

**The Influence of Islam on Auditors' Professional  
Judgments in Pakistan**

A thesis submitted to Macquarie University in fulfilment of the requirement of the degree of Doctor of  
Philosophy

By

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## Statement of Candidate

I certify that the:

- The work presented in this thesis has not been submitted for a higher degree to any other university or institution.
- The sources of information used, and the extent to which the work of others has been utilized, is acknowledged in the thesis.
- Ethics Committee approval has been obtained for the research presented in this thesis (reference number: 5201400804).

The following summarizes my particular contribution (conception, data collection, analysis and writing) to each of the joint-authored papers in this thesis:

Study 1: *The influence of Islamic religiosity on auditors' preference for more or less judgment*: Conception (50%), data collection (100%), analysis (80%) and writing initial drafts (70%).

Study 2: *The influence of client's religious adherence and gender on auditors' evidence reliability judgment in an Islamic context*: Conception (50%), data collection (100%), analysis (80%) and writing initial drafts (70%).

Study 3: *The influence of auditors' Islamic religiosity and client's religious adherence on conservatism in auditors' judgment*: Conception (50%), data collection (100%), analysis (80%) and writing initial drafts (70%).

**Nazia Adeel**

## **Dedication**

This thesis is dedicated to Abu for making me strong enough to believe in myself and in my dreams and for investing whatever you had in me to make me capable of fulfilling my dreams and to face the world without you.

This thesis is dedicated to Ami for making me a woman as strong as you were.

This thesis is dedicated to Adeel, for your unconditional love, support, and understanding.

This thesis is dedicated to my children Hibba and Ayham for giving me a purpose in life!

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## Abstract

This thesis by publication contributes to the literature on auditors' judgment and decision making by investigating the influence of Islam on auditors' professional judgments. Pakistan, this study's proxy for Islamic countries, provides an appropriate national setting because over 97% of the population strongly identifies with Islam. Pakistan is selected as a proxy for Islamic countries given its adoption, without modifications, of the International Standards on Auditing (ISAs) in 2005 as part of international auditing and accounting convergence. Given the growing influence of Islam on accounting and auditing practices, it is timely to examine its influence on auditors' professional judgments. Auditors' professional judgments pervade virtually all aspects of contemporary financial statement audits and is selected for examination in this thesis because the exercise of informed judgments is referred to as the most important element in applying the firm's audit approach at the various stages of the audit.

This thesis consists of three individual studies. Study 1 is based on a survey conducted in medium-tier auditing firms. Given the calls to provide causal evidence in audit research, Studies 2 and 3 adopted 2x2 between-subjects experimental designs and collected data from Big 4 firms. The overall aim of this thesis is to investigate the influence of Islamic culture on auditors' judgments. Prior research provides evidence of the influence of culture as a broad variable on auditors' judgments; this thesis "unpacks" culture by invoking the concept of Islamic religiosity, which provides sharper insights into auditors' judgments. As such, this thesis contributes to the literature by introducing an Islamic religiosity measure to the audit judgment literature. Together, the three interrelated studies of the thesis provide holistic insights into the influence of Islam on auditors' professional judgments.

Specifically, Study 1 investigates the influence of Islamic religiosity on auditors' preference for more or less judgment in a doubtful debt provision context. This doubtful debt assessment scenario is selected because it involves a considerable level of judgment and is relevant to various audit seniority levels. The Muslim Religiosity Personality Inventory (MRPI), a well-validated and extensively used Islamic religiosity framework, is selected in this study to measure auditors' Islamic religiosity. Based on Krauss et al. (2005) framework, "Islamic values" are referred to as Islamic worldview and "Islamic rituals" are referred to as religious personality. Islamic worldview represents deeply held, core Islamic values while religious personality measures believers' perceptions of rituals, prayers, and worship. The survey was conducted with a sample of 66 auditors in medium-tier auditing firms. Medium-tier auditing firms were selected as an appropriate sample for participation given their mandatory adoption of ISAs. In addition, owing to their smaller size and limited integration with international networks, their firm culture was expected to be similar to other local organizations. The results suggest that auditors who scored high on the overall Islamic religiosity and Islamic worldview scales, on average, have a preference for more judgment. However, the results are not significant for auditors' religious personality levels. The results, however, indicate that regardless of auditors' preference for more or less judgment, there is an issue with the quality of those judgments. More specifically most auditors based their final judgment (the adjustment to the provision for doubtful debt) on unverified information provided by the client. The results suggest evidence reliability assessment concerns, non-compliance with ISAs, inappropriate level of professional scepticism, and conservatism.

Given the auditors' reliance on unverified client-provided information in Study 1, Study 2 introduces a manipulated cultural variable, that is, clients' religious adherence (manipulated as low and high adherence to Islamic religious practices). Clients' gender is also manipulated. Study 2 investigates the influence of clients' religious adherence and gender on auditors' evidence reliability judgments. A 2x2 between-subjects experiment was conducted with 97 auditors in Big 4 auditing firms. Big 4 firms were selected for examination because audit methodologies adopted by Big 4 firms are in line with ISAs, they exhibit a similar organizational culture, and represent a relatively homogenous sample. The results provide evidence that audit evidence provided by a client with high religious adherence is assessed by auditors to be more reliable. However, the gender of the client did not significantly influence audit evidence reliability judgments. The results raise further concerns that are similar to those in Study 1 regarding non-compliance of ISAs within the context of audit evidence reliability assessments, an

inappropriately low level of professional scepticism, and conservatism resulting in negative consequences for audit quality.

Study 3 extends the research by focusing on the level of conservatism in auditors' judgments by specifically examining the influence of auditors' Islamic religiosity and clients' religious adherence on the level of conservatism. Conservatism is selected for examination because it is a core cultural value in society and influences almost all aspects of personal and professional conduct. The MRPI is adopted to measure auditors' Islamic religiosity, Islamic worldview, and religious personality. Clients' religious adherence to Islamic practices is manipulated between subjects as high versus low. The results of a 2x2 between-subjects experiment with 105 auditors in Big 4 auditing firms provide support for the hypotheses that auditors who scored high on the overall Islamic religiosity and Islamic worldview scales, on average, exhibit a higher level of conservatism in their judgments. However, clients' religious adherence and auditors' religious personality do not impact the level of conservatism in auditors' judgments. The results further support the concerns raised by the results of Studies 1 and 2 of this thesis regarding auditors' non-compliance with ISAs and exercise of an inappropriate level of professional scepticism and conservatism resulting in reduced audit quality and materially misstated financial information.

Overall the results of this thesis demonstrate the importance of Islam (specifically Islamic religiosity and religious adherence) as a cultural variable in the auditing context. The results from the three studies highlight a number of significant biases resulting in non-compliance with ISAs, exercise of an inappropriate level of professional scepticism, and conservatism. The results of this thesis also support the recent findings of the International Forum of Independent Audit Regulators' (IFIAR) global annual audit inspection survey (IFIAR, 2018), which highlights many instances of auditors' failure to assess the reasonableness of assumptions, including consideration of contrary or inconsistent evidence regarding accounting estimates (IFIAR, 2018, p. 10).

The findings of this thesis have a number of important implications for cultural audit research, global and regional standards setters, and global audit firms either operating in Islamic countries or employing auditors with an Islamic cultural background. Particularly, the findings of this thesis provide greater insights into auditors' judgments in an Islamic cultural context and will assist global standard setters and auditing firms enhance the quality and consistency of audit practices within and across countries, particularly in response to the international convergence of ISAs as well as the growing cultural diversity in auditing firms. The findings suggest that understanding Islamic culture will assist global standard setters and multinational auditing firms in considering the potential implications of cultural variables such as Islamic religiosity on auditors' judgments and assist them and professional bodies in developing relevant policies, procedures, and training to overcome potential consequential culturally induced biases with a negative impact on audit quality.

## List of abbreviations and acronyms

AAOIFI	Accounting and Auditing Organization for Islamic Financial Institutions
ADB	Asian Development Bank
ANCOVA	Analysis of co-variance
ANOVA	Analysis of variance
AOSSG	Asian-Oceanian-Standard Setters Group
AUD	Australian dollars
CFO	Chief financial officer
CII	Council of Islamic Ideology
GIFR	Global Islamic Finance Report
GOP	Government of Pakistan
HDR	Higher degree research
IAASB	International Auditing and Assurance Standards Board
IAS	International Accounting Standards
ICAP	Institute of Chartered Accountants of Pakistan
IFAC	International Federation of Accountants
IFIAR	Independent Forum of Independent Audit Regulators
IFRS	International Financial Reporting Standards
ISA	International Standards on Auditing
MRPI	Muslim Religiosity Personality Inventory
NRV	Net Realisable Value
PCAOB	Public Company Accounting Oversight Board (US)
PKR	Pakistani rupees
SBP	State Bank of Pakistan
SD	Standard deviation
SDRB	Social desirability response bias
SECP	Securities and Exchange Commission of Pakistan
UAE	United Arab Emirates
USD	United States dollars
WEF	World Economic Forum

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# Chapter 1

## 1. Introduction

### 1.1 Background and context

This thesis provides empirical evidence on the influence of Islam<sup>1</sup> on auditors' professional judgments. Auditing is a judgment-laden venture (Nelson & Tan, 2005; Trotman, Bauer, & Humphreys, 2015) and auditors make continual judgments during the audit process, including whether accounting estimates are reasonable, which accounting methods are appropriate in a given circumstance, and whether internal controls over financial reporting are functioning adequately. Auditors also assess risk and materiality and determine which evidence to collect, and decide whether evidence is sufficient to support a particular audit opinion. Auditing methodologies and standards are designed to support the auditor in obtaining reasonable assurance and require that the auditor exercise professional judgment and maintain professional scepticism throughout the planning and performance of the audit (IFAC, 2014b). Auditors' judgments collectively determine audit quality and, by extension, the quality of the associated financial reports (Griffith et al., 2015).

Auditors' requirement to exercise "appropriate professional judgment" is identified as one of the key elements that create an environment for audit quality, as per the Audit Quality Framework issued by the International Auditing and Assurance Standards Board (IAASB) (IAASB, 2014, p. 12). As part of the recent developments in the global convergence of International Standards on Auditing (ISAs), developed by the IAASB, over 113 jurisdictions have adopted or are in the process of adopting the clarified ISAs into their national auditing standards or using them as a basis for preparing national

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<sup>1</sup> Islam is numerically the second-largest religion, with 1.8 billion followers, and follows the Judaeo-Christian heritage as the third and last of the great monotheistic religions. The word Islam means "tranquillity" or "peace" or "to submit oneself with complete peace of mind" or "to give oneself up to God. Those who "submit to" this path form the umma, the community of Muslims (Lewis, 2001). It is important to note the difference between *Islam* and *Islamic culture*. Islam is the religion that upholds specific basic beliefs and principles which in some cases cannot be compromised. Islam is a comprehensive, prescriptive and rule-based religion with a strict code of *Shariah* (*Quran* and *Sunnah*) that needs to be followed by every believer in every condition (Janin & Kahlmeyer, 2007). In contrast, "Islamic culture," broadly represents many diverse Muslim cultural groups, such as Asian, Middle Eastern, African, European and American Muslims, each with their variations in customs and traditions (Ansari, 2018). Islamic culture (or Islamic based culture) constitutes practices which have developed around Islam and embraced by the people or society (Daniels, 2016). Some customs and traditions may be more motivated by culture than by religion. In some cases, Islamic culture may have imbued local traditions, which are deemed suitable to be integrated within the Islamic community" (Metcalf, 2014).

auditing standards (IFAC, 2017b). This move towards a single set of global auditing standards is driven by assumptions and assertions based on enhancing comparability in audit reporting and improving global audit quality, both within and across jurisdictions. However, there is concern that the substantial cultural differences among countries are likely to influence the implementation of ISAs in different countries (Alagoa, 2015).

Culture has been identified as a confounding element in discussions on auditors' judgment across jurisdictions (Borker, 2012) and is documented as a significant variable in numerous audit judgment studies (Nolder & Riley, 2013). Culture is a complex phenomenon whose abstract nature makes it rigorously difficult for research to adequately investigate it as one unified concept. Thus researchers have identified the need to "unpack" culture in order to understand its underlying influences and their behavioural consequences (Patel, 2004, 2006, Ying & Patel, 2016). However, research to date has generally failed to tease out the constructs of culture that are most likely to influence judgment and decision making, such as religion, values, motives, beliefs, and personality variables (Patel, Harrison, & McKinnon, 2002; Patel, 2004, 2006). In contrast to the assumptions of global standards setters that auditors throughout the world would make similar judgments, cross-cultural research has provided strong evidence that accountants' judgments are not neutral and value-free, and contextual factors, especially culture, influence their judgments (Heidhues & Patel, 2012; Ying & Patel, 2016).

Religion is a central part of culture and has been identified as a variable of interest in numerous audit judgment studies (McGuire, Omer, & Sharp, 2011; Omer, Sharp, & Wang, 2016). Since there is no universally accepted definition of religion, in this research, religion is treated as a cultural system (Geertz & Banton, 1966). The psychology literature suggests that the relationship between religion and culture is very complex: "religion can be a part of culture, can constitute culture, can include and transcend culture, and can be influenced by culture, can shape culture, or can interact with culture in influencing cognitions, emotions and actions" (Saroglou & Cohen, 2011, pp. 1309-1310). Indeed, the growing recognition of religion as a component of culture is evident in contemporary societies and analysis of its role in today's multicultural settings, and globalized accounting firms is much needed (Christiano, Swatos Jr, & Kivisto, 2015).



Islam is one of the most prominent religions in the world (Khalid, 2014). It is important to note the difference between *Islam* and *Islamic culture*. Islam is the religion that upholds specific basic beliefs and principles which in some cases cannot be compromised. Islam is a comprehensive, prescriptive and rule-based religion with a strict code of *Shariah* (*Quran* and *Sunnah*) that needs to be followed by every believer in every condition (Janin & Kahlmeyer, 2007). In contrast, “Islamic culture,” broadly represents many diverse Muslim cultural groups, such as Asian, Middle Eastern, African, European and American Muslims, each with their variations in customs and traditions (Ansari, 2018). Islamic culture (or Islamic based culture) constitutes practices which have developed around Islam and embraced by the people or society (Daniels, 2016). Some customs and traditions may be more motivated by culture than by religion. In some cases, Islamic culture may have imbued local traditions, which are deemed suitable to be integrated within the Islamic community (Metcalf, 2014).

The recent emergence and implications of Islamic *Shariah* accounting, auditing, and corporate governance standards in the context of global convergence make an examination of the influence of Islam on auditors’ professional judgments in Islamic countries timely (Abdul-Baki, Uthman, Olanrewaju, & Ibrahim, 2013; Abdelsalam & El-Komi, 2016). This development has led to a number of collaborative discussions between global and regional standard setters, such as the Asian-Oceanian Standard-Setters Group (AOSSG), the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), and the International Federation of Accountants (IFAC), on issues concerning the suitability of IFRS/ISAs in Islamic countries (AOSSG, 2011). As a result, there have been calls in the literature to investigate the influence of Islam in all domains of business, especially accounting and auditing (Deloitte, 2013; AOSSG, 2014). This thesis responds to these calls by providing empirical evidence of the influence of Islam on auditors’ professional judgments.

Within the context of Islamic influence on auditing and accounting, this thesis sets out to investigate the influence of Islam on auditors’ professional judgments in Pakistan. Pakistan is considered an appropriate setting for this thesis because Islam is the dominant religion and Pakistan has recently attracted international attention owing to the ever-increasing role of Islam in the country’s social and business environments (Reetz, 2009). This overriding influence of Islam on business and economic

activity provides a unique opportunity to investigate the impact of Islam on auditors' professional judgments. Importantly, the constitution of the Islamic Republic of Pakistan mandates that all laws must conform to Islam (GOP, 2018). The Institute of Chartered Accountants of Pakistan (ICAP), the main accounting/auditing standard-setting body, works closely with Securities and Exchange Commission of Pakistan (SECP) and the State Bank of Pakistan (SBP) and is required to observe the pronouncements of the IFAC/IAASB.

This thesis examines the influence of Islam in two ways. First, auditors' Islamic religiosity level is examined by adopting a well-validated and reliable Islamic religiosity framework, the Muslim Religiosity Personality Inventory (MRPI), developed by Krauss et al. (2005). In Studies 1 and 3 of the thesis, auditors' Islamic religiosity level is measured as an independent variable using the MRPI. Second, the influence of Islam is also examined as clients' religious adherence to Islamic practices, which is a manipulated independent variable. Studies 2 and 3 of this thesis adopt 2x2 between-subjects experiments and manipulate the level of clients' religious adherence to Islamic practices. In Study 2 clients' religious adherence is manipulated as high versus low and clients' gender is manipulated as male versus female. In Study 3, a combination of both measured and manipulated Islamic religiosity variables are utilized. Auditors' Islamic religiosity level is measured by using the MRPI religiosity scale, and clients' religious adherence is manipulated as high versus low. Overall the three studies examine the influence of Islamic religiosity and religious adherence by adopting different audit judgment scenarios and aim to provide a holistic examination of the influence of Islam on auditors' judgments.

The remainder of this overview chapter is organized as follows. Section 1.2 provides insights into relevant literature. Section 1.3 presents the aims and objectives of this thesis and includes a summary of the three studies comprising the thesis. Section 1.4 concludes the chapter by outlining the structure of the thesis.

## 1.2 Literature summary

This thesis consists of three individual research papers which are situated within the cross-disciplinary literature involving auditors' professional judgment, international accounting and auditing, the convergence of ISAs, and Islamic influences on accounting and auditing. Additionally, each research paper is based on a different scenario and contains different auditing judgment contexts. A review of the literature summary on the three different auditors' professional judgment contexts adopted in this thesis is provided in this section.

### *1.2.1 Auditors' professional judgment*

For the purpose of this thesis auditors' professional judgment is defined as “the application of relevant training, knowledge, and experience, within the context provided by auditing standards, in making informed decisions about the courses of action that are appropriate in the circumstances of the audit engagement” (IAASB, 2012c, p. 77). Judgment is the most important aspect of auditing as it has a pivotal role in auditors' decision making (Octavian, Mihaela, & Eugeniu, 2010). Regarding auditing, Solomon (1995) concludes that professional judgment pervades virtually all aspects of contemporary financial statement audits. Moreover, the risk-based auditing methodologies of auditing firms reinforce that “the single most important element in applying the firm's audit approach is the exercise of informed judgment at the various stages of audit” (Trotman, 1996, p. 2).

**Professional judgment** is necessary in every engagement that considers audit risk and materiality; the nature, extent, and timing of audit procedures; evaluating the appropriateness and reasonableness of financial statement assertions; and the applicable financial reporting framework. The requirement for auditors to exercise “appropriate professional judgment” is identified as one of the key elements that create an environment for audit quality, as per the Audit Quality Framework issued by the IAASB (IAASB, 2014).

In the global move to adopt a single set of auditing standards countries' unique contextual factors, including culture, can easily be overlooked (Chand & White, 2006; Chand, Patel, & Patel, 2010). A number of studies provide evidence that culture influences auditors' judgment and decision making

(Borker, 2012; Nolder & Riley, 2013; Alzeban, 2015; Bik & Hooghiemstra, 2016; Ying & Patel, 2016; Sunderland & Trompeter, 2017; Houjeir & Brennan, 2017; Bik & Hooghiemstra, 2018). However, operationalization of culture adopted by these studies is considered to be “too broad” and has been criticized for its limited ability to provide richer insights into auditors’ judgments (Patel et al., 2002; Heidhues & Patel, 2011a). Very few studies have “unpacked the black box of culture” to identify its various components and dimensions, which are likely to influence judgments (Patel, 2006, p. 13).

Researchers have emphasized the need to “unpack” culture in order to understand the underlying dimensions of cultural influences and their behavioural consequences (McCort & Malhotra, 1993; Patel, 2006). However, research to date has largely failed to tease out the constructs of culture, such as religion, values, motives, beliefs, and personality variables, that are most likely to influence judgment and decision making (Patel et al., 2002; Patel, 2004, 2006). To unpack the concept of culture in an Islamic context, this thesis invokes the concept of Islamic religiosity, which is a commitment to the empirical and theoretical fundamentals of Islam through which Muslims fulfil the right of God, protect the rights of others, adhere to the divine decrees, abstain from wrong deeds, and worship (Al-Goaib, 2003).

A number of studies have investigated the influence of religiosity in accounting and auditing in the Anglo-American context (Hilary & Hui, 2009; McGuire et al., 2011; Walker, Smither, & DeBode, 2012; Hickman, 2013; Jaggi & Xin, 2014; Walker, Jones-Farmer, DeBode, Smither, & Smith, 2015; Omer et al., 2016; Jaggi & Lewis, 2017; Sauerwein, 2017; Bik & Hooghiemstra, 2018), but most of these studies have used very simplistic proxies for measuring religiosity. For example, Hilary and Hui (2009), McGuire et al. (2011), and Jaggi and Lewis (2017) examine religiosity according to the geographical location of audit offices in religious or non-religious areas. In addition, categorization of high and low religiosity areas in most of these studies is based on a single measure of church attendance (Walker et al. (2012) Hilary and Hui (2009). Evidence suggests that individual religiosity is a better measure and can provide a sharper insight into judgments (Tarakeshwar, Stanton, & Pargament, 2003). This thesis has adopted Islamic religiosity and religious adherence as two independent variables in an Islamic context.

### ***1.2.2 Islamic religiosity***

Al-Goaib (2003) defines Islamic religiosity as the commitment to the empirical and theoretical fundamentals of the religion (Islam) through which Muslims fulfil the rights of God, protect the rights of others, adhere to the divine decrees, abstain from wrong deeds, and worship. Nasr (1987) views Islamic religiosity as the primary means by which Muslims cultivate their connection with God, which is demonstrated through Islamic rituals of prayer, fasting, pilgrimage, and performing charitable deeds. The Islamic religiosity variable, owing to its multidimensional nature, can essentially capture the essence of Islam and is an excellent method to examine religious influence in Islamic cultural contexts (Krauss et al., 2005a; Souiden & Rani, 2015; Usman, 2016).

To provide insights into auditors' judgments in an Islamic cultural context, this thesis adopted an Islamic religiosity framework developed by Krauss et al. (2005): the MRPI, a well-validated and extensively used Islamic religiosity framework (Krauss et al., 2007; Rehman & Shahbaz Shabbir, 2010; Annalakshmi & Abeer, 2011; Othman & Hariri, 2012; El-Bassiouny, 2014). Based on Krauss et al.'s (2005) framework, "Islamic values" are referred to as Islamic worldview, and "Islamic rituals" are referred to as religious personality. This thesis suggests that Islamic worldview, which represents deeply held, enduring, stable, core Islamic values, is likely to influence auditors' judgments while the religious personality construct, which exemplifies rituals, dress code, and appearance and differs from the core values embedded in Islamic worldview, is not likely to influence auditors' judgments.

### ***1.2.3 Religious adherence***

"Religious adherence" is defined as the degree to which an individual adheres to the values, beliefs, and practices promulgated by religion and it plays a major role in individual decision making (Weaver & Agle, 2002; Vitell & Paolillo, 2003; Shukor & Jamal, 2013; Leventis et al., 2018). A number of studies provide evidence of the impact of religious adherence on auditors' judgments in an Anglo-American context (Walker et al., 2012; Omer et al., 2016; Leventis et al., 2018).

Religious adherence is an integral part of Islamic culture (Esposito, 2016). Prior research shows that individuals who have high religious adherence are likely to receive more social acceptance and credibility within an Islamic cultural context (Johansson-Stenman et al., 2009; Jamshidi & Hussin, 2016).

Importantly, views expressed by religious individuals are considered to be more reliable in the cultural context of Pakistan (Maron, 1957; Baqai, 1975; Delavande & Zafar, 2011; Sohaib & Kang, 2014). Therefore, given the importance of religious adherence in the socio-cultural context of Pakistan, this variable is selected for examination in this thesis.

#### ***1.2.4 Audit judgment contexts***

The influence of Islamic religiosity and religious adherence is examined in this thesis in three different audit judgment contexts: auditors' preference for more or less judgment; auditors' audit evidence reliability judgments; and the level of conservatism in auditors' judgments. A brief review of the background literature on the three audit judgment contexts is provided in this section.

#### ***Auditors' preference for more or less judgment***

Recent evidence from cross-cultural audit judgment research shows that cultural variables are important in investigating the differences between auditors' preference for more or less judgment (Schultz & Lopez, 2001; Doupnik & Richter, 2003, 2004; Doupnik & Riccio, 2006). Although this strand of research provides evidence that culture affects auditors' judgments, very few studies that have examined the influence of cultural variables on auditors' preferences for judgment uncritically adopt and operationalize the cultural variables based on Hofstede's (1980) cultural dimensions. For example, Schultz and Lopez (2001), Doupnik and Richter (2003), Doupnik and Richter (2004), Doupnik and Riccio (2006), Chand et al. (2012), and Tsunogaya et al. (2016) uncritically adopt Hofstede's cultural dimensions and Gray's (1988) accounting classification in determining accountants' preference for judgment in cross-cultural settings. Schultz and Lopez (2001) provide evidence that owing to a low score on a cultural measure of uncertainty avoidance; US accountants prefer rules-based judgments. Doupnik and Richter (2003), Doupnik and Richter (2004), and Doupnik and Riccio (2006) provide evidence of the influence of culture on the rules-based interpretation of uncertainty expressions embedded in accounting standards. Futher, Chand et al. (2012) provide evidence that Chinese students exhibit greater conservatism and secrecy than Australian students and have a preference for rules-based judgments in the interpretation and application of IFRS.

