-way analysis of variance test and the Kruskal-Wallis were applied to the twenty-eight scales (statements) that measure the message(s) that are (or are not) communicated in the unqualified audit report. The results indicate that there are 15 statistically significant divergences between groups. They are as follows:

- The financial statements are free from fraud.
- Efficiency of the entity.
- Bias in the financial statements.
- Auditor's responsibility regarding fraud detected.
- Auditor's responsibility regarding internal control.
- Auditor's responsibility regarding the maintenance of accounting records.
- Auditor's responsibility regarding the production of financial statements.
- Auditor's responsibility regarding fraud prevention.
- Auditor's integrity.

- Auditor's judgement.
- Auditor's assurance.
- The financial statements presented fairly.
- Freedom of the entity from illegal acts.
- The entity well managed.
- Specific versus whole.

The one-way analysis of variance test and the Kruskal-Wallis, were applied to the sixteen scales (statements) that measure the usefulness of adding some matters to be reported by auditors. The results indicate that, out of those the sixteen statements, there are fourteen statistically significant differences between the three groups. Two items are statistically insignificant, these being:

- Usefulness of the free form report to increase the amount of information conveyed to the users of the financial statements, and;
- Usefulness of the free form report to increase the user's understanding of the role of the auditor.

While the twenty- eight scales (statements) concerning the message(s) that are (or are not) communicated in the current audit report used in Saudi Arabia as well as the sixteen statements or proposals to improve such a document seem to be useful for comprehending the views shared by the respondents, interpreting them simultaneously would be cumbersome. Thus, these forty-four statements were factor analysed in order to transform them into a reduced number of underlying factors. The responses provided by 146

participants on these the 44 items clustered around eight measure factors. Five of them were concerned with the message(s) communicated in the audit report and three with the usefulness matters.

The one-way analysis of variance test was applied to the five factors concerning the message (s) that may or may not be communicated in the unqualified audit report. The results indicate that there are statistically significant differences between the three groups in relation to the following factors:

- Responsibility factor
- Assurance of future viability factor.

The one-way analysis of variance test was also applied to the three factors that measure the usefulness of adding some matters to be reported by auditors. The results indicate that there are statistically significant differences between the three groups out of those three factors in relation to:

- Usefulness of expanding the scope of auditors opinion factor.
- Usefulness of expanding the audit report factor.

In the next chapter, Chapter Six, the Discussion Chapter we will discuss the results identified by the current study.

6-1 Introduction:

Chapter Five displayed the results achieved by the current research. These results provide answers to the research objectives but they now require some elucidation. Thus, the aim of this chapter is to discuss these results. In order to specifying how the twenty-eight scales measured the message(s) that are (or are not) communicated in the unqualified audit report and the sixteen statements that measured the usefulness matters that would be useful to be reported upon should be grouped together, the researcher conducted an exploratory factor analysis on these items. The use of factor analysis is based on the assumption that these scales are related to each other in ways that can be captured by a few underlying dimensions and by summarizing them with a small number of derived variables. Subsequently, relationships between extracted factors were analysed.

The lack of similar studies in Saudi Arabia has prevented the researcher from integrating his results with such findings, for it may be the first attempt to investigate the existence of an audit expectation gap and the first estimation of the usefulness of the audit report. Thus, the researcher compared the findings of this study with findings in other studies conducted in different countries, particularly in Australia, the US and the UK. One common factor, which links the current study with others, is the use of the cross-sectional

research design. Therefore, it seems logical to conclude that the ideal situation with which to compare our results is one based on both a comparable environment and measures of both issues: the message communicated and the expansion of such a document.

Before we proceed to discuss the results derived from analysing the variables tackled by this study in relation to relevant literature, it is essential that we determine how we identified them. There are two types of variables which have been identified, and their sources are discussed below.

The first batch of these variables consists of participants' responses to the scales that were presented in the survey instrument. The second group of variables consists of practice factors developed for the current research. The main source of information for developing these variables was the perceptions of auditors, preparers and the users of financial statements toward the 28 scales measuring the message(s) that are conveyed in the unqualified audit report and the 16 statements or proposals that may be useful to be reported upon by auditors to improve communication in such a document. Applying the Principal Components Analysis technique to those 44 items included in the instrument, as explained in Chapter Five, meant that we able to derive eight valid and reliable factors.

This chapter has been structured into the following three sections. Section One (6-1) is a background and introduction to the chapter. Section Two (6-2) presents the discussion of the study's results. A summary of the study's findings is provided in Section Three (6-3).

6-2 Discussion of the Results:

A number of variables were examined in this study. They were grouped into two main subsections: Subsection One would be targeted at discussing the results achieved from assessing the perceptions of the three groups participating in this study toward the factors related to messages that are (or are not) communicated in the standard report, the focus of Subsection Two would be a discussion of the results achieved from assessing the perceptions of the three groups which participated in this study toward the factors related to potential improvements of such a document. Each of these categories consists of a number of variables. Taking into account the background of the study and its variables, the following sections reveal discussions relevant to the results achieved by the current research.

6-2-1 Discussion of the Results Achieved From Assessing the Perceptions of the Respondents Toward the Factors Related to the Message(s) Communicated in the Unqualified Audit Report

This subsection presents a discussion of the results gleaned from the factors of the instrument which tapped into the perceptions of the three groups of subjects toward the message(s) conveyed by the unqualified audit report currently used in Saudi Arabia. The 'audit expectation gap' here refers to difference in beliefs between auditors and the public about the messages communicated in the audit report. The results suggest that there was an expectation gap between the beliefs of auditors and the rest of the group in relation to the unqualified audit report currently used in Saudi Arabia.

6-2-1-1 Audit Purpose Factor:

The purpose of an audit report is to communicate the outcome of the auditor's review of financial statements. Ultimately, this is done through the expression an opinion following their audit work (GAO, 1996; AICPA, 1988). In Saudi Arabia, the whole purpose of an external audit is to enable an auditor to "express his opinion on the quality of the financial statement and to assess whether a set of financial statements are presented fairly" (Saudi audit report standard , para 3501) (SOCPA, 2001).

Six scales are relevant to this factor, and they are as follows:

- Clarity of the purpose of an audit (statement 27).
- Clarity of giving a 'present fairly' (statement 19).
- Clarity of extent of assurance (statements 18).
- Clarity of extent of audit work (statement 21).
- Readability of audit report (statement 28).
- Credibility (statement 26).

Table 5-1 provides details of the results of the mean responses ratings concerning these six statements associated with the purpose of an audit. As indicated in this table, no evidence was found of an expectation gap existing in Saudi Arabia (i.e. there no significant differences between the groups) concerning the clarity of the communicated purpose of audit in the audit report (statement 27), the clarity of communication of the extent of audit work (statement 21), whether the audit report is a readable document

(statement 28), and whether inclusion of the audit report would enhance the credibility of the financial statements (statement 26).

The direction and the level of responses to statement 27 indicate that all subject groups believe that the purpose of an audit is clearly communicated in the current audit report used in Saudi Arabia. This result is consistent with previous results (e.g. Kelly and Morach, 1989; Hatherly et al, 1991; Innes et al, 1997, and Manson and Zaman, 2001).

The mean level of responses is slightly above the midpoint concerning the extent of audit work performed (statement 21). Interestingly the auditors groups hold the lowest mean score rating (3.5) which is even less than that of the users (3.6). This may imply as Schelluch (1996) indicates, that there is considerable room for improvement of the audit report message concerning the extent of work performed.

The groups are in agreement that the audit report is a readable document (Statement 28). This result is not unexpected. It supports the contention that the audit report is valuable (Manson and Zaman; 2001). Manson and Zaman (2001), for example, found that user group believe that an audit report is more readable than auditor group do. In this study, the auditors group was more readily agreeable that the audit report is a readable document than where the others groups.

Responses to statement 26 indicated that all groups have a strong believe that the inclusion of the audit report enhances the credibility of the audited financial statements. The result of this scale is consistent with audit literature since it is widely that the purpose of the external audit is to add credibility to the management's representations (Higson, 2003, p. 143). Lee (1986, p. 31) considered that the current primary objective of external audit was 'attesting credibility of financial statements'.

Evidence of an expectation gap appeared between users of the financial statements and other groups concerning the extent of assurances given by the auditor (statement 18) and the clarity of giving a 'present fairly' view of financial statements (statement 19).

In relation to statement 18, all groups are in agreement that the extent of assurance given by auditors is clearly communicated in the current audit report used in Saudi Arabia. However, an inspection of **Table 5-1** shows that the users are less willing to offer agreement on the issue than the other groups. This would tend to suggest that there is some room for improvement in clarifying the audit report message in terms of the extent of assurance provided by the auditors.

The direction and the level of responses to statement 19 indicate that all subject groups believe that the financial statements are presented fairly. Auditors' beliefs are obviously stronger than those of their non auditor counterparts, whilst the preparers group is more sceptical than the users are about the statement. This may be an indication of some degree of

disillusionment on the part of the preparers group about the recent requirements stipulated by the Saudi Ministry of Commerce. Financial directors of Saudi corporations were obligated to provide a statement of declaration in conjunction with the financial statements as a signed verification that all statements have been presented in the best of their knowledge.

The application of ANOVA test to this factor as shown in (Table 5-6) produced overall result indicated that there is no expectation gap (no statistical differences) in existence concerning the clarity of the message communicated in current audit report in Saudi Arabia, in relation to the purpose of an audit. This lack of significant difference between the groups makes it further evident that the audit report is a successful vehicle through which communicate the purpose of the audit. The consensus of opinion ceases to add weight to the argument that the audit report is such a successful mean of conveyance of the audit's purpose if one were to assume that the users of financial statements should a group belief that the purpose of an audit should go beyond that stated in the audit report.

6-2-1-2 Auditors' Responsibility Factor:

Table 5-1 however, provides details of the results of the mean responses concerning five responsibility statements associated with the use of audited financial statements. These statements are the auditor's responsibilities in relation to:

- The auditor's responsibility in relation to preventing fraud. (Statement 13)

- The auditor's responsibility in relation to the soundness of the internal control structure. (Statement 10)
- The auditor's responsibility in relation to producing financial statements. (Statement 12)
- The auditor's responsibility in relation to maintaining accounting records. (Statement 11)
- The auditors' responsibility in relation to detecting fraud. (Statement 9).

In all the five statements (scales) representing this factor, an audit expectation gap (indicated by significant differences) was detected between auditors and the two other respondent groups (preparers and users). In relation to the auditor's responsibility for prevention of fraud (statement 13), the auditor's responsibility for detection of fraud (statement 9), the results indicate that auditors believe they have little responsibility for fraud detection and prevention, whilst preparers and users appear to place an emphatic and significant responsibility on auditors for these duties. This would appear to be the most obvious area where a quantifiably large expectation gap exist in Saudi Arabia.

An audit expectation gap was also detected between auditors and investors regarding the auditor's responsibility for the soundness of the internal controls of the entity (statement 10). As indicated by Schelluch (1996), this could be reduced by the use of improved audit report wording. An audit expectation gap was also detected in relation to the auditor's responsibility for maintenance of accounting records (statement 11). The result of this scale

indicated that auditors believe management is responsible for maintenance of accounting records, whereas users appear to attribute some responsibility for this issue to auditors.

All three groups were in agreement and had fairly strong beliefs that auditors have no responsibility for producing financial statements (statement 12), with strong credence on the part of the auditors group that wordings in the audit report clearly communicating such a responsibility. The level of response of users (2.3) however, indicates that they do not hold strong beliefs about auditors responsibility for producing the financial statements.

The overall result for this factor as presented in **Table 5-8** indicates that auditors believe they have little responsibility for the tasks that are represented by this factor, while users and preparers appear to place significant responsibility on auditors for these tasks. This would appear to be an area where it is possible that one could refer to an expectation gap being in existence in Saudi Arabia, and this would indeed be consistent with audit expectation gap literature. An inspection of the result reveals that the biggest differences were between the auditors and the users group. This is consistent with the Bailey et al. (1983), Epstein and Geiger (1994) and Monroe and Woodliff (1994) who took the collective view that the difference in perceptions between sophisticated users (financial directors) and auditors were smaller than the difference between unsophisticated users and auditor.

6-2-1-3 Assurance of Future Viability Factor:

The auditing profession is concerned that users may infer that an unqualified auditors' report is an assurance about the future viability of the entity. This factor broke down into four scales (statements), each scale relating to a quality that the audit report might arguably touch upon:

- Efficiency of the entity. (Statement 4)
- The entity is well managed. (Statement 24)
- Freedom of the entity from illegal acts. (Statement 20)
- The entity as a going concern. (Statement 6).

