

AN EMPIRICAL STUDY OF THE AUDIT EXPECTATION GAP IN YEMEN AND HOW TO NARROW THE GAP

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Abstract

A survey research was conducted on a sample of 288 auditors and users of financial statements. Of the 288 questionnaires distributed, 75.69% were returned and analyzed. The results suggested the existence of wide audit expectation gap between the two groups, with respect to auditors' performance. Hence it is suggested that in order to improve the degree of accounting profession and auditing practices in Yemen, authorities may consider adapting accounting and auditing standards, that are suitable to the country's business environment. These standards will provide guidance and rules for all related parties, which have interest and concern, in the accounting and auditing profession. This study adds evidence to the important debate about audit expectation gap, from a region that is relatively under researched.

Keywords: *Audit Expectation Gap; Audit Quality; Financial Statements and Yemen*

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1. Introduction

The financial scandals, such as of Polly Peck (UK), BCCI (U.K.), Enron (U.S.), WorldCom (U.S.) and Parmalat (Italy), have shown that financial crises naturally will result in the reduction of confidence in the auditing profession. This phenomenon may be due to common belief that the stakeholders of the company should be able to rely on its audited accounts as a guarantee of its solvency, propriety and business viability. But the nature and objectives of auditing have been perceived differently by the users and these misperceptions are known as the “audit expectation gap” (Michael and Dixon, 2019). Moreover, the audit expectation gap is not a unilateral phenomenon as it means different things to different people. The existence of the gap cannot be attributed to the failure of the auditors alone and other stakeholders should also share part of the responsibility (Xu and Akther, 2019). In addition, the influence of the economic, political, legal and social environments, which shape the profession, cannot be sidelined. As such, the results, recommendations and treatment recommended for one society, may not be accepted or practical in another (Hudaib and Haniffa, 2007). Accordingly, Zaid (1997) proposes that auditing standards and regulations should be developed on the basis of the society’s values and expectations because otherwise the profession will fail to meet its objectives. Hence in order to solve the profession’s problems, it is imperative to take into consideration the perception of the auditors and users of ‘audit’ and the ‘auditors’ performance’ in the context of the environment being studied (Kunz and de Jager, 2019). Majority of studies on the audit expectation gap have been conducted in developed Western countries, but the extent of such gap has not been investigated in many least developed countries, especially those in the

Middle-Eastern region (Sidani, 2007). Despite the importance of this region, to the world economy, lack of effort has been attributed to these issues. Thus, there is an urgent need for the undertaking of more studies in this region to understand the nature of the audit expectation gap, which may exist. One of these countries is the Republic of Yemen.

The Republic of Yemen is characterized as the least developed country in the Arab world, located at the southern corner of the Arabian Peninsula. Yemen has just recently adopted an open policy for investment, of attracting foreign and domestic investors and boosting economic development and hence there is the need for professional audit services (Tamimi, 2008). Although this means more job positions for auditors, it also translates to more pressure on the profession to effectively perform duties and responsibilities with professionalism. Audit profession in Yemen has substantially changed during the last two decades, due to new policies implemented by the Yemeni government, that have changed the audit market. These changes include the incremental implementation of privatization policy in 1995, which, in turn, changed the public companies’ ownership. Another change is the issuance of the Company Law No.22 in 1997, that regulates companies’ incorporation in Yemen. Further, it mandates the companies’ financial statements to be audited by external auditors. As a result, there is an increasing demand for audit services in Yemen, that has led the Yemeni government, to issue the Law of the Central Agency for Control Audit No. 39 and the Auditing Law No.26 in 1999, which regulate the auditors’ work in the Yemeni audit market (Al-Tamimi and Zidane, 2004). The absence of auditing and accounting standards to be issued by authorities concerned and the professional associations, as well as the lack of professionalism, pose a major threat to

practitioners, customers and other parties **(Jubran, 2010)**. Consequently, the auditors' performance towards the users of financial statements' will be undermined, which in turn, can lead to the emergence of a confidence gap between the auditors and users of financial statements. Yemen has witnessed economic transformation, which subsequently has increased the demand for auditing and assurance services. Together with development, however, auditing in the Republic of Yemen has also faced a crisis of responsibility, credibility and loss of confidence, due to increased financial and economic crises, at both local and global levels. This, in turn, has led many potential investors and shareholders, who have suffered damage as a result of bankruptcy and collapse of many companies, to wonder why auditors did not give warning signals about the economic situation of these companies. A good example for this is what happened in the National Bank, which is one of the largest banks in Yemen, audited by one of the biggest four audit firms, namely; Deloitte and Touche **(Jubran, 2010)**. Various reasons prompted the Researcher to attempt investigating the existence of audit expectation gap in the Republic of Yemen. A number of studies, on the audit expectation gap, have been conducted in countries with established laws and regulations, particularly in developed and newly industrialized countries. The results of these studies show that the audit expectation gap still exists, and as a consequence, they have issued a more extensive set of regulations and standards for professional control but the problem continues to exist **(Turner, et al. 2010)**. Thus, the examination of this issue, in the context of Yemen, is interesting for several reasons.