Researchers have repeatedly criticized the simplistic assumptions and the theoretical and methodological limitations of Hofstede's (1980) and Hofstede and Bond's (1988) cultural dimensions, and Gray's (1988) accounting values (Baskerville-Morley, 2005; Patel, 2006; Heidhues & Patel, 2011a). For example, Hofstede's (1980) and Hofstede and Bond's (1988) cultural dimensions are criticized because their data are outdated and they equate nation states with cultures based on the simplified assumption and categorization that any society is homogenous, thereby overlooking within-country cultural values (Baskerville, 2003). Therefore, it is suggested that relevant contextual factors, such as religion, motives, beliefs, and values, be incorporated to provide a richer and deeper understanding of the interrelationships between cultural values and auditing judgments (Heidhues & Patel, 2011; Patel, 2004, p. 71).

This thesis supports the critical evaluation of such deterministic and narrowly focused frameworks. Culture has been characterized as "too broad," and researchers have repeatedly criticized its limited ability to provide richer insights into perceptions and judgments (Harrison & McKinnon, 1999; Patel et al., 2002). Cross-cultural auditing research is also in danger of relying on overgeneralizations and an obsession with categorizations and cultural dimensions that often fail to capture the complexity and dynamics of cultures (Heidhues & Patel, 2011a). To overcome this theoretical limitation, this thesis examines the influence of auditors' Islamic religiosity on auditors' preference for more or less judgment and suggests that it is important to "unpack the black box of culture" to identify its various components and dimensions, which are likely to influence these judgments (Patel, 2006, p. 13). Specifically, by invoking the concept of Islamic religiosity in an Islamic cultural context, this thesis suggests that religiosity provides a much stronger and sharper focus for analyzing auditors' preference for more or less judgment in Islamic cultures in comparison with Hofstede's (2011) and Gray's (1988) frameworks. Thus Study 1 of this thesis responds to and investigates the influence of auditors' Islamic religiosity level on auditors' preference for more or less judgment.

### ***Auditors' audit evidence reliability judgments***

Prior research provides evidence that audit evidence reliability judgments have been examined using a number of client-related factors, namely, client competence (Rebele, Heintz, & Briden, 1988; Hirst, 1994; Anderson & Koonce, 1994), client objectivity (Hirst, 1994; Reimers & Fennema, 1999), and client integrity (Goodwin, 1999; Zakari & Ahmad, 2014). Other studies have focused on the impact of audit firm-related factors on audit evidence reliability judgments, such as expert judgments within the audit team (Bamber, 1983), auditors' specialist qualifications (Griffith, 2015), and review partner reactions (Ayers & Kaplan, 2003). Prior studies on auditors' evidence reliability judgments have not considered the possible influence of clients' religious adherence on auditors' judgments.

While the literature has acknowledged the role of religious adherence in the corporate governance environment (Parboteeah, Hoegl, & Cullen, 2008; Hilary & Hui, 2009; Callen, Morel, & Richardson, 2011; Gundolf & Filser, 2013; Du, Jian, Lai, Du, & Pei, 2015), very few studies have addressed this issue in the auditing domain (Sunder, 2005; Alteer, Yahya, & Haron, 2013; Jha & Chen, 2014; Omer et al., 2016; Jaggi & Lewis, 2017; Leventis, Dedoulis, & Abdelsalam, 2018). The limited research conducted so far provides strong evidence of the influential role of religious adherence on auditing judgments, such as ethical judgments (Walker et al., 2012; Hickman, 2013; Saat, Porter, & Woodbine, 2016), going concern judgments (Omer et al., 2016), and audit pricing decisions (Jha & Chen, 2014; Leventis, Dedoulis, & Abdelsalam, 2015; Jaggi & Lewis, 2017).

However, prior research has operationalized religious adherence in two major ways. First, a number of studies have examined religious adherence as a measured independent variable, including belief, rituals, practices, memberships, and religious affiliation (Weaver & Agle, 2002; Muhamad, 2009; Hickman, 2013; Saat et al., 2016; Haron, 2016; Alshehri, Fotaki, & Kauser, 2016; Sauerwein, 2017). Second, researchers interested in examining religious adherence at the audit firm level have operationalized it by adopting very simplistic and crude variables, such as, the number of sights for religious activities (e.g., churches), the religiosity of the religious population as a proportion of the total population (Boone, Khurana, & Raman, 2013), the extent of religious participation within the country where the firm is located (Dyreng, Mayew, & Williams, 2012; Callen & Fang, 2015), geographical



proximity of audit offices within religious and non-religious areas (McGuire et al., 2011; Omer et al., 2016), and a single-item measure of religiosity based on church attendance (Walker et al., 2012).

This thesis extends prior research by adopting a more nuanced approach and for the first time examines clients' religious adherence as a manipulated independent variable and its impact on auditors' evidence reliability judgments. Therefore, this thesis differs significantly from previous research in a number of ways. Jaggi and Lewis (2017) suggest that local religiosity has a significant impact on auditors' risk and trust behaviour, and show that high religiosity enhances mutual trust among auditors and managers, thereby encouraging auditors to recognize the higher reliability of information prepared by managers operating in high religiosity areas. This study extends this relationship of trust and religiosity in auditor–client interaction and investigates whether auditors trust the evidence received from a client with high religious adherence. While Omer et al. (2016) examined the influence of local religiosity on the propensity of auditors to issue a going concern judgment, and Jha and Chen (2014) and Leventis et al. (2018) focused on the impact of religious adherence on audit pricing, this thesis specifically investigates an important area of inquiry, auditors' evidence reliability judgments.

Given that religious adherence is a significantly important variable in the social and religious context in Islamic countries, this thesis suggests that clients' religious adherence is likely to be an important factor in auditor–client interactions. This thesis suggests that if a client's religious adherence level is high, auditors are more likely to trust the information received from them. These predictions are tested in Study 2 of this thesis.

### ***Conservatism in auditors' judgments***

The third relevant stream of literature in this thesis is conservatism in auditors' judgments. A number of studies have examined auditors' conservatism judgments in an Anglo-American context (Kim, Chung, & Firth, 2003; Lee, Taylor, & Taylor, 2006; DeZoort, Harrison, & Taylor, 2006; Firth, Mo, & Wong, 2014; Boyle, DeZoort, & Hermanson, 2015; Chen, Li, Liu, & Lobo, 2015; Lennox & Kausar, 2015; Desai & Chang, 2016; Illueca Muñoz, Norden, & Udell, 2016). However, most previous research has examined auditors' conservatism judgments in relation to a firm's financial information, for example, timeliness of earnings (Basu, 1997; Basu, Hwang, & Jan, 2002), earnings forecast (Lee et al., 2006),

financial information quality (Pae, 2010), and earnings management (Kim et al., 2003). Auditors' conservatism in their judgments is increased by stronger regulatory sanctions specifically with risky clients (Firth et al., 2014), a high estimated risk on clients' bankruptcy (Lennox & Kausar, 2015), and more accountability pressure (DeZoort et al., 2006). Additionally, a number of studies have investigated audit engagement and firm-related factors, such as issues in auditor-client negotiations (Antle & Nalebuff, 1991), decreased auditor independence (Lin, Lin, & Yen, 2014), and increased auditor legal liability (Liao & Radhakrishnan, 2015), and found that these variables increase the level of conservatism in auditors' judgments. An increase in auditors' conservatism after specific events, such as prior audit failure in Big 4 firms (Fafatas, 2010), the global financial crises (Chen, Lam, Smieliauskas, & Ye, 2016) and the collapse of Enron (Cahan & Zhang, 2006; Feldmann & Read, 2010), have also been documented.

However, very few studies have investigated the influence of cultural variables on the level of conservatism in auditors' judgments (Askary, 2006; Mohamed Yunus, Ismail, & Smith, 2012; Kanagaretnam, Lim, & Lobo, 2013; Salter, Kang, Gotti, & Douppnik, 2013; Chen et al., 2015; AlAbbad, 2016). Most of these studies uncritically adopt Hofstede's (2011) and Gray's (1988) cultural frameworks for examining conservatism practices. Chen et al. (2015) provide evidence that clients located in high-trust regions are less likely to receive a modified audit opinion, suggesting that client trustworthiness lowers auditors' reporting conservatism. Kanagaretnam et al. (2013) investigated the cultural dimensions of individualism and uncertainty avoidance in the international banking industry and provide evidence that individualism is negatively related to conservatism and uncertainty avoidance is positively related to conservatism. Additionally, there is evidence of a positive influence of social and family values on accounting conservatism in family-based firms (Ferramosca & Ghio, 2018). Salter et al. (2013) compared social and accounting values in 22 countries and provide evidence that accounting conservatism is greater in countries with more conservative societal and accounting values.

It is important to note that prior research has mostly focused on Anglo-American countries and have suggested that social norms and local values are likely to increase the level of conservatism in auditors' judgments; however, there is not enough evidence of this influence within an Islamic cultural context. Conservatism is one of the basic foundations of Islamic society and most religious,

anthropological, and political literature supports the notion that Islamic doctrines are based on conservatism (McIntosh & Islam, 2010). Some studies have investigated conservatism in accounting and auditing contexts in Islamic countries, but most of these adopt a different context than that applied in this study. For example, Mohamed Yunus et al. (2012) investigated the influence of two ethnic groups in Malaysia on accounting conservatism. This research, however, provides additional insights into understanding auditors' conservatism in an Islamic cultural context by invoking the concept of Islamic religiosity as an independent measured variable. In this regard, it differs from Mohamed Yunus et al. (2012) and suggests that a measured Islamic religiosity variable is a sharper variable than ethnicity in examining auditors' judgments. Additionally, most studies in Islamic countries have investigated conservatism in the Islamic banking and finance industry (Awan & Shahzad Bukhari, 2011; Souiden & Rani, 2015; AlAbbad, 2016; Abdelsalam, Dimitropoulos, Elnahass, & Leventis, 2016). Islamic banks have strong religious norms and moral accountability constraints and thus adopt more conservative accounting policies (Abdelsalam et al., 2016). Most of these studies provide evidence that consumers who score higher on the Islamic religiosity scales exhibit higher conservatism in their decision making and are more likely to prefer an Islamic bank over a conventional bank.

Study 3 of this thesis investigates the influence of auditors' Islamic religiosity level and clients' religious adherence on the level of conservatism in auditors' judgments.

### **1.3 Aims and objectives**

This is a "thesis by publication" which consists of three empirical studies. The thesis aims to provide empirical evidence of the influence of Islam on auditors' professional judgments in Pakistan. The influence of Islam is examined by measuring auditors' level of Islamic religiosity (in Studies 1 and 3) and by manipulating the client's religious adherence level (in Studies 2 and 3) as independent variables. The three dependent variable contexts involve examination of auditors' preference for more or less judgment (in Study 1), auditors' audit evidence reliability judgments (in Study 2), and the level of conservatism in auditors' judgments (in Study 3). The three studies aim to investigate the influence of:

1. Islamic religiosity on auditors' preference for more or less judgment.

2. Clients' religious adherence and gender on auditors' evidence reliability judgments in an Islamic context.
3. Auditors' Islamic religiosity level and clients' religious adherence on the level of conservatism in auditors' judgments.

A summary and overview of the aim of this thesis and the individual objectives of the three empirical studies that comprise the main part of this thesis are shown in Figure 1.1 and 1.2.

**Figure 1.1: Aims and objectives of the thesis and the three studies**

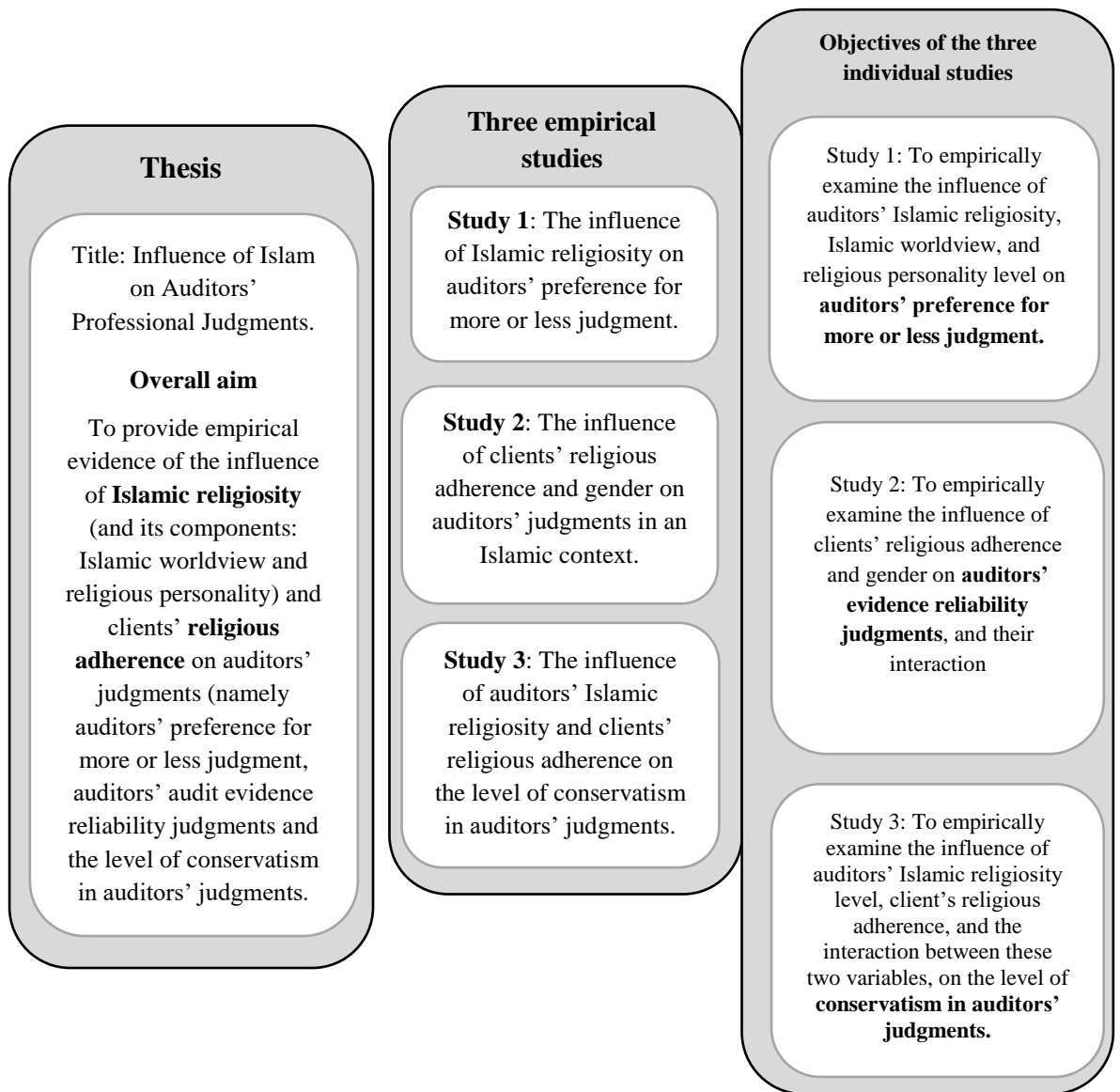
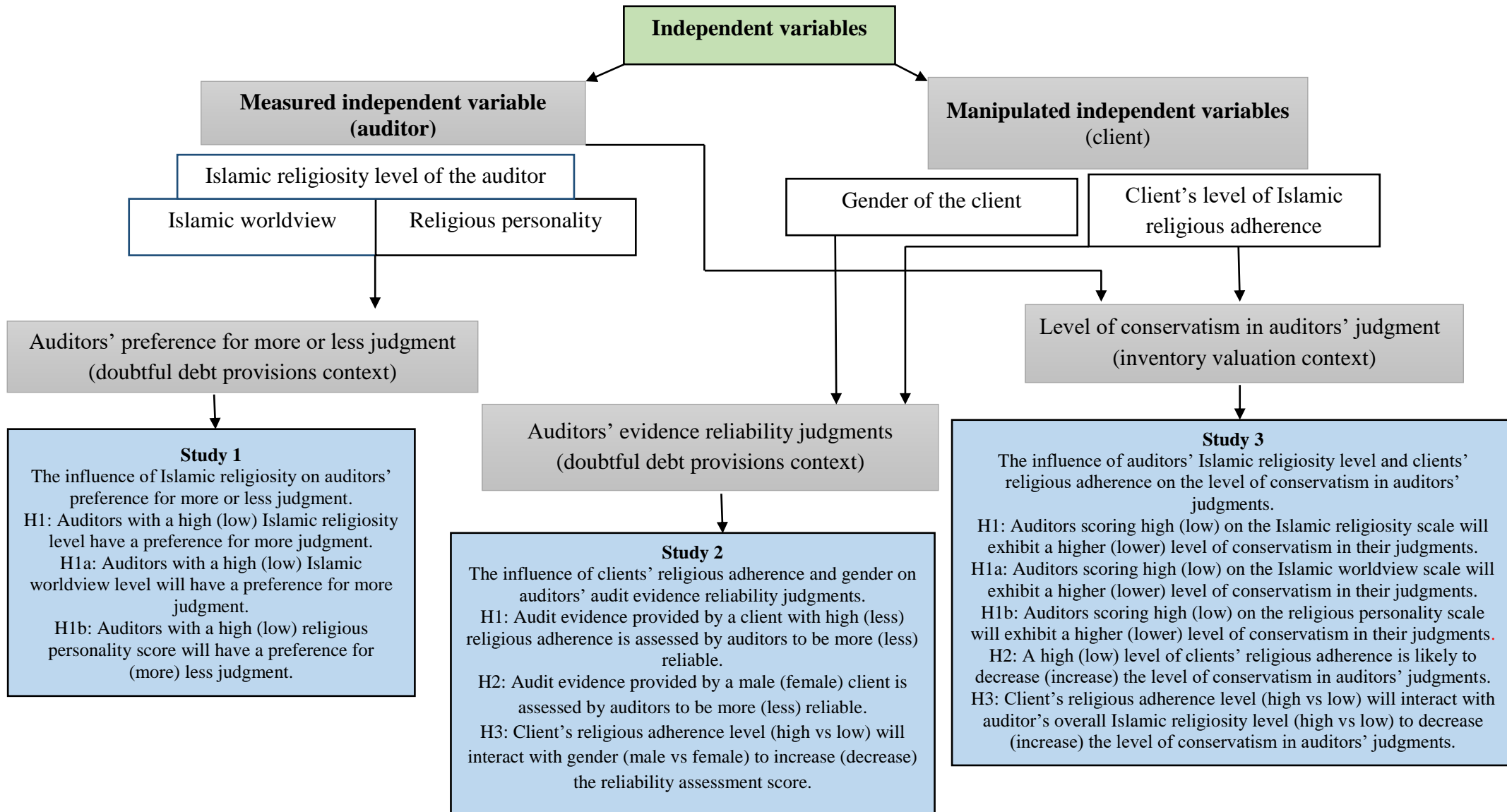


Figure 1.2: Conceptual map of the thesis



### ***1.3.1 Study 1: The influence of Islamic religiosity on auditors' preference for more or less judgment***

This study contributes to the literature by examining the influence of Islamic religiosity on auditors' preference for more or less judgment. ISAs are principles-based standards and require extensive exercise of auditors' professional judgment. Islam, the official religion of Pakistan, however, is primarily legalistic and rules-based and requires little exercise of individual judgment (Maurer, 2010). Pakistan, as a proxy for Islamic countries that have adopted ISAs, provides an appropriate national context to examine auditors' preference for more or less judgment. Evidence shows that the rules-based nature of Islam has a significant influence on accounting and auditing practices in an Islamic context and this might pose a challenge in implementing the principles-based ISAs in Islamic countries. However, prior research has not investigated auditors' preference for judgment in an Islamic cultural context. This study investigates the impact of Islamic religiosity, which is one of the most important cultural forces and is likely to influence auditors' judgments and decision making. It refers to the commitment to the empirical and theoretical fundamentals of Islam through which Muslims fulfil the right of God, protect the rights of others, adhere to the divine decrees, abstain from wrong deeds, and worship (Al-Goaib, 2003), on auditors' preference judgments.

The MRPI framework, a well-validated and reliable Islamic religiosity framework, has been selected to measure auditors' level of Islamic religiosity. The MRPI has been used extensively in business research has been tested for validity and reliability in a number of Islamic countries including Pakistan (Othman & Hariri, 2012). Based on this framework, auditors' Islamic religiosity is categorized into Islamic worldview and religious personality. Islamic worldview represents deeply held, core Islamic values and religious personality measures believers' perceptions of rituals, prayers, and worship.

A survey was conducted with a sample of 66 auditors working in medium-auditing firms in Pakistan. The results from the survey provide support for the hypotheses that auditors who score high on overall Islamic religiosity and Islamic worldview prefer more judgment. The results also provide support for the hypothesis that religious personality has no impact on auditors' preference for more or less judgment. Unexpectedly the results of this study also provide evidence that although auditors have a preference for more judgment, the quality of those judgments is problematic, suggesting auditors' non-compliance with ISAs (and instead a reliance on verbal, unverified client-provided information), an

inappropriately low level of professional scepticism, and conservatism resulting in negative consequences for audit quality.

The findings have implications for global standards setters, international auditing firms, and cross-cultural audit research. The results may also be useful to multinational companies that employ a significant number of Muslims.

### ***1.3.2 Study 2: The influence of clients' religious adherence and gender on auditors' evidence reliability judgments in an Islamic context***

The results of Study 1 highlight potential issues with auditors' reliance on unverified verbal information received from clients and raise concerns about the quality of auditors' evidence reliability judgments. Study 2 examines this issue further and contributes to the literature by examining the influence of contextually relevant cultural variables, namely, client's religious adherence and gender on auditors' evidence reliability judgments. Auditors' judgments of audit evidence reliability are important because the inferential value of the audit evidence must always be considered in light of its source. Client's religious adherence refers to the level of engagement with the Islamic religion and is selected here for examination given its positive relationship with trust, credibility, and social acceptance. Individuals with a high level of religious adherence enjoy social recognition and acceptance in the socio-cultural context of Pakistan. Gender is selected for examination because the interaction between accounting and gender has been a subject of debate recently, and gender inequality within the accounting profession globally remains a serious concern. Additionally, gender is a sensitive and controversial topic in relation to both Islam and Pakistan (ADB, 2016). Pakistan is a patriarchal society with strictly defined roles and responsibilities for women, and this has resulted in significant gender inequality.

A 2x2 between-subjects experiment was administered to 95 auditors in Big 4 auditing firms in Pakistan. Manipulated variables are client's religious adherence (high vs low) and gender (male vs female). The results support the hypothesis that information received from a client with high religious adherence is assessed by auditors to be more reliable. However, the gender of the client has no significant influence on auditors' audit evidence reliability judgments. This result provides evidence that clients' religious adherence is an important cultural variable in Islamic cultures within the context of audit evidence reliability judgments.



Furthermore, the results similarly to study 1, suggest that regardless of client's religious adherence level and gender auditors trust the information provided by the client and are willing to materially reduce the provision for doubtful debt judgment based on insufficient evidence of very low reliability (i.e., internal verbal evidence without any corroborating evidence). These results are of concern as they indicate that auditors exhibit an inappropriately low level of professional scepticism and conservatism in their judgments and are not compliant with the specific principles of ISA 500 *Audit Evidence*. Therefore, auditors' professional scepticism and conservatism in an Islamic context is an area worth investigating in future research.

The findings have implications for standard setters and audit professionals with specific reference to auditing practices and the resulting audit quality in Islamic countries.

#### ***1.3.3 Study 3: The influence of auditors' Islamic religiosity and clients' religious adherence on the level of conservatism in auditors' judgments***

This study contributes to the literature by investigating the influence of auditors' Islamic religiosity level and clients' religious adherence on the level of conservatism in auditors' judgments. By investigating auditors' conservatism judgments in an Islamic cultural context, Study 3 adds depth and extends the findings of Studies 1 and 2, which highlight issues with auditors' non-compliance with ISAs, inappropriately low level of conservatism, and failure to apply appropriate and required professional scepticism in their judgments. The results of Studies 1 and 2 suggest issues with non-compliance of ISAs in the presence of a moderate risk within a doubtful debt scenario and client-provided information. Study 3 further addresses this issue by incorporating a "high-risk" audit judgment scenario which involves client's inventory write-down assessment, client-provided information, and contradictory past audit evidence. Study 3 thus investigates the influence of auditors' overall Islamic religiosity and clients' religious adherence on the level of conservatism in their judgments in an inventory write-down judgment scenario. Auditors' Islamic religiosity was measured with the MRPI Islamic religiosity framework (Krauss et al., 2005). Based on the MRPI framework Islamic religiosity is categorized into Islamic worldview and religious personality. Islamic worldview encompasses deeply held, core, and enduring Islamic values and beliefs, whereas religious personality represents the external manifestations of religiosity such as prayer and worship. Clients' religious adherence to Islamic practices is manipulated

as low versus high. The level of conservatism in auditors' inventory valuation judgments is the dependent variable examined.