Table 5-1 provides details of the results of the mean response ratings concerning these four statements associated with the use of the audited financial statements. As indicated in this table, evidence was found of an expectation gap existing in Saudi Arabia (i.e. there are significant differences between the groups) in relation to the statement that the unqualified audit report communicated that the entity is run efficiently (statement 4), the entity is well managed (statement 24) and the entity is free from illegal acts (statement 20).

The level of responses of users' and preparers' groups are slightly above the midpoint concerning whether or not the unqualified audit report communicates that the entity is run efficiently and that it is well managed (statements 4 and 24). The auditors' group holds the lowest mean score ratings concerning these statements and in this regard they differ significantly from the mean scores ratings of the other groups. The results of these scales are consistent with expectations that the audit opinion and

financial statements make no explicit assertion about management of the entity concerned (King and Higson, 1994; Schelluch, 1996). **Table 5-1** indicates that auditors had significantly stronger beliefs than the other two respondent groups with regard to whether the entity is free from illegal acts (statement 20).

Taking all these points into consideration there is, however, no evidence of an expectation gap appearing between auditors and the rest of the groups concerning the statements that the entity is a going concern (Statement 6). Responses to statement 6 indicate that all groups are quite convinced that the auditor has assessed whether an entity being audited is a going concern before an unqualified audit report is issued. The mean score ratings of the auditors' group (4.2) would point to the notion that the auditors' group believe going-concern is more important.

The overall results of this factor as indicated in **Table 5-10** show that an audit expectation gap exists in Saudi Arabia in relation to assurance of an entity in its future viability. The users' group and preparers hold a belief that the unqualified audit report communicated some message about the assurance viability of the audited entity. It is interesting that the auditors' group held the lowest mean score rating. Being significantly different from the mean scores ratings of the preparers group can be interpreted as an indication that the auditors' group may believe that the wording of the unqualified audit report may be improved to more successfully outline their responsibilities in relation to the assurance of the entity as a going concern.

6-2-1-4 Reliability of the Financial Statements Factor:

One of the explanations often offered by the audit profession in Anglo-Western countries for the existence of an expectation gap is the lack of user understanding of the nature of the audit and the work carried out by auditors. The connection between reliability and verifiability of financial information is made by leading financial accounting theorists such as Chamber (1966) (see Lee, 1993, and Higson, 2003).

The factor of reliability in this research included three scales associated with reliability of financial statements. These scales are:

- That the financial statements are free from errors. (Statement 7).
- That the financial statements are free from fraud. (Statement 2).
- That the auditors have verified the data in the financial statements. (Statement 1)

With respect to those scales associated with reliability of the financial statements, **Table 5-1** reveals a significant difference between auditors and the rest of the groups concerning the issue that the financial statements are free from fraud (statement 2). The level of auditors' group response (2.2) indicates that they were more sceptical about the absence of fraud, reflecting their perceived lack of responsibility for prevention and detection. This finding supports the evidence of an expectation gap existing in Saudi Arabia concerning the issue of fraud as indicated by the findings for statements 9 and 13

The three groups are in agreement that the auditors have verified the data in the financial statements, and what is more, this is coupled with a high level of conviction (belief) from the auditors' group (statement 1). This result is perhaps to be expected because, as Mautz and Shraf (1961, pp. 41-42), make clear on this issue: "Unless financial data are verifiable, auditing has no reason for existence". They qualified this by conceding that "verifiable was not taken to mean 'beyond all doubt' instead, verification was a process that 'carries one to position of confidence about any given proposition'" (Higson, 2003, p. 142). Higson (1991) found that more than 56% of the auditors interviews were not happy with it use. However, the results of the preparers group are consistent with that of King and Higson (1994) who found that almost 87% of the financial directors respondents considered the auditors' report implies verification of the data in the financial statements, with over 33% expressing strong agreement (p. 5).

There is no expectation gap to talk of since there are no significant differences in subject groups' responses to statement 7 that the financial statements are free from error. The level of score ratings in response to the statement is in the midpoint thereby indicating that the three groups appear to consider the wording used in unqualified audit report inexplicit to the extent that it cannot be used to denote that the financial statements are free from error.

The overall result of this factor indicates as shown in **Table 5-12**, that there are no significant differences between the subject groups in their responses. In other words, there is no expectation gap that can be said to exist regarding

the reliability of the audited financial statements. It is noticeable here, however, that the auditor group had the lowest mean score among the groups. This may possibly indicate that the words used in the audit report are not explicit enough to denote the reliability of the audited financial statements in relation to auditor's work. The lack of any significant differences between the auditors group and the rest of the groups however, is an indication that the current unqualified audit report used in Saudi Arabia successfully communicates the reliability of the audited financial statements.

6-2-1-5 Usefulness of Decision Making Factor:

Table 5-1 provides details of the results of the mean responses concerning three 'decision usefulness' statements associated with the use of audited financial statements. Tasks include:

- That the audited financial statements are useful for making decisions. (Statement 23)
- That the audited financial statements are useful in monitoring the performance of the entity. (Statement 22)
- That the entity is a good investment. (Statement 3)

The results in the tables indicate that no evidence of an expectation gap was found on the issues of the usefulness of audited financial statements for making decisions (statement 23), the entity being a good investment (statement 3) and the usefulness of audited financial statements in monitoring the performance of the entity (statement 22).

The level of responses of all subjects groups, in particular with the users' group, are slightly above the midpoint concerning these scales associated with the usefulness of the audited financial statement. In relation to statement 23, that the audited financial statements are useful for making decisions, the auditors' group held the highest mean score ratings which were insignificantly different from that of the rest of the groups. This is concurrent with the findings of the study by Schelluch (1996) which found auditors' beliefs to be significantly stronger than those of shareholders with regard to the usefulness of audited financial statements. However, as seen in Chapter three PwC in December 2002 has decided to amend the wording of its opinion, this was to limit liability from legal action by banks (Accountancy, 2002). Inspection of the response ratings of non-auditors groups, particularly the preparers group, indicates a degree of disillusionment in that they do not believe that the message(s) communicated in the audit reports make explicit assertion with regard to these tasks.

The over all results of this factor (as shown in **Table 5-14**) indicate that there is no expectations gap existing in such an area. The level of subjects' responses supports the contention that the audit report is a valuable means of monitoring and making decision on a company being audited.

The next section on the other hand, discusses the results achieved by this study in relation to the usefulness of the expanded audit report by adding some useful issues to be reported by auditors.

6-2-2 Discussion of the Results Achieved From Assessing the Perceptions of the Respondents Toward the Usefulness of Adding Additional Matters to the Unqualified Audit Report:

This section presents the discussion of the results pertaining to the perceptions of the three groups of subjects on the usefulness (or otherwise) of adding additional matters to be reported upon by an auditor.

The results of the 15 statements or proposals are presented under the three factors that were extracted from the results of applying the Principal Components Analysis technique to those 16 statements included in the instrument, as explained in Chapter Five, which resulted in deriving these three valid and reliable factors.

6-2-2-1 Usefulness of the Expansion of the Scope of Auditors' Opinion Factor:

Various approaches have been suggested and examined by researchers and professional bodies to narrow the audit expectation gap to improve communication with users of financial statements. One of these approaches is expansion of auditors' responsibilities. Knutson (1994), for example, proposed a standard for addressing the expectation gap. His opinion is that the fairest standard is to hold auditors responsible for what they should have known, and not to set an impossibly high standard of what they could have known. On the other hand, Hatherly argued that future developments in audit reporting will be necessary in respect of new and emerging audit services such as reporting the information included in the annual report but outside the financial statements (1997, p. 192).

For most companies worldwide, the Annual Report is normally a detailed document containing many items other than the financial statements. Much as the audit report specifies the pages in the Annual Report that have been subjected to audit, a certain amount of doubt may still remain as to whether other information has been subject to scrutiny by the auditor. This is especially the case when other statements in the Annual Report contain financial information.

In recent years voluntary presentation graphics are increasingly used in annual reports of large companies in many countries (see, for example, Beattie and Jones, 2001; 2002). People tend to perceive and retain graphic information more quickly and easily than through narrative discussion or numerical tabulation. Graphs are effective because they are easily understood by both financial and nonfinancial people (Wainer, 1992). In a country such as the US, the auditor may be requested to include a variety of materials with the basic financial statements being presented to owners/managers of privately held companies. This type of report is commonly called a "long-form" report, although that term is no longer used in authoritative literature (Schroeder, 1991).

Unlike the developed world, the annual report published by Saudi companies is the only main formal source available to external users. Users (investors and creditors) can get information from the company management through direct contacts. In Saudi Arabia, section 123 of the Saudi Companies Act requires auditors to check the consistency of the information included in the entity's annual report with the financial statements subject to audit.

Similarly, The Auditing Standards Committee of SOCPA professional opinion No. 8 runs: “Information in documents attached to financial statements audited by the auditor”, requires that auditors ‘should read the other information and if as a result they become aware of apparent misstatements therein, or identify any material inconsistencies with the audited financial statements, they should seek to resolve them’ (SOCPA, 2001).

Six proposals are represented by this factor:

- The usefulness of expanded auditors’ role and responsibility (the scope of auditor’s opinion) to study the chairman’s statement. (Statement 5a)
- The usefulness of expanded auditors’ role and responsibility (the scope of auditor’s opinion) in studying the directors’ report. (Statement 5b).
- The usefulness of expanded auditors’ role and responsibility (the scope of auditor’s opinion) to study any information included in the annual report but outside the financial statements. (Statement 5c)
- The usefulness of graphs and visual media as a way to improve the audit report. (Statement 11).
- The usefulness of expanded auditors’ role and responsibility (the scope of auditor’s opinion) to audit the graphs that are included in the annual report. (Statement 12).
- The usefulness of expanded auditors’ role and responsibility (the scope of auditor’s opinion) to give more information in audit report. (Statement 2).

- The usefulness of expanded auditors' role and responsibility (the scope of auditor's opinion) in adding an explicit statement in the auditor report which elucidates on the auditors' finding in relation to fraud and illegal acts. (Statement 4).

The responses for question 5a) and question 5c) suggest that both the auditors and the directors groups were partly opposed to suggestions of the usefulness of the auditors stating the extent of their examination of the Chairman's Statement and other information that is included in the Annual Report. Conversely, the users group was slightly in favour of such statements being included, i.e. about the extent of their examination of these two items. For the auditors, it may seem rather perplexing that they appear slightly unwilling to make any statement even if that statement only amounted to saying that they did not audit the Chairman's Statement or analyse any other information but had read the disclosures with a view to identifying misstatements or inconsistencies.

However, it is perfectly possible that auditors take it that by including reference to the page numbers of the Annual Report in the audit report that come under their opinion scope, they have made abundantly clear the extent of their duties or they are supporting for not detailing of the scope of audit work in the audit report and crowding it. They might believe that the audit report was not the best place for such issues (Higson, 2003). Similar patterns of responses can be noted between the responses to question 5b) and those of question 5a) and question 5c) where the user group would like some statement of the extent of the auditors' examination of the Directors' Report

but the auditors are slightly less keen to include such a statement. The auditors' reluctance to include some description of the extent of their examination is somewhat at variance with the fact that the Saudi Companies Act specifically provides that they are required to check if the content of the Annual Report is consistent with the figures in the financial statements that are subject to audit.

The mean score for the users group in answering this question, although approximating a neutral response, is significantly different from the scores ratings for the preparers and auditors groups. In general, the responses to question 5 indicate that users would like additional information and for the auditor to state the extent of their examination of that information.

The pattern of mean responses to statement 11, statement 12 and statement 2 is similar to that of statement 5a), statement 5b) and statement 5c). Users believe the use of graphs and an expanded auditors role to audit such graphs would be useful and they are keen for more information to be conveyed in the audit report. On the other hand, the auditors group believe they would not be useful in enhancing the value of the audit report. The difference between the two groups is significant. The mean value of the response of the preparers group falls some way in-between the other two groups which points to a certain level of neutrality to such tasks on their part.

In the same way, the incidence of fraud and or illegal acts may have significance beyond its mere occurrence. This is because potentially it signals higher risk, poor internal controls, lack of integrity and inadequate attention

by directors and senior management in deterring and preventing fraud or illegal acts. From the point of view of the auditors group, they seem unlikely to want to be explicit about issues which by their nature are hard to assess and where an incorrect assessment by them might leave them open to litigation.

The overall result of this factor indicates, as shown in **Table 5-16**, that the groups were mildly in favour of the auditors to expand their opinion scope. However, it is obvious that the mean score ratings are different. For example, the users seem to be slightly in favour of expanding the scope of auditors' opinion to include an increased amount of information. In contrast, the auditors groups were significantly against such an expansion. Thus we could conclude that the three groups are not in total agreement about the usefulness of expanding the auditors' opinion scope.