Firstly, the extant literature on audit expectation gap has been conducted in developed countries and developing countries, which have their own stock market and

implement international auditing standards. Yemen, on the other hand, is a country considered as the least developed country, having no local auditing standards and no laws requiring the auditors to follow the international auditing standards **(Al-Matari, 2008)**. Secondly, there is no stock market in the Republic of Yemen. As stated before, the Republic of Yemen needs to attract foreign and domestic investments. This presents a problem to the auditing profession in the Republic of Yemen, which is not regulated by any known auditing standards. This persuaded the Researcher, to investigate this issue thoroughly, with the hope of highlighting the audit expectation gap in the Republic of Yemen. In the wake of transforming the Republic of Yemen towards a better economy, it is vital to instill confidence among investors. The ill-performed auditing of financial statement, by Deloitte and Touche, led to the collapse of the National Bank in 2005. The bankruptcy of the National Bank weakened the public's trust in Yemeni Banking sector in general. As a result, the role and image of auditing in the Republic of Yemen was badly affected **(Economic, 2006)**.

Thirdly, in Yemen, the audit function has not been amply highlighted. Also, obtaining work, in the Yemeni market of audit services, relies heavily on social relations rather than qualifications. For instance, some cultural characteristics of Yemen, such as strong hierarchical social structure, religion, importance of kinship and personal relationships where tribalism dominates, the meanings of professionalism, accountability and trust can not be expected to influence the auditing profession practices. Fourthly, the accumulating empirical research studies, on the audit expectation gap, might be perceived as a predictor of the seriousness of the problem, indicating the need for investigating the problem. Therefore, this study intends to investigate this gap in the special

context of the Republic of Yemen. This study attempts to contribute to the knowledge body of audit expectation gap in the least developed countries. It attempts to identify the extent to which the audit expectation gap may exist between auditors and users of the financial statements in the Yemeni context, and to highlight possible causes and provide suggestions and recommendations. The Republic of Yemen is chosen as a region to explore and explain the influence of environmental social factors in the audit function and accountability relationships between auditors and users. This choice is justified in terms of access, feasibility in conducting the study there, and most importantly, the Researcher's intimate knowledge of all aspects of Yemeni culture.

Thus, it is the aim of the study, to provide answers to the question of to which extent the audit expectation gap exists in Yemen. In particular, the study aims at answering the following question: How are auditors successful at carrying out their assumed specific functions and roles? This question seeks to explain participants' responses concerning their conceptions regarding the properties related to the auditor's performance. The set of questions, used to identify aspects of auditor performance, consisted of a semantic differential-testing instrument, requiring participants to assess the auditors' performance in several activities.

2. Review of Literature

The expectation gap between auditors and users of financial statements undoubtedly exists all over the globe. It is without a doubt that the audit expectation gap has been in the limelight and it has been a well investigated topic, among professionals and academics, due to the users' concerns regarding the auditors' performance in the past decades (**Kunz and de Jager, 2019**). The issue has been exhaustively highlighted in

the audit profession from the middle of the 1970s to the current time. The audit expectation gap can be viewed from two varying perspectives – from the users' and the auditors' points of view. It is the gap, which exists between what the public expects or needs and what auditors can and should reasonably be expected to accomplish (**Humphrey, et al., 1993**), (**Naynar, et al., 2018**), (**Fulop et al., 2019**) and (**Glover et al., 2019**). It exists because of the auditors' failure to satisfy the different stakeholders' needs and it exists in all economies, whether developing or developed. Studies all around the world investigating the issue, highlight the existence of the gap and various efforts have been expended to narrow it (e.g. in the U.S., **Frank, et al., (2001)**; in the U.K., **Humphrey et al., 1993**; in the Netherlands, **Hassink, et al., 2009**; in Malaysia, **Ariff and Rosmaini, 2008**; in Egypt, **Anis, 2017**; in Jordan, **Masoud, N. 2017**, in Vietnam, **Dung, N and Dang, A, 2019**; and in Saudi Arabia, **Haniffa and Hudaib, 2007**).