Conservatism in auditors' judgments is defined as auditors' preference for income-decreasing accounting choices (Kim et al., 2003). A number of studies have investigated the level of conservatism in auditors' judgments in an Anglo-American context (Lennox & Kausar, 2015). However, few of these have incorporated the influence of cultural factors. Given the importance of conservative values in an Islamic cultural context (Gesink, 2014), it is surprising that no prior studies have examined the influence of Islamic religiosity and religious adherence on auditors' conservatism judgments.

The experiment was conducted with 105 auditors in Big 4 auditing firms in Pakistan. By manipulating the religious adherence level of the client as high versus low in a 2x2 between-subjects experiment, this study also investigated the impact of clients' religious adherence on the level of conservatism in auditors' judgment. The results provide support for the hypotheses that a high score on the overall Islamic religiosity and Islamic worldview scales increase the level of conservatism in auditors' judgments. The results also suggest that auditors' religious personality and client's level of religious adherence have no significant impact on the level of conservatism in auditors' judgments. Further, the results of the interaction hypothesis show that when auditors' Islamic religiosity level is high, the level of conservatism in their judgments is also high irrespective of the religious adherence level of the client. However, when auditors' Islamic religiosity level is low, the level of conservatism in their judgments is decreased in the presence of a client with high religious adherence. The results of this study confirm the results obtained from the two earlier studies regarding auditors' Islamic religiosity level and clients' religious adherence.

Although the results of this study suggest that auditors who score high on the Islamic religiosity and Islamic worldview scales exhibit a higher level of conservatism in their judgments, auditors did not write down the inventory to its full net realizable value (NRV) in accordance with accounting standard IAS 2 *Inventories* (IFRS, 2018). Auditors, on average, recommended an overstated inventory write-down balance resulting in both the inventory and profit being materially overstated. These results suggest non-compliance with not only the accounting standards but also with ISAs (i.e., reliance on insufficient and unreliable evidence in a high audit risk scenario) and exercise of an inappropriately low

level of professional scepticism leading to material misstatement. Thus the results of this study further support the concerns, already raised in Studies 1 and 2 of this thesis, about auditors in an Islamic context exhibiting non-compliance with ISAs and demonstrating inappropriately low levels of professional scepticism and conservatism resulting in reduced audit quality and materially misstated financial information.

The results of this study contribute to the literature on auditors' conservatism judgments in an Islamic cultural context and are also relevant for auditing firms operating in Islamic countries that employ a significant number of Muslims.

#### **1.4 Structure of the thesis**

This thesis consists of five chapters. Chapter 1 provided the context and motivation for the thesis, an overview of previous literature within which the thesis is situated, and the aims and objectives of the three individual studies. The next three chapters consist of three studies that make up the three distinct, interrelated studies as outlined above. Chapter 2 is Study 1, which examines the influence of Islamic religiosity level on auditors' preference for more or less judgment. Chapter 3 presents Study 2, which examines the influence of clients' religious adherence and gender on auditors' audit evidence reliability judgments in an Islamic context. Chapter 4 presents Study 3, which examines the influence of auditors' Islamic religiosity level and clients' religious adherence on the level of conservatism in auditors' judgments. Chapter 5 concludes the thesis by summarizing and synthesizing the three studies and discussing the implications of the findings along with the limitations of the research.

## Chapter 2

### Study 1: The influence of Islamic religiosity on auditors' preference for more or less judgment<sup>2</sup>

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<sup>2</sup> An earlier version of this paper was presented at the 28<sup>th</sup> Asian-Pacific Conference (APC) on International Accounting Issues held on 6–9 November 2016 in Maui, Hawaii, USA.

- Adeel, N., Martinov-Bennie, N., and Patel, C. (2016), “The influence of Islamic religiosity on auditors' preference for principle-based or rule-based judgments in Pakistan.” 28<sup>th</sup> APC conference proceedings and program, page 112.
- This paper will be submitted to the *International Journal of Auditing*.

## **The influence of Islamic religiosity on auditors' preference for more or less judgment**

### **Abstract**

This study contributes to auditors' judgment research by investigating the influence of an important cultural variable – Islamic religiosity – on auditors' preference for more or less judgment. Pakistan, this study's proxy for Islamic countries, provides an appropriate context given that Islam is its official religion and it has adopted the principles-based International Standards on Auditing (ISAs) without any amendments. ISAs are principles-based standards and require extensive exercise of auditors' professional judgment. However, research to date generally suggests that the rules-based nature of Islam has a significant influence on accounting and auditing practices in Islamic countries, a potential challenge to implementing ISAs. This study contributes to the audit literature by utilizing, for the first time, a well-validated and reliable Muslim Religiosity Personality Inventory (MRPI) measure. The study also investigates the impact of the two separate components of overall Islamic religiosity – Islamic worldview and religious personality – on auditors' judgments. Islamic worldview represents deeply held core Islamic values while religious personality measures the believers' perceptions of rituals, prayers, and worship. The results, contrary to prior research that uses more simplistic proxies and measures of Islamic religiosity, suggest that auditors with high overall Islamic religiosity and Islamic worldview scores prefer more rather than less judgment. The results also suggest that auditors' religious personality score has no impact on their preference for judgment. The findings have implications for global standards setters, international auditing firms, and cross-cultural audit research, particularly in Islamic countries. The results may also be useful to multinational companies that employ a significant number of Muslims.

**Keywords:** International Standards on Auditing (ISAs); Auditors' preference for more judgment; Islamic religiosity; Pakistan

## 2.1 Introduction

The paper contributes to the literature on auditors' judgment by investigating the influence of an important cultural variable, namely, *Islamic religiosity* on auditors' preference for more or less judgment in Pakistan. The exercise of auditors' professional judgment is arguably the most important aspect of auditing (Octavian et al., 2010) and has been identified as one of the key elements that create an environment for audit quality (IFAC, 2014b, p. 12). Solomon (1995) concludes that professional judgment pervades virtually all aspects of contemporary financial statement audits. Moreover, the risk-based methodologies in auditing firms reinforce that "the single most important element in applying the firm's audit approach is the exercise of informed judgment at the various stages of audit" (Trotman, 1996, p. 2). Auditors' preference for judgment has gained importance with the global convergence of the principles-based International Standards on Auditing (ISAs) (Backof, Bamber, & Carpenter, 2016). Over 113 jurisdictions apply or are in the process of adopting ISAs issued by the International Auditing and Assurance Standards Board (IAASB) (IAASB, 2018).

ISAs are principles-based and are developed based on a "substance over form" approach and require extensive exercise of auditors' professional judgment (Bennett, Bradbury, & Prangnell, 2006; Agoglia, Douppnik, & Tsakumis, 2011; Heidhues & Patel, 2011b; Kang, Trotman, & Trotman, 2015). Standard setters have advocated that auditing judgments must reflect the "economic substance"<sup>3</sup> of transactions rather than their "legal form" (Baker & Hayes, 2004; Patel, 2006; Williams, 2016). The exercise of professional judgment in a principles-based regime is imperative for audit quality, as an excessive emphasis on rules is regarded as an inappropriate substitute for well-reasoned professional judgment (Blokdiik, Driehhuizen, Simunic, & Stein, 2003).

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<sup>3</sup> The substance over form approach in an audit process is a highly debatable and important part of Anglo-American auditing. Substance over form or faithful representation is "when financial information represents the substance of an economic phenomenon rather than merely representing its legal form". Internationally accepted standards in accounting and auditing (IFRS and ISAs) are based on this approach, which has a strong reliance on professional judgments (Heidhues & Patel, 2011).

One of the implicit assumptions underlying the convergence towards a single set of auditing standards is that auditors worldwide have a preference for judgment (Chand et al., 2010; Dwita, 2014; Tsunogaya, Sugahara, & Chand, 2016). However, Islam is a rules-based and prescriptive religion, and the *Shariah*-based accounting and auditing standards derived from Islamic law are also rules-based and do not encourage the exercise of individual judgment (Rahman, 2000; Maurer, 2010). Furthermore, the Accounting and Auditing Organization for Islamic Financial Institutions, which is the prominent standard-setting body for Islamic countries, does not endorse the substance over form approach in standard setting and implementation (Rahman, 2010; Maurer, 2010). Most scholars in Islam also suggest that recognition and measurement of an Islamic financial transaction should have prominence over its legal form and claim that substance over form is “an unconcealed violation of *Shariah*” (Ismail & Sori, 2017, p. 5). Researchers have suggested that this preference for rules in Islam is likely to pose a challenge in implementing principles-based standards in Islamic countries such as Pakistan (Maurer, 2002; Joshi, Yapa, & Kraal, 2016).

Pakistan is a proxy for Islamic countries and is appropriate for this research because Pakistan adopted ISAs without any amendments in 2005 (ICAP, 2015). Although the concept of statutory audit was introduced into Pakistan by the British (Ashraf & Ghani, 2005), Pakistan draws standards primarily from Islamic law, which is essentially rules-based with a legalistic influence (Ibrahim, 2006). Moreover, there is evidence that the Islamization of social, political, and economic activities in Pakistan in the 1980s encouraged rules-based standards in all domains of personal and professional life (Haque & Gardezi, 1991). Therefore, given the convergence of principles-based ISAs in Pakistan, it is important to understand whether auditors have a preference for more or less judgment.

The global move to adopt a single set of auditing standards implies that countries’ unique contextual factors, including culture, can easily be overlooked (Chand & White, 2006; Chand et al., 2010). However, a number of studies provide evidence that culture influences auditors’ judgment and

decision making (Borker, 2012; Nolder & Riley, 2013; Alzeban, 2015; Bik & Hooghiemstra, 2016; Ying & Patel, 2016; Sunderland & Trompeter, 2017; Houjeir & Brennan, 2017; Bik & Hooghiemstra, 2018). However, culture is considered to be “too broad” and has been criticized for its limitation in providing richer insights into auditors’ judgments (Patel et al., 2002; Heidhues & Patel, 2011a). Very few studies have “unpacked the black box of culture” to identify its various components and dimensions, which are likely to influence judgments (Patel, 2006, p. 13).

To “unpack” the concept of culture in an Islamic context, this study invokes the concept of Islamic religiosity, which is a commitment to the empirical and theoretical fundamentals of Islam through which Muslims fulfil the right of God, protect the rights of others, adhere to the divine decrees, abstain from wrong deeds, and worship (Al-Goaib, 2003). A number of studies provide evidence that Islamic religiosity has influenced accounting and auditing practices in Islamic countries, including Pakistan (Alshehri et al., 2016; Mostafa, Ehab, & Hussain, 2017). The Muslim Religiosity Personality Inventory (MRPI), a valid and reliable Islamic religiosity scale adopted from Krauss et al. (2005), is used in this study to measure auditors’ Islamic religiosity level. The MPRI framework has been extensively used in prior research to investigate the influence of Islamic religiosity on judgments (Krauss, Hamzah, & Idris, 2007; Rehman & Shahbaz Shabbir, 2010; Annalakshmi & Abeer, 2011; Othman & Hariri, 2012; El-Bassiouny, 2014).

Scholars broadly classify Islamic religiosity according to two theoretical constructs: “Islamic values” and “Islamic rituals” (Krauss et al., 2005; Ji & Ibrahim, 2007b; Tiliouine & Belgoumidi, 2009; Abou-Youssef, Kortam, Abou-Aish, & El-Bassiouny, 2011). Based on Krauss et al. (2005) framework, Islamic values are referred to as “Islamic worldview,” and Islamic rituals are referred to as “religious personality”. Islamic worldview represents deeply held, enduring, stable, and core Islamic values and is likely to influence auditors’ preference for judgment while religious personality, which exemplifies



rituals and worship, differs from the core values embedded in Islamic worldview, and is not likely to influence auditors' preference for judgment.

A survey questionnaire was administered to 66 professional auditors<sup>4</sup> working in medium-tier auditing firms<sup>5</sup> in Pakistan. Medium-tier auditing firms were selected for examination because, in Pakistan, it is mandatory for them to adopt ISAs. The audit methodologies of these firms are in line with ISAs (ICAP, 2015, 2016a, 2017b) and the organizational culture of these firms is also likely to be influenced by local cultural and religious values (Khilji, 2003; Patel, 2006; Trompenaars & Hampden-Turner, 2011). The results of the study support the hypothesis that auditors who score high on overall Islamic religiosity and Islamic worldview have a preference for more judgment. The results also support the hypothesis that auditors' religious personality has no impact on auditors' preference for judgment. The results contribute to the literature on Islamic religiosity and its influence on auditors' preference for judgment.

The remainder of the paper is organized as follows. Section 2.2 presents the literature review. Section 2.3 details the selection of Pakistan, while section 2.4 discusses the theory development and hypotheses. Section 2.5 explains the research method, and section 2.6 provides the results and a discussion. Section 2.7 concludes the study.

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<sup>4</sup> Professional auditors in Pakistan are members of the Institute of Chartered Accountants of Pakistan (ICAP), they have practiced as an Associate accountant for five years or a non-practicing Associate for 10 years, and have completed all requirements of Chartered Accountancy plus three years of professional experience (ICAP, 2014).

<sup>5</sup> Medium-tier auditing firms in Pakistan include local and international firms who need to have satisfactory Quality Control Review ratings from the ICAP (ICAP, 2016a). All medium-tier auditing firms in Pakistan have adopted the ISAs.

## **2.2 Literature review**

This study investigates two important streams of literature regarding the influence of Islamic religiosity on auditors' preference for more or less judgment. They are prior literature on auditors' preference for more or less judgment and prior literature on the influence of religiosity on auditors' judgments.

### ***2.2.1 Prior research on auditors' preference for more or less judgment***

Recent evidence from cross-cultural audit judgment research shows that cultural variables are important in investigating the differences between auditors' preference for more or less judgment (Schultz & Lopez, 2001; Douppnik & Richter, 2003, 2004; Douppnik & Riccio, 2006). However, a substantial portion of previous research has been dedicated to investigating the impact of rules-based and principles-based standards on auditors' judgments (Psaros & Trotman, 2004; Psaros, 2007; Segovia, Arnold, & Sutton, 2009; Jamal & Tan, 2010; Agoglia et al., 2011; Collins, Pasewark, & Riley, 2012; Cohen, Krishnamoorthy, Peytcheva, & Wright, 2013; Backof et al., 2016; Tsunogaya et al., 2016; Scott Asay, Brown, Nelson, & Jeffrey Wilks, 2017); the impact of rules-based accounting standards on litigation (Donelson, McInnis, & Mergenthaler, 2012); rules versus principles in ethical standards and their impact on auditors' independence judgment (Herron & Gilbertson, 2004); and evaluation of rules-based versus principles-based corporate reporting standards (Tschopp & Nastanski, 2014).

Although this strand of research provides evidence that culture affects auditors' judgments, few studies that have examined the influence of cultural variables on auditors' preferences for judgment uncritically adopt and operationalize the cultural variables based on Hofstede's (1980) cultural dimensions. For example, Schultz and Lopez (2001), Douppnik and Richter (2003), Douppnik and Richter (2004), Douppnik and Riccio (2006), Chand, Cummings, and Patel (2012), and Tsunogaya et al. (2016) uncritically adopt Hofstede's cultural dimensions and Gray's (1988) accounting classification in determining accountants' preference for judgment in cross-cultural settings. Schultz and Lopez (2001) provide evidence that owing to a low score on a cultural measure of uncertainty avoidance; US

accountants prefer rules-based judgments. Doupnik and Richter (2003), Doupnik and Richter (2004), and Doupnik and Riccio (2006) provide evidence of the influence of culture on the rules-based interpretation of uncertainty expressions embedded in accounting standards. Futher, Chand et al. (2012) provide evidence that Chinese students exhibit greater conservatism and secrecy than Australian students and have a preference for rules-based judgments in the interpretation and application of IFRS.

Researchers have repeatedly criticized the simplistic assumptions and the theoretical and methodological limitations of Hofstede's (1980) and Hofstede and Bond's (1988) cultural dimensions, and Gray's (1988) accounting values (Baskerville-Morley, 2005; Patel, 2006; Heidhues & Patel, 2011a). For example, Hofstede's (1980) and Hofstede and Bond's (1988) cultural dimensions are criticized because their data are outdated and they equate nation states with cultures based on the simplified assumption and categorization that any society is homogenous, thereby overlooking within-country cultural values (Baskerville, 2003). Therefore, it is suggested that relevant contextual factors, such as religion, motives, beliefs, and values, be incorporated to provide a richer and deeper understanding of the interrelationships between cultural values and auditing judgments (Heidhues & Patel, 2011; Patel, 2004, p. 71).

This paper supports the critical evaluation of such deterministic and narrowly focused frameworks. Culture has been characterized as "too broad," and researchers have repeatedly criticized its limitation in providing richer insights into perceptions and judgments (Harrison & McKinnon, 1999; Patel et al., 2002). Cross-cultural auditing research is also in danger of relying on overgeneralizations and an obsession with categorizations and cultural dimensions that often fail to capture the complexity and dynamics of cultures (Heidhues & Patel, 2011a). To overcome this theoretical limitation, this study examines the influence of auditors' Islamic religiosity on auditors' preference for more or less judgment and suggests that it is important to "unpack the black box of culture" to identify its various components and dimensions, which are likely to influence these judgments (Patel, 2006, p. 13). Specifically, by

invoking the concept of Islamic religiosity in an Islamic cultural context, this study suggests that religiosity provides a much stronger and sharper focus for analyzing auditors' preference for more or less judgment in Islamic cultures in comparison with Hofstede's and Gray's frameworks.

Some studies have examined the application of principles-based standards (IFRS and ISAs) in the Islamic cultural context, especially with regard to global convergence: in Bahrain (Joshi, Bremser, & Al-Ajmi, 2008); Saudi Arabia (Nurunnabi, 2017); Iran (Paknejad, 2017); Malaysia (Joshi et al., 2016); Indonesia (Harto & Paranti, 2017); and the UAE (Trabelsi & Trabelsi, 2014). However, most of these studies limit their discussion to a number of within-country contextual factors which are likely to influence IFRS implementation. Studies have also reviewed the influence of IFRS adoption on market performances, such as Paknejad (2017) in Iran, Harto and Paranti (2017) in Indonesia, and Trabelsi and Trabelsi (2014) in the UAE. A number of studies (e.g., Dima, Dima, Megan, and Paiusan (2014) El Razik (2009) Joshi et al. (2016) have focused on comparative analysis within Islamic countries concerning challenges and impediments to IFRS adoption.

Although most of these studies acknowledge the possible influence of Islam on auditing practices (Joshi et al., 2008; Joshi et al., 2016; Nurunnabi, 2017), they do not provide a thorough review of the influence of Islam and Islamic religiosity on auditors' judgments within the context of convergence, despite calls for research on the influence of Islam on auditing within the Islamic world (Lewis, 2001; Vinnicombe & Park, 2007; Kamla, 2009; Shafii & Zakaria, 2013; Haniffa & Hudaib, 2014). This paper responds to these calls by providing empirical evidence of the influence of Islam, operationalized as Islamic religiosity, on auditors' judgments.

Additionally, research on auditors' preference for judgment within the convergence of ISAs in Pakistan is scarce. Previous studies on the convergence of international standards are narrowly focused on the adoption and influence of IFRS on corporate governance and firm performance (Ashraf & Ghani,

2005; Azeem & Kouser, 2011; Hossain & Nurunnabi, 2011; Rashid, Amin, & Farooqui, 2012; Anwar, Anwar, & Khan, 2013; Malik & Ali, 2013; Ahmed & Ali, 2015), and the influence of contextual factors, such as political, legal, economic, and corporate governance, on IFRS implementation (Ashraf & Ghani, 2005; Hossain & Nurunnabi, 2011; Rashid et al., 2012; Baig & Khan, 2016). Despite these studies providing evidence of the impact of international standards adoption on firm performance, they provide a limited discussion of the possible influence of contextual factors, such as Islamic religiosity, within the context of convergence.

Indeed, very few studies discuss the influence of Islam or Islamic religiosity in an accounting context. Ashraf and Ghani (2005) elaborate on the external and internal factors that have affected the development of accounting practices in Pakistan. However, they do not identify Islam as an important contextual variable in convergence. Rammal and Parker (2013) limit their discussion to the role of Islam in history, emergence and accountability in Islamic banking in Pakistan.

### ***2.2.2 Prior research on religiosity and auditors' judgments***

There are several reasons for considering Islamic religiosity as a significant variable that is likely to influence judgments. First, being a continuous variable, Islamic religiosity is measurable by several religiosity scales available in the literature (Abou-Youssef et al., 2011). Second, Islamic religiosity is a multidimensional concept with a number of theoretical constructs that can explain differences in individuals' judgments based on which dimension of Islamic religiosity is more dominant (Krauss et al., 2005; Ji & Ibrahim, 2007b; Tiliouine & Belgoumidi, 2009; Abou-Youssef et al., 2011). The literature shows that Islamic religiosity plays a fundamental role in influencing judgments in an Islamic organizational context (Khashan & Kreidie, 2001; Muhamad & Ghani, 2006; Barhem, Younies, & Muhamad, 2009; Terzi, Alserhan, & Altunişik, 2016).

A number of studies have investigated the influence of religiosity in accounting and auditing in the Anglo-American context (Hilary & Hui, 2009; McGuire et al., 2011; Walker et al., 2012; Hickman,

2013; Jaggi & Xin, 2014; Walker et al., 2015; Omer et al., 2016; Jaggi & Lewis, 2017; Sauerwein, 2017; Bik & Hooghiemstra, 2018), but most of these studies have used simplistic proxies for measuring religiosity. For example, Hilary and Hui (2009), McGuire et al. (2011), and Jaggi and Lewis (2017) examine religiosity according to the geographical location of audit offices in religious or non-religious areas. In addition, categorization of high and low religiosity areas in most of these studies is based on a single measure of church attendance (Walker et al. (2012) Hilary and Hui (2009). Evidence suggests that an individual measure of religiosity is a better measure and can provide a sharper insight into judgments (Tarakeshwar et al., 2003). This study uses a different and more sophisticated measure, that of Islamic religiosity, which involves examination of Islamic religiosity at both the worldview level and religious personality level. This study also introduces a multidimensional measure of religiosity, rather than relying on a single-item measure.

A number of researchers have investigated the influence of Islamic religiosity in Islamic organizations (Stack, 2006; Rashid & Ibrahim, 2008; Adamu, Kedah, & Osman-Gani, 2011; Othman & Hariri, 2012; Osman-Gani, Hashim, & Ismail, 2013) and its positive influence on auditors' ethical judgments (Rashid & Ibrahim, 2008; Maisarah, Stacey, & Gordon, 2009; Haron, Ismail, & Na, 2015; Mamsori, Rezaee, Homaoun, & Noghondari, 2015; Alshehri et al., 2016; Saat et al., 2016; Mostafa et al., 2017). However, almost all of the audit judgment studies that have been conducted in Islamic countries have focused on the ethical judgments of auditors and accountants. Several studies have provided evidence of a strong correlation between Islamic religiosity and Muslim consumers' judgments (El-Bassiouny, 2014; Mathras, Cohen, Mandel, & Mick, 2015; Ahmad, Rahman, & Ab Rahman, 2015a).

An important contribution of this study to the literature on Islamic religiosity in Islamic countries is the use of the Muslim Religiosity Personality Inventory (MRPI) scale to audit judgment research. Previous studies provide evidence that the MRPI is used in a broad range of disciplines, including marketing (El-Bassiouny, 2014; Shabbir, 2010), accounting (Othman & Hariri, 2012), and

sociology and psychology (Annalakshmi & Abeer, 2011; Krauss et al., 2006; Mohamadamin, 2011). The scale has been validated in Malaysia (Krauss et al., 2007, 2012), Pakistan (Shabbir, 2010), Iran (Mohamadamin, 2011), and India (Annalakshmi & Abeer, 2011). However, the majority of research (e.g., (Rehman and Shahbaz Shabbir (2010); El-Bassiouny (2014)) has focused on the use of the MRPI in marketing and consumer research. Additionally, Othman and Hariri (2012) utilize the MRPI to provide evidence that Islamic religiosity constructs are likely to predict whistleblowing practices in Islamic financial institutions. By employing the MRPI to investigate auditors' preference for more or less judgment, this study provides an original contribution to the audit judgment and decision-making literature in Islamic countries.