6-2-2-2 Usefulness of Expanded Audit Report Factor:

Numerous studies done have found that among the factors contributing to the expectations gap is the perception of respondents that a clean (unqualified) audit report signifies the audited entity is a going concern (see Humphrey, 1997). In light of this, some of these respondents suggested that auditors should respond by accepting that they could do more to provide users with assurance about going concerns and the possibility of fraud (see section 3-3 of Chapter three of this thesis). It should also be acknowledged that the auditor respondents, however, usually coupled the increase in their responsibilities with a requirement that any changes should not leave them open to expensive litigation (Manson and Zaman, 2001).

Although there has been considerable discussion of the need for disclosures about an entity's internal control system, the importance attached in many quarters to internal control is an acknowledgement of its link with such issues as the safeguarding of a company's assets and also, in more general terms, as an indicator of how competently the entity is being managed. It is likely that added impetus was given to the debates about the need for disclosures about internal control by well-publicized scandals, such as Enron and WorldCom, which highlighted the costly consequences of deficiencies therein.

It is within this context that we are here discussing the degree to which our three groups would welcome the expanded standard unqualified audit report currently used in the Kingdom with its additional disclosure requirements for auditors to relate to internal controls, materiality level and for them to the extent to which the entity is a going concern.

Four proposals are represented by this factor. These are:

- The usefulness of the expanded audit report in indicating the scope of auditors' study of the internal control structure of the entity audited. (Statement 6a).
- The usefulness of the expanded audit report which indicates the extent to which the auditors rely on the internal control of the entity in course of their audit. (Statement 6b).
- The usefulness of the expanded audit report which goes to length of indicating the materiality level that is used by auditors. (Statement 6c).

- The usefulness of the expanded audit report in adding an explicit statement of the auditors' assessment of the going concern status of the audited entity. (Statement 3).

The data shows that the users' group is interested in the issue of internal control and in particular the extent to which the auditors have examined and relied upon the internal controls. This is evidenced by the mean responses to statement 6a) and statement 6b) and can be seen in **Table 5-2**. The likelihood is that the users believe that the disclosures would provide them with some impression of risk. For instance, if the auditors have not relied on the internal controls, this would suggest they did not consider them strong enough to reduce their tests of detail. The fact that the response of the auditor group is significantly different from that of the user group may indicate that they do not believe that the disclosures would enhance the value of the audit. On the other hand, auditors may believe that users are not adequately familiar with the practices of auditing to fully understand the nature and potential limitations of disclosures.

The response (the mean score ratings) for the preparers group fell in the agreement side which differed significantly from that of the other two groups, which indicates that they keen and believe that such disclosures would improve on the value of the audit or at least added more credibility to their representations. This result may support the result of statement 19 in pervious section that, this may be an indication of some degree of disillusionment on the part of the preparers group about the recent requirements stipulated by the Saudi Ministry of Commerce. Financial

directors of Saudi corporations were obligated to provide a statement of declaration in conjunction with the financial statements as a signed verification that all statements have been presented in the best of their knowledge.

Auditors normally undertake their audit work and give their report within the context of materiality. For instance, when auditors give an opinion, they are not saying that the financial statements are free of all fraud and error; only it is their opinion that there is no material fraud or error in the statement. Disclosure of the materiality level might provide guidance to users of the extent to which the financial statements could potentially be misstated.

An alternative way of looking at this is to suggest that it provides the quantitative context in which the auditors have arrived at their opinion that the financial statements are 'presented fairly'. The pattern of mean responses to question 6c) is similar to that of question 6a) and question 6b). Users believe such disclosures would be useful. On the other hand, the auditors group believe they would not be useful in enhancing the value of the audit. The difference between the two groups is significant. As with question 6a) and question 6b), the mean value of the response of the preparers group is in-agreement side strongly than of the other two groups which points to a certain level of agreement of beliefs toward this disclosure.

The possible reasons why the auditor group do not believe disclosure of their materiality level would enhance the value of the audit are numerous. Foremost, they may regard the materiality level as sensitive information that

they do not wish to be known to users, preparers or management from among their clients. Second, it is possible that they might regard a quantitative assessment of materiality as too crude a measure of their judgmental process as to whether an item in the financial statements is material or not and, as such, could potentially mislead users. Lastly, as mentioned by Manson and Zaman (2001) additional disclosures such as this are likely to be seen to remove some of the mystique surrounding the audit process with a disclosure in quantitative terms perhaps, suggesting that an audit is more mechanistic than audit practitioners proclaim.

The results for statement 3 clearly indicate that users (4.0) are particularly keen that the auditors include a statement in the audit report of their assessment of the going concern status of the client. The preparers' responses also actually suggest that they are slightly in favour of the inclusion of a statement about going concern in the audit report. On the other hand, the auditors group was slightly against the inclusion of a statement about going concern in the audit report. The responses to this statement provide evidence that the user group expects much more from auditors in the audit report than auditors seem actually willing to provide. That all the three groups take these issues to be important is not unexpected or surprising. From the point of view of the user group, the ability of the entity to remain a going concern is ineluctably linked with the value of their investment. From the perspective of the auditor group they are unlikely to want to be explicit about issues that by their nature are difficult to assess and where an incorrect assessment by them might leave them likely to face litigation.

The overall results for this factor (as shown in **Table 5-18**) indicated that the three groups are not in agreement about the usefulness of expansion of the current audit report used in Saudi Arabia by disclosing more information about the entity internal control and assessment of it as going concern as a way to improve communication in the audit report. This result is unexpected because, as has been explained above, auditors are unwilling to disclose such information for fear of potential litigation. It would thus appear that the SOCPA needs to seriously consider how they can move towards satisfying a demand by the user group by, perhaps, supplying additional information on the assurance of going concern issues while at the same time limiting the potential litigation risk to auditors.

6-2-2-3 Usefulness of the Adoption of the Free-Form Report Factor:

Estes (1982, p.93) was one among the first to call for a 'free-form' audit report- one that does not have standard wording but is written 'anew, from scratch for each audit'. Hatherly (1997, p. 192) argued that the adoption of the free form report is one of the two possible interrelated developments of the traditional reporting function in the financial statements. An important argument in favour of free-form reporting is that the process of auditing audit is articulated judgment and the free form report allows the auditor's judgment to be visible to the user. Thus, readers can make their own judgment of audit quality (Hatherly et al, 1998, p. 29).

However, Higson (2003, p.153) argues that it is not appropriate to adopt a free-form report unless the auditors agree about the message that they are

trying to communicate at the end of an audit. He states “if auditors struggle to agree on the general message they are trying to communicate at the end of the audit, it is likely that the message specific to a particular company would be even harder to formulate” (2003, p.153).

Hatherly and Brown (1996) suggested that the free-form report should have a section disclosing the issues arising from the audit and their resolution. Traditionally at the end of an audit the company will be sent a management letter by their auditors outlining any issues arising during the audit and also containing advice about how the company could, for example, improve its systems. This letter is usually sent to the board of directors of a company and its content is not divulged to shareholders or any other interest group. Thus, although the auditors legally act on behalf of the shareholders, the latter receive very little in the way of communication or explanation from the auditors. This perspective is at odds with the generally held view that information is a valuable commodity in decision-making. It can be argued that the onus should be on the profession to demonstrate that additional disclosure of issues arising during the audit and other similar disclosures would not be of benefit to users.

It is within this context that the three groups have been asked about the extent to which they would welcome adoption of the free-form reporting by auditors and welcome additional statements about the matters arising during an audit.

Four proposals are represented by this factor.

- The usefulness of the free-form report in its potential for increasing the amount of information conveyed to the users of the financial statements (statement 8).
- The usefulness of the free-form report in increasing the users' ability to evaluate the audited entity's exposure to risk (statement 9).
- The usefulness of the free-form report for increasing the user's understanding of the auditor's role (statement 10).
- The usefulness of reported the difficulties issues arising during an audit (statement 7).

The mean responses to statement 8 and statement 10 indicate that the user and preparers groups are interested in the issue of a free-form report and more specifically, they are slightly above the middle-point of agreement on the usefulness of the free-form report in terms of increasing the amount of information conveyed to the users of the financial statements (statement 8). They are also interested in the usefulness of the free-form report in the way it could possibly increase the user's understanding of the auditor's role (statement 10). As for the auditor group, it is evident that their response for is insignificantly different from that of the user and a preparers group. This would indicate that they do not believe the adoption of such a report would enhance the users' understanding of their role. The mean score for the auditor group (2.9) could actually indicate that they may believe that users are insufficiently familiar with the practice of auditing to fully understand the nature and potential limitations of the their role and duties.

The pattern of mean responses to statement 9 is rather similar to that of statement 8 and statement 10. Users and preparers believe that adopting such a report would be useful, whereas the auditor group believe that it would not be useful. The difference between the three groups is significant. The possible reason why the auditors group do not believe in the usefulness of the free-form report for increasing the users' ability to evaluate the audited company's exposure to risk is, they might regard the users' assessment of the company's exposure to risk as too crude a measure of their judgmental process and, as such, could potentially mislead users.

In response to question 7 the mean value for the user group indicates that they believe the value of the audit would be slightly enhanced by this disclosure. In contrast the mean value for the auditor group suggests that they do not believe the disclosure would enhance the value of the audit. The difference between the mean scores ratings of these three groups was statistically significant. The response from the preparers group indicates that they were less convinced that the disclosure would enhance the value of the audit. Their agreement with the statement was, however, not as strong as that of the users group. The response to this question provides additional evidence that the auditor group is unwilling to provide additional information about the results of their audit and their responses stand in contrast to that of the user group who indicated a preference for additional information.

The overall result of this factor, as shown in **Table 5-20**, point out that there is no significant differences between the groups. The level of agreements also

indicates that all the three groups are not interested in adoption of such a report. This might show that the three groups found the free form report is somehow ambiguous as to how it should be interpreted or it could conceivably be that they dislike its format which has elsewhere been found to increase the users perceptions of the usefulness and rigour of the audit process (Hartherly et al., 1998).

6-3 Summary and Conclusion:

The aim of this chapter was to discuss the results achieved from having engaged in this study. A belief differentials instrument to measure the message(s) communicated through the standard (unqualified) audit report and the usefulness of improvement to such a document was developed, as explained in Chapter Four. The final instrument comprises two parts. The first (Part I) was designed to measure beliefs about the message(s) conveyed by the audit report while Part II dealt with agreement of the three groups to the usefulness in going beyond the standard audit report currently in use.

The research instrument was, as explain in Chapter Four, administered to: members of the Saudi Organization for Certified Public Accountants (Auditors group); Financial directors of the Saudi's Listed Corporations (preparers group); and the users of financial statements (users group).

The results of this study concerning the assessment of the message communicated in the current audit report used in Saudi Arabia found an expectation gap which was quite wide, especially in relation to the

responsibility factor. More specifically, this the expectation gap was found to be particularly wide on the issues of the auditor's responsibilities for fraud prevention and detection, and the auditor's responsibilities for maintenance of accounting records. To a lesser extent, an expectation gap was also found concerning the auditor's responsibility for the soundness of internal controls and the auditor's responsibility in relation to production of the financial statements.

The results gleaned from the factor which dealt with of the purpose of an audit suggest that the current standard audit report is a readable document, enhancing the credibility of the financial statements. Also, the document in current use has been successful in clarifying the purpose of the audit. An audit expectation gap has been seen to exist between auditor and non-audit group concerning the extent of assurance given by auditors, the 'present fairly' and the extent of audit work performed.

In relation to the assurance of entity future viability factor, it has been seen from the results that an audit expectation gap exists over the question of whether the unqualified audit report communicate that the entity management efficiency and the usefulness of audited financial statements in monitoring the performance of the entity.

These findings present a serious challenge for Saudi's professional accounting bodies, as they indicate that considerable potential value from the financial reporting process is being lost as a result of the quite considerable expectation gap in existence in this country. These findings also support the

call by previous studies worldwide for a change from a short-form audit report to the long-form audit report and the need to educate the users about the nature of the audit and the responsibilities and duties of auditors. This is also closely in line with the Saudi policy-makers comment that “we are sympathetic with the attitude which argues that a statement should be included in the scope paragraph of the audit report as to the auditors’ responsibility for fraud, but find it very difficult to express the approach in the audit report in natural language which can be understood by the reasonably competent reader without considerably enlarging the term of the engagement” (Saudi Audit report standard, para 3614).