3. Statement of the Problem

Such financial scandals, as Polly Peck (U.K.), BCCI (U.K.), Enron (U.S.), WorldCom (U.S.), and Parmalat (Italy), have shown that financial crises naturally result in the reduction of confidence in the auditing profession. This phenomenon may be due to common belief that the stakeholders of the company should be able to rely on its audited accounts as a guarantee of its solvency, propriety, and business viability. But the nature and objectives of auditing have been perceived differently by the users, and these misperceptions are known as the "audit expectation gap".

The financial scandals in the Yemeni setting cannot be ignored. The bankruptcy of the Yemeni National Bank in 1998, reduced financial statement users' confidence and made them

question the auditors' role, responsibilities, and performance. This indicated the existence of the audit expectation gap. The problem of this gap exists in developed and developing economies. One common recommendation, suggested by interested academicians and professional bodies, to narrow this gap in developed and developing countries, is to issue more accounting and auditing standards and guidelines. However, this recommendation would not work in the context of Yemen because it is considered one of the least developed countries and has no local auditing standards and no laws requiring auditors to follow international auditing standards. This is supported by the fact that the influence of the economic, political, legal, and social environments, which shape the profession, cannot be ignored. As such, the results, recommendations, and treatment recommended for one country, may not be accepted or practical in another. Therefore, Yemen needs to set accounting and auditing standards to reduce the gap.

4. Need of the Study

This study would contribute to the auditing literature by enhancing the understanding of the nature of the audit expectation gap in the Republic of Yemen. Such an understanding is important in that it provides an insightful and useful framework for studying the audit expectation gap in some depth. In addition to the contribution to the literature, the Researcher anticipates that the findings of this research may be influential in the formation of policies and will be useful, in particular, to the professional body to develop recommendations to regulators, academics, and other researchers in general. In addition, extant research has been carried out in countries that are different from the Republic of Yemen in terms of economy, politics, social, culture, and legal framework, and education. Consequently, the level of audit expectation gap

reported and the methods suggested to narrow the gap, have taken into consideration the setting of these countries, implying that the results of the previous studies might not be applicable to Yemen. This study reports the level of the audit expectation gap in a unique setting of a country such as Yemen, which has no auditing and accounting standards. This circumstance distinguishes the current study from previous ones, as previous studies examined the respondents' perceptions towards the contribution of auditing and accounting standards in narrowing the audit expectation gap while the present study examines the respondents' perceptions towards the contribution of setting up new auditing and accounting standards towards narrowing the gap.

5. Objective of the Study

The main objective of this study was to investigate whether auditors were successful in carrying out their particular responsibilities.

6. Hypothesis of the Study

Based on the above presented literature, the hypothesis was formulated, as follows:

NH-1: The perceptions concerning the auditors' performance differ substantially among auditors and users of financial statements.

7. Research Methodology

7.1 Sample Selection

Data for the study were obtained, through the distribution of questionnaires to respondents, which comprised auditors and the users of financial statements in Yemen (expert users, bankers and investors). The differences, if any, in the perspectives of these groups was the central focus of the study. There were 272 auditors for the year ended 2014 (Yemeni Association of Chartered Certified Accountants, 2014). Auditors were selected to represent the opinion of the audit profession. With respect to

the users of financial statements in Yemen, there were three types of users. (1) Expert users: there were 85 publicly-held local corporations in Yemen divided into six sectors. These sectors were the manufacturing sector (31 companies), trading sector (20 companies), finance sector, including 9 companies, service sector (17 companies), telecommunication sector (4 companies) and construction/real estate sector (4 companies) (Ministry of Industry and Trade of Yemen, 2014). The users and sample were chosen from these sectors. These included five respondents, from each company, comprising of chief executive officers, finance directors, financial controllers or managers, accountants and internal auditors. The total number of the expert users was 425. Key persons were expected to have some accounting and auditing professional background and were expected to provide a professional opinion. (2) Bankers: There were 17 local banks incorporated in Yemen. The sample of the bankers included four key persons; the manager, financial directors, financial controllers and investment manager. The total number of bankers was 68 (Ministry of Industry and Trade of Yemen, 2014). This group of bankers reported a high degree of exposure to the accounting and auditing work. They participated and contributed to the strategic policies of the companies, by getting involved in transactions related to issuing loans, company's explanation and investment based on their reviewing of the audited financial statements. (3) Investors: Based on the official document issued by the Yemeni Tax Authority, 69 publicly-held companies were owned by local and foreign investors. According to the United Nations Conference on Trade and Development [UNCTAD], (2010), if any foreign investor owns a 10% or more of the company's ordinary shares, the company is considered as a foreign investment. The foreign companies were divided