Most religiosity studies conducted in Pakistan in recent years have investigated the influence of Islamic religiosity on Muslim consumers' *halal* choices in marketing (Ilyas, Hussain, & Usman, 2011; Yousaf & Malik, 2013; Baig & Baig, 2013; Ahmad & Afridi, 2013; Ansari, 2014). Some studies investigate the positive role of Islamic religiosity in organizational behavior (Zafar, 2011), life satisfaction (Khan, Subhani, & Ara, 2013), and health and subjective well-being (Gull & Dawood, 2013). The few studies that investigate the influence of religion include Badshah, Mellemvik, and Timoshenko (2013), who explore the influence of Islam on the development of public sector accounting practices, and Rammal and Parker (2013), who limit their discussion to the evolution of Islamic banking in Pakistan.

This study contributes to the Islamic religiosity literature in a number of ways. First, it invokes the concept of Islamic religiosity in the audit judgment context, which has been neglected by previous research. Second, it contributes to the literature that identifies the importance of cultural variables more broadly, but it provides a much sharper insight into judgments by using Islamic religiosity. Lastly, this study examines the influence of Islamic religiosity constructs such as Islamic worldview and religious

personality on audit judgment and decision-making research in Islamic countries and Pakistan for the first time.

### **2.3 The Pakistani context**

Auditing in Pakistan has witnessed many changes over the years. The concept of limited liability and the statutory audit (the true and fair view), was introduced in Pakistan during British colonization in the middle of the 19<sup>th</sup> century (Ashraf & Ghani, 2005). Pakistan began adopting ISAs in 2005 and has successfully adopted almost all of the clarified ISAs issued by the IAASB (ICAP, 2015).

Pakistan is one of the few Islamic countries in the world that are officially ruled by the Islamic laws or *Shariah* since 1956. Interestingly, due to its historical link to Britain, Pakistan's educational and professional developments have to a certain extent been "influenced" by the Western's system (Ashraf and Ghani, 2005). Specifically, for the accounting and auditing profession, accounting professional bodies such as the Institute of Chartered Accountants England and Wales (ICAEW), The Chartered Institute of Management Accountants (CIMA UK) are among the most popular providers of professional accounting qualifications for the country. Although an Islamic state, Pakistan also opens its doors to adopt international standards such as International Financial Reporting Standards (IFRS) and the International Standards of Auditing (ISA) (ICAP, 2015).

Pakistan is a common law country, and it is therefore presumed that there exists a non-legalistic orientation towards accounting standard-setting and implementation (Černe, 2009). However, conflicting literature shows that religious influence, ownership structure, and the family-oriented corporate governance environment in Pakistan resembles countries that follow the code law system (Ashraf & Ghani, 2005; Ibrahim, 2006). Additionally, Pakistan draws ethical principles primarily from Islamic law because the Constitution mandates that all laws must conform to Islam,<sup>6</sup> which has a

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<sup>6</sup> Article 227 of the Constitution of Pakistan states in part: "All existing laws shall be brought in conformity with the Injunctions of Islam as laid down in the Constitution of the Islamic Republic of Pakistan".



legalistic influence given the rules-based nature of Islamic *Shariah* (Ibrahim, 2006). Also, the Islamization of social, political, and economic activities in Pakistan in the 1980s set a precedent for the application of rules-based Islamic principles in all domains of personal and professional life (Haque & Gardezi, 1991).

A steady increase in the adoption and popularity of highly prescriptive rules-based Islamic finance, accounting, and *Shariah* auditing standards by the Institute of Chartered Accountants of Pakistan (ICAP) is also likely to encourage rules-based preferences in auditing (SBP, 2014). It is therefore unclear whether Pakistani auditors prefer judgment in the application of ISAs. Since accounting practices and preferences emerge from the legal system in a country (Choi, Meek, & Fang, 2005), Pakistan provides an appropriate national context to investigate the impact of Islam on auditors' preference for more or less judgment.

## **2.4 Theory development and hypothesis formulation**

### **2.4.1 Religiosity**

Religiosity is the degree to which beliefs in specific religious values and ideals are held and practiced by an individual (Minton, 2013). Religiosity is a major cohesive force because its value system is accepted unquestioningly by many members of society (Mokhlis, 2009). Since religiosity is a comprehensive sociological term used to refer to the numerous aspects of religious activity, dedication, and belief (Petruța-Paraschiva & Turliuc, 2011), it is also likely to provide insights into auditors' judgment and decision making. It is important to examine religiosity because it has provided the "value systems around which groups and nations have coalesced" (Gunter & Furnham, 2014, p. 57). Additionally, religiosity is a "critical subsystem of any culture which is likely to provide a fruitful focus in the search for attitude structures of the people, that not only influence their belief systems but also their actions that they take according to their belief" (Weissbrod, 1983, p. 189).

Perhaps the most developed theoretical framework for understanding the influence of religiosity on judgments, symbolic interactionism<sup>7</sup> (Stryker & Serpe, 1982; Wimberley, 1984; Blumer, 1986; Wimberley, 1989), emphasizes the idea of role expectations and religious identity. Using this framework, Weaver and Agle (2002) explain how religiosity affects a person's judgments in organizations through religious role expectations, which are reflected externally through individual religiosity constructs. Social structural symbolic interactionist theory posits that an individual's religious role expectations constitute a person's religious self-identity, which, in turn, influences judgments and behaviour (Stryker, 1980). These religious role expectations are reflected externally through the individual level of religiosity, which is an important variable in the examination of judgments (Huber & Huber, 2012), and thus is selected for examination in this research.

Religiosity is a multidimensional construct, and numerous studies have attempted to identify the dimensions that are likely to influence judgment and decision making (Holdcroft, 2006). Scholars of religion do not agree as to which construct of religiosity is more influential in influencing judgments (Glock, 1959; Hill, 1999; Fontaine, Duriez, Luyten, Corveleyn, & Hutsebaut, 2005). It is argued that this is because there are differences in the conceptualization and measurement of religiosity, which involves a complex, multifaceted individual experience (Holdcroft, 2006).

Research has classified Christian religiosity according to a number of constructs. For example, Glock, Stark, and McNally (1965) classify religious values into ideological, experiential, ritualistic, intellectual, and consequential dimensions, and Fukuyama (1960) classifies religiosity into cognitive, creedal, ritual, and devotional dimensions. Prior research suggests that amongst these constructs the ideological and ritualistic constructs of religiosity are most relevant for investigating judgments and

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<sup>7</sup> The three basic tenets of symbolic interactionism are: (i) human beings act towards things on the basis of the meaning that the things have for them; (ii) the meaning of things is derived from the social interaction that one has with one's fellows; and (iii) these meanings are handled in and modified through an interpretative process used by the person in dealing with the things they encounter (Blumer, 1986).

decision making (Moberg, 1965; Wilde & Joseph, 1997; Holdcroft, 2006). Given the importance of the ideological and ritualistic construct in prior literature, this research selects the ideological and ritualistic construct of Islamic religiosity to examine auditors' preference for judgment in an Islamic cultural context.

### ***Islamic religiosity***

To provide a holistic and comprehensive insight into the influence of Islamic religiosity on auditors' judgment, this section draws on the literature on Islamic religiosity to complement cultural studies in organizational behaviour in accounting, which largely focus on quantified and dimensional approaches (e.g., Hofstede and Bond (1988). Researchers have also called for more holistic approaches drawing on cultural, religious, psychological, or other relevant literature to enrich our understanding of the complexity of cultural influences on auditors' judgments (Harrison & McKinnon, 1999; Heidhues & Patel, 2011; Patel, 2004). This study responds to these calls by drawing on Islamic religiosity to provide additional insights into relevant Islamic religiosity constructs and their likelihood of influencing auditors' preference for more or less judgment.

*Islamic religiosity* is the belief that Islam should direct one's social, political, personal, and professional life (Fuller & Kurpershoek, 2013). It also refers to the extent of one's beliefs and level of agreement with Islamic religious doctrines and adherence to actual practices, such as prayer and worship (Krauss et al., 2005). Islamic religiosity is defined as the commitment to the empirical and theoretical fundamentals of the religion (Islam) through which Muslims fulfil the rights of God, protect the rights of others, adhere to the divine decrees, abstain from wrong deeds, and worship (Al-Goaib, 2003).

Islamic religiosity has been theorized to examine religious influence in Islamic cultural contexts in previous research (Muhamad, 2009; Souiden & Rani, 2015; Usman, 2016). A number of Islamic scholars have developed similar multidimensional theoretical constructs that comprise Islamic

religiosity (Olufadi, 2017; (Tiliouine and Belgoumidi (2009); El-Menouar (2014))Krauss et al., 2005; Ji and Ibrahim, 2007; Tiliouine et al., 2009). However, almost all of these scholars divide Islamic religiosity into Islamic values and Islamic rituals, which is consistent with the MRPI framework adopted in this research.

Islamic values and rituals are based on the *Quran*, Islam's holy book. *Sunnah* is another source of Islamic values and rituals, which represents the sayings of the Prophet and deeds as reported by others, and the opinions of early jurists based on their interpretation of the sources of Islamic law mentioned above (Alsharif et al., 2011). Islamic values and rituals are strongly interrelated since devout Muslims' day-to-day practices and behaviour are guided by the existence of internally held core Islamic values; the deeper the belief in these values, the stronger the practice (Koenig & Shohaib, 2014). Thus, by measuring these two separate constructs, this study provides insights into the religiosity measurement in audit judgment research.

### ***Islamic worldview (values)***

Values constitute a person's life goals and reflect what is most fundamental to them (Rokeach, 1973). Values are the ideological dimensions of religiosity and are "constituted by expectations that the religious will hold to certain beliefs" (Glock et al., 1965). Values are based on experience and established throughout one's life and tend to be relatively stable (Schwartz & Bilsky, 1987). Values are a central part of any culture; while the external behavioural part of the culture (symbols and rituals) may change the "software" of the culture, the deep-seated values remain constant. Values have long been considered an important antecedent of individual behaviour (Glew, 2009). Values also support beliefs and the influence of these beliefs on individual judgment in day-to-day life (Moberg, 1965). The literature provides evidence that religious values are more likely to influence judgment and decision making than religious rituals (Schwartz & Bilsky, 1987; Weaver & Agle, 2002; Glew, 2009).

There are a number of fundamental Islamic values that have great importance in the everyday lives of Muslims (Lewis, 2001). The core Islamic values are based on the six articles of faith: belief in one God, the angels, the prophets of God, the revealed books of God, the day of judgment, and the divine decree (Rahman, 2010). According to the MPRI framework adopted in this research, Islamic worldview is based on Islamic values. A worldview is the central cognitive orientation of an individual and consists of presuppositions and assumptions they hold about their world (Sire, 2015). A worldview is the set of beliefs about fundamental aspects of reality that ground and influence all one's perceiving, thinking, knowing, and doing.

Islamic worldview is a “comprehensive conception of the universe and man's relation to it from the Islamic perspective and serves as one's philosophy or outlook of life” (Abdullah & Nadvi, 2011, p. 271). Regarded as a central cognitive orientation, Islamic worldview reflects the doctrine of the divine unity of God and ascertains one's level of agreement with basic Islamic values, beliefs, and creed (Krauss et al., 2005, p. 138).

Prior literature suggests that Islamic worldview is an important religiosity construct and is likely to influence individual judgment and behaviour in almost all areas of inquiry. For example, Badawi (2002) suggests that Islamic worldview is the primary motivator behind the extraordinary transformation of Islamic civilization throughout history. Choudhury (2015) holds that Islamic worldview provides the foundation for the moral–social reconstruction of ethical business practices in Islamic countries, and a stronger Islamic worldview is likely to develop more ethical business practices. Research on Islamic consumers and marketing also provides evidence that Islamic worldview is likely to influence consumer decision making (Arham, 2010; Ilyas et al., 2011; El-Bassiouny, 2014; Ahmad et al., 2015a). Furthermore, research on Islamic influence on corporate governance shows that Islamic corporate governance principles are established on the values derived from the Islamic worldview (Asri & Fahmi, 2004; Alam Choudhury & Nurul Alam, 2013). More importantly, there is evidence of a positive

influence of Islamic worldview on ethical decision making in an organizational context in Islamic countries (Rahman, 2003) and on principles of Islamic economics in creating an Islamic welfare state (Asutay, 2007). Given its importance in influencing judgments, Islamic worldview, an important component of Islamic religiosity, is selected for examination in this research.

### ***Religious personality (rituals)***

Rituals are a very important form of human expression (Turner, 1973). A ritual is defined as “a sequence of activities involving gestures, words, and objects, performed in a sequestered place, and performed according to set sequence” (Webster, 2017). A ritual is a repetitive social or religious practice, and it follows some ritual schema (Schultz & Lavenda, 1998). One distinguishing feature of rituals is that they can be formal and rules-governed, which, according to anthropologists, is different from informal, spontaneous, or mundane activities that individuals perform on a daily basis (Mahmood, 2001).

Rituals play a significant role in an individual’s emotional well-being, communal harmony, and social integration (Irani & Funk, 1998). Since rituals stem from certain religious frameworks, and can be conventional or socially prescribed, the emphasis on structure, detailed instructions, and guidelines is more evident in ritual practices than it is in other forms of human behaviour (Bloch, 2004; Turner, 2017).

Many scholars contend that rituals are part of “extrinsic religiosity” and suggest that in most cases these actions are motivated by extrinsic benefits, such as social benefits (Fischer, Callander, Reddish, & Bulbulia, 2013; Sauerwein, 2017; Turner, 2017). Rituals are often measured by outward expressions of religion, such as attendance at institutional gatherings, the number of times one prays during a week, or how much one gives in charity to a religious institution (Spilka, Hood, Hunsberger, & Gorsuch, 2003). A number of studies provide evidence of the importance of rituals in an

organizational context (Kidwell, Stevens, & Bethke, 1987; Conroy & Emerson, 2004; Walker et al., 2012; Singhapakdi, Vitell, Lee, Nisius, & Grace, 2013).

Islam is a ritual-rich religion (Erdal & Borchgrevink, 2017). Muslims are required to perform specific rituals as an expression of their faith on a daily basis. Rituals such as prayer and fasting promote a sense of religious community among Muslims (Brass, 2000). As Riaz Hassan (2013, p. 49) explains, the ritual practices of Islam, while introducing a social dimension, also entail a “complex interaction between individual meaning and experience and social values and expectations.”

In the present study, Islamic rituals are represented by religious personality, which measures a person’s level of commitment to ritualistic behaviour.<sup>8</sup> Religious personality is the outlet through which an individual expresses his or her religious beliefs according to the worldview and performs rituals and worships motivated by God consciousness. Religious personality is divided into two kinds of worship: special worship (*ibadat*), which are the rituals and prayers that reflect one’s direct relationship with God (e.g., prayers, fasting, and pilgrimage); and general worship (*muuamlat*), which is religiously guided behaviour towards one’s family, fellow human beings, colleagues, animals, environment, and nature (Krauss et al., 2005).

#### **2.4.2 Hypotheses formulation**

##### ***Influence of overall Islamic religiosity on auditors’ preference for more or less judgment***

The development of hypotheses in this study is based on two strands of literature, namely, Islamic religiosity and auditors’ preference for judgment literature.

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<sup>8</sup> A number of Muslim scholars argue that ritualistic behaviour is not a superficial expression of one’s prayers and worship, but in fact represents a far deeper and experiential connection with God (Hassan, 2007; Ahmad, Shrama, Shukla, Pant, & Tripathi, 2015b). The present research does not contest the importance of rituals in Islamic societies, but suggests that, compared to the Islamic worldview, Islamic ritual (religious personality) is less likely to influence judgments.

Evidence shows that in Islamic countries, a higher score on Islamic religiosity results in increased ethical sensitivity among accounting professionals (Muhamad & Ghani, 2006; Abuznaid, 2009; Muhamad, 2009; Alshehri et al., 2016), has a positive influence on accountants' ethical judgments (Abdul-Baki et al., 2013), and has a positive relationship with social responsibility and entrepreneurial judgments in Islamic organizations (Adamu et al., 2011).

Earlier studies investigating religiosity and auditors' judgments have adopted simplistic proxies for religiosity (McGuire et al., 2011; Omer et al., 2016) such as geographical proximity of audit offices in religious or non-religious areas (McGuire et al., 2011), distance of audit offices from the church (Omer et al., 2016; Jaggi & Lewis, 2017), and single-item measures of religiosity based on church attendance (Walker et al., 2015).

This study extends prior research and provides more rigour by adopting a more sophisticated measure of Islamic religiosity which is based on multidimensional constructs of the Islamic worldview (a judgment-related construct) and religious personality (a compliance-related construct). The MPRI Islamic religiosity framework, and the nature of the two autonomous constructs that make up Islamic religiosity, allow for differentiation between the influence of each of these constructs on auditors' preference for more or less judgment (see Figure 2.1). Thus the hypotheses developed in this research are more nuanced and differ from earlier studies that predict a simple, positive relationship between Islamic religiosity and compliance with Islamic values (Rehman & Shahbaz Shabbir, 2010; Idris, Bidin, & Saad, 2012). Thus, the first hypothesis predicts that auditors who score high on the overall Islamic religiosity scale (and therefore most likely on Islamic worldview) will prefer more judgment compared to those who score low:

**H1:** Auditors with a high (low) Islamic religiosity score have a preference for more (less) judgment.



### ***Influence of Islamic worldview on auditors' preference for more or less judgment***

Figure 2.1 illustrates the two hypotheses based on Islamic worldview and religious personality, the two components of Islamic religiosity. Islamic worldview is a “comprehensive conception of the universe and man’s relation to it from the Islamic perspective and serves as one’s philosophy or outlook of life” (Abdullah & Nadvi, 2011, p. 271). Regarded as a central cognitive orientation, Islamic worldview ascertains one’s level of agreement with basic Islamic values, beliefs, and creed (Krauss et al., 2005, p. 138). As individual judgments are driven by values (Torelli & Kaikati, 2009), Islamic worldview, grounded as it is in core Islamic values, is likely to be a dominant factor in influencing judgments in a business context.

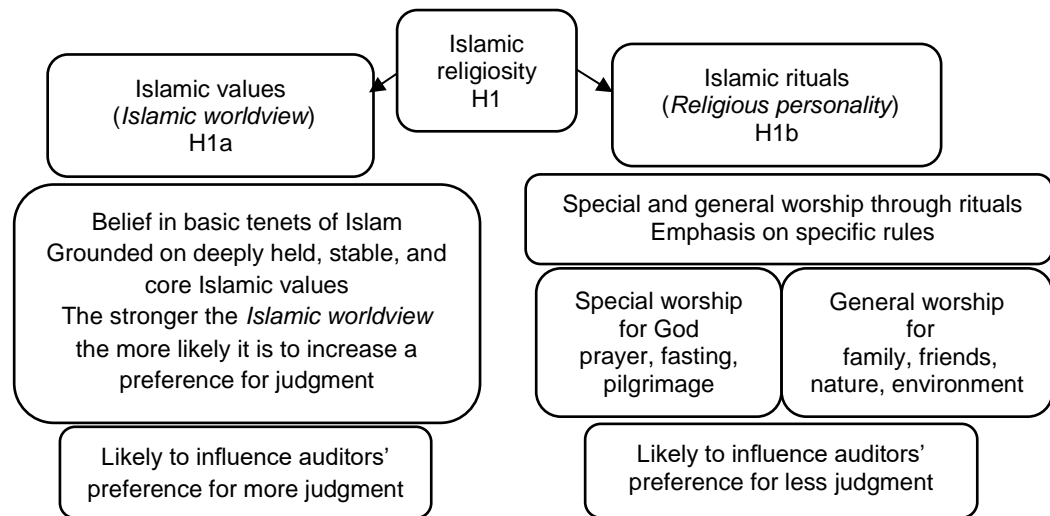
Prior literature in history, ethics, and marketing provide evidence of the influence of Islamic worldview on judgments. For example, Badawi (2002) suggests that Islamic worldview is the primary motivator behind the extraordinary transformation of Islamic civilization throughout history. Islamic worldview also provides the foundation for the “moral–social reconstruction” of ethical business practices in Islamic countries and a stronger Islamic worldview results in more ethical business practices in Islamic financial institutions (Asri & Fahmi, 2004; Choudhury, 2015). Studies in marketing also provide evidence that a higher score on Islamic worldview results in more ethical judgments by Muslim consumers (Arham, 2010; Ilyas et al., 2011; El-Bassiouny, 2014; Ahmad et al., 2015a).

To date, the influence of Islamic worldview has not been investigated in the audit judgment context in an Islamic cultural context. Furthermore, as this study’s participants are audit practitioners with extensive training in risk-based audit methodologies and experience in making informed audit judgments, the “worldview religiosity” construct is likely to be more influential on their audit judgments (Buchholz, 2012). Based on the nature of the Islamic worldview concept and given that this study was conducted with audit practitioners, this study predicts that the worldview construct will dominate individuals’ (i.e., auditors’) decision making in a business context and thus will significantly influence

their judgment. Therefore, the second hypothesis predicts that auditors who score high on the Islamic worldview will have a preference for more judgment:

**H1a:** Auditors with a high (low) Islamic worldview score have a preference for more (less) judgment.

**Figure 2.1: Diagrammatical representation of Hypotheses 1a and 1b**



### ***Influence of religious personality<sup>9</sup> on auditors' preference for more or less judgment***

Prior research provides evidence that Islamic rituals in Islamic countries are important socially, personally, professionally, and organizationally (Ali & Weir, 2005). Islamic rituals are detailed, structured, and predominantly rules-based. Scholars have labelled these ritual aspects of Islam “legalistic” (Trimingham, 1998; Farooq, 2011) and “mechanical” (Bennett (2009). “Islamic legalism” refers to the interpretation of aspects of Islam without human intellect or judgment playing a vital role (Farooq, 2011).<sup>10</sup>

Religious personality represents external forms of worship, special prayers, and religious rituals (Krauss et al., 2005, p. 140). It reflects an individual’s direct relationship with God through ritualistic

<sup>9</sup> The term “personality” in the religious personality construct is limited to its use in the MRPI scale and only represents the ritual dimensions of religiosity in this study. The term “personality” as defined and used in the psychology literature is not applicable in this study.

<sup>10</sup> “Islamic legalism” is defined as the historical emergence of a dominant mode of thinking in some sections of Islamic communities in the 18<sup>th</sup> to the 21<sup>st</sup> century. The legalistic interpretation of Islam suggests “form should take over substance” and treats *Shariah* as a stagnant resource of rules and rigid guidelines. There are some aspects of *Shariah* that do not require interpretation, for example, rituals and worship. However, scholars warn that this approach in other areas of inquiry leads to substantive degeneration that reduces Islam to a shell of codes rather than a dynamic and value-oriented religion (Farooq, 2011). However, Islamic accounting standard setters suggest that application of Islamic *Shariah* to financial banking and contracts emphasises “form as well as substance”.

acts such as prayer, fasting, reading the holy scriptures, and obedience to the external Islamic discipline, such as dress code and appearance, as well as items specific to Islamic legal rulings (Krauss et al., 2005, p. 179). Religious personality measures one's level of commitment to ritualistic behaviour and reflects a variety of behaviours to assess the extent to which they reflect Islamic teachings.

Figure 2.1 illustrates the two kinds of worship that comprise Islamic rituals: special worship and general worship (Krauss et al., 2005). Given the rules-based and prescriptive nature of both kinds of worship, there are expectations of compliance with their rigid requirements. Thus, this study suggests that this component of Islamic religiosity involves limited exercise of judgment.

Prior research investigating religiosity and audit judgment adopts various religious ritual proxies such as church attendance and proximity of audit offices to non-religious areas (McGuire et al., 2011; Omer et al., 2016). This study, however, predicts that rituals and worship (i.e., religious personality) are external manifestations of religiosity requiring compliance, and thus are less likely to drive preference for judgment in a professional audit context. Thus the third hypothesis predicts that:

**H1b:** Auditors with a high (low) religious personality score have a preference for less (more) judgment.

## 2.5 Research method

### 2.5.1 Participants

Professional auditors<sup>11</sup> working at various levels of seniority<sup>12</sup> in medium-tier auditing firms<sup>13</sup> in Pakistan participated in the survey. Medium-tier auditing firms were selected as an appropriate sample for participation given their mandatory adoption of ISAs. Owing to their smaller size and limited integration with international networks, their firm culture was expected to be similar to other local organizations (Khilji, 2003).

One-hundred and fifty questionnaires were distributed, and 66 usable responses were received, resulting in a relatively high response rate of 44%.<sup>14</sup> The sample was distributed across all levels of seniority with the majority at audit senior level or above (66%), 20–30 years of age (75%), and average audit experience of 3.58 years. Approximately 82.4% of the participants were practicing members of the ICAP.

A majority of the participants (94%) reported being familiar with ISAs (mean = 5.24 on a Likert scale of 1–7, where 1 = very unfamiliar and 7 = very familiar) and had task-specific experience with provision for doubtful debt judgments (mean = 4.60 on a Likert scale of 1–7, where 1 = no prior experience and 7 = dealt with very often). Both the familiarity with ISAs and the task-specific experience

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<sup>11</sup> Professional accountants/auditors in Pakistan who are members of the ICAP have completed all academic and professional Chartered Accountancy requirements and hold a minimum three years' professional audit/accounting experience (ICAP, 2017a).