However, previous research findings clearly indicate that many of the audit expectation gap being experienced in Saudi Arabia is likely to be significantly reduced by changes made to the audit report form and its wording as well as through education of the users of the financial statements, assuming the results in USA, UK and Australia on this issue can be generalised to the situation in Saudi. Of course, the problem with assumptions is that they are not founded on evidence, empirical or otherwise. However, given the vast sway of influence which the Anglo-Western ‘Big 5’ auditing firms have had over Saudi auditing practices (see Chapter two), it would seem that to generalise the situation in this case is more a case of ‘reasoned assumption’ than a haphazard and groundless one.

In relation to assessment of the usefulness of additional matters that would be useful if reported upon by auditors to improve communication in the audit report, three factors have been proposed and suggested. These are that: the

expanded the auditors scope of opinion, expanded the audit report to disclose the internal control of the entity and the free form report format should be adopted.

Interestingly, the results reveal significant differences in respondents' views concerning expansion of the scope of auditors' opinion (expanding auditors responsibilities). Both users and directors consider that it would be useful if the auditor indicated either in the audit report or in a separate statement the extent of their examination of the Directors' Report and the Chairman's Statement, but auditors are somewhat reluctant to do so.

Concerning the expanded audit report factor we asked respondents if the value of the audit report would be enhanced if the auditors reported the scope of their study of the client's internal controls, the extent to which they relied on internal controls and the materiality level they used. Users, in contrast to the auditors, believe that such disclosure would be useful in enhancing the value of the audit. Users are particularly keen for there to be an explicit statement, in the audit report, of the auditors' assessment of the going concern status of a company. Directors are also mildly in favour of this, while auditors are slightly against the inclusion of such statements.

In relation to the issue of the usefulness of adoption of the free form report factor, all three groups are in agreement that they are not interested in such a report. The response to the scale about reporting on issues arising during the audit provides further evidence that auditors are unwilling to provide additional information about the results of their audit and their responses

stand in contrast to those of users who indicated a preference for additional information.

Overall, It can be argued that the audit report is of limited value to users and that it needs to be extended to include information about the results of the audit. It is notable that while there have been significant developments in audit methodologies of accounting firms there has been no similar development in the communication of audit findings to users.

Based on these results, the presentation of specific recommendations and their implications is the focus of the next chapter. It hoped that these recommendations might help in making future interventions more successful in tackling the reduction of the audit expectation gap and improve communication of the current unqualified audit report.

Chapter Seven

Summary and Conclusions

7-1 Introduction:

The aim of this chapter is to provide an overall summary and reflect upon the conclusions drawn from the research. It has been structured into four sections. The first section provides a brief summary of the study objectives and how these objectives have been achieved. Section 7-2 deals with the implications for the auditing profession and provides the findings of the study in summary form. This is followed by contributions of the current research in section 7-3 while section 7-4 presents the limitations of the study as well as avenues for future research.

This study aimed to contribute to the literature that has contributed to the debate on the audit expectation gap and the usefulness of audit report. A great deal of auditing literature has acknowledged the existence of an audit expectation gap based on audit report and there has a call to reduce it. One way of achieving such reduction is by altering and changing the wording of the audit report. However, while the study here is of importance to Saudi Arabia, the main focus of these previous literatures has been Anglo-American countries (Australia, New Zealand, UK and US). Accordingly, Garcia Benau and Humphrey (1992) have called for more studies of auditing in non- Anglo-American context, while Christiansen and Loft (1992) highlighted the

importance of examining the increasing internationalisation of the auditing function. Such calls have produced studies of auditing in its international context in Europe and, to a lesser extent, in Asia (see Sakagami et al, 1999; and Ping Hao, 1999). Despite these advances and developments in auditing research and in particular, research into the audit expectation gap based on the audit report, very few studies have focused on the existence of an audit expectation gap within the audit report (one example being Best et al (2001) who examined the existence of an audit expectation gap in Singapore, as has been discussed in Chapter Three).

Thus, the thesis sought, specifically, to examine: (i) the message(s) that are (or are not) communicated in the current unqualified audit report used in Saudi Arabia by examining the extent to which auditors, preparers and users of financial statements appear to be satisfied that such an audit report successfully communicates certain key issues. Of prime consideration was whether differences had arisen in the perceptions of the three groups. Quite logically, any differences in perception would serve as evidence of an audit expectation gap in Saudi Arabia. Identification of these differences would provide a starting point for possible pro-active changes to reduce the expectation gap; and (ii) the extent to which the three groups consider that it would be useful for additional matters to be reported upon by the auditor to improve such a document.

The thesis adopted a similar framework to that of Hatherly et al (1992) and Innes et al (1997) in addressing of an audit expectation gap. An "audit expectation gap" was defined to exist where there are differences in beliefs

between the auditor and the public about the duties and responsibilities assumed by auditors, and the message(s) conveyed by audit reports. The gap comprises the following three levels (see **Figure 1.4** in chapter one):

- What the role and responsibilities of the auditor ideally should be.
- What the responsibilities currently are.
- How these responsibilities are currently carried out.

The first level (**Level 1**) concerns differences in beliefs about what auditors' duties and responsibilities should be. The second level (**Level 2**) reflects differences in beliefs about the duties and responsibilities of the parties to an audit and the messages communicated through the audit reports. The difference between level 1 and 2 is a service vacuum, which represents a shortfall in current audit standards against expectations of auditors and financial reports users.

Two main research designs appeared in previous literature to investigate empirically the existence of any audit expectation gap within the audit report. These are survey design and experimental laboratory techniques. Since the aim of this research was investigate the existence of the expectation gap based in the current unqualified audit report in use as well as to investigate the perception of the three groups participating in this study about the usefulness to go beyond such a report by adding some useful matters to be reported upon by the auditor, it was thought that experimental laboratory techniques would be unsuitable to the tasks, since it lacks the necessary external validity. A better appreciation of the gap could be explored by gaining access to subjects' responses to the concepts in general, rather than

their responses to artificial situations or tasks. For these reasons, this study adopts a survey design using cross-sectional survey methodology. Additionally, it might be worthwhile mentioning that this study is policy-oriented in that it intends to provide policymakers with specific recommendations, based on empirical evidence, in relation to the existence of an audit expectation gap in Saudi Arabia within the current unqualified audit report and the usefulness of improved communication in such document.

The thesis then provides the setting in which auditing is being done in Saudi Arabia. In particular, it describes the development of the auditing profession in the country as well as providing some information about the audit market. Also notable in this background information is the fact that the first national accounting body, the Saudi Organization of Certified Public Accountants (SOCPA), was formed as recently as 1992.

After presenting the nature of the research, a review of relevant literature on the development of audit reports and auditors assurance as well as the empirical academic investigation into the existence and nature of an expectation gap within the audit report was done. There was no evidence, prior to this thesis, of differences in beliefs between auditors and the Saudi financial statements users about the duties and responsibilities assumed by auditors, and the messages conveyed by the unqualified audit report. The majority of the evidence collected, as mentioned above, is from the Anglo-American context (US, UK and Australia). This evidence has indicated the existence of differences in beliefs about auditors' duties between auditors and audit beneficiaries with the differences being more pronounced for the

unsophisticated users. It was actually found out that generally, the more knowledgeable users placed less responsibility on auditors than less knowledgeable users. The evidence from the rest of the world has mainly been concerned with differences in beliefs between auditors and sophisticated users, while some research has investigated the effect that modified wording of audit reports has on users perceptions.

To achieve the research objectives a research instrument was needed, in order to formulate the research instrument, the researcher had to undertake a number of processes conducive to the development and validation of such an instrument.

These processes are as follows: -

- Choice of a scaling procedure to measure beliefs about the meaning in the audit report.
- Identifying the frame of reference.
- Identifying conceptual dimensions under which the researcher can generate a number of scales or variables.
- Generating scales or items under each of the identified conceptual dimensions.
- Collecting data from a pilot study to purify the developed instrument, using the Cronbach alpha approach (Cronbach, 1951).
- Collecting data required by this study, via the research instrument; and

- Evaluating the reliability, dimensionality, and validity of the scales tackled by the current research.

Thus, a belief differentials instrument to measure the message communicated through the standard (unqualified) audit report and the usefulness of improving such a document was developed. The final instrument comprised two parts. The first (Part I) was designed to measure beliefs about the message(s) conveyed by the audit report while Part II dealt with the level of agreement between the three groups of the usefulness of going beyond the standard audit report currently used.

The research instrument was administered to: members of the Saudi Organization for Certified Public Accountants (auditors group); Financial Directors of the Saudi Corporations (preparers group); Saudi financial statement users e.g., loan officers and financial analysts in the 10 Saudi commercial banks and institutions and private shareholders (users group). A pilot study had been carried out prior to the main survey in an effort to refine the instrument design and to identify any errors in the research instrument. In total, twenty-nine out of fifty questionnaires, distributed by drop-off and pick-up methods, were successfully administered. Some of the advantages of using a questionnaire are: it provides a relatively simple and straightforward approach to the study of attitudes, values, beliefs and motives; it may be adopted to collect generalizable information from almost any human population; and highly structured surveys have high amounts of data standardization.

After the methodology section, the thesis then displays the results achieved by mean of the current research. These results provide clear answers to the research objectives, and their clarity forms a basis for the comprehensive discussion of the results which then follows. Among the most important findings, an expectation gap was found to exist especially between the sophisticated users and the un-sophisticated users. Thus the next section provides a summary of the findings and implications of these finding to the Saudi profession.

7-2 Findings Summary and Implications to the Audit Profession:

The results of this study concerning the first objective (regarding the assessment of the message communicated in the current audit report used in Saudi Arabia) found an expectation gap which was noticeably wide, especially in relation to the factor of auditors responsibility. The audit expectation gap was found to be most particularly wide on the issues of the auditor's responsibilities for fraud prevention and detection, and the auditor's responsibilities for maintenance of accounting records. To a minor degree, an expectation gap was also visible on the matter of the auditor's responsibility for the soundness of internal controls and, the auditors' responsibility in relation to production of the financial statements.

The results of the purpose of an audit factor suggest that current standard audit report is a readable document, enhancing the credibility of the financial statements. Also, it has been successful in clarifying the purpose of the audit.

An audit expectation gap was found to exist between auditor and non-audit group concerning the extent of assurance given by auditors, the fairly presented view of the financial statements and the extent of audit work performed.

In relation to the factor of assurance of the entity's future viability, an audit expectation gap was found to exist regarding whether the entity was well managed, whether the entity was run efficiently and if it had been kept free from illegal acts. The overall results of this factor also found an audit expectation gap existed in relation to the auditors' responsibility for such issue (entity future viability). However, these audit expectation gaps may be ameliorated or reduced by changing the unqualified report wordings to more successfully outline the auditor responsibilities in relation to such issue, particularly as it is been observed from the response of this study's subjects in relation to the usefulness of expanded audit report by adding an explicit statement of auditors' assessment of going concern status of the audited entity.

A quite marked expectation gap in the Kingdom of Saudi Arabia leaves the Saudi's professional accounting bodies, in dilemma or at least a challenge that could turn out to be quite serious. These findings indicate that substantial potential value from the financial reporting procedure is being lost as a consequence of this expectation gap. These findings also support the call by previous studies worldwide for a change from a short-form audit report to the long-form audit report and the need to educate the users about the nature of audit and responsibilities and duties of auditors. This is also

closely in line with the views of Saudi policy-makers who have stated that, as much as they are sympathetic with the attitude which argues that a statement should be included in the scope paragraph of the audit report as to the auditors' responsibility for fraud, it is also nigh difficult to express the approach in the audit report in less specialist technical language which can be deciphered and understood by the reasonably competent reader without considerably enlarging the term of the engagement.

Prior research findings of Schelluch (1996) as an example and others clearly indicate that much of the audit expectation gap being experienced in Saudi Arabia is likely to be significantly reduced by changes made to the audit report form and wording as well as through education of the users of the financial statements, but one must also permit the likes of McEnroe and Martens (2001) to air their alternative course of action, that being to have the auditor provide an explanation of his responsibilities at the annual shareholders' meeting and field questions regarding the nature and the scope of the audit. This may be a possible solution assuming the results in the USA, UK and Australia on this issue can be generalised to the situation in Saudi.

The auxiliary, but by no mean inferior objective of this study was to asses the usefulness of additional matters that could be useful if reported upon by auditors as a mean of improving communication in the audit report. Three proposal factors have been suggested, and, to recap, these are: expansion of the auditors' scope of opinion; expansion of the audit report to disclose the internal control of the entity; and adoption of free form report.