into seven sectors. These sectors were manufacturing, trading, finance, service, telecommunication, construction, real estate and oil and gas sectors. The selection sample in these foreign companies included five key persons like chief executive officers, finance directors, financial controllers or managers, accountants and internal auditors. The total number of investors, as of 31st December 2014, was 343. It is noteworthy that the 343 respondents were chosen as five key persons from 67 companies, which represented 335 respondents while the rest of eight respondents were selected as 4 persons from two companies. The latter respondents are four not five because the financial directors in these two companies also work as the financial controllers. The justification of selecting this group was the same reason for selecting the key persons in the local companies. In addition, these key persons were grouped together as proxies for the perception of the foreign investors they worked in.

7.2 Source of Data

The study was wholly based on primary data. The questionnaire was constructed in the form of statements, based on a five-point Likert scale, that included five different scales for the answers to the questions; Extremely successful, Successful, Neither successful nor unsuccessful, Unsuccessful, and Extremely unsuccessful. Moreover, it was designed to determine the respondents' perceptions, regarding auditors' performance.

7.3 Period of the Study

The data were collected, for the study, during the year 2014.

7.4 Tools Used in the Study

The Mann-Whitney U Test was applied, as it is considered particularly powerful in this type of research. It was used to test for significant

differences between pairs of groups. In other words, this test will tell the source of the difference.

8. Data Analysis

Multiple comparisons, using the Mann-Whitney Test, were carried out to report the differences in responses between particular groups. The model adopted the Mann-Whitney-U non-parametric test, for identifying significant difference between auditors and each non-audit group (expert users, investors, and bankers) from one side, and between auditors and the overall non-audit groups from the other side. The main purpose of this section is to report the sample groups' perceptions about auditors' performance. The participants were asked to rate the success of auditors against 11 different attributes of performance activities. The overall mean response of the sample groups was above 1.28 but less than 3.15 for all statements. The results indicated that there was slight tendency towards agreement by the four groups, that auditors were successful in performing these activities. However, significant differences in responses were found to exist among the groups. These responses are included in **Table-1**.

Significant differences were noted in response to the statement about the success of auditors at providing a useful service to society. The auditors' group believed that the auditors were successful at providing the service while the non-auditors groups did not fully support the statement. The Mann-Whitney Test confirmed that the responses of the auditors were significantly different from the responses of the non-auditors' group. It was not unexpected that the overwhelming majority of auditors were more willing to be satisfied about them being successful in providing a useful service to society. Significant differences were observed in the responses to the statement about the success

of auditors at detecting errors and irregularities, with the mean responses of the auditors' group at 1.43 and that of non-auditors' group at 2.59. This result indicated that the auditors' group believed that the auditors were extremely successful at detecting errors and irregularities. Also, it indicated that there was slight agreement by non-auditors groups, regarding the success of auditors at detecting errors and irregularities. In other words, there were significant differences in perceptions between auditor group and non-auditor group, toward this statement.

Other significant differences, in the perceptions, were related to the success of auditors at complying with professional rules. The auditors considered themselves as extremely successful at complying with professional rules while the non-auditors' group was divided on this. The results of the Mann-Whitney Test confirmed that the responses between the two groups revealed significant differences. There was strong agreement by auditors' group, with respect to the success of auditors, at enforcing legal requirements. On the other hand, investors disagreed with this assessment of success while bankers and expert users agreed. Therefore, there was significant difference between auditors' group and non-auditors' groups, regarding the success of auditors, at enforcing legal requirements.

In the next statement, the auditors believed themselves to be extremely successful at truthful reporting. In contrast, less agreement was reported by the non-auditors' group, regarding the success of auditors at truthful reporting. Moreover, the Mann-Whitney Test reveal of that the responses of auditors were significantly different from the responses of the non-auditors' group. Similarly, there was agreement among different groups, concerning the success of the auditors at providing useful service to clients. Auditors' group agreed strongly that they were

successful at providing useful service to clients and non-auditors' group also agreed but to a lesser degree. The Mann-Whitney Test indicated that there were significant differences in perception between auditors' group and non-auditors' group. It was not unexpected that the overwhelming majority of auditors were more willing to be satisfied about them being successful in providing useful service to clients. The results of the Mann-Whitney Test revealed two significant differences in the views, related to: (a) Auditors being even-handed with the interests of others. (b) Success of auditors at obtaining sufficient evidence. Thus there was significant difference between the perceptions of the auditors' group and the non-auditors' groups, due to the different degrees of agreement, within different groups.