<sup>12</sup> Participants were audit trainees (16.7%), audit seniors (37.9%), assistants (22.7%), managers (16.7%), and partners (6.1%). The audit task selected in this study was appropriate across the various seniority levels in the sample.

<sup>13</sup> Medium-tier auditing firms in Pakistan are both local and international non-Big 4 auditing firms, which have adopted ISAs and have satisfactory Quality Control Review ratings from the ICAP (ICAP, 2016a). Under the Companies Ordinance of 1984, all companies in Pakistan are required to be audited using standards adopted by the ICAP. The Audit Oversight Board, which was established in 2016 under the amended Securities and Exchange Commission of Pakistan Act of 1997, oversees the work of the ICAP to ensure that auditing standards adopted and issued by the ICAP conform to ISAs issued by the IAASB (IFAC, 2017a).

<sup>14</sup> Recently published examples from audit judgment research show low survey response rates. For example, a response rate of 20.7% in Abbott, Daugherty, Parker, and Peters (2016) and 26% in Mohd Sanusi, Iskandar, Monroe, and Saleh (2017).

scores indicated that the participants possessed the requisite knowledge and experience to participate in the study.

The sample consists of 91% males and 9% females, which is consistent with Pakistan's ranking on the Global Gender Gap Index (ADB, 2016, p. 70). Pakistan has witnessed persistent gender inequality, specifically in the accounting and business professions, and this sample is representative of the existing gender gap in the workforce. Being a male-dominated society, especially with respect of workforce participation in businesses and accounting (Pakistan Bureau of Statistics, 2018), only 20% of the auditors were female.

A summary of the demographic information for the participants is presented in Table 2.1.

Table 2.1: Demographics					
Item	N	%			
Gender					
Male	60	90.9			
Female	6	9.09			
Age					
20–30	50	75.8			
30–40	13	19.7			
40–50	2	3.0			
50–60	1	1.5			
Membership					
ICAP (CA/ICAP)	53	82.4			
Other professional bodies	13	17.6			

Item	Current position in firm	Total audit experience Years	Experience at current level years	Task-specific experience* (1–7)	Familiarity with ISAs (1–7)**
	<i>N (%)</i>	<i>Range (mean)</i>		<i>Mean</i>	
Audit trainees	11 (16.7)	0–4 (1.47)	1–3 (1.09)	4.0	5.0
Assistants	15 (22.7)	0–5 (2.5)	3–6 (2)	4.07	5.0
Audit seniors	25 (37.9)	2–7 (4.3)	3–6 (2.3)	4.84	5.28
Managers	11 (16.7)	3–17(6.9)	1–20 (5)	5.0	5.45
Partners	4 (6)	10–15 (12)	6–15 (9)	5.50	6.0
Total/Mean	66 (100)	3.85	2.9	4.60	5.24

\* where 1 = no prior experience and 7 = dealt with very often

\*\* where 1 = very unfamiliar and 7 = very familiar

### 2.5.2 Research design and procedure

A survey questionnaire was designed and administered to test the hypotheses in this study (refer to research instrument in Appendix B). The survey method was selected to facilitate the collection of a

broad range of data from a large number of participants by employing a variety of questions. The survey method provides extensive flexibility in data analysis and for determining the statistical significance between variables of interest (Singleton & Straits, 2010). A doubtful debts judgment task, tested for reliability and validity in prior research (Reimers & Fennema, 1999; Huang, Ku, Chu, & Hsueh, 2002; Anderson & Fleming, 2014), was selected and tailored for the purposes of this study. The scenario involves a considerable level of judgment and is relevant to various audit seniority levels. The survey was administered in English and was extensively pilot tested to ensure readability and clarity,<sup>15</sup> and relevance to the Pakistani audit context (refer to the research instrument in Appendix B).

A number of medium-tier auditing firms in Pakistan were contacted via email to obtain permission to conduct the survey in their respective firms. The firms were informed of the ethics approval and the voluntary nature of the research. Both the firms' and individual participants' confidentiality were assured. After the firms agreed to participate and provide an estimate of the number of potential participants, the sealed questionnaire packs were distributed to the assigned contact person at each firm. Each questionnaire pack included a cover letter, instructions to participants, and the research instrument (see Appendix B). The survey was conducted during training sessions held at the respective auditing firms. As instructed in the questionnaire pack, the participants placed the completed questionnaires in the envelopes provided and sealed them. The questionnaire packs were then collected from the contact person at each firm by the researcher.<sup>16</sup>

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<sup>15</sup> Feedback was sought from 13 professional auditors, two accounting professors, and two accounting regulators from Pakistan. Their comments were incorporated into the final version of the questionnaire. Pilot testing also confirmed that auditors in Pakistan would have no problem in understanding and responding to the survey in English.

<sup>16</sup> To comply with the ethical requirements of the research, the researcher did not come into direct contact with the participants during data collection to minimize coercion. Thus, the management of the auditing firms administered the survey.

### ***2.5.3 Research instrument and variables***

The research instrument consists of three sections. The first section contains an accounts receivable valuation scenario (i.e., adequacy of a provision for doubtful debt assessment), and is followed by the dependent variable measures. The second section collects participants' demographic information and responses to three control variables. The third section contains an Islamic religiosity scale, which measures auditors' Islamic religiosity (refer to the research instrument in Appendix B).

The participants were asked to assume the role of a senior auditor and were requested to evaluate provision for doubtful debts for a hypothetical client, Nature-Pakistan Limited (Nature), by making a series of related judgments. It was made clear that this issue was the only material issue remaining on the audit. The scenario provided an accounts receivable aging schedule for Nature, summarizing the actual balances and predicted provision for doubtful debts based on the average percentages of the balances not collected in prior years. The participants were further informed that the client, that is, the chief financial officer (CFO), believed that the two accounts that made up a large portion of the overdue debt (PKR 2000 (AUD 22.8) million), 50% of which had historically not been collected), would be paid in full by each debtor. According to the CFO, the delay in payment had been caused by the seasonal payment cycle of the two customers, and the full payment would be made within a few weeks. After being provided with the relevant information, the participants were required to make a series of related judgments.

### ***Independent variables***

Auditors' overall Islamic religiosity level is the main independent variable. In this study, the MRPI<sup>17</sup> is utilized to measure auditors' overall Islamic religiosity level and its two separate constructs, Islamic worldview, and religious personality. The Islamic worldview scale consists of 20 items (13 items are

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<sup>17</sup> The MRPI was selected to ensure the construct validity of the study. The MPRI scale has strong psychometric properties regarding internal reliability and consistency (Cronbach's alpha reliability scores: Islamic worldview = 0.83 and religious personality = 0.90) (Krauss, 2011).



reverse scored), and the religious personality scale contains 28 items (Krauss, 2011). The scale enables reporting of auditors' Islamic worldview and religious personality scores both as continuous and categorical measures (high vs low) (Krauss, 2011).

The Islamic worldview scale assesses participants' levels of belief in core Islamic values. For example, item 6, "All Islamic laws can be modified to fulfill contemporary needs" measures believers' perceptions about the fundamental importance of adhering to core Islamic values. And item 11, "Islamic values are applicable only in certain situations, places, and times" measures believers' perceptions about Islamic values and their importance in almost all activities. The religious personality scale includes items that measure compliance and observance of Islamic rituals. For example, item 4 states, "I make an ongoing effort to increase the frequency of my non-obligatory prayers," and item 9 is "I find time to recite the Holy Book (*Quran*) even if I am busy." Both the Islamic worldview and religious personality scales measure responses on a Likert scale of 1 (strongly disagree) to 5 (strongly agree).

Individual religiosity scores were determined according to the MRPI scoring manual, with each scale summed up and divided by the number of items in that scale. For example, for the Islamic worldview scale, which has 20 items, if the total score was 86, 86 was divided by 20 which is 4.3, the scaled score for that participant. This score was then categorized based on the threshold values of high and low religiosity (Krauss, 2011). The threshold value for Islamic worldview is 4.19 (Krauss, 2011, p. 2). All those auditors who scored higher or equal to 4.19 were categorized as having a high Islamic worldview score and those who scored less than 4.19 were categorized as scoring low on the Islamic worldview scale. For religious personality, the threshold value was 3.55. Subjects who scored higher or equal to 3.55 were categorized as having a high score on the religious personality construct, and those who scored less than 3.55 were categorized as low (Krauss, 2011, p. 2).<sup>18</sup> For overall Islamic religiosity,

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<sup>18</sup> Theoretically, the possible range for scores for overall Islamic religiosity is from a high of 10.0 to a low of 1.0, and for both the Islamic worldview and religious personality scales, it is from a high of 5.0 to a low of 1.0 (Krauss, 2011).

the threshold value for each participant was determined based on the mean of the combined scores for Islamic worldview and religious personality. Subjects who scored higher or equal to 8.44 were categorized as high, and those who scored less than 8.44 were categorized as low.

### ***Dependent variables***

After familiarizing themselves with the background information and the audit issue, participants were required to make a series of audit judgments. In the first judgment, the main dependent variable measures auditors' preference for more or less judgment and is captured as both categorical and continuous measures to ensure the reliability of the responses. Moreover, the two dependent variable measures (continuous and categorical) of the same dependent variable allow the use of both parametric and nonparametric tests for hypotheses testing.

First, auditors' preference for more or less judgment was recorded in item 1 (part one) of the research instrument as a categorical variable. In this item auditors were required to select their preference for more or less judgment while estimating the provision for doubtful debts as either (i) the percentage method based on the history of previous years' amounts not collected (more guidance/less judgment) or (ii) the judgment based on the aged balances of each overdue debtor together with the review of the analysis of their sales and history of payment (less guidance/more judgment). Both options require judgments but one of these pertains to more judgment (item ii) and the other (item i) pertains to less judgment.

Auditors' preference for more or less judgment was also measured by item d (part two) of the questionnaire as a continuous variable with auditors rating their preference for judgment on a Likert scale from 1–7 (with 1 = very low and 7 = very high). This supplementary measure is also used as the main dependent variable in the analysis of the data.

In item e (part two), this study also captures auditors' levels of preference for rules on a Likert scale from 1–7 (with 1 = very low and 7 = very high). This additional variable was included to check

the veracity of the responses for preference for judgment and as a countercheck on the main dependent variable. Ideally, auditors with more preference for judgment should score low on this item (i.e., these two variables are expected to be negatively correlated with each other).

In addition, participants were asked to recommend an adjustment to the doubtful debts provision (ranging from PKR 0–1200 (AUD 0–13.7) million),<sup>19</sup> with the scale point increasing in PKR 200 (AUD 2.28) million increments.

### ***Additional variables***

The second part of the research instrument collected demographic data and a number of control variables including participants' age, gender, professional membership, current position in their firm, experience (general audit experience and task-specific experience), familiarity with ISAs, and their perceived level of risk in relation to the collectibility of debtors.

## **2.6 Results and discussion**

### ***2.6.1 Descriptive statistics***

The summary of descriptive statistics is presented in Tables 2.2 and 2.3. Data were checked for normality and social desirability response (SDR) bias and no significant issues were identified.

To address the potential SDR bias in this study, the MRPI framework has an embedded "lie scale" in the religious personality component. There are five items in the scale. It is suggested that with regard to these five items, respondents who score a total exceeding 20 (> 80%) be removed from the analysis (Krauss, 2011). Eight participants scoring higher than the threshold value for SDR were removed from the original sample. Removal of these participants from the sample does not qualitatively

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<sup>19</sup> All number values are in Pakistan rupees (PKR) which is the official currency of Pakistan (1 AUD = 80 PKR, 1 USD = 104.8 PKR).

change the significance of the statistical tests. However, the results reported are those following the removal of those participants from the sample.

Gender, age, professional membership, current position, general audit experience, and task-specific experience were also tested for significance, and no significant results for participants' judgment preference were identified ( $p > 0.000$ ).

**Table 2.2: Summary of descriptive statistics for religiosity continuous independent variables and dependent variables (n = 66)**

	Mean (range)	Std deviation
<b>Independent variables</b>		
<i>Overall Islamic religiosity</i>	8.44 (6.50–9.40)	0.625
<i>Islamic worldview</i>	4.15 (3.30–4.90)	0.380
<i>Religious personality</i>	4.29 (2.90–4.90)	0.418
<b>Dependent variables</b>		
Auditors' preference for judgment (1 = very low and 7 = very high)	5.29	0.873
The amount by which the provision should be reduced (0–1200 PKR)	736.36	363.164
<b>Control variables</b>		
Perceived level of risk in relation to the collectability of debtors (1 = very low and 7 = very high)	5.02	1.170
Familiarity with ISAs (1 = very unfamiliar and 7 = very familiar)	5.24	0.993
General audit experience (number of years)	3.85	3.438
Task-specific experience (1 = no prior experience and 7 = dealt with very often)	5.24	0.993

From Table 2.2, the mean (standard deviation) score on overall Islamic religiosity is 8.44 (0.625), the mean score on Islamic worldview is 4.15 (0.380), and the mean score on religious personality is 4.90 (0.418). The mean score of auditors' preference for judgment is 5.29 (0.873). The mean score of auditors' familiarity with ISAs is 5.24, and the mean score of auditors' task-specific experience with doubtful debts is also 5.24.

<b>Table 2.3: Summary of descriptive statistics for religiosity categorical independent variables and continuous dependent variables</b>				
		<b>N</b>	<b>Mean</b>	<b>Std deviation</b>
<i>Overall Islamic religiosity</i>				
Auditors' preference for more judgment (1 = very low and 7 = very high)	Low	28	5.0	0.943
	High	38	5.42	0.793
<i>Islamic worldview</i>				
Auditors' preference for more judgment (1 = very low and 7 = very high)	Low	31	4.81	0.833
	High	35	5.63	0.731
<i>Religious personality</i>				
Auditors' preference for more judgment (1 = very low and 7 = very high)	Low	23	5.22	0.998
	High	43	5.26	0.819

Table 2.3 indicates that 28 participants scored low on overall Islamic religiosity, and 38 scored high.<sup>20</sup> The mean preference score for those with low religiosity was 5.0 compared to 5.42 for those who scored high on overall Islamic religiosity. Similarly, 31 participants scored low on Islamic worldview, and 35 scored high. The mean preference for more judgment for those who scored low is 4.81, and for those who scored high is 5.63. Additionally, the results show that 23 participants scored low on religious personality and 43 scored high. The mean preference for more judgment for those who scored low is 5.22, and for those who scored high, it is 5.26. The Cronbach's alpha value for Islamic worldview is 0.702, and for religious personality, the value is 0.701. Cronbach's alpha is a measure of internal consistency, that is, how closely related a set of items are as a group and is considered to be a measure of scale reliability (Santos, 1999). According to Sekaran (2003), an alpha value of less than 0.60 is poor,

<sup>20</sup> Research has suggested that unequal cell size can pose a challenge in comparison studies. To address this concern, in this study data were checked for normality prior to analysis and assumptions of homogeneity of variance were not violated (Levene's test for significance was not significant,  $p > 0.05$ ), which is an essential requirement for ANOVA testing. Additionally, if the minimum number of participants in each cell is 20, the inequality of cell size might not affect the validity of the results (Weiss, 2006).

between 0.70–0.80 is acceptable, and over 0.80 is good. The results add to the reliability of the MPRI scale in Pakistan.

### 2.6.2 Validity test for independent variables

To ensure that the assumptions around the nature of the two constructs, Islamic worldview and religious personality, hold true, a correlation analysis was conducted. The results of the Pearson correlation coefficient provided in Table 2.4 show that although both of these constructs are significantly correlated with overall Islamic religiosity ( $p = 0.000$ ), they are not significantly correlated with each other ( $p = 0.076$ ). The results verify that Islamic worldview and religious personality are two distinct and separate constructs of religiosity and support the validity of Krauss et al. (2005) Islamic religiosity framework adopted in this study.

**Table 2.4: Pearson correlation coefficients for independent variables**

		<i>Islamic worldview</i>	<i>Religious personality</i>	<i>Overall Islamic religiosity</i>
<i>Islamic worldview</i>	Pearson correlation	1	.220	.757**
	Sig. (two-tailed)		.076	.000
	N	66	66	66
<i>Religious personality</i>	Pearson correlation	.220	1	.804**
	Sig. (two-tailed)	.076		.000
	N	66	66	66
<i>Overall Islamic religiosity</i>	Pearson correlation	.757**	.804**	1
	Sig. (two-tailed)	.000	.000	
	N	66	66	66

\*\* indicates correlation is significant at the 0.01 level (two-tailed).

Additionally, the nonparametric Wilcoxon signed-ranks test shows that out of 66 participants, 35 participants scored high on Islamic worldview compared to their religious personality score, and 27 scored high on religious personality compared to their scores on Islamic worldview. Four participants

scored equally on both of the constructs.<sup>21</sup> These results indicate that participants who score high on one construct do not generally score high on the other and provide further support for the religiosity constructs utilized.

### **2.6.3 Hypotheses tests**

#### ***H1: Overall Islamic religiosity and auditors' preference for more or less judgment***

Hypothesis 1 predicts that auditors with high overall Islamic religiosity scores will have a preference for more judgment. Using categorical measures and a non-parametric Chi-square test for association, Table 2.5 shows a significant positive association between overall Islamic religiosity level and auditors' preference for more judgment ( $\chi^2(1,66) = 3.179$ ;  $p = 0.043$ ). The majority of the participants (69%) who scored high on overall Islamic religiosity prefer more judgment, and 59% of the participants who scored low on overall Islamic religiosity also prefer more judgment. The results in Table 2.5 indicate a significant positive effect of overall Islamic religiosity on auditors' preference for more judgment, supporting Hypothesis 1 ( $p = 0.043$ ).

Using continuous measures and parametric tests, linear regression analysis was conducted between auditors' overall Islamic religiosity level and their preference for more judgment. The results in Table 2.6 ( $R = 0.345$ ) indicate a moderate correlation between the variables and provide evidence that auditors with a high level of overall Islamic religiosity have a significant preference for more judgment ( $F = 8.655$ ,  $p = 0.005$ ).

Additionally, the one-way ANOVA between categorical measures of *overall Islamic religiosity* and the continuous measure of auditors' preference for more judgment (see Table 2.7) provides evidence that there is a significant difference between the mean preference scores at the two levels of overall

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<sup>21</sup> Four of the participants had equal scores on Islamic worldview and religious personality, so they were eliminated from the sample and tests were rerun. However, this did not statistically change the significance of the results, which are reported for these participants.

Islamic religiosity ( $F(1,64) = 3.870$ ,  $p = 0.050$ ). The mean preference for more judgment scores for auditors who scored high on the overall Islamic religiosity scale is significantly higher ( $n = 38$ , mean = 5.42,  $SD = 0.793$ ) compared to those who scored low on overall Islamic religiosity ( $n = 28$ , mean = 5.00,  $SD = 0.943$ ). Overall, the results using both categorical and continuous measures provide evidence that auditors who scored high on overall Islamic religiosity have a preference for more judgment and support Hypothesis 1.

**Table 2.5: Chi-square test for Hypotheses 1 and 2**

Dependent variable	Overall Islamic religiosity			Islamic worldview			Religious personality		
	Value	df	one-sided sig.	Value	df	one-sided sig.	Value	df	one-sided sig.
Auditors' preference for more judgment									
Pearson Chi-square	3.179	1	<b>0.043</b>	7.505	1	<b>0.006</b>	0.000	1	<b>0.589</b>
	Low		High	Low		High	Low		High
Preference (% within)									
Less judgment	41%		31%	61.8%		30%	44.4%		44.7%
More judgment	59%		69%	38.2%		70%	55.6%		55.3%

#### ***H1a: Islamic worldview and auditors' preference for more or less judgment***

Hypothesis 1a predicts that auditors with a high Islamic worldview score will have a preference for more judgment. Using categorical measures and a non-parametric Chi-square test for association, Table 2.5 suggests a positive association between Islamic worldview and auditors' preference for more judgment ( $\chi^2(1,66) = 7.505$ ;  $p = 0.006$ ) with a majority of participants (70%) who scored high on Islamic worldview preferring more judgment. Additionally, 61.8% of the participants who scored low on Islamic worldview also prefer more judgment. The results in Table 2.5 indicate a significant positive effect of auditors' Islamic worldview on auditors' preference for more judgment ( $p = 0.006$ ).

Additionally, using continuous measures, linear regression analysis in Table 2.6 shows that  $R$  is 0.430, which indicates a moderate correlation between the two variables and support that a high level of Islamic worldview significantly influences auditors' preference for more judgment ( $F = 14.502$ ,  $p =$



0.000). One-way ANOVA results (Table 2.7) provide evidence of a statistically significant difference ( $F(1,64) = 18.229, p = 0.000$ ) between the mean preference scores at the two levels of Islamic worldview (high vs low), supporting Hypothesis 1a. The mean preference for judgment scores for auditors who scored high on Islamic worldview is significantly higher ( $n = 35$ , mean = 5.63,  $SD = 0.731$ ) than those who scored low on Islamic worldview ( $n = 31$ , mean = 4.81,  $SD = 0.833$ ). The results from statistical tests using both categorical and continuous measures support Hypothesis 1a.

<b>Table 2.6: Linear regression analysis for Hypotheses 1, 1a, and 1b</b>									
<b>Ind. Variables</b>	<b>Dependent variables</b>	<b>Durbin Watson</b>	<b>R</b>	<b>R<sup>2</sup></b>	<b>Adjusted R square</b>	<b>F</b>	<b>p</b>	<b>Mean (SD) n = 66</b>	<b>Beta</b>
<i>Overall Islamic religiosity</i>	Preference for more judgment	1.531	0.345	0.119	0.105	8.655	<b>0.005</b>	5.24 (0.303)	0.345
<i>Islamic worldview</i>	Preference for more judgment	1.558	0.430	0.185	0.172	14.502	<b>0.000</b>	5.24 (0.377)	0.430
<i>Religious personality</i>	Preference for less judgment	1.328	0.124	0.015	0.000	1.006	0.320	5.24 (0.878)	0.124

#### ***H1b: Religious personality and auditors' preference for more or less judgment***

Hypothesis 1b predicts that auditors with a high score on religious personality will have a preference for less judgment. Using categorical measures and a Chi-square test for association, Table 2.5 shows a non-significant association between the two variables ( $\chi^2(1,66) = 0.00; p = 0.589$ ); 55.6% of the participants who scored low on religious personality prefer less judgment and 55.3% of participants who scored high on religious personality prefer less judgment. Using continuous measures, the linear regression analysis also indicates the non-significance of the relationship ( $F(1,64) = 1.006, p = 0.320$ ) between auditors' religious personality and auditors' preference for less judgment (see Table 2.6).

Additionally, the one-way ANOVA results (Table 2.7) for religious personality and its influence on auditors' preference for less judgment are also not significant ( $F(1,64) = 0.028$ ,  $p = 0.867$ ). The results from both categorical and continuous measures do not support Hypothesis 1b.

Table 2.7: One-way ANOVA results for Hypotheses 1, H1a, and H1b										
Independent variables	Level of religiosity	n	Dependent variable Mean (SD) (preference for more/less judgment)	Levene's statistics (sig.)	F	P	Between n Within	Sum of squares	df	Mean square
<i>Overall Islamic religiosity</i>	Low	28	5.00 (0.943)	0.006 (0.937)	3.870	<b>0.050</b>	Between	2.858	1	2.858
	High	38	5.42 (0.793)				n groups Within groups	47.263	64	0.738
<i>Islamic worldview</i>	Low	31	4.81 (0.833)	0.027 (0.870)	18.229	<b>0.000</b>	Between	11.111	1	11.111
	High	35	5.63 (0.731)				n groups Within groups	39.010	64	0.610
<i>Religious personality</i>	Low	23	5.22 (0.998)	1.559 (0.216)	0.028	0.867	Between	0.022	1	0.022
	High	43	5.26 (0.819)				n groups Within groups	50.009	64	0.783

#### 2.6.4 Additional analysis

##### *Influence of auditors' Islamic religiosity level on their provision for doubtful debt adjustment*

In addition to examining auditors' preference for more or less judgment, this study also captures auditors' final judgments (i.e., decisions) about the adjustment to the provision for doubtful debts. As outlined in section 2.5.3, auditors were required to assess the final provision for doubtful debts by indicating an amount by which the provision for doubtful debt should be adjusted (in PKR million). Based on the information provided in the scenario it was expected that auditors would provide different responses according to their preference for more or less judgment and whether or not they accepted the CFO's information regarding the payment of the two specific, large, overdue debtors.

Participants with a preference for the percentage method (i.e., less judgment) were expected to make no adjustment or only a small adjustment if they accepted that the debts would not be repaid. However, if they accepted that the two debts would be repaid in full, a reduction of the full amount of PKR 1000 (AUD 11.4) million or close to it was expected. On the other hand, a wider range of adjustment (between zero and PKR 1000 (AUD 11.4) million) was expected for participants with a preference for more judgment, depending on whether they believed that the two doubtful debts were collectible or not.