The results reveal significant differences in respondents' views concerning expansion of the scope of auditors' opinion (expanding auditor responsibilities). Two out of the three groups participated in this study, the users and the preparers consider that it would be useful if the auditor indicated in the audit report the extent of their examination of the Directors' Report and the Chairman's statement. However, auditors took what they might term a pragmatic approach and are somewhat reluctant to do so.

Concerning the factor of expansion of audit report by disclosing of some information about the internal control of the entity being audited and the auditor's assessment of its going concern status, the users, in contrast to the auditors, were of opinion that such disclosure would be useful in enhancing the value of the audit. Users are singularly keen for there to be an explicit statement, in the audit report, of the auditors' assessment of the going concern status of a company. Preparers are also moderately in favour of this, but auditors are slightly against the inclusion of such statements.

In relation to the issue of the usefulness of adoption of the free form report factor, all three groups are in agreement that they are not interested in such a report. More specifically, the response to the scale about reporting on issues arising during the audit provides further evidence that auditors are unwilling to provide additional information about the results of their audit and their responses are asymmetrical to those of the users who express predilection for additional information.

All things considered, it can be argued that the audit report is of limited value to users and that it needs to be extended to include information about the results of the audit. It is notable that while there have been significant developments in audit methodologies of accounting firms, there has been no similar development in the communication of audit findings to users.

What lies ahead? For the Saudi audit professional body (SOCPA) it is to move forward towards facilitating the provision of more information to users about the findings of the audit as well as more assurance about issues such as fraud.

As on the end note, it is not only the Saudi Arabia Auditing profession that can benefit from the findings of the current research in relation to resetting and revising its audit report standard: the new Gulf Corporation Council Accounting and Auditing Organisation (GCCAAO) may benefit also from the results of this study in setting its audit report standard.

7-3 Contribution of the Study:

Conducting this research has made a number of interesting achievements. These can be summarised into: First, the fundamental challenge, which has faced the researcher, is to develop an instrument that measures the message that are communicated in the current standard report as well as improve such a report. By developing valid and reliable factors and establishing a specific consistent pattern of relationships between them, this study has contributed toward overcoming such a challenge. As Rudestam and Newton (2001, p.86) reported: "Research that concentrates on instrument

development is a valuable enterprise and often makes greater contributions than research which attempts to relate existing measures to each other in some new and yet untried fashion".

Secondly, because there is no theory specifying how the twenty-eight scales that measure the messages that are (or are not) communicated in the unqualified audit report as well as the sixteen statements that measured the usefulness of adding some matters to develop communication in such a document for this study should be grouped together, the researcher conducted an exploratory factor analysis on these items. The use of factor analysis is based on the assumption that these scales are related to each other in ways that can be captured by a few underlying dimensions: the forty-four scales describing the message and the developments of the audit report by summarizing them with a small number of derived variables. Subsequently, relationships between extracted factors were analysed. Thus, these results fill a gap in the literature concerning such relationships.

Thirdly, existing literature on the study of the audit expectation gap and the message that is communicated in the audit report has focused on auditors' views (e.g., Higson, 1991) or those of auditors and MBA students (e.g. Hatherly et al, 1991; Innes et al, 1997). Thus, there is, as King and Higson (1994) suggested, a need for more research comparing the responses of managers. By collecting data from both managers and users and comparing their perceptions with those of auditors, this study has therefore, filled an apparent gap in the literature.

Fourthly, while the findings of this study are bound by the context of the research, they are supported by similar findings in other studies conducted in different countries, particularly in the United States and the United Kingdom. Such supportive confirmation makes the results of this study worthwhile for replication in a number of different contexts.

Fifthly, this study might be the first endeavour to engage in depth in the developing countries. Furthermore, the study could be the first attempt to investigate the existence of an audit expectation gap between auditors and the users of financial statements outside the Western countries context.

7-4 Limitation of the study and avenues for future research:

Researchers identify specific limitations not only to show the extent to which they are prevented from making their findings more rigorous and conclusive but also to help others to avoid them to the benefit of their own field of investigation. This study, indeed, is no exception. Thus, the following limitations need to be listed and noted by researchers interested in the investigation of the existence of an audit expectation gap and the usefulness of an expanded audit report. The limitations and the future research of this research may be summarized in terms of cultural and methodology factor.

Firstly, any study is limited by its research methodology. The empirical evidence of this study is based on a questionnaire survey and therefore the

usual limitations of this kind of method apply here also (see, for example, Bryman (2001); Oppenham (2000)). Thus, this study may not capture the richness of the respondent's views that might be obtained from using alternative research methods. However, the researcher feels that it is possible to argue that the research method was appropriate in providing insight into the research questions posed in the thesis (see, Chapter Four for justifications of using such a method).

Secondly, this research enclosed a copy of the unqualified audit report together with the instrument and required the subject to read it. The research result may therefore be affected by the question of external validity if the audit report was not read in detail but instead treated as a code or symbol (Innes et al 1997; Sedler, 1979).

Thirdly, this study is limited by its context; its results may be applicable only to the Saudi environment and not necessarily to other developing countries, particularly the Gulf Countries which share the influence of a similar socio-economic environment. Hence, it would be interesting to extend the study to such countries, especially after the establishment of the new Gulf Corporation Council Accounting and Auditing Organisation (GCCAA).

Finally, the lack of similar studies in Saudi Arabia has prevented the researcher from integrating his results with such findings. Although this is a limitation, it is, at the same time, one of the strengths of this study, as stated above, for it may be the first attempt to investigate the existence of audit expectation gap based on the audit report and the usefulness of additional

improvements of such a document. Thus, this study invites other researchers to build on its conclusions.

In addition to the above discussion points (avenues) that come with the study limitations there are some area of interest for future research may also investigation of the level of sophistication factor by using the level of accounting education as a suitable proxy for level of sophistication. Future research that further refines the demographic information may determine such a task.

The general similarity of findings of this study and those of other empirical researches (e.g. Schelluch 1996; Best et al 2001; Manson and Zaman 2001) suggests that the globalisation of financial reporting may be leading to a lessening of between-country differences in perceptions and the use of audit terms such as 'true and fair view' or 'present fairly' in financial reporting. This may also partially counter the conclusions by Higson and Blake (1993) that the 'true and fair view' concept contributes to deharmonisation. Thus, it too is an interesting starting point for further research to attempt to clarify the issues involved.

The results of this study provide evidence of the existence of an expectation gap with the current audit reporting standard that is in use in Saudi Arabia. In fact, this standard is similar to that of American SAS 24. In an Islamic society, professional standards that are not compatible with Islam are not possible and are expected to face wide criticism. As Al-Rumaihi (1997) indicates, "one should not put a lot of expectation on the acceptance of

models (e.g. Western models) which are in conflict with Islamic rules” (p. 195). The focus of this thesis was not to provide evidence of the influential role of US practices on the regulation of the auditing profession and the setting of auditing standards in Saudi Arabia. However, given the Islamic nature of Saudi society, an interesting research agenda may be to examine the compatibility of the issued audit report standard with Islamic teachings. Another fruitful research venture would be the possibility of developing Islamic auditing standards.

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Appendices:

Appendix A: Profile of the Kingdom of Saudi Arabia.

Appendix B: Letter of Support.

Appendix C: The Final Questionnaire in Arabic.

Appendix D: The Final Questionnaire in English.

Appendix E: Multiple Comparisons: Users, Preparers, and Auditors: Frequency, LSD test and Kruskal-Wallis regarding Part I of the questionnaire.

Appendix F: Multiple Comparisons: Users, Preparers, and Auditors: Frequency, LSD test and Kruskal-Wallis regarding Part II of the questionnaire.

Appendix A:



The Kingdom of Saudi Arabia

The story of the Kingdom of Saudi Arabia started on the 23rd of September 1932 when Abdul-Aziz Al-Saud, after having militarily united most parts of the Arabian Peninsula, gained world recognition and acceptance of the sovereignty of his newly established nation, the Kingdom of Saudi Arabia (Al-Rehaily, 1992). Such an establishment was, and is still, based on the concepts of the Islamic religion (Al-Farsy, 1997).

The year 1938 was a remarkable year in the history of the Kingdom, when oil fields containing 25% of the world's proven oil resources were discovered in the eastern parts of the country (Al-Farsy, 1997). The discovery of oil had, and is still having, a strong impact on all aspects of life in Saudi Arabia, especially since the 1970s when oil revenue began to rise. (For details on Saudi Arabia and oil, see: Al-Sahlawi (1992), Looney (1992) and Al-Sahlawi (1997)).

Up to the late 1980s, the Saudi economy had been highly dependent on oil revenue. Therefore, an extraordinary rise in the Kingdom's gross domestic product was achieved during the period when oil prices were high, followed by an equally dramatic fall when prices began to decline (for more details, see: Al-Rehaily, 1992; Al-Farsy, 1997).

Following the peak years of oil revenues (from 1980 to 1983) it became necessary to undertake a very considerable downward adjustment in the government's level of expenditure. At the same time, the Saudi economy as a whole, after such rapid development, had to come to terms with the more modest circumstances. To a large extent, the Saudi government's success in coping with these circumstances was attributable to the Kingdom's national long-term economic planning process implemented since 1970 (Ba-Eissa, 1984; Al-Rehaily, 1992; Al-Farsy, 1997). Moustafa (1985) has summarised the historical development of the Saudi economy as comprising five major stages of development, evolving from: an economy based on trade and simple commercial activities to, an economy based on exporting crude oil to, an economy based on refining and exporting crude oil and its products to, an economy bolstered by a substantial increase in oil prices and characterized by diversification and promotion of industry and service-type activities to, an economy impacted by worldwide economic recession, reduction in oil prices, and political instability and local wars (Moustafa, 1985, p. 198).

The Saudi government has been implementing continuous five-year plans aimed at achieving development in most aspects of the Saudi socio-economic and political life (e.g. education, health, human resources, the infrastructure, administration, defence, external assistance, emergency funds, etc.), while reducing the country's dependence on oil and creating a more broadly based economy. The enormous jump in price in the international oil market in 1973 allowed considerable effort to be put into strengthening the private sector's role and to improving education, healthcare and other public services in the country. The earlier development plans were, thus, centred on ensuring that

the huge oil revenues were applied to the establishment of fundamental requirements to economic development. Subsequent development plans, taking into account the prevailing economic climate, focused resources more on consolidation and the government implementation of the Privatisation policy (Al-Farsy, 1997).

Privatisation was identified as a policy objective for the first time in the Kingdom in the Fourth Development Plan 1985-1990. Privatisation became a basic strategic principle of the plan with the private sector given the opportunity to acquire, manage and operate projects operated by the government and provided that a lower cost service or product resulted. (Al-Sarhan and Presley, 2001). These privatisation programs aimed at reducing government expenditure and inviting the private sector to take a more effective part in shaping the national economy. So it was that, Saudi authorities introduced a number of measures as a clear indication of their intention to transform the economy.

In April 2000, the Saudi government issued a law that allowed foreign investors, for the first time, to invest in Saudi Arabia. The new law gave tax incentives to foreign investors exemplified by what the Saudi Finance Minister outlined as a corporate tax rate on foreign investment that would not exceed 30% of the reported income (Alsharq Al-Awsat, April 12, 2000, Wednesday [7806], p. 11). This was by no means, however, the first turn of the key in opening the door to outsiders. In 1997, foreigners were invited to participate in the Saudi equity market through the Saudi Arabian Investment Fund (SAIF), instituted in London. Since November 1999, foreigners have

also been afforded the privilege of being able to participate in the Saudi equity market through open-ended mutual funds offered by Saudi banks (viewed at SAMA web site on 24 June, 2003). Furthermore, Gulf Countries Corporation Council (GCC) citizens are permitted to invest directly in the Saudi equity market. More importantly, the Saudi Finance Minister emphasized that Saudi Arabia was to undergo a wholesale improvement in the accounting and auditing systems that involve the Department of Zakat (Almsgiving) and Income Tax authorities. As recently as 16th June 2003, the Saudi government issued a decree for a project that provided for the establishing of a stock market, which would be the first to operate in the country on an official basis (Al-Eqtisadiyah, June 16, 2003, Monday [3535], p. 1).

Central to an analysis of the turn to an increasingly “laissez-faire” approach by the government and something which is of great import to many of the above mentioned developments is the annual report published by companies operating in Saudi Arabia. This published report is the main vehicle firms use to communicate information to external users. Given that the report invariably contains information on a firm's profitability and liquidity, it is expected to help investors, creditors, and other users make informed decisions about the company.