Other significant differences were revealed in the perceptions, relating to the success of auditors, at making appropriate judgments. While there was agreement by the auditors' group about this statement, there was disagreement by bankers and expert users and less agreement by investors. The Mann-Whitney Test indicated that there were significant differences in perceptions between auditors' group and non-auditors' group. Significant differences in opinions were also found, with respect to the last statement - "act independently without regard to self-interest". There was strong agreement by auditors' group, with respect to the success of auditors to act independently without regard to self-interest while non-auditors' group also concurred. However, there was significant difference between the auditors' group and overall non auditors' group, due to the inconsistency of agreement among the diversified groups towards this issue. This result was not surprising owing to the personal relationships and tribalism in Yemen. In general, results were not surprising in the light of the

collapse of the largest bank in Yemen, after the auditor indicated the bank's success. In addition, Yemeni society is characterized as highly tribal, based on personal relations.

9. Findings of the Study

According to the present study, there were major significant differences in the perceptions of the auditors' group and the non-auditors' groups, indicating the existence of a gap between what the stakeholders, represented by expert users, investors and bankers' expectations of auditors' performance and auditors' actual performance. The existence of an auditing expectations gap should be narrowed effectively.

10. Suggestions

The results of this study recommend to the Yemeni Government to increase the awareness of the importance of developing and applying appropriate rules and regulations, in both accounting and auditing professions, to meet the current needs in Yemen. In other words, it is important to revise and improve the Yemeni laws, regarding both professions.

11. Conclusion

The main aim of the present study was to investigate the existence of the auditing expectation gap and the various methods of narrowing this gap. Therefore, the empirical analysis was initiated with the confirmation of the existence of the gap in Yemen. The findings indicated that the auditors' group cared about the way external auditors fulfilled their tasks as the analysis of the perceptions of the groups, regarding the auditors' success in carrying out various activities, revealed a gap in various aspects. The descriptive statistics analysis particularly showed the non-auditor group's tendency towards agreeing to auditors' success but the auditor group's tendency was greater.

12. Limitations of the study

The study's limitation was that it was applied only to the Yemeni context, without a comparison with any developed or even developing country.

13. Scope for Future Research

Future studies may consider the comparison of the Yemeni context, with any developed or even developing country. This comparison is expected to provide new insights into the audit expectation gap.

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Table-1: Perceptions toward how Successful Auditors are at Particular Activities

Statements	Mean responses (P-Value)				
	Auditors	Bankers	Expert users	Investors	Overall
	n=65	n=13	n=83	n=57	n=153
Diagnose problems.	1.62	2.69*≠	2.06*≠	2.05*≠	2.11*≠
		0	0	0	0
Provide a useful service to society.	1.91	2.69*≠	2.49*≠	2.63*≠	2.56*≠
		-0.002	0	0	0
Detect errors and irregularities.	1.43	2.54*≠	2.53*≠	2.68*≠	2.59*≠
		0	0	0	0
Comply with professional rules.	1.28	1.85*≠	2.13*≠	2.14*≠	2.11*≠
		-0.005	0	0	0
Enforce legal requirements.	1.37	2.23*≠	2.42*≠	3.04*≠	2.63*≠
		-0.006	0	0	0
Report truthfully.	1.31	2.85*≠	2.52*≠	2.51*≠	2.54*≠
		0	0	0	0
Provide a useful service to clients	1.68	2.62*≠	2.43*≠	2.33*≠	2.41*≠
		0	0	0	0
Are even-handed with the interests of others.	1.37	2.31*≠	2.27*≠	2.23*≠	2.25*≠
		0	0	0	0
Obtain sufficient evidence.	1.38	2.00*≠	2.24*≠	2.23*≠	2.22*≠
		-0.014	0	0	0
Make appropriate judgments.	1.95	3.15*≠	3.07*≠	2.68*≠	2.93*≠
		0	0	0	0
Act independently without regard to self-interest.	1.58	2.85*≠	2.53*≠	2.54*≠	2.56*≠
		0	0	0	0

Source: Primary Data (2019) computed using SPSS

Note: Five-point Likert Scale

“1” = Extremely successful; “2” = Successful; “3”= Neither successful nor unsuccessful; “4”= Unsuccessful; and “5”= Extremely unsuccessful. *Significantly different from auditors at p d” 0.05 (Mann-Whitney U-test), ``significantly different from auditors at t d” 0.05 (t-test)