The descriptive results show that almost 94% of the participants reduced the total amount of the provision for doubtful debts. The average amount of reduction in the provision was PKR 736.36 (AUD 8.42) million,<sup>22</sup> a material amount. Approximately 40% (26 out of 66) of the participants recommended a reduction of around PKR 1000 (AUD 11.4) million and 64% of the participants reduced the total amount of provision by between PKR 800 and 1000 (AUD 9.1 and 11.4) million.

Additional one-way ANOVA analysis (see Table 2.8) was conducted to examine whether auditors' Islamic religiosity influenced the final adjustment amount. Although the mean amount of adjusted provision is higher for those who scored high on overall Islamic religiosity ( $n = 38$ , mean = 778.36, SD = 337.84) than those who score low on overall Islamic religiosity ( $n = 28$ , mean = 678.57, SD = 393.80), the results are not significant ( $F(1,64) = 1.236$ ,  $p = 0.270$ ). However, the auditors' Islamic worldview religiosity component was significant in determining the amount of adjustment ( $F(1,64) = 7.424$ ,  $p = 0.008$ ). The adjusted provision balance recommended by auditors who scored high on Islamic worldview ( $n = 35$ , mean = 845.71, SD = 233.065) is on average significantly higher than those who scored low on Islamic worldview ( $n = 31$ , mean = 612.9, SD = 441.015).

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<sup>22</sup> Planning materiality for this client was set at PKR 500 million (AUD 5.6 million).

**Table 2.8: One-way ANOVA results for amount of provision reduced in auditors' opinion**

Panel independent variables	N	Dependent variable Mean (SD) (amount of provision)	Levene's statistics	F	P	Between Within	Sum of squares	df	Mean square
<i>Overall Islamic religiosity</i>									
Low	28	678.57 (393.80)	3.169 sig. = 0.080	1.236	0.270	Between groups	162426.52	1	162426.5
High	38	778.36 (337.84)				Within groups	8410300.7	64	131410.9
<i>Islamic worldview</i>									
Low	31	612.9 (441.015)	24.264 sig. = 0.000	7.424	<b>0.008</b>	Between groups	891031.42	1	891031.4
High	35	845.71 (233.065)				Within groups	7681695.8	64	120026.4
<i>Religious personality</i>									
Low	23	695.65 (350.945)	0.078 sig. = 0.781	0.440	0.510	Between groups	58510.89	1	58510.89
High	43	758.14 (371.761)				Within groups	8514216	64	133034.6

Evidence in support of Hypothesis 1a suggests that auditors who scored high on Islamic worldview have a preference for more judgment. The results in Table 2.8 further suggest that auditors who prefer more judgment appear to take into account (and believe) the new information provided by the CFO that the two doubtful accounts will be repaid in full. However, auditors' religious personality level is not a significant influence for the revised amount of provision recommended by the auditors ( $F(1,64) = 0.440$ ,  $p = 0.510$ ), which is consistent with the results obtained for Hypothesis 1b.

### ***Influence of auditors' preference for more or less judgment on revising the provision for doubtful debt***

The analysis above focused on how auditors' levels of overall Islamic religiosity, Islamic worldview, and religious personality influence their final judgment on revising the provision for doubtful debts. In this section, additional analysis is conducted to investigate the influence of auditors' preference for more or less judgment<sup>23</sup> on their final adjustment of the provision for the doubtful debts balance. The results of

<sup>23</sup> Apart from measuring auditors' preference for more judgment, the study also used an additional measure of auditors' preference for less judgment (i.e., their preference for rules or more guidance). This measure was utilized to test the validity of the main dependent variable. As discussed in section 2.6.3 it was expected that these two measures would be negatively

ANOVA (see Panel A, Table 2.9) show that auditors' preference for more judgment is significant for the amount of provision for the doubtful debts adjustment decision ( $F(1,64) = 0.4.451$ ,  $p = 0.039$ ). The mean recommended amount for reducing the provision for doubtful debts by those auditors who prefer more judgment is 822.86 (260.187), which is significantly higher than the mean amount of 638.71 (436.408) for auditors who prefer less judgment.

Table 2.9: ANOVA results: One-way ANOVA between auditors' preference for more or less judgment and amount of provision									
Panel A: One-way ANOVA between auditors' preference for more or less judgment and amount of provision									
Independent variables	n	Dependent variable mean (SD) Provision for doubtful debt	Levene's statistics	F	P	Between Within	Sum of squares	df	Mean square
Less judgment	31	638.71 (436.408)	20.906 sig. =	4.451	0.039	Between groups	557464.600	1	557464.60
More judgment	35	822.86 (260.187)	0.000)			Within groups	8015262.67	64	125238.47
Panel B: 2x2 ANCOVA between auditors' preference for more or less judgment and amount of provision to be reduced in auditors' opinion									
Independent variables	Type III sum of squares	df	Mean square	F	Sig.	Partial eta squared			
Auditors' preference for more or less judgment <i>Control variable</i>	474895.907	1	474895.907	3.768	.057	.056			
Perceived level of risk in relation to collectability of debtors	74316.591	1	74316.591	.590	.445	.009			
a. R Squared = .074 (adjusted R Squared = .044)									

The results are of concern as they suggest that although auditors with higher overall Islamic religiosity and Islamic worldview scores prefer more rather than less judgment, they also exhibit less sceptical judgment and conservatism in agreeing with the client's aggressive treatment based on low-reliability evidence (i.e., the internal client provided verbal evidence).

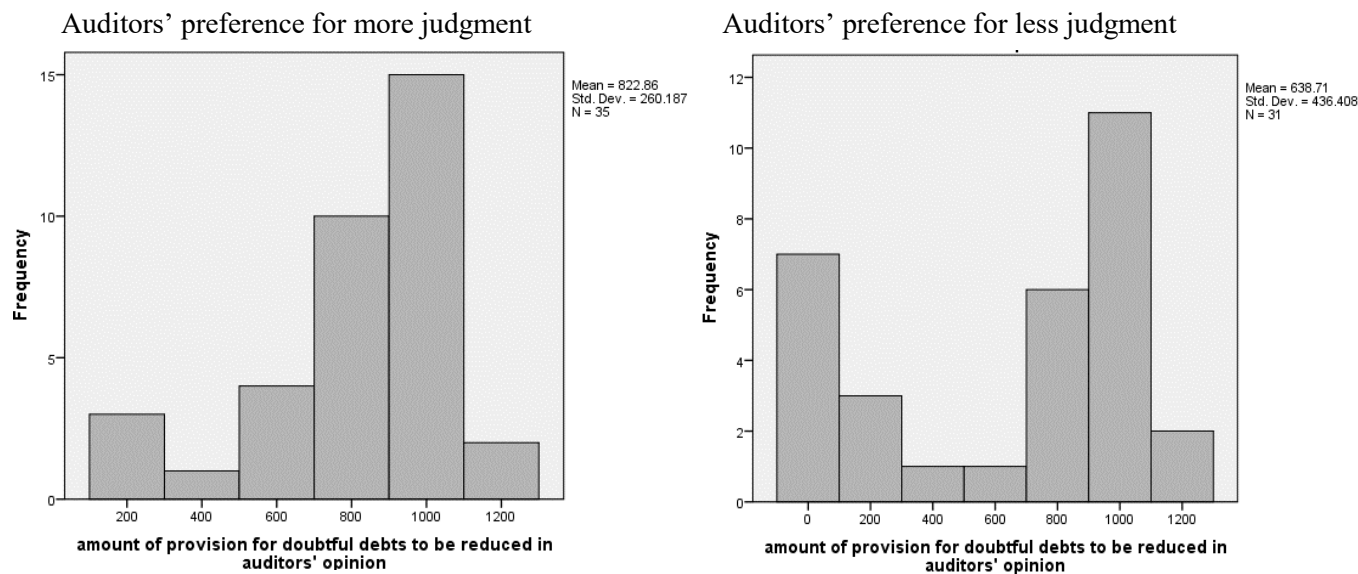
correlated. A Pearson correlation test between auditors' preference for more or less judgment shows a weak negative linear relationship ( $r = 0.10$ ) and non-significance ( $p = 0.408$ ).

Graphical representation of the differences between the “spread” of auditors’ preference for more or less judgment and the amount of doubtful debt adjustment (see Figure 2.2) shows significant differences in the patterns of the adjustments between the two groups of auditors. These different patterns suggest that auditors in the two groups have adopted a different process for arriving at the judgment about the adjustment.

It was expected that auditors who prefer less judgment (i.e., the percentage method) are either likely to indicate no revision in the amount of provision for doubtful debt or a large revision of around 1000 PKR (AUD 11.4) million. Figure 2.2 supports this expectation with the auditors’ adjustment amount clustering around either none/very small adjustments (PKR 0–200 (AUD 0 – 2.28) million) or close to a maximum/large adjustment of PKR 1000 (AUD 11.4) million, presumably depending on whether they take into account the new information provided by the CFO or not. Auditors who have a preference for more judgment and less guidance, on the other hand, have a different pattern to their adjustments. Figure 2.2 shows that auditors’ adjustments cluster around the maximum amount with 40% of the participants recommending a reduction of around PKR 1000 (AUD 11.4) million. Overall Figure 2.2 suggests that auditors, especially those with a preference for judgment, appear to take into account (and believe) the new information provided by the CFO that the two doubtful accounts are not doubtful and will be paid.

This study also examined auditors’ risk evaluation of the doubtful debt balance as a potentially important factor influencing their judgments. The result of a 2x2 ANCOVA (see Table 2.9) between auditors’ preference for more or less judgment and their final revision of a provision for doubtful debts with auditors’ risk assessment as a covariate was not significant ( $F = 0.590$ ,  $p = 0.445$ ). The results suggest that auditors perceive the collectability of the debtors to be at only a moderate level of risk.

**Figure 2.2: Spread of auditors' preference for more or less judgment and their final judgment on the amount of provision for doubtful debt**



## 2.7 Conclusions

Auditing is a judgment-based task (Nelson & Tan, 2005; Trotman, 2014), and auditors' exercise of their professional judgment is integral to deciding whether accounting estimates, such as provision for doubtful debt estimates examined in this study, are reasonable. Auditing judgment determines audit quality and, by extension, the quality of associated financial reports (Griffith & Young, 2016). This study contributes to the literature on auditors' judgment and decision making by examining the influence of a relevant and important cultural variable – Islamic religiosity – on auditors' preference for more or less judgment. It extends previous research into cultural influences on auditors' judgment generally and auditors' preference for more or less judgment specifically.

ISAs are principles-based and require auditors to make judgments. However, prior research (e.g., Schultz and Lopez (2001) Doupnik and Richter (2003) Doupnik and Riccio (2006) Chand et al. (2012); Tsunogaya et al. (2016) provides evidence that cultural variables are likely to influence auditors' preference for judgment. In these studies, however, culture is considered to be very “broad” and few of

these studies “unpack the black box of culture” to identify the various components and dimensions which are likely to influence judgments (Patel, 2006). To contribute to cultural research on auditors’ judgment, this study invokes the concept of Islamic religiosity to provide sharper insights into cultural influences in an Islamic context.

Unlike earlier research which utilises simplistic proxies of religiosity (e.g., church attendance and audit office location) in investigating auditors’ judgments (McGuire et al., 2011; Omer et al., 2016), this study adopts a more sophisticated measure of Islamic religiosity, namely the MPRI framework and its two components, Islamic worldview and religious personality (Krauss et al., 2005), to investigate their influence on audit judgment. Given the fundamental differences (as illustrated in Figure 2.1) between the nature of these two constructs, and in contrast to prior studies, this study predicts and provides evidence of their differential impact on auditors’ preference for more or less judgment. Specifically, the results provide evidence that auditors who score high on overall Islamic religiosity and Islamic worldview have a preference for more judgment. Auditors’ religious personality score, however, has no impact on auditors’ preference for less judgment. Also, the study provides a number of unexpected findings, including that participating auditors appear to accept client-provided information (i.e., a source credibility issue) and exhibit an inappropriately low level of professional scepticism and conservatism in their suggested audit adjustments.

Prior research suggests that the rules-based and prescriptive nature of Islam has a significant influence on accounting standard setting and implementation (Haque & Gardezi, 1991; Ahmed, 2011; SBP, 2014; ICAP, 2015; Shahzad, Ehsan, & Saeed, 2016). However, unlike these prior studies, the results of this study do not support the general assumptions of many Muslim scholars who view Islam as a rules-based resource rather than a dynamic and fluid source of knowledge (Usmani, 2004; Mashhour, 2005; Farooq, 2011). By providing empirical evidence that Islamic religiosity and Islamic



worldview influence auditors' preference for judgment, this research contests these assumptions in a professional context.

The findings of this study offer a number of important contributions. First, the findings are likely to interest global standard setters such as the International Federation of Accountants (IFAC) and more specifically the IAASB, and their calls for more research to investigate the influence of cultural variables on auditing judgments in Islamic countries (IFAC, 2014a). Additionally, the findings are relevant for regional standard-setting bodies such as the Accounting and Auditing Organization for Islamic Financial Institution (AAOIFI) and the Asian-Oceanian Standard-Setters Group (AOSSG) who are aiming to facilitate the emerging Islamic convergence (AOSSG, 2011, 2014), that is, efforts by global and Islamic standard setters to identify and address the potential influence of Islamic values on the convergence of IFRS and ISAs in Islamic countries (Askari, Iqbal, & Mirakhor, 2010).

Second, the recently published Framework for Audit Quality (IFAC, 2014b) by the IAASB highlights that “national culture” is likely to have a direct effect on the judgments of accountants and auditors involved in financial reporting (IFAC, 2014b, p. 60). By “unpacking culture” into a stronger and sharper variable, namely, Islamic religiosity, this study provides evidence of the importance of Islamic religiosity in understanding auditors' judgments in Islamic countries.

Third, the findings of this study are particularly relevant for multinational auditing firms operating in Islamic countries and also for those firms that employ a significant number of Muslims. Given the global convergence of auditing standards and the emphasis on the exercise of judgments in the principles-based ISAs, these findings are particularly relevant for global audit firms. Internationally operating audit firms rely heavily on global firm policies and audit methodologies to ensure the consistency of audits across jurisdictions (Bik & Hooghiemstra, 2016). The risk-based audit methodologies embodied in ISAs and practiced by international auditing firms require auditors to

oversee or avoid certain biases in judgment and decision making. The results of this study suggest that judgment biases can exist due to cultural (i.e., religious) influences and auditing firms should consider developing specialized training programs to eradicate such potential biases.

Additionally, global and multinational accounting firms are under increasing pressure to include measurable cultural diversity and gender-based targets in firm composition (Durkin, 2017). In response to the demands of major clients, who will not engage with firms who do not present a culturally diverse management team, global accounting firms are re-structuring to improve their diversity (Taurian, 2017). Thus, the current focus on increasing cultural diversity within accounting firms and the profession makes the findings of this study even more relevant. The findings suggest that understanding Islamic culture will assist multinational auditing firms in considering the potential implications of Islamic religiosity on auditors' judgments and assist them in developing relevant policies and procedures to identify such influences.

Further, given the incorporation of Islamic and *Shariah* accounting and auditing standards within accounting and auditing domains in Islamic countries, prior research suggests that convergence with principles-based auditing practices might remain a challenging issue for both multinationals and local professional accounting firms (Saba, Kibriya, & Kouser, 2015; Alam, Hassan, & Ferdous, 2017).<sup>24</sup> The findings of this study suggest that further examination of accounting and auditing judgment within Islamic countries and Islamic financial institutions is required. Finally, the findings may also interest auditing standard setters and regulators in Pakistan, such as the ICAP and the Securities and Exchange

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<sup>24</sup> The Securities and Exchange Commission of Pakistan additionally requires companies under its purview to comply with Islamic Financial Accounting Standards (IFAS) issued by the Institute of Chartered Accountants of Pakistan (ICAP). Furthermore, the State Bank of Pakistan in its Strategic Plan for Islamic Banking Industry in Pakistan (2014 – 2018) has indicated that it supported the issuance of further Islamic accounting standards (AOSSG, 2015, p. 56).

Commission of Pakistan, in developing relevant training methodologies and tools to understand and eradicate any possible influence of religious or cultural biases on auditors' judgments.

The findings of this study should be considered in the light of its limitations. First, and as with most single-country studies, caution needs to be exercised in generalizing the findings to other countries. Second, an issue in any religiosity study is a reliance on the self-reported responses of the participants and challenges with endogeneity and SDR bias. In this study, a "lie scale" embedded in the MRPI was used to mitigate SDR bias (Krauss, 2011). Third, the study investigates two constructs of Islamic religiosity. However, the nature of Islamic religiosity is very complex, and future research should examine the influence of other multidimensional theoretical constructs of religiosity to provide further insights into auditors' judgments and decision making. Finally, the scenario used in this study may not fully invoke real-world pressures and contexts faced by auditors.

Overall the results of this study suggest that future research may benefit from an examination of auditor judgment-related issues identified in this study. First, a majority of the auditors based their final judgment (on the reduction of the amount of provision for doubtful debt) on unverified information provided by their client. Future studies could examine the influence of a client's Islamic religiosity on auditors' evidence reliability judgments. Second, the results highlight that auditors exhibited an inappropriately low level of professional scepticism and this issue may be further explored. Future research may examine the influence of Islamic religiosity on auditors' professional scepticism. Finally, the results also indicate that auditors exhibited a low level of conservatism, and future research could, therefore, examine auditors' conservatism judgments.

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## Chapter 3

### **Study 2: The influence of clients' religious adherence and gender on auditors' evidence reliability judgments in an Islamic context<sup>25</sup>**

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<sup>25</sup> An earlier version of this paper was presented at the 40<sup>th</sup> Annual Congress of the European Accounting Association (EAA) held on 6–9 May 2017 in Valencia, Spain.

- Adeel, N., Martinov-Bennie, N., and Patel, C. (2017), "Influence of religiosity and gender of the information source on auditors' judgments." 40<sup>th</sup> EAA conference proceedings and program.
- This paper will be submitted to *Auditing: A Journal of Practice and Theory* (an American Accounting Association journal ranked A\* by the ABCD).

## **The influence of clients' religious adherence and gender on auditors' evidence reliability judgments in an Islamic context**

### **Abstract**

This study contributes to auditor's judgment research by investigating the influence of clients' religious adherence and gender on auditors' evidence reliability judgments. Pakistan, this study's proxy for Islamic countries, is an appropriate context given that both religious adherence and gender are important in its social context. A 2x2 between-subjects experiment involving client-provided information and two independent variables, namely, client's religious adherence level (high vs low) and client's gender (male vs female) was administered to 97 professional auditors from Big 4 auditing firms. The results suggest that, on average, audit evidence provided by a client with high religious adherence is considered by auditors to be more reliable, but the gender of the client has no significant influence on auditors' evidence reliability judgments. Additional interaction analysis shows that, when the client's religious adherence is high, auditors consider the evidence to be highly reliable irrespective of the client's gender. However, when the client's religious adherence is low, the gender effect becomes significant. Overall the results of this study provide evidence that clients' religious adherence and gender are relevant within the context of audit evidence reliability judgments in Islamic countries. The findings have implications for standard setters, global audit firms, and audit professionals, specifically those operating in Islamic countries.

**Keywords:** Audit evidence reliability judgments; client's religious adherence; client's gender; International Standards on Auditing (ISAs)



### 3.1 Introduction

This paper contributes to the literature on auditors' judgment by investigating the influence of the client's (the chief financial officer, CFO) Islamic religious adherence and gender on audit evidence reliability judgments. "Religious adherence" is defined as the degree to which an individual adheres to the values, beliefs, and practices promulgated by religion; it plays a major role in individual decision making (Weaver & Agle, 2002; Vitell & Paolillo, 2003; Shukor & Jamal, 2013; Leventis et al., 2018). A number of studies provide evidence of the impact of religious adherence on auditors' judgments in an Anglo-American context (Walker et al., 2012; Omer et al., 2016; Leventis et al., 2018). Religious adherence has also been recognized as an integral part of Islamic culture (Esposito, 2016) and prior research shows that individuals who have high religious adherence are socially acceptable and are perceived to be more credible within an Islamic cultural context (Johansson-Stenman, Mahmud, & Martinsson, 2009; Jamshidi & Hussin, 2016). Moreover, views expressed by religious individuals are considered to be more reliable in the cultural context of Pakistan (Maron, 1957; Baqai, 1975; Delavande & Zafar, 2011; Sohaib & Kang, 2014). This study examines the influence of clients' Islamic religious adherence on auditors' assessments of the reliability of the audit evidence received from the client.

Audit evidence is defined as the "information used by the auditor in arriving at the conclusions on which auditor's opinion is based" (IAASB, 2012a, p. 382). Audit evidence consists of information that supports and corroborates management's assertions regarding financial statements or internal controls over financial reporting (PCAOB, 2016, p. 105). Auditing standards and pronouncements, including ISA 500 *Audit Evidence* and ISA 330 *Auditors' Response to Assessed Risk* issued by the IAASB (IAASB, 2012a, 2012d), require auditors to assess the reliability of the audit evidence, including information received from clients.<sup>26</sup>

ISA 500 (para. A1) requires that audit judgments are based on sufficient and appropriate audit evidence. Sufficiency is a measure of the quantity and appropriateness is the measure of the quality,

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<sup>26</sup> According to ISA 500, audit evidence obtained from a knowledgeable source that is independent of the company is more reliable than evidence obtained only from internal company sources. The reliability of information generated internally by the company is increased when the company's controls over that information are effective. Evidence obtained directly by the auditor is more reliable than evidence obtained indirectly. Evidence provided by original documents is more reliable than evidence provided by photocopies or facsimiles, or documents that have been filmed, digitized, or otherwise converted into electronic form, the reliability of which depends on the controls over the conversion and maintenance of those documents. The standards further emphasise that verbal audit information received from the client is not sufficient and needs to be corroborated by other evidence (IAASB, 2012d).

which refers to relevance and reliability of the audit evidence received (IAASB, 2012d, p. 384). The reliability of audit evidence is influenced by the source and nature of the evidence and the circumstances in which it is obtained (IAASB, 2012a, p. 389; PCAOB, 2016, p. 106). Since the persuasiveness or quality of audit evidence depends on the reliability of its source, audit evidence reliability judgments are an important area of audit inquiry (Gronewold, 2006; Missah, 2008). Additionally, auditors' evaluations of audit evidence have consequences for audit quality (Bhattacharjee, Moreno, & Riley, 2012; Cefaratti & Bhattacharjee, 2013; Maksymov, 2015).

Audit evidence reliability judgments have been examined with regard to a number of client-related factors, namely, competence (Rebele et al., 1988; Hirst, 1994; Anderson & Koonce, 1994); objectivity (Hirst, 1994; Reimers & Fennema, 1999) and integrity (Goodwin, 1999; Zakari & Ahmad, 2014). Other studies have focused on the impact of audit firm-related factors on audit evidence reliability judgments, such as expert judgments within the audit team (Bamber, 1983), auditors' specialist qualifications (Griffith, 2015), and review partner reactions (Ayers & Kaplan, 2003). Prior studies on auditors' evidence reliability judgments have not considered the possible influence of clients' religious adherence on auditors' judgments.

While the literature has acknowledged the role of religious adherence in the corporate governance environment (Parboteeah et al., 2008; Hilary & Hui, 2009; Callen et al., 2011; Gundolf & Filser, 2013; Du et al., 2015), very few studies have addressed this issue in the auditing domain (Sunder, 2005; Alteer et al., 2013; Jha & Chen, 2014; Omer et al., 2016; Jaggi & Lewis, 2017; Leventis et al., 2018). The limited research conducted so far provides strong evidence of the influential role of religious adherence on auditing judgments, such as ethical judgments (Walker et al., 2012; Hickman, 2013; Saat et al., 2016), going concern judgments (Omer et al., 2016), and audit pricing decisions (Jha & Chen, 2014; Leventis et al., 2015; Jaggi & Lewis, 2017).

However, prior research has operationalized religious adherence in two major ways. First, a number of studies have examined religious adherence as a *measured* independent variable, for example, beliefs, rituals, practices, membership, and religious affiliation (Weaver & Agle, 2002; Muhamad, 2009; Hickman, 2013; Saat et al., 2016; Haron, 2016; Alshehri et al., 2016; Sauerwein, 2017). Second, researchers interested in examining religious adherence at the audit firm level have operationalized it by

adopting simplistic and crude variables including: number of sights for religious activities (e.g., churches); religious population as a proportion of total population (Boone et al., 2013); the extent of religious participation within the country where the firm is located (Dyrenge et al., 2012; Callen & Fang, 2015); the geographical proximity of audit offices within religious and non-religious areas (McGuire et al., 2011; Omer et al., 2016); and a single-item measure of religiosity based on church attendance (Walker et al., 2012).