As seen in Chapter One, the Saudi's Companies Act 1965 section 132 states that a company's financial statements are required to be laid before the company in its annual general meeting. The Act also requires the auditor of a company to provide a report to its members of on the accounts presented at

the annual general meeting. Thus, the auditor's report is a necessary attachment to any Saudi firm's published annual report. It is by the Act addressed to company shareholders and contains the auditor's opinion about whether the company's financial statements are fairly presented. It can thus enhance or weaken the credibility of the management's representations in their financial statements.

The following provides a brief profile of the Kingdom of Saudi Arabia.

Country Name	<p>Conventional long form: Kingdom of Saudi Arabia</p> <p>Conventional short form: Saudi Arabia</p> <p>Local form: Al Mamlakah al Arabiyah as Suudiyah.</p>
Location	Middle East, bordering the Persian Gulf and the Red Sea, north of Yemen
Capital City:	Riyadh (<i>Ar Riyád</i>)
Main Cities:	Makkah, Medina, Jeddah, Dammam
Population:	23,513,330 <i>note:</i> includes 5,360,526 non-nationals (July 2002 est.) (CIA, the World Factbook, 2003)
Population growth rate.	3.27% (2002 est.) (Ibid)
Area	[Sq.km]: 2,149,690
Currency:	1 Saudi riyal = 20 qursh = 100 halala
Language	Arabic
Religion	Muslim
Legal system	Based on Islamic law, several secular codes have been introduced; commercial disputes handled by special committees; has not accepted compulsory ICJ jurisdiction.

Executive Branch:	<p>Chief of state: King and Prime Minister FAHD bin Abd al-Aziz Al Saud (since 13 June 1982); Crown Prince and First Deputy Prime Minister ABDALLAH bin Abd al-Aziz Al Saud (half-brother to the monarch, heir to the throne since 13 June 1982, regent from 1 January to 22 February 1996); note - the monarch is both the chief of state and head of government.</p> <p>Head of government: King and Prime Minister FAHD bin Abd al-Aziz Al Saud (since 13 June 1982); Crown Prince and First Deputy Prime Minister ABDALLAH bin Abd al-Aziz Al Saud (half-brother to the monarch, heir to the throne since 13 June 1982, regent from 1 January to 22 February 1996); note - the monarch is both the chief of state and head of government</p> <p>cabinet: Council of Ministers is appointed by the monarch.</p>
GDB	Purchasing power parity - \$241 billion (2001 est.) (Ibid)
GDB-real growth rate	1.6% (2001 est.) (Ibid)

الرقم : ٥ / ٥.٢
التاريخ : ١٤٤٣ / ٣ / ٦
السوافق : ٢٠٢٢ / ٥ / ١٨

الهيئة السعودية للمحاسبين القانونيين
SOCPA
Saudi Organization For Certified Public Accountants

الإخوة / أعضاء الهيئة السعودية للمحاسبين القانونيين المحترمين

السلام عليكم ورحمة الله وبركاته ،،

في إطار الجهود التي تقوم بها الهيئات الأكاديمية للنبوض بالمينة في المملكة ، يقوم الباحث / سالم عبدالله العتيبي بإجراء بحث تحت عنوان :

قياس وتطوير كفاءة الإتصال في تقرير مراجع الحسابات

وأعد الباحث إستبياناً يطلب بموجبه من ذوي الإهتمام والإختصاص النظر في مساعدته لاستكمال الإستبيان المرفق.

لذا نأمل النظر في مساعدة الباحث ؛ شاكرين لكم حسن تعاونكم.

وتقبلوا تحياتي ،،

الأمين العام

يوسف محمد المبارك

Appendix C: The Questionnaire in Arabic



إستبيان عن تقرير المراجع

حفظه الله

عزيزي المشارك في الاستبيان

السلام عليكم ورحمة الله وبركاته

تهدف هذه الدراسة إلى قياس وتطوير كفاءة الاتصال في تقرير مراجع الحسابات. وحيث اقتضى الأمر استخدام الاستبيان كأداة أساسية لجمع البيانات في هذا البحث، وحيث أنه لن يتم إكمال البحث بدون مشاركتكم وتفاعلكم، لذا تجدون برفقته استبيان لإبداء مرئياتكم عن عدد من الجوانب المتعلقة بتقرير المراجع. أمل التكرم بالاجابه عن الأسئلة المرفقة بصورة دقيقة نظراً لأن إجاباتكم سيكون لها قيمة وتأثير على نتائج الدراسة.

إنني بدون مساعدتكم ودعمكم ساجد نفسي عاجز عن تحقيق أهداف هذه الدراسة مع تقديم الشكر لكم سلفاً فاني اؤكد لكم بأن ما سوف تدلون به من آراء سوف لن يستخدم إلا لأغراض البحث العلمي فقط وانه لن يطلع على إجاباتكم غير الباحث ومن غير معرفة لاسم المشارك في الاستبيان. وأعدكم بإرسال تقريراً ملخصاً عن نتائج الدراسة إذا رغبتم في ذلك.

تقبلوا خالص تحياتي

سالم عبدالله العتيبي

مرشح للدكتوراة في جامعة لفبرا - بريطانيا

إرشاد إلى طريقة إكمال الاستبيان:-

لقد روعي في إعداد هذا الاستبيان أن لا يأخذ من وقتك وجهتك إلا القليل مع تقديري التام لمشاركتك الثمينة في هذا البحث. تتطلب منك معظم فقرات هذا الاستبيان وضع إشارة (✓) في المربع الذي يعبر عن رائك. بالنسبة للجزء الثاني- القسم الأول من هذا الاستبيان فالمطلوب منك عملين متتاليين: أن تقوم بقراءة تقرير مراجع الحسابات المرفق مع هذا الاستبيان بعناية، ثم بعد ذلك تبدي درجة موافقتك من عدمها أمام كل عبارة بوضع علامة (✓) في المربع الذي يعبر عن إجابتك. تذكر أنك تسأل هنا عن إعتقادك بالنسبة لك عبارة، بمعنى أنه ليس هنالك إجابة صحيحة أو غير صحيحة.

كما أود ان أوضح المقصود من بعض المصطلحات الواردة في الاستبيان:

التقرير غير المعياري (التقرير الحر): هو التقرير الذي لا يلزم المراجع باتباع شكل أو ألفاظ أو عبارات أو فقرات محدده ونمطيه، وإنما يتغير بناء على كل عملية مراجعة تبعا لطبيعة نشاط الشركة وتقديرا للمعلومات التي يرى المراجع توضيحها لمستخدمي القوائم المالية.

إذا كان لديك أي تسأل فلا تردد في الاستفسار. وتقبل خالص تقديري

الاسم	فاكس	صندوق بريد	المدينة	هاتف
سالم عبدالله العتيبي	025709995	50168	مكة المكرمة	055577443

الجزء الأول

1_ فضلا حدد العلاقة التي تجعلك تقيم بالقوائم المالية للشركات المساهمة ومن ثم تقرير مراجع الحسابات؟ ارجوا أن تختار علاقة واحدة:

- مستثمر خاص.
- محلل أو مستشار مالي.
- تمويل مصرفي للشركات المساهمة.
- مسئول في احد صناديق الاستثمار الأسهم.
- مسئول عن إعداد القوائم المالية في شركة مساهمة.
- مراجع حسابات

2_ كم مدة خبرتك في عملك الحالي:

- 1-5 سنوات
- 6-10 سنوات
- 11-15 سنة
- أكثر من 16 سنة

3_ ما هو المؤهل الحاسبي الذي تحمله؟

- لا يوجد
- دبلوم
- بكالوريوس
- ماجستير
- دكتوراه

4_ كم مدة خبرتك في مجال المحاسبة؟

- لا يوجد
- 1-5 سنوات
- 6-10 سنوات
- 11-15 سنة
- أكثر من 16 سنة

الجزء الثاني-القسم الاول

بالنسبة لهذا الجزء من هذا الاستبيان فالمطلوب منك فضلا أن تقوم بقراءة تقرير مراجع الحسابات التالي بعناية، ثم بعد ذلك تبدي درجة موافقتك من عدمها ألام كل عبارة بوضع علامة (✓) في المربع الذي يعبر عن إجابتك.

من..... المحاسب القانوني

إلى مساهمي شركة.....

الموضوع: تقرير المراجع

السلام عليكم ورحمة الله وبركاته :

لقد راجعنا قائمة المركز المالي لشركة..... كما هي عليه في..... وقائمة الدخل وقائمة الأرباح المبقاة وقائمة التدفقات النقدية للسنة المنتهية في ذلك التاريخ، والإيضاحات من رقم (.....) إلى رقم (.....) (.....) المتعبة جزءا من هذه القوائم المعدة من قبل الشركة وفقا لنص المادة (123) من نظام الشركات والمقدمة لنا مع كافة المعلومات والبيانات التي طلبناها. وكانت مراجعتنا وفقا لمعايير المراجعة المتعارف عليها، واشتملت على فحص السجلات المحاسبية والإجراءات الأخرى التي رأيناها ضرورية لتكوين درجة معقولة من القناعة تمكنا من إبداء الرأي على القوائم المالية.

وفي رأينا أن القوائم المالية المذكورة أعلاه ككل:

(1) تظهر بعدل المركز المالي لشركة..... كما هو في..... ونتائج أعمالها وتدفقاتها النقدية للسنة

المنتهية في ذلك التاريخ، في ضوء العرض والإفصاح للمعلومات التي تحتوي عليها القوائم المالية وفقا للمعايير المحاسبية المتعارف عليها الملزمة لظروف الشركة.

(2) تتفق مع متطلبات نظام الشركات والنظام الأساسي لشركة فيما يتعلق بأعداد وعرض القوائم المالية.

التاريخ:.....

التوقيع:.....

المرخص له برقم:.....

أوافق بشدة	أوافق	لا رأي لي	لا أوافق بشدة	أوافق بشدة
				1) أن المراجع قد تحقق من صحة البيانات المشمولة في القوائم المالية.
				2) أن القوائم المالية للشركة خالية من الغش.
				3) أن الشركة ملائمة لآخذ قرارات الاستثمار.
				4) أن الشركة تدير بكفاءة وفعالية.
				5) أن القوائم المالية عادلة (غير مضللة).
				6) أن المراجع ليس لديه شك في استمرارية الشركة.
				7) أن القوائم المالية خالية من الأخطاء.
				8) أن المراجع راضي عن القوائم المالية للشركة.
				9) المراجع مسئول عن اكتشاف كل أنواع الغش.
				10) المراجع مسئول عن قوة وسلامة نظام الرقابة الداخلية للشركة.
				11) المراجع مسئول عن الاحتفاظ بالسجلات المحاسبية للشركة.
				12) المراجع غير مسئول عن إعداد القوائم المالية للشركة.
				13) المراجع غير مسئول عن منع الغش.
				14) المراجع موضوعي وغير متحيز.
				15) المراجع لم يعتمد على الحكم المهني في اختيار إجراءات المراجعة.
				16) مستخدم القوائم المالية يستطيع أن يحصل على قناعة تامة أنها خالية من الأخطاء الجوهرية.
				17) المراجع غير موافق على السياسات المحاسبية المستخدمة في إعداد القوائم المالية.
				18) درجة القناعة في إبداء المراجع لرأيه على القوائم المالية مشار إليها بوضوح في التقرير.
				19) القوائم المالية تظهر بعدل المركز المالي للشركة.
				20) الشركة خالية من التصرفات غير المشروعة.
				21) نطاق عملية المراجعة المنجز واضح في التقرير.
				22) القوائم المالية المدققة من مراجع الحسابات غير مفيدة في مراقبة أداء الشركة.
				23) القوائم المالية المدققة من مراجع الحسابات غير مفيدة في اتخاذ القرارات.

أوافق بشدة	أوافق	لا رأي لي	لا أوافق بشدة
(6) أن عملية المراجعة سوف تكسب قيمة أو أهمية أكبر لو أن المراجع وضح في تقرير المراجعة:			
			(أ) نطاق دراسته لنظام الرقابة الداخلية للشركة.
			(ب) درجة قناعته عن نظام الرقابة الداخلية للشركة.
			(ج) درجة الأهمية النسبية المستخدمة.
			(7) أن عملية المراجعة سوف تكسب قيمة أو أهمية أكبر لو أن المراجع شرح في تقريره أهم الصعوبات التي واجهها أثناء عملية المراجعة وكيفية تغلبه عليها؟
			(8) أن استخدام المراجع للتقرير غير المعياري سوف يمكنه من إعطاء معلومات أكثر لمستخدمي القوائم المالية؟
			(9) أن استخدام المراجع للتقرير غير المعياري سوف يزيد من قدرة مستخدمي القوائم المالية على متابعة احتمالية تعرض الشركة للفشل أو الإلحار؟
			(10) أن استخدام المراجع للتقرير غير المعياري سوف يزيد من قدرة المستخدمين على فهم دور ومستولية المراجع؟
			(11) أن استخدام الرسوم البيانية في تقرير المراجع يكسب التقرير أهمية أكبر؟
			(12) أن دور ومستولية المراجع يجب أن توسع لتشمل فحص الرسوم البيانية الواردة في التقارير السنوية؟

شكرا جزيلاً على تفضلكم بتعبئة هذا الاستبيان ، فضلاً تأكد من أجابتك لجميع الأسئلة ثم أعده بواسطة الفاكس أو البريد إلى:-

سالم بن عبدالله العتيبي ص.ب. :- 50168 مكة المكرمة هاتف:- 055577443 فاكس:- 025709995

إذا كنت ترغب في الحصول على ملخص لنتائج هذه الدراسة فضلاً أكمل البيانات أدناه:

الاسم:-..... الفاكس:-.....

العنوان:-..... الهاتف:-.....

ص.ب:-.....

Appendix D: Final Questionnaire in English



Dear Participant,

This study is conducted to assess the effectiveness of the audit report currently in use in Saudi Arabia by focusing on the messages communicated in the unqualified audit report as well as the usefulness for additional matters that would be useful to be reported upon by the auditors to improve communication in such a document. This, however, would not be possible without your contribution. Therefore, I shall be grateful if you could spare some of your precious time in completing the enclosed questionnaire. I assure you that all complete questionnaires will be dealt with in strict confidence and will be treated anonymously.

Your Sincerely,

Salem Alotaibi

Guidelines for completion of the questionnaire

The questionnaire has been designed to take up a little of your time as possible. The first section of this questionnaire is about demographical data. The second section is contained two parts. **Part I** of this section is contained differential belief statements concern with the message conveyed by the audit report. For this part **Please** read the attach audit report carefully and then tick (✓) your agreement/disagreement to the statement given. The following part, **Part II**, concerns with additional matters that would be useful to be reported upon by the auditor to improve communication of current form audit report used in Saudi Arabia. You also required to tick (✓) your agreement/disagreement with the statements given. **Remember** it is your beliefs that are being asked for- there is no correct or incorrect response. **N.P:** The None Standard Report (Free Form Report) is the audit report which does not follow any standard wording but is written 'anew, from scratch for each audit'.

Thank you very much for help in this matter. If you have any enquire please do not hesitate to contact me:

Name	P.O.Box	City	Fax	Tel
S.Alotaibi	50168	Makkah	025709995	055577443

Section One

Please answer the following.

1. Please indicate which is the role you are usually in when you make a decision about a company? Please choose one.

- Individual Investor/Shareholder.
- Financial Analyst.
- Creditor.
- Institutional Investor.
- Financial Director.
- Auditor.

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

- 1-5 years
- 6-10 years
- 11-15 years
- Over 15 years

3. Please indicate the accounting qualification that you have:

- None
- Diploma
- Bachelors
- Masters
- Doctorates

4. Please indicate the approximate length of your accounting experience:

- None
- 1-5 years
- 6-10 years
- 11-15 years
- Over 15 years

Section Two: Part I

Please Read the attach audit report carefully.

Auditors' Report to the Annual General Meeting of Members of X company

Scope of audit:

We have audited the statements of financial position of X Company Limited as at xx and the related statements of income, retained earnings and source and applications of funds for the year ended. The financial statements are set out on page x to x. In accordance with article 123 of the Company Law, the overall responsibility for the preparation of the financial statements is that of the Company's management. We have obtained all information and explanations, which we considered necessary for our audit. We conducted our audits in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinion.

Unqualified opinion:

In our opinion, such financial statements taken as a whole:

- 1) Present fairly, in all material respects, the financial position of the Company as at xx and the results of its operations and its cash flows for the year then ended in conformity with generally accepted accounting principles; and,
- 2) Comply with the requirements of the Regulations for the Companies and the Company's Articles of Association with respect to preparation and presentation of financial statements.

Signature

License Number.....

Date.....

Now that you have read the audit report please indicate the extent to which you agree/disagree with each of the following statements.

	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
1- The auditor has verified the data in the financial statements.					
2- The financial statements are free from fraud.					
3- The entity is a good investment.					
4- The entity is run efficiently.					
5- The financial statements are free from bias.					
6- The entity is a going concern.					
7- The financial statements are free from error.					
8- The auditor is satisfied with the financial statements.					
9- The auditor is responsible for detecting fraud.					
10- The auditor is responsible for the soundness of the internal control structure of the entity.					
11- The auditor is responsible for maintaining accounting records.					
12- The auditor is not responsible for producing the financial statements.					
13- The auditor is not responsible for preventing fraud.					
14- The auditor is unbiased and objective.					
15- The auditor does not exercise judgment in the selection of auditor procedures.					
16- Users can have absolute assurance that the financial statements are free from material misstatements.					
17- The auditor does not agree with the accounting policies used in the financial statements.					
18- The extent of assurance given by the auditor is clearly indicated.					
19- The financial statements presented fairly.					
20- The entity is free from illegal acts.					

	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
21- The extent of audit work performed is clearly communicated.					
22- The audited financial statements are not useful in monitoring the performance of the entity.					
23- The audited financial statements are not useful for making decisions.					
24- The entity is well managed.					
25- The audit report attaches to the financial statements as a whole and not to any specific items or groups of items.					
26- The inclusion of an audit report enhances the credibility of the financial statements.					
27- The purpose of the audit is clearly communicated in the audit report.					
28- The audit report is readable.					

Section Two: Part II

Please indicate the extent to which you agree/disagree with each of the following statements.

	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
1- The information conveyed in the current audit report meet users needs.					
2- The auditor should give more information in the audit report.					
3- In future, there should be an explicit statement in the audit report of the auditors' assessment of going concern status of the client.					
4- In future, there should be an explicit statement in the audit report of the auditors' findings in relation to fraud or illegal acts.					
5- It would be useful for auditor to indicate in the audit report the extent of their examination of:					
a) The Chairman's Statement.					

	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
b) The Director's Report.					
c) Any other information included in the annual report but outside the financial statements.					
6- The value of the audit would be enhanced if the auditor reported in the audit report in respect of each audit engagement:					
a) The scope of their study of the client's internal controls.					
b) The extent to which they relied on the internal controls.					
c) The materiality level they used.					
7- the value of the audit would enhance if, for each audit, the report explained the most difficult issues arising in the audit and how they had been resolved.					
8- The non-standard wording report form would increase the amount of information conveyed to the users of the financial statements.					
9- The non-standard wording report form would increase the user's ability to evaluate the audited companies' exposure to risk.					
10- The non-standard wording report form would increase the user's understanding of the role of the auditor.					
11- The use of graphs in audit report makes it more understandable.					
12- The auditor's role should be expanded to include auditing the graphs.					

Thank you for completing this questionnaire. Please return it in the replay paid envelope or send it by Fax to:

Mr. Salem A. Al-Otaibi , P.O. Pox 50168 Makkah, Fax 02-5709995 Mobile 055577443

Appendix E
Multiple Comparisons: Users, Preparers, and Auditors: Frequency, LSD test and Kruskal-Wallis towards the message items

The statements	Sample	SD* (%)	DA* (%)	N* (%)	A* (%)	SA* (%)	Mean (St.D)*	LSD TEST	K-W (Chi-sq.)
1- The Auditor has verified the data in the financial statements	Users	4.5	4.5	4.5	54.5	31.8	4.0 (0.98)	NS	4.03
	Preparers	3.6	0	0	71.4	25	4.1 (0.76)	NS	
	Auditors	2.1	6.4	0	42.6	48.9	4.3 (0.93)	NS	
2- The financial statements are free from fraud	Users	13.6	30.3	15.2	34.8	6.1	2.9 (1.2)	Sg. at 0.03 from Au	10.676**
	Preparers	13.8	37.9	0	24.1	24.1	3.1 (1.5)	Sg. at 0.03 from Au	
	Auditors	20.8	56.3	8.3	10.4	4.2	2.2 (1.0)	Sg. 0.03 from both Us & Pr	
3- The entity is a good investment	Users	1.5	26.2	3.1	60	9.2	3.5 (1.0)	NS	0.955
	Preparers	0	17.2	13.8	48.3	20.7	3.7 (0.99)	NS	
	Auditors	2	22	4	62	10	3.6 (1.0)	NS	

4- The entity is run efficiently	Users	4.7	28.1	7.8	51.6	7.8	3.3 (1.1)	Sg. 0.001 from Au	14.739** *
	Preparers	7.1	21.4	14.3	50	7.1	3.3 (1.1)	Sg. 0.003 from Au	
	Auditors	6.5	60.9	8.7	21.7	2.2	2.5 (0.98)	Sg.at 0.001from Us & 0.003 from Pr.	
5- The financial statements are free from bias	Users	1.5	6.1	12.1	43.9	36.4	4.1 (0.93)	Sg.at 0.032 from Pr. & at 0.02 from Au.	8.483*
	Preparers	0	3.4	3.4	37.9	55.2	4.4 (0.74)	Sg.at 0.032 from Us.	
	Auditors	0	0	0	46	54	4.5 (0.50)	Sg.at 0.002 from Us.	
6- The entity is a going concern	Users	1.5	16.9	7.7	41.5	32.3	3.9 (1.1)	NS	1.67
	Preparers	3.4	13.8	10.3	34.5	37.9	3.9 (1.2)	NS	
	Auditors	0	6.3	4.2	54.2	35.4	4.2 (0.73)	Ns	
7- The financial statements are free from error	Users	3	25.8	7.6	54.5	9.1	3.4 (1.0)	NS	2.739
	Preparers	3.4	31	0	55.2	10.3	3.4 (1.1)	Ns	
	Auditors	12	32	4	44	8	3.0 (1.2)	Ns	

8- The Auditor is satisfied with the financial statements	Users	3	16.7	7.6	54.5	18.2	3.7 (1.1)	NS	1.726
	Preparers	0	31	13.8	37.9	17.2	3.4 (1.1)	NS	
	Auditors	6	24	4	52	14	3.4 (1.2)	NS	
9- The Auditor is responsible for detecting fraud	Users	14.9	34.3	4.5	23.9	22.4	3.0 (1.4)	Sg.at 0.01 from Pr & at 0.001 from Au.	35.908* **
	Preparers	4.1	55.2	3.4	13.8	3.42	2.2 (1.1)	Sg.at 0.01 from Us & at 0.027 from Au.	
	Auditors	57.1	36.8	0	6.1	0	1.4 (0.50)	Sg.at 0.001 from Us & at 0.27 from Pr.	
10- The Auditor is responsible for the soundness of the internal control structure of the entity	Users	9.1	30.3	6.1	36.4	18.2	3.2 (1.3)	Sg.at 0.001 from Au.	28.182* **
	Preparers	13.8	37.9	3.4	34.5	10.3	2.9 (1.3)	Sg.at 0.001 from Au.	
	Auditors	30	58	0	12	0	1.9 (0.85)	Sg.at 0.001 from both Us & Pr.	
11- The Auditor is responsible for maintaining accounting records	Users	10.4	44.8	6	22.4	16.4	2.9 (1.3)	Sg.at 0.001 from both Au & Pr.	33.991** *
	Preparers	34.5	48.3	6.9	0	10.3	1.6 (0.61)	Sg.at 0.001 from Us.	