This study extends prior research by adopting a more nuanced approach. It examines the religious adherence of the client as a *manipulated* independent variable and examines its impact on auditors' evidence reliability judgments. By doing so, the study differs significantly from previous research in a number of ways. Jaggi and Lewis (2017) suggest that local religiosity has a significant impact on auditors' risk and trust behaviour, and show that high religiosity enhances mutual trust among auditors and managers, which encourages auditors to recognize information prepared by managers operating in high religiosity areas as more reliable. This study extends this relationship of trust and religiosity in auditor-client interactions and investigates whether auditors are more likely to trust the evidence received from clients with high than low religious adherence. While Omer et al. (2016) examine the influence of local religiosity on the propensity of auditors to issue a going concern judgment, and Jha and Chen (2014) and Leventis et al. (2018) focus on the impact of religious adherence on audit pricing, this study specifically investigates auditors' evidence reliability judgments, which is an important but different area of inquiry.

The study also examines the influence of clients' (CFOs) gender on auditors' judgments of audit evidence reliability. Pakistan was considered an appropriate context for this research as both religious adherence and gender are sensitive and important factors in the country's Islamic culture (Afzal-Khan, 2007; Delavande & Zafar, 2013). With its patriarchal society and gender-based social system, gender discrimination is evident in both personal and professional contexts in Pakistan (Bhattacharya, 2014) and thus the gender of clients is likely to be an important consideration for auditors. Specifically, in relation to the assessment of audit evidence reliability, this study suggests that auditors are less likely to question the reliability of audit evidence received from a male client (CFO) compared to that received from a female client (CFO).

A 2x2 between-subjects experiment was conducted with 97 professional auditors working in the Big 4 auditing firms in Pakistan. The results of the main effect provide support that audit evidence received by a client with high religious adherence is considered by auditors to be more reliable but do not provide support that audit evidence provided by a male client is considered by auditors to be more reliable than evidence provided by a female client. The results of the interaction also show that when clients' religious adherence level is high, auditors consider the reliability of audit evidence to be high irrespective of the gender of the client. However, when the religious adherence level of the client is low, the gender effect becomes significant, and auditors consider audit evidence received by a male client to be more reliable than that received from a female client.

The results of the study contribute to the current literature in a number of ways. The primary contribution is the finding that the level of Islamic religious adherence has an impact on auditors' evidence reliability judgments. While previous literature has primarily focused on client-related and audit firm-level factors (Bhattacharjee et al., 2012; Cefaratti & Bhattacharjee, 2013; Zakari & Ahmad, 2014), this research extends prior literature by bringing forward a non-organizational factor, namely, religious adherence, which is related to the broader social and cultural context and lies beyond management control. Second, although the results of this study provide non-significant results for client gender on auditors' evidence reliability judgments, under the low religious adherence treatment, auditors do consider evidence provided by a male client to be more reliable than evidence provided by a female client.

Additional analysis indicates that although the level of clients' religious adherence is a significant factor in auditors' evidence reliability judgments, it does not significantly impact auditors' follow-up judgments regarding the likelihood of an adjustment to clients' provision for doubtful debt. However, overall, auditors recommended a relatively high reduction (on average PKR 490 (AUD 5.76) million in the provision for doubtful debt balance, which is of concern. The results suggest that auditors not only trust the information provided by the client but more importantly are willing to materially<sup>27</sup> reduce the provision for doubtful debt judgment based on insufficient evidence of low reliability (i.e., internal verbal evidence with any corroborating evidence). The results suggest that auditors exhibit an

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<sup>27</sup> Materiality specified for the client in the research instrument is PKR 500 (AUD 5.6) million.

inappropriately low level of professional scepticism and conservatism in their judgments and are not complying with the specific principles of ISA 500. These results suggest that there are religious and cultural biases in auditors' judgments and non-compliance with ISAs. Given the familiarity of auditors with ISAs, exposure to risk-based audit methodologies, and an emphasis on professionalism within the Big 4 firms, the results of this study are unexpected and suggest that further studies are needed to examine these variables in detail. Therefore, auditors' professional scepticism and conservatism in an Islamic context is an area worth investigating in future research.

The remainder of the paper is organized as follows. Section 3.2 details the literature review and hypotheses, section 3.3 presents the research method, section 3.4 details the results, and section 3.5 concludes the study.

### **3.2 Literature review and hypotheses development**

#### ***3.2.1 Audit evidence reliability***

One important source of audit evidence is the information received from clients during the audit process (Bhattacharjee et al., 2012). Auditors' judgments of audit evidence reliability are important because the inferential value of the audit evidence must always be considered in light of its source (Hirst, 1994). Source reliability refers to the degree to which a person believes a source has provided accurate and unbiased information, and it increases with source expertise and objectivity (Birnbaum & Stegner, 1979; Xu, 2014). Given the application of risk-based audit methodologies, according to International Standard on Auditing 330 and 500<sup>28</sup> (IAASB, 2012a, p. 383), there is an increased focus on auditors' responsibility to obtain sufficient and appropriate audit evidence (IAASB, 2012d, p. 344). Sufficiency is a measure of the quantity of the audit evidence and appropriateness is the measure of the quality, which refers to the relevance and reliability of the audit evidence obtained during the audit. The reliability of audit evidence is assessed according to the nature of the source. Hirst (1994) provides evidence that audit evidence reliability is integral to audit judgment because auditors must evaluate audit

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<sup>28</sup> According to ISA 330, the auditor needs to evaluate the sufficiency and appropriateness of the audit evidence received. The auditor's judgment as to what constitutes sufficient appropriate audit evidence is influenced by the "source and reliability of the available information" (paras 25–27, A62). Also according to ISA 500, the auditor needs to evaluate the relevance and reliability of the information to be used as audit evidence objectively if the source is management (paras A1–25) (IAASB, 2012f).

evidence in light of its source. Thus auditors' audit evidence reliability judgments is an important area for investigation.

A number of studies have addressed audit evidence reliability in the Anglo-American context (Joyce & Biddle, 1981; Bamber, 1983; Hirst, 1994; Anderson & Koonce, 1994; Reimers & Fennema, 1999; Anderson, Kadous, & Koonce, 2004; Kaplan, O'Donnell, & Arel, 2008; Liu, 2012; Cefaratti & Bhattacharjee, 2013; Griffith, 2014). A review of the literature suggests that prior research focuses on the characteristics of audit evidence reliability, namely, the competence, objectivity, and integrity of the information source (Bhattacharjee et al., 2012; Cefaratti & Bhattacharjee, 2013).

Findings suggest that auditors are sensitive to source competence and place more weight on competent sources of information in evaluating the reliability of audit evidence (Bamber, 1983; Anderson & Koonce, 1994; Hirst, 1994; Zakari & Ahmad, 2014; Maksymov, 2015; Sonnier, Lassar, & Lassar, 2015; Griffith, 2015). A number of studies investigate the objectivity component of auditors' source reliability judgments. Anderson et al. (2004) suggest that auditors are sensitive to the objectivity of the source and consider evidence from a fellow auditor to be more objective than evidence from client management. Zakari and Ahmad (2014) provide evidence that the source of audit evidence has a direct impact on audit quality in Libya. For example, they suggest that external sources of evidence are considered more reliable than internal sources. Evidence from previous audits, other audit team members, and fellow auditors is also considered more reliable, as is evidence obtained from accounting systems. A number of studies also suggest that management integrity is related to preliminary risk assessments, and to the persuasiveness, timing, and extent of planned audit procedures, and has a direct influence on auditors' evaluation of source credibility (Kizirian, Mayhew, & Sneathen Jr, 2005). A higher level of management integrity is likely to increase the reliability of the information received from management (Peecher, 1996; Goodwin, 1999; Maksymov, 2015).

Bhattacharjee et al. (2012) provide evidence that interpersonal effect or likability of the client leads to positive or negative mood effects and eventually influences auditors' evidence reliability judgments. In general, prior research on audit evidence reliability concludes that with regard to compliance with auditing standards, auditors are more reliant on information received from more competent, objective sources, and those with higher integrity (Kaplan et al., 2008; Maksymov, 2015).

While auditing research has examined how client characteristics can influence auditors' evidence reliability judgments (e.g., Bhattacharjee et al., 2012; Cefaratti and Bhattacharjee, 2013; Kaplan *et al.*, 2008) relatively little auditing research to date has examined culture-specific client characteristics that are relevant for auditors' evidence reliability assessments. Prior research on audit evidence reliability judgment in Anglo-American cultures suggests that auditors' identification with their client is a sensitive issue and it reduces auditors' objectivity in such a way that an identifying auditor tends to acquiesce to a client's preferred accounting position (Bamber & Iyer, 2002; Bamber & Iyer, 2007). Svanberg and Öhman (2015) provide evidence that auditors who identify relatively more with their client are more likely to acquiesce to client-preferred treatment. These results suggest that client characteristics, specifically those that impact the level of trust that the auditor has in the client, are important and relevant for an investigation. "Trust" in the information source is strongly associated with the perceived credibility of the source and thus is likely to be relevant for auditors' reliability judgments (Xu, 2014). However, prior research has focused on Anglo-American cultures, with little emphasis on clients' culture-specific characteristics beyond those cultures.

This paper, however, suggests that two culture-specific client characteristics in Islamic culture are relevant for auditors' evidence reliability judgments: religious adherence of the client and gender of the client. Both of these variables have a strong relationship with interpersonal trust, for example, higher religious adherence increases interpersonal trust (Branas-Garza, Rossi, & Zacciver, 2009; Charles, 2010; Sohaib & Kang, 2014) and gender and trust are also interrelated (Inoue, Akutsu, Katsumura, & Yamagishi, 2016).

Specifically, in Islamic cultures, individuals who have a high level of religious adherence are socially more reputable and enjoy greater credibility (Ali & Ushijima, 2005). Similarly, males, compared to females, are considered more reliable in Islamic culture (Afzal-Khan, 2007). Given the importance of religious adherence and gender in the Islamic cultural context, this paper suggests that these two variables are likely to influence auditors' evidence reliability judgments in an auditor–client context. Based on the above discussion three hypotheses are proposed in the following sections.

### ***3.2.2 Religious adherence of the client***

Previous research in the Anglo-American context provides evidence that auditor identification with the client is likely to impact auditors' objectivity in assessing the information received from the client and,

in turn, comprises auditors' objectivity (Bamber & Iyer, 2002; Bamber & Iyer, 2007; Svanberg & Öhman, 2015). Viewing oneself as a member of a particular social group has an immediate consequence for how people perceive, feel, and act towards others (Dovidio, Glick, & Rudman, 2005). Individuals experience more positive affect toward other members of their social group, particularly those who are more prototypical of their group norms (Perdue, Dovidio, Gurtman, & Tyler, 1990). In a religious group, it is expected that individuals assess each other based on their religious affiliations, group membership, and religious adherence levels (Argyle & Beit-Hallahmi, 2014). If individuals have a strong attachment to a particular religion, they tend to have difficulty in objectively evaluating information from members who belong to the same religion (Brewer & Hewstone, 2004).

With a rigid and hierarchical cultural system, Islamic society is socially cohesive and characterized by a strong sense of intergroup unity (Verkuyten, 2007). In Islam, religious adherence is an important aspect of social and cultural integration (Lapidus, 2014). Individuals who show higher religious adherence are more successfully integrated and more respected within the community. Triandis (1992, p. 239) points out that in certain collectivist cultures such as Islamic cultures "one either is or is not a member of the in-group." In Islamic culture, group identification is not so much a matter of degree, and one cannot be more or less identified with a group. Moreover, orientation and commitment to the in-group are normative and compulsory, rather than optional (Verkuyten, 2007). Individuals in Islamic culture thus show a greater sense of duty and obligation towards the interests of the religion (Basabe & Ros, 2005).

Given the social emphasis that is placed on religious adherence in both personal and professional contexts, it is expected that religious adherence within an Islamic culture is positively related to the tendency to favour that group over other groups (Verkuyten, 2007). This social structure gives rise to interdependence and mutual trust within society with religious adherence regarded as an important determinant of trust. Supporting this, experimental research in psychology has also determined that religious individuals are considered more trustworthy by society (Paciotti et al., 2011).

Intergroup trust within social and religious groups in Pakistan is evident and has had a large impact on corporate governance practices (Mirza & Azfa, 2010). Additionally, previous experimental evidence in Pakistan suggests that highly religious individuals are considered more trustworthy in



educational institutions (Delavande & Zafar, 2011). It is also suggested that individuals who exhibit a high level of religious adherence are likely to be more trusted in society (Tan & Vogel, 2008). Within the particular context of auditor–client interaction, it is therefore expected that auditors will be compelled to trust a client who exhibits a high level of religious adherence. As a result, auditors are less likely to question the reliability of the audit evidence received from a client with high religious adherence and will consider it to be more reliable.

In contrast, when the religious adherence level of the client is low, the level of trust that the auditor has in the client is also reduced. Given that, in Islam, specific religious behaviour and norms are compulsory, and the religious scriptures detail strict consequences for not following Islamic injunctions (Rehman, 2010), the social acceptance and credibility of an individual is considerably decreased if they do not exhibit religious adherence (Anjum, 2011). Additionally, individuals might experience extreme social exclusion and isolation if they do not show adherence to the Islamic way of life (Miller, 2000). As a result, auditors are more likely to question the reliability of the audit evidence received from a client who exhibits low religious adherence. Thus, based on the above discussion, it is predicted that in an auditor–client context, information received from a client with high religious adherence is considered by auditors to be more reliable compared to information received from a client with low religious adherence. Therefore, the first hypothesis is:

**H1:** Audit evidence provided by a client with high (low) religious adherence is considered by auditors to be more (less) reliable.

### **3.2.3 Gender**

The psychology literature suggests that “gender” reflects a social category, which individuals consider during their information processing and judgment-forming activities (Maccoby, 1988; Wood & Eagly, 2015). Individuals tend to engage in the process of “stereotyping” other people in groups of easily recognized members (Bodenhausen, Macrae, & Sherman, 2016). Stereotyping helps individuals to facilitate decision making. Once a person has been stereotyped as a member of a particular social category, for example, male or female, decision makers often make biased assumptions about the target person’s behaviours, skills, and capabilities (Haines, Deaux, & Lofaro, 2016).

Further, gender acts as a primary cultural framework that people rely on to initiate the process of making sense of one another to organize social relations (Ridgeway, 2009; Mark, 2017). Individuals tend to use gender stereotyping to create a gender-based social system of differences and inequality (Ridgeway, 2009, p. 189). In the workplace and home, women's expected competence and authority compared to that of men, in turn, contributes to the sex-segregation of jobs, a gender gap in wages and authority, and an unequal household division of labour (Mark, 2017). For instance, most individuals tend to associate the male gender with greater overall ability in a professional context (Wilson, 2017). Additionally, some management research shows that individuals perceive male managers to possess high managerial abilities and expect female managers to lack the necessary qualities for managerial success (Schein, 2001). Further, an individual's receptiveness to influence or persuasion is also influenced by gender stereotyping. Research suggests that people tend to agree with male opinions to a greater extent than they do to those of women (Baron-Cohen, 2002) particularly in domains that are stereotypically masculine, such as management and public accounting (Gardiner & Tiggemann, 1999; Brody, Cox, & Kern, 2016).

A number of researchers have investigated the influence of gender in accounting firms (Lee Cooke & Xiao, 2014; Francis, Hasan, Park, & Wu, 2015; Ho, Li, Tam, & Zhang, 2015; Adapa, Rindfleish, & Sheridan, 2016; Siboni, Sangiorgi, Farneti, & De Villiers, 2016; Petersen, 2016; Haynes, 2017). Prior research provides evidence that there are significant differences between the judgments of male and female accountants, specifically in relation to risk assessment (Chung & Monroe, 2001), information processing (Graham, Stendardi Jr, Myers, & Graham, 2002), ethical decision making (Albaum & Peterson, 2006; Keller, Smith, & Smith, 2007; Ballantine & McCourt, 2011; Bobek, Hageman, & Radtke, 2015), and investment strategies (Graham et al., 2002).

Further, accounting has been accused of reinforcing or sustaining relationships between individuals in the auditing profession along "gendered lines" (Haynes, 2017, p. 110). Researchers posit that organizational culture in international auditing firms mostly favours "masculine characteristics," with both male and female auditors rejecting feminine stereotypes and adopting masculine stereotypes as a condition of moving up the corporate hierarchy (Maupin & Lehman, 1994). Specifically, a number of studies provide evidence of gender stereotyping and discrimination in public accounting firms

(Komori, 2008; Thiruvadi, 2012; Hardies, Breesch, & Branson, 2013; Dalton, Cohen, Harp, & McMillan, 2014; Lee Cooke & Xiao, 2014; Bobek et al., 2015; Haynes, 2017). However, most prior evidence relates to the gender of the auditor, whereas the current study specifically focuses on the gender of the client.

Auditors interact with a variety of individuals at all management levels within the organization, but a common point of contact for auditors is the company's chief financial officer (CFO). Although there has been a growing gender shift towards female CFOs, male CFOs still predominate. For example, there are only 58 (11.6%) women CFOs among Fortune 500 companies (Wechsler, 2015). Since male CFOs dominate in corporate leadership, the literature on top management decision making suffers from an implicit masculine bias (Ho et al., 2015). Although there is abundant literature on the differences between men and women managers, the influence of CFO gender on auditors' judgments is largely unexplored. This study investigates the influence of the gender of the client (i.e., the CFO) on auditors' audit evidence reliability judgments.

A noteworthy concern in the literature on gender in accounting firms is that research on gender issues is narrowly focused on Anglo-American societies, where the accounting profession is powerful and has "well-established feminist movements" (Komori, 2008, p. 508). The major consequence of this focus is a generalization of the role of women in accounting, which may not hold true in other social contexts (Komori, 2008). Since the identification of behaviour as masculine or feminine is culturally determined, there are likely to be differences in different cultures. In the Islamic world, for example, women occupy a different position within a patriarchal construct (Joseph, 1994). According to Olmsted (2005, p. 71), women in Islamic cultures generally and Arab cultures specifically are cared for under a "family-based social security system." The system implies that women occupy a private space, which is located in the home, and men are guardians of the public space (outside organizations, markets, etc.), which is considered more powerful than the private space (Olmsted, 2005). Women have little or no autonomy in the public space, which has resulted in the extreme marginalization of females in corporate governance and the business sector.

Muslim countries worldwide have issues with gender equality. They dominate the bottom 10 countries in the Global Gender Gap Report, and none of the 10 most successful countries offering equal

opportunities for men and women are Muslim (WEF, 2017). Under a typical patriarchal Islamic cultural system, once a male reaches adulthood, he gains an increased level of control and authority over the female members of the family irrespective of their seniority (Olmsted, 2005). Given that male members of society are considered to be “responsible” for making decisions on behalf of the female members of the family, society expects males to be more reliable than females (Ali et al., 2011; Delavande & Zafar, 2013).

Pakistani society, in particular, is fragmented and polarized along gender and religious lines (Talbot, 2009). There are distinct social and religious forces that define gender roles in Pakistan (Jamal, 2014). Furthermore, several religiously driven discriminatory laws against the female population have aggravated the status of women in Pakistan (Roomi & Parrott, 2008). Economically, it has also been observed that working women in Pakistan do not enjoy the same status and credibility as their male counterparts and women entrepreneurs do not enjoy the same opportunities as men (Aslam & Rawal, 2013; Bhattacharya, 2014). This study focuses on Pakistani society because gender inequality is particularly pronounced in Pakistan and gender issues are deep-rooted (Ali et al., 2011; Delavande & Zafar, 2013). The current status of women in Pakistan provides us with a classic example of a state where the dominant patriarchal set-up has resulted in disadvantaged practices against women in a personal and professional context (Bhattacharya, 2014). Based on the above discussion, this study suggests that in an auditor–client relationship, male CFOs will be considered more reliable than female CFOs and information provided by male CFOs will be considered by auditors to be more reliable. Thus, the second hypothesis proposed in this study is:

**H2:** Audit evidence provided by a male (female) client is considered by auditors to be more (less) reliable.

#### ***3.2.4 Interaction between clients’ religious adherence and gender***

Next, this study examines whether clients’ religious adherence and gender are likely to interact. This hypothesis examines whether there is any influence of an interaction between clients’ religious adherence and gender on auditors’ audit evidence reliability judgments. The review of the religious and accounting literature does not reveal one consistent, directional prediction in this regard. This hypothesis relies solely on earlier propositions from Hypotheses 1 and 2.

Hypothesis 1 indicates that information received from a client with high religious adherence is likely to be more reliable than that received from a client with low religious adherence. Hypothesis 2 indicates that information received from a male client is assessed by auditors to be more reliable than information received from a female client. The interaction hypothesis predicts that these two client attributes, when combined in the experimental treatment, are likely to interact. Given religion and gender are interwoven in the social fabric in Islamic countries (Mashhour, 2005; Essers & Benschop, 2009; Grünenfelder, 2013), this study suggests that audit evidence received from a male client with high religious adherence is considered by auditors to be more reliable than that received from a female client with low religious adherence. The third hypothesis of this study is thus:

**H3:** Client's religious adherence level (high vs low) will interact with gender (male vs female) to increase (decrease) the reliability assessment score.

### **3.3 Research method**

#### **3.3.1 Participants**

Professional auditors<sup>29</sup> working at various levels of seniority in the Big 4 auditing firms in Pakistan participated in the experiment. A sample of participants from the Big 4 firms was selected for examination because audit methodologies adopted by Big 4 firms are in line with ISAs,<sup>30</sup> they exhibit a similar organizational culture to each other, and represent a relatively homogenous Pakistani sample.

Two-hundred and thirty questionnaires were distributed, with 97 usable responses received, giving a response rate of 42%.<sup>31</sup> The majority of the sample consisted of audit seniors (42%) and assistants (39%). Most of the participants (57%) were aged between 20 and 30 years, and 25% were aged between 30 and 40 years. The average audit experience of partners was 10 years, for managers it was nine years, and for audit seniors it was four years. Approximately 88.7% of the participants were practicing members of the ICAP.

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<sup>29</sup> Professional accountants/auditors in Pakistan are members of the Institute of Chartered Accountants of Pakistan (ICAP), have completed all academic and professional Chartered Accountancy requirements, and have a minimum of three years' professional audit/accounting experience (ICAP, 2017a).

<sup>30</sup> Under the Companies Ordinance of 1984, all companies in Pakistan are required to be audited using standards adopted by the ICAP (ICAP, 2017). The ICAP has adopted the 2009 Clarified ISAs as issued by the IAASB and the standards are not translated as English is the official business language of Pakistan. The Audit Oversight Board, which was established in 2016 under the amended Securities and Exchange Commission of Pakistan Act of 1997, oversees the ICAP's work to ensure that auditing standards adopted and issued by the ICAP conform to ISAs as issued by the IAASB (IFAC, 2017).

<sup>31</sup> Recently published examples from audit judgment research show low survey response rates. For example, a response rate of 20.7% in Abbott et al. (2016) and 26% in Mohd Sanusi et al. (2017).

Additionally, 86.7% of participants reported being “somewhat familiar” with ISAs (a mean score of 5.57 on a Likert scale of 1–7, where 1 = very unfamiliar and 7 = very familiar). The overall mean score for auditors’ task-specific experience with provision for doubtful debt judgments was 4.94 on a Likert scale of 1–7, where 1 = no prior experience and 7 = dealt with very often. Both the ISA familiarity scores and the task-specific experience indicate that the participants possessed the requisite knowledge and experience to complete the task.

The sample consisted of 86% males and 14% females, which is consistent with Pakistan’s ranking on the Global Gender Gap Index (WEF, 2017). Pakistan has witnessed persistent gender inequality in the accounting and business professions, and this sample is representative of the existing gender gap in workforce participation. A summary of the demographic information for the participants is provided in Table 3.1.

Table 3.1: Demographics						
Item	N (97)		%			
<i>Gender</i>						
Male	83		85.6			
Female	14		14.4			
<i>Age</i>						
20–30	55		56.7			
30–40	25		25.8			
40–50	15		15.5			
50–60	2		2.0			
<i>Membership</i>						
ICAP (CA/)	86		88.7			
Other professional bodies	11		11.3			
Item	Current position in the firm		Total audit experience Years	Experience at current level Years	Task-specific experience (1–7)*	Familiarity with ISAs (1–7)**
	<i>N (%)</i>		<i>Range (mean)</i>		<i>Mean</i>	
Audit trainee	7	(7.2)	1–2 (1.43)	1–2 (1.43)	2.71	5.37
Assistant	38	(39.2)	1–5 (3.05)	1–5 (2.61)	4.92	5.37
Audit senior	41	(42.3)	2–8 (4.35)	1–8 (4.17)	5.20	5.80
Manager	7	(7.2)	4–15 (8.71)	1–15 (6.57)	5.43	5.49
Partner	4	(4.1)	1–16 (10)	2–16 (9)	5.50	5.50
Total	97	(100)	1–16 (4.18)	1–16 (3.73)	4.94	5.57
* where 1 = no prior experience and 7 = dealt with very often						
** where 1 = very unfamiliar and 7 = very familiar						

### 3.3.2 Research design and procedure

A 2x2 between-subjects experiment was designed and administered to test the hypotheses. The experimental design was selected to provide a strong cause–effect relationship between the variables of interest with higher reliability and internal validity.