	Auditors	47.9	50	0	0	0	2.1	1.6 (0.71)	Sg.at 0.001 from Us.	
12- The Auditor is responsible for producing the financial statements	Users	25.8	47	6.1	13.6	7.6	2.3 (1.2)	Sg.at 0.001 from Pr & Au.		14.42***
	Preparers	27.6	31	0	24.1	17.2	1.5 (0.51)	Sg.at 0.001 from Us.		
	Auditors	55.1	38.8	0	6.1	0	1.4 (0.50)	Sg.at 0.001 from Us.		
	Users	10.4	32.8	4.5	37.3	14.9	3.1 (1.3)	Sg.at 0.029 from Pr & at 0.001 from Au.		
13- The Auditor is responsible for preventing fraud	Preparers	17.2	51.7	0	20.7	10.3	2.5 (1.3)	Sg.at 0.029 from Us & at 0.009 from Au.		31.297** *
	Auditors	40.8	51	2	4.11	2	1.8 (0.90)	Sg.at 0.001 from Us & at 0.009 from Pr.		
	Users	1.5	7.5	6	47.8	37.3	4.1 (0.92)	Sg.at 0.001 from Au.		
14- Auditor unbiased and objective	Preparers	0	3.4	3.4	55.2	37.9	4.3 (0.70)	NS		10.960* *
	Auditors	2	2	0	30	66	4.6 (0.70)	Sg.at 0.001from Us		
	Users	16.7	43.9	6.1	31.8	1.5	2.6 (1.1)	Sg.at 0.001 from bot Pr & Au.		
15- Auditor exercises judgement in selection of audit procedure	Preparers	20.7	55.2	0	20.7	3.4	4.1 (0.56)	Sg.at 0.001 from Us & at 0.01 from Au.		13.559** *

	Auditors	0	26.5	22.4	36.7	14.3	4.4 (0.49)	Sg.at 0.001 from Us & at 0.01 from Pr.	
16- Users can have absolute assurance that the financial statements are free from material misstatements.	Users	1.5	23.9	4.5	52.2	17.9	3.6 (1.1)	NS	1.122
	Preparers	3.4	13.8	3.4	55.2	24.1	3.8 (1.1)	NS	
	Auditors	4.2	18.8	2.1	50	25	3.7 (1.1)	NS	
17- The Auditor does agrees with the accounting polices used in the financial statements.	Users	1.5	19.4	16.4	40.3	22.4	3.7 (1.1)	NS	4.046
	Preparers	3.4	10.3	10.3	51.7	24.1	4.1 (1.0)	NS	
	Auditors	4.1	10.2	2	51	32.7	4.2 (1.0)	NS	
18- The extent of assurance given by the Auditor is clearly indicated.	Users	1.5	14.9	6	55.2	22.4	3.8 (0.99)	Sg.at 0.015 from Au.	7.969**
	Preparers	6.9	0	0	65.5	27.6	4.1 (0.96)	NS	
	Auditors	0	4.1	2	53.1	40.8	4.3 (0.78)	Sg.at 0.015 from Us.	
19- The financial statements presented fairly.	Users	3	7.5	7.5	55.2	26.9	3.9 (0.96)	Sg.at 0.004 from Au & at 0.001 from Pr.	8.545**
	Preparers	3.4	37.9	0	58.6	0	3.4 (0.80)	Sg. At 0.001 from both Us &Au.	
	Auditors	0	6	0	44	50	4.4 (0.70)	Sg.at 0.004 from Us & 0.001 from Pr..	

20- The entity is free from illegal acts.	Users	7.5	38.8	19.4	28.4	6	2.8 (1.1)	Sg.at 0.003 from Au.	9.740** *
	Preparers	10.3	41.4	13.8	20.7	13.8	2.9 (1.3)	Sg.at 0.015 from Au.	
	Auditors	29.2	37.5	16.7	14.6	2.1	2.2 (1.1)	Sg.at 0.003 from Us.& at 0.015 from Pr.	
21- The extent of Audit work performed is clearly communicated.	Users	4.5	12.1	13.6	56.1	13.6	3.6 (1.0)	NS	0.252
	Preparers	6.9	10.3	3.4	65.5	13.8	3.9 (1.1)	NS	
	Auditors	6	20	4	52	18	3.5 (1.2)	NS	
22- The Audited financial statements are useful in monitoring the performance of the entity.	Users	3	9	11.9	65.7	10.4	3.8 (0.80)	NS	0.182
	Preparers	0	13.8	13.8	58.6	13.8	3.7 (0.88)	NS	
	Auditors	2	24.5	4.1	53.1	16.3	3.5 (1.0)	NS	
23- The Audited financial statements are useful for making decisions.	Users	1.5	10.4	7.5	67.2	13.4	3.8 (0.85)	NS	1.092
	Preparers	3.4	17.2	3.4	58.6	17.2	3.7 (1.1)	NS	
	Auditors	0	10.2	6.1	63.3	20.4	4.0 (0.81)	NS	
24- The entity is well managed.	Users	4.5	23.9	17.9	50.7	3	3.3 (0.95)	Sg.at 0.002 from Au.	11.53***
	Preparers	3.4	20.7	13.8	51.7	10.3	3.4 (1.0)	Sg.at 0.002 from Au.	

	Auditors	10.6	36.2	25.5	27.7	0	2.7 (0.99)	Sg.at 0.002 from both Us & Pr.	
25- The Audit report attaches to the financial statements as a whole and not to any specific items or groups of items.	Users	1.5	6	11.9	55.2	25.4	4.0 (0.86)	Sg.at 0.001 from Au.	10.601**
	Preparers	0	6.9	0	55.2	37.9	4.2 (0.78)	NS	
	Auditors	0	2	2	46	50	4.5 (0.54)	Sg.at 0.001 from Us.	
26- The inclusion of an Audit report enhances the credibility of the financial statements.	Users	0	10.6	0	47	42.4	4.3 (0.83)	NS	3.395
	Preparers	0	6.9	0	48.3	44.8	4.3 (0.80)	NS	
	Auditors	0	2	0	40	58	4.6 (0.76)	NS	
27- The purpose of the Audit is clearly communicated in the Audit report.	Users	3	7.5	7.5	52.2	29.9	3.9 (0.96)	NS	3.871
	Preparers	0	3.4	3.4	65.5	27.6	4.2 (0.65)	NS	
	Auditors	0	8	2	44	46	4.3 (0.84)	NS	
28- The Audit report is readable.	Users	0	3	10.4	71.6	14.9	4.0 (0.62)	NS	4.993
	Preparers	0	3.4	3.4	72.4	20.7	4.1 (0.61)	NS	
	Auditors	0	10	4	46	40	4.2 (0.91)	NS	

* SD= Strongly Disagree, DA= Disagree, N=Neutral, A= Agree, St.D= Standard Deviation

Appendix F
Multiple Comparisons: Users, Preparers, and Auditors: Frequency, LSD test and Kruskal-Wallis towards the expanded statements

The statements	Sample	SD* (%)	DA* (%)	N* (%)	A* (%)	SA* (%)	Mean (St.D)*	LSD TEST	K-W (Chi-sq.)
1- The information conveyed in the current Audit report meet user's needs.	Users	0	34.3	13.4	47.8	4.5	3.2 (0.92)	Sg. At 0.001 from Au.	13.093**
	Preparers	0	24.1	3.4	72.4	0	3.5 (1.1)	NS	
	Auditors	0	14	8	56	22	3.8 (0.87)	Sg. At 0.001 from Us.	
2- The Auditor should give more information in the Audit report.	Users	0	19.4	3	52.2	25.4	3.8 (1.0)	Sg. At .001 from Au	26.725***
	Preparers	0	27.6	13.8	41.4	17.2	3.5 (1.1)	Sg. At 0.003 from Au	
	Auditors	2	54	12	30	2	2.7 (0.80)	Sg. At .001 from Us & at .003 from Pr.	
3- In future, there should be an explicit statement in the Audit report of the Auditor's assessment of going concern status of the client.	Users	0	16.4	1.5	47.8	34.3	4.0 (1.0)	Sg. At 0.001 from Au.	32.460***
	Preparers	0	27.6	0	41.4	31	3.8 (1.1)	Sg. At 0.001 from Au.	
	Auditors	10	46	14	24	6	2.7 (1.1)	Sg. At 0.001 from both US & Pr	

4- In future, there should be an explicit statement in the Audit report of the Auditor's findings in relation to fraud or illegal acts.	Users	0	29.9	1.5	41.8	26.9	3.7 (1.2)	Sg. Ato.001 from AU.	25.434 ***
	Preparers	0	41.4	3.4	20.7	34.5	3.5 (1.3)	Sg. At 0.001 from AU.	
	Auditors	10.2	59.2	8.2	18.4	4.1	2.4 (1.0)	Sg. At 0.001 from both US &Pr	
5a-The Chairman's Statement	Users	4.5	27.3	4.5	53	10.6	3.4 (1.1)	Sg. Ato.001 from both Au.& Pr.	21.403 ***
	Preparers	10.3	51.7	20.7	13.8	3.4	2.5 (0.99)	Sg. At 0.001 from Us.	
	Auditors	8.2	59.2	10.2	20.4	2	2.4 (0.96)	Sg. At 0.001 from Us.	
5b- The Director's Report	Users	4.5	23.9	4.5	55.2	11.9	3.5 (1.1)	Sg. Ato.001 from both Au.& Pr.	24.219 ***
	Preparers	6.9	51.7	20.7	17.2	3.4	2.6 (0.99)	Sg. At 0.001 from Us.	
	Auditors	8	62	8	18	4	2.4 (0.96)	Sg. At 0.001 from Us.	
5c- Any other information included in the annual report but outside the financial statements	Users	4.5	23.9	9	50.7	11.9	3.4 (1.1)	Sg. Ato.001 from both Au.& Pr.	27.219 ***
	Preparers	6.9	58.6	10.3	20.7	3.4	2.5 (1.0)	Sg. At 0.001 from Us.	
	Auditors	12	58	12	18	0	2.3 (0.92)	Sg. At 0.001 from Us.	
6a-The scope of their study of the client's internal controls	Users	0	16.4	9	47.8	26.9	3.8 (1.0)	Sg. At 0.007 from AU.	10.829 **

	Preparers	0	17.2	0	48.3	34.5	4.0 (1.0)	Sg.at 0.005 from Au.	
	Auditors	4.2	29.2	4.2	56.3	6.3	3.3 (1.1)	Sg. At 0.007 from Us & at 0.005 from Pr	
	Users	0	17.9	4.5	50.7	26.9	3.9 (1.0)	Sg.at 0.011 from Au.	10.997 **
6b- The extent to which they relied on the internal controls	Preparers	0	10.3	3.4	51.7	34.5	4.0 (0.90)	Sg.at 0.003 from Au.	
	Auditors	4.2	25	4.2	60.4	6.3	3.4 (1.0)	Sg.at 0.011 from Us & at 0.003 from Pr.	
6c- The materiality level they used	Users	1.5	19.7	21.2	42.4	15.2	3.5 (1.0)	Sg.at 0.019 from Au.	
	Preparers	0	10.3	20.7	51.7	17.2	3.8 (0.87)	Sg.at 0.003 from Au.	7.729*
7- The value of the Audit would enhanced if, for each Audit, the report explained the most difficult issues arising in the Audit and how they had been resolved	Users	7.5	23.9	11.9	34.3	22.4	3.4 (1.3)	Sg.at 0.001 from Au.	
	Preparers	6.9	27.6	17.2	31	17.2	3.2 (1.2)	Sg.at 0.004 from Au.	17.028 ***
8- Non-standard wording would	Auditors	16.3	51	12.2	14.3	6.2	2.4 (1.1)	Sg.at 0.001 from Us & at 0.004 from Pr.	
	Users	10.4	17.9	22.4	43.3	6	3.2 (1.1)	NS	1.246
	Preparers	3.4	31	20.7	41.4	3.4	3.1 (1.0)	NS	

increase amount of information	Auditors	8	38	12	36	6	2.9 (1.1)	NS	
9- The non-standard wording report form would increase the amount of information conveyed to the users of the financial statements	Users	9	16.4	19.4	40.3	14.9	3.3 (1.2)	Sg.at 0.001 from Au.	13.800 ***
	Preparers	3.6	14.3	32.1	42.9	7.1	3.3 (0.94)	Sg.at 0.007 from Au.	
	Auditors	12	44	18	22	4	2.6 (1.1)	Sg.at 0.001 from Us & at 0.007 from Pr.	
	Users	0	23.9	25.4	44.8	6	3.3 (0.92)	Sg.at 0.026 from Au.	
10- The non-standard wording report form would increase the user's understanding of the role of the Auditor	Preparers	0	48.3	10.3	37.9	3.4	3.0 (1.1)	NS.	5.885
	Auditors	8	36	20	32	4	2.9 (1.1)	Sg.at 0.026 from Us.	
	Users	6	22.4	7.5	46.3	17.9	3.5 (1.2)	Sg.at 0.001 from Au.	
11- The use of graphs in an Audit report make it more understandable	Preparers	0	37.9	13.8	37.9	10.3	3.2 (1.1)	Sg.at 0.011 from Au.	18.221 ***
	Auditors	12	54	8	22	4	2.5 (1.1)	Sg.at 0.001 from Us & at 0.011 from Pr.	
	Users	6	32.8	4.5	41.8	14.9	3.3 (1.2)	Sg.at 0.001 from Au.	
12- The Auditor's role should be expanded to include Auditing the graphs.	Preparers	3.4	51.7	6.9	31	6.9	2.9 (1.1)	Sg.at 0.04 from Au.	16.114 ***
	Auditors	16.3	57.1	4.1	20.4	2	2.3 (1.0)	Sg.at 0.001 from Us & at 0.04 from Pr.	

* SD= Strongly Disagree, DA= Disagree, N=Neutral, A= Agree, St.D= Standard Deviation