Big 4 auditing firms in Pakistan were contacted via email to obtain permission to conduct the experiment in their respective firms. The firms were informed about the ethical approvals and the

voluntary nature of the research. Both the firms' and the individual participants' confidentiality were assured. After the firms agreed to participate and provided an estimate of the number of potential participants, the sealed questionnaire packs were distributed to the assigned contact person at each of the firms. Each questionnaire pack included a cover letter,<sup>32</sup> instructions to participants, and the research instrument (see Appendix C for details). The experiment was conducted during training sessions held at the respective auditing firms. As instructed in the questionnaire pack, the participants placed the completed questionnaires and sealed them in the envelopes provided. The questionnaire packs were then collected from the contact person at each of the firms by the researcher.<sup>33</sup>

### ***3.3.3 Research instrument and variables***

The research instrument consisted of two sections. The first section contained an accounts receivable valuation scenario (i.e., adequacy of a provision for doubtful debt assessment) and dependent variable measures. The second section collected participants' demographic information and responses to three control variables (see research instrument in Appendix C for details).

#### ***The scenario***

This research examines auditors' assessments of the reliability of the audit evidence provided by clients. A doubtful debt judgment task, including client-provided information, which has been tested for reliability and validity in prior research (Reimers & Fennema, 1999; Huang et al., 2002; Anderson & Fleming, 2014), was selected. The reliability of client-provided audit evidence on accounting estimates is a significant contextual factor influencing auditors' judgments because auditors rely to a greater extent on clients' assertions about future events (Griffith, 2015). Also, client-provided information is considered less reliable than evidence collected directly by auditors or from external independent sources (Rennie, Kopp, & Lemon, 2010; IAASB, 2012b, p. 391). According to ISA 500, verbal client-provided evidence is insufficient and needs to be supported/corroborated by other evidence (IAASB, 2012, p. 391). This context provides a "grey area" for audit evidence reliability judgments and thus was selected in this study.

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<sup>32</sup> The cover letter included information about the researchers, institutional affiliation, general aim of the research, information on ethical approvals, and the voluntary nature of the study.

<sup>33</sup> According to the ethical approvals and requirements of the research, the researcher should not come in direct contact with the participants during data collection to minimize coercion; thus the management of the auditing firms administered the survey.

Additionally, the audit judgment scenario utilized by this study involves a considerable level of judgment and is relevant and appropriate to various audit seniority levels. The experiment was administered in English, and the research instrument was extensively pilot-tested to ensure readability and clarity,<sup>34</sup> and relevance to the Pakistani audit context.

Participants evaluated a doubtful debt provisions scenario in a hypothetical company, Nature-Pakistan Limited (Nature), and made a series of related judgments. The scenario provided information about an accounts receivable aging schedule of Nature's provision for doubtful debt, the only outstanding material issue remaining on the audit. The accounts receivable aging schedule summarized the actual balances and predicted provision for doubtful debt based on the average percentages of the balances not collected in prior years. The participants were informed that the client, that is, the CFO of the company, provided the audit team with some further relevant additional information. According to the CFO, the two 120 days overdue accounts totalling PKR 2000 (AUD 23) million, representing 50% of the total estimated doubtful debt provision) were expected to be paid in full by each debtor. In both cases, the delay in payment had been caused by the seasonal payment cycle of these two customers, and payment was expected to be made within a few weeks. Information about the professional experience of the CFO was also provided followed by the experimental manipulation of religious adherence (high vs low) and the gender of the CFO (male vs female).

The CFO provided information to the auditors regarding the overdue debt payments verbally. However, according to ISA 500, "audit evidence in documentary form, whether paper, electronic, or another medium, is more reliable than evidence obtained orally" (e.g., a contemporaneously written record of a meeting is more reliable than a subsequent oral representation of the matters discussed) (IAASB, 2012f, p. 388). Since the reliability of information to be used as audit evidence is influenced by its source and its nature, and the circumstances under which it is obtained, auditors have additional responsibility for verifying any verbal audit evidence by further testing. Thus according to ISA 500, the CFO verbal information was insufficient and of low reliability.

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<sup>34</sup> Extensive pilot-testing to ensure the readability, understanding, and practical relevance of the survey was conducted. Feedback was sought from 13 professional auditors, two accounting professors, and two accounting regulators from Pakistan. Their comments were incorporated into the final version of the questionnaire. Pilot-testing also confirmed that auditors in Pakistan would have no problem in understanding and responding to the survey in English.



### ***Manipulated independent variables***

The religious adherence of the CFO was manipulated as high versus low, and the gender of the CFO was manipulated as male versus female.

The CFO's religious adherence manipulation adopted ensured relevance and appropriateness to the Islamic cultural context and was based on prior literature in an Islamic context (Krauss et al., 2005).<sup>35</sup> In the high religious adherence treatment of the CFO, the participants were informed that the *CFO strictly follows the Quran and Sunnah in matters of personal and professional life*. In contrast, that is, in the low religious adherence treatment, the participants were informed that the *CFO prefers to use his/her judgment rather than the Quran and Sunnah*. Following the *Quran* and *Sunnah* in one's personal and professional life is regarded as an indication of high religious adherence in Islamic culture (Krauss et al., 2005).

Consistent with prior audit judgment literature, this study adopted the Goldberg experimental paradigm for manipulating the gender of the CFO (Goldberg, 1968; Chung & Monroe, 2001; Bobek et al., 2015; Little, 2016). In the male experimental treatment, the name of the CFO was male, and the title used was "Mr". For the female experimental treatment the name of the CFO was female, and the title used was "Mrs".

There were four versions of the research instrument: (i) male CFO with high religious adherence; (ii) female CFO with high religious adherence; (iii) male CFO with low religious adherence; and (iv) female CFO with low religious adherence. The four versions of the research instrument were distributed randomly to the participants.

### ***Manipulation check***

To assess the effectiveness of the experimental manipulation of the religious adherence of the CFO, a manipulation check question was added in the second part of the research instrument. Participants indicated "how religious they perceived the CFO (Mr or Mrs) to be" on a Likert scale from 1–7, with 1 = not at all religious and 7 = very religious. The results from this item were used to assess whether the experimental manipulation was successful or not.

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<sup>35</sup> Krauss et al. (2005) provide a number of items that measure the level of religious influences, including following the *Quran* and *Sunnah* in professional and personal matters, and this was adopted as an indication of the CFO's higher religious level in this experiment.

### ***Control variables***

In an experimental setting, factors other than the main independent variables that could affect the outcome of the experiment should be controlled. Control variables help to eliminate alternative explanations for the results. Three control variables were measured in this study: (i) auditors' perceived level of risk regarding the collectibility of debtors; (ii) auditors' experience (general audit experience and task-specific experience); and (iii) auditors' familiarity with ISAs.

First, auditors' perceived level of risk regarding the collectibility of debtors was selected for examination as a control variable because previous evidence shows that auditors' risk perceptions influence auditors' judgments in a variety of contexts (Chen, Huang, & Barnes, 2007; Hogan & Wilkins, 2008; Johnson, Kuhn Jr, Apostolou, & Hassell, 2012). This control variable allowed the researcher to investigate whether auditors' risk perceptions also influence auditors' evidence reliability judgments.

Second, prior research provides evidence that auditors' experience is likely to influence their judgment and decision making (Choo & Trotman, 1991; Moroney & Carey, 2011). This study measured auditors' total audit experience (in years) as well as their task-specific experience with doubtful debt provision judgments (i.e., the number of times they were exposed to a judgment task). Participants rated their experience with doubtful debt provisions on a Likert scale from 1–7 (where 1 = no prior experience and 7 = dealt with very often).

Third, prior studies have shown that auditors' familiarity with ISAs is an important factor and is likely to influence auditors' judgment and decision making (Chand et al., 2010). This study measures auditors' familiarity with ISAs on a Likert scale from 1–7 (where 1 = very unfamiliar and 7 = very familiar).

A number of demographic variables were also included in the second section of the research instrument, including participants' age, gender, professional membership, and current position in their auditing firm.

### ***Dependent variables***

After participants read the research instrument, they were required to make a series of related judgments about the provision for doubtful debt. In the first judgment, participants rated the reliability of the audit

evidence by indicating how reliable they considered the information provided by the CFO to be on a Likert scale from 1–7, where 1 = very unreliable and 7 = very reliable. This measure represents auditors' evidence reliability judgment and is used as the main dependent variable throughout the analysis.

Participants also rated the likelihood of revising the provision for doubtful debt on a Likert scale from 1–7 and the likelihood of reducing the total amount of doubtful debt provision being considered on a Likert scale from 1–7. In their fourth and final judgment, participants were asked to recommend an adjustment, if any, to the amount of provision for doubtful debt. Participants responded on a seven-point scale ranging from PKR 0–1200 (AUD 0–13.8) million<sup>36</sup> with the scale points increasing in PKR 200 (AUD 2.3) million increments.

### **3.4 Results**

#### **3.4.1 Descriptive statistics**

Table 3.2 summarizes the descriptive statistics for the independent and dependent variables. Data were checked for normality, and no significant issues were identified. Gender, age, professional membership, and participants' current position in their audit firm were also tested for significance, and no significant results for participants' evidence reliability judgments were identified.

Forty-eight participants received the high religious adherence treatment, and 49 received the low religious adherence treatment. Forty-one participants received the male treatment, and 56 received the female treatment.

The mean score of auditors' audit evidence reliability judgments, the main dependent variable, is 4.30 on a Likert scale from 1–7, where 1 = not at all reliable and 7 = very reliable. The mean score for auditors' likelihood of revising the CFO's provision for doubtful debt and the likelihood of reducing the total amount being considered is 3.72 and 3.91 respectively. The results suggest that, overall, auditors perceive a moderate level of risk about the collectibility of the debtors (mean of 4.77 on a Likert scale of 1–7, where 1 = very low and 7 = very high). The average reduction in the amount of provision in auditors' opinion is PKR 487.63 (AUD 5.64) million.

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<sup>36</sup> PKR stands for Pakistan rupee. All number values in the questionnaire are reported in PKR (PKR 80 = AUD 1).

**Table 3.2: Descriptive statistics for independent and dependent variables**

<b><i>Independent variables</i></b>	N
High religious adherence of the CFO	48
Low religious adherence of the CFO	49
Male CFO	41
Female CFO	56
<b><i>Dependent variable</i></b>	
Reliability of the information by CFO (1 = very unreliable to 7 = very reliable)	4.03 (1.131)
<b><i>Auditors' intermediate and final judgments</i></b>	
Likelihood of revising the CFO's provision for doubtful debt (1 = very unlikely to 7 = very likely)	3.72 (1.76)
Likelihood of reducing the total amount being considered (1 = very unlikely to 7 = very likely)	3.91 (1.84)
Amount of the provision to be reduced by in auditors' opinion (PKR 0–1200 million)	487.63 (429.452)
<b><i>Control variables</i></b>	
Perceived level of risk regarding the collectability of debtors (1 = very low to 7 = very high)	4.77 (1.24)

### 3.4.2 Manipulation check

To assess the effectiveness of the experimental manipulation, a manipulation check was included in part two of the research instrument. The participants were asked to rate whether they perceived the CFO's religious adherence to be high or low on a Likert scale from 1–7 (where 1 = not at all religious and 7 = highly religious). The results show that 93% of the participants responded correctly to their experimental condition.<sup>37</sup> The mean score for the low religious adherence treatment is 3.62 (SD = 1.63, n = 49) which is significantly ( $p = .001$ ) lower than the mean score of 5.01 (SD = 1.47, n = 48) for the group who received the high religious adherence treatment. The results indicate that manipulation of the CFO's religious adherence was successful.

### 3.4.3 Hypotheses tests

#### ***Religious adherence of the CFO and auditors' evidence reliability judgments***

Hypothesis 1 predicts that audit evidence provided by a CFO with high religious adherence is considered by auditors to be more reliable. From Panel A, Table 3.3, a 2x2 ANOVA shows a significant main effect with the reliability of information received by a CFO with high religious adherence significantly higher than the reliability of information received from a CFO with low religious adherence ( $F = 5.691$ ,  $p = 0.019$ ). The mean reliability score of (4.33(0.903)) for information received from a CFO with high religious adherence is significantly greater than the mean reliability score of (3.79(1.267)) for

<sup>37</sup> The analysis was repeated excluding the 7% of participants who failed the manipulation test, and the results were consistent with the main results. Thus overall results including all participants are reported in this paper.

information received from a CFO with low religious adherence. The results, therefore, support Hypothesis 1.

**Table 3.3: ANOVA results: Religious adherence and gender of the CFO and auditors' evidence reliability judgments**

<b>Panel A: ANOVA model (dependent variable: reliability of information received by the client)<sup>a</sup></b>				
<b>Source</b>	<b>df</b>	<b>Mean square</b>	<b>F</b>	<b>Sig.</b>
Religious adherence of CFO	1	6.761	5.691	0.019*
Gender of CFO	1	4.085	3.438	0.067
Religious adherence of CFO * Gender of CFO	1	0.765	0.644	0.424
Error	93	1.188		
Total	97			
Total * sig. at $p < 0.05$ R-squared = .101 (Adjusted R-squared = .072)				
<b>Panel B: Descriptive statistics for independent variables and dependent variables</b>				
	<b>Mean reliability score (SD)</b>			
<i>CFO's religious adherence</i>				
Low	3.798(0.157)			
High	4.332(0.160)			
<i>Gender of CFO</i>				
Male	4.273(0.170)			
Female	3.857(0.146)			

#### ***Gender of the CFO and auditors' evidence reliability judgments***

Hypothesis 2 predicts that information provided by a male CFO is considered by auditors to be more reliable than information provided by a female CFO. Panel A, Table 3.3 shows that the main effect of the CFO's gender on auditors' evidence reliability judgments is not significant ( $F = 3.438$ ,  $p = 0.067$ ). Specifically, when the CFO is male, the mean evidence reliability judgment is 4.273 (0.170), which is higher than the mean of 3.857 (0.146) for female CFOs but the difference is not significant. Therefore, Hypothesis 2 is not supported.

#### ***Interaction between gender and religious adherence of CFO and its impact on auditors' evidence reliability judgments***

Hypothesis 3 predicts that there is an interaction between the gender (male vs female) and the religious adherence level (high vs low) of the CFO. Auditors are likely to consider information received from a male CFO with high religious adherence to be more reliable than information received from a female CFO with low religious adherence.

Table 3.4 details the descriptive statistics for the four experimental treatments.<sup>38</sup> They show that the mean (SD) evidence reliability judgment score of (4.45(0.826)) for a male CFO with high religious

<sup>38</sup> Twenty participants received the male CFO with high religious adherence treatment, 28 participants received the female CFO with high religious adherence treatment, 21 participants received the male CFO with low religious adherence treatment, and 28 responded to the female CFO with low religious adherence treatment.

adherence is highest, and the mean is lowest (3.50(1.478)) for a female CFO with low religious adherence. However, in Panel A, Table 3.3, 2x2 ANOVA results show a non-significant interaction between the gender and religious adherence of the CFO ( $F = 0.644$ ,  $p = 0.424$ ). Hypothesis 3 is therefore not supported.

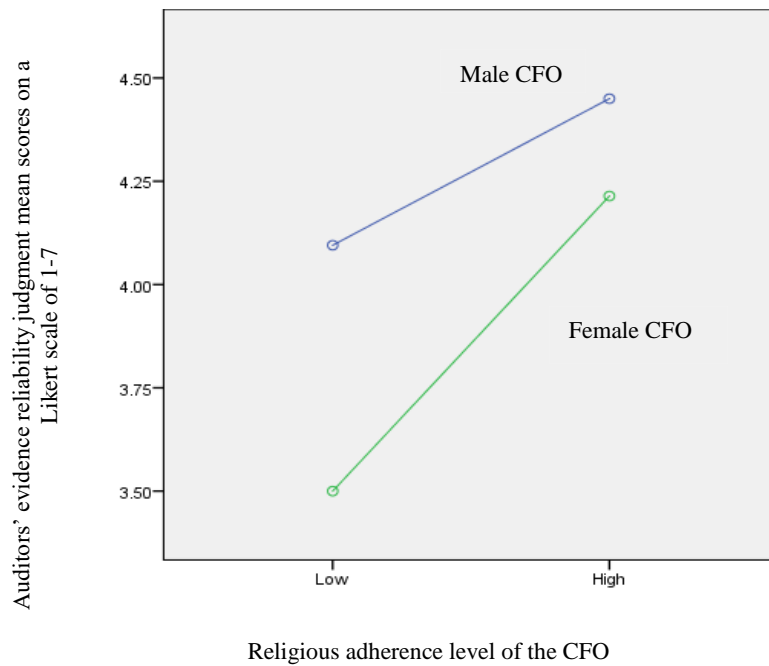
However, in Panel B, Table 3.4, the follow-up univariate tests of the 2x2 ANOVA reported in Table 3.3 reveal a significant main effect of religious adherence of the CFO at each level of the gender variable (male vs female). The results show that there is a statistically significant main effect of religious adherence of the CFO on auditors' evidence reliability judgments for female CFOs only ( $F = 6.013$ ,  $p = 0.016$ ). The results suggest that the mean reliability scores of 4.21 (0.957) for a female CFO with high religious adherence is significantly higher than the mean of 3.50 (1.47) for a female CFO with low religious adherence. The result suggests that auditors are likely to rely more on information provided by CFOs with high religious adherence, especially when the CFO is female.

<b>Table 3.4: Descriptive statistics for independent variables and dependent variables for experimental treatments and follow-up univariate test for the main effect of CFO's religious adherence</b>				
<b>Panel A: Descriptive statistics for independent variables and dependent variables for experimental treatments</b>				
<i>CFO's religious adherence</i>	<i>Gender of CFO</i>	<b>Mean reliability score (SD)</b>	<b>N</b>	
High	Male	4.45 (0.826)	20	
	Female	4.21 (0.957)	28	
Low	Male	4.10 (0.831)	21	
	Female	3.50 (1.478)	28	
<b>Panel B: Follow-up univariate test for the main effect of CFO's religious adherence</b>				
Auditors' audit evidence reliability judgment	<b>df</b>	<b>Mean square</b>	<b>F</b>	<b>Sig.</b>
Main effect of CFO's religious adherence (contrast)				
Male CFO	1	1.289	1.085	0.300
Female CFO	1	7.143	6.013	0.016*
CFO with low religious adherence	1	4.252	3.579	0.062
CFO with high religious adherence	1	0.648	0.546	0.462
<sup>a</sup> The following potential covariates are non-significant ( $p > 0.05$ ): age of participants, gender, current position in audit firm, experience at current level, familiarity with ISAs, task-specific experience of treatment with doubtful debt provisions.				

The results of a 2x2 ANOVA plot in Figure 3.1 depict the interaction between the two manipulated independent variables. An interaction is significant if the effect of the variation in one independent variable differs as a function of the level of the other independent variable (Trotman, 1996). In this particular context auditors' evidence reliability judgment is not only influenced by the religious adherence level of the CFO but also by each level of their gender. The graph shows that the interaction between the religious adherence and gender of the CFO is "ordinal". In an interaction graph, if the lines do not cross and the slope of the lines is not parallel (such as in Figure 3.1), the interactions are "ordinal" interactions (Field, 2013).

Panel A, Table 3.4 shows that information provided by a CFO with high religious adherence is assessed by auditors to be more reliable irrespective of the gender of the CFO, that is, 4.45 (0.826) for males and 4.21 (0.957) for females. However, when the CFO has low religious adherence, the gender effect becomes more important, and auditors rate the information received from a male CFO to be more reliable than that received from a female CFO, that is, 4.10 (0.831) for male CFOs and 3.50 (1.478) for female CFOs. The results suggest that a CFO's religious adherence has a different impact on each level of the gender of the CFO concerning auditors' evidence reliability judgments.

**Figure 3.1: Estimated marginal means for auditors' assessment of audit evidence reliability of the information received from client**



#### 3.4.4 Additional analysis

##### *Auditors' response to intermediate judgments*

In addition to examining the influence of the CFO's gender and religious adherence on auditors' evidence reliability judgments, this study also captures auditors' responses to a number of intermediate judgments including auditors' likelihood of revising the clients' provision for doubtful debt and auditors' likelihood of reducing the total amount.

Table 3.5 shows that auditors' likelihood of revising the clients' provision for doubtful debt is least for the treatment in which the CFO is a male with high religious adherence, that is, 3.25 (0.416). In contrast, the mean likelihood of revising the client's provision is highest in the treatment in which the CFO is a male with low religious adherence, that is, 4.29 (0.332). The mean of auditors' likelihood of reducing the total amount being considered is also high for the treatment in which the religious adherence of a male CFO is very high, that is, 4.29 (0.415).



**Table 3.5: Descriptive statistics for independent variables, intermediate and final judgments, and control variables**

<i>Variables</i>	Religious adherence of CFO		Religious adherence of CFO	
	<b>High</b>		<b>Low</b>	
	Male N = 20	Female N = 28	Male N = 21	Female N = 28
<b><i>Auditors' intermediate and final judgments</i></b>				
Likelihood of revising the client's provision for doubtful debt	3.25 (0.416)	3.71 (0.348)	4.29 (0.332)	3.64 (0.334)
Likelihood of reducing the total amount being considered	3.85 (0.460)	3.86 (0.352)	4.29 (0.415)	3.71 (0.321)
The amount by which the provision should be reduced	575.00 (108.063)	500.79 (0.349)	504.76 (95.238)	400.75 (0.593)
<b><i>Control variable</i></b>				
Perceived level of risk regarding the collectability of debtors	4.55 (0.887)	4.79 (0.254)	4.86 (0.311)	4.86 (0.240)

***Auditors' final judgment on adjustment to the amount of provision for doubtful debt***

The results in Table 3.5 show that auditors' reduction of the provision balance is highest (PKR 575 (AUD 6.69) million) when the CFO is a male with high religious adherence. A higher reduction of the provision indicates that auditors trust the information provided by the CFO and expect that the debtors will repay the amount. The results also suggest that there is some level of interaction between the two manipulated variables.

A summary of 2x2 ANOVA tests for the influence of independent variables on auditors' intermediate and final judgments is provided in Table 3.6. The results indicate that neither the CFO's religious adherence nor their gender significantly influence auditors' likelihood of revising the clients' provision for doubtful debt ( $F = 1.775$ ,  $p = 0.186$ ), the likelihood of reducing the total amount being considered ( $F = 0.146$ ,  $p = 0.704$ ), and the auditors' final judgment of the adjustment amount to the provision for doubtful debt ( $F = 0.920$ ,  $p = 0.340$ ). These results suggest that although auditors consider CFOs' religious adherence to be an important factor in their audit evidence reliability judgments, it is not significant for their intermediate and final judgments on the provision for doubtful debt.

**Table 3.6: 2x2 ANOVA result:**  
**Influence of CFO's religious adherence and gender on control variable, auditors' intermediate and final judgments on provision for doubtful debt**

<b>Control variable</b>	<b>df</b>	<b>Mean square</b>	<b>F-stat</b>	<b>Sig.</b>
<i>Perceived level of risk regarding the collectability of debtors</i>				
Religious adherence of CFO	1	0.848	0.534	0.467
Gender of CFO	1	0.329	0.207	0.650
Religious adherence * Gender of CFO	1	0.329	0.207	0.650
<b>Intermediate and final judgments</b>				
<i>Likelihood of revising the client's provision for doubtful debt</i>				
Religious adherence of CFO	1	5.501	1.775	0.186
Gender of CFO	1	.189	0.061	0.806
Religious adherence * Gender of CFO	1	7.251	2.340	0.129
<i>Likelihood of reducing the total amount being considered</i>				
Religious adherence of CFO	1	.507	0.146	0.704
Gender of CFO	1	1.884	0.541	0.464
Religious adherence * Gender of CFO	1	1.980	0.568	0.453
<i>The amount by which the provision should be reduced</i>				
Religious adherence of CFO	1	171436.955	0.920	0.340
Gender of client	1	191155.265	1.026	0.314
Religious adherence * Gender of CFO	1	5239.772	0.028	0.867

#### ***Auditors' response to control variables***

The results from Table 3.5 show that auditors perceive a moderate level of risk in relation to the collectibility of debtors in CFOs' low religious adherence treatments, irrespective of their gender. For male CFOs with low religious adherence the mean perceived risk is 4.86 (0.311), and for female CFOs with low religious adherence, the mean perceived risk is 4.86 (0.240).

Additional ANCOVA analyses were conducted to test for the influence of the three control variables examined, that is, perceived level of risk regarding the collectability of the debtors, auditors' experience (general audit experience and task-specific experience), and auditors' familiarity with ISAs. The results of 2x2 ANCOVA are presented in Table 3.7. The results are consistent with those obtained for Hypothesis 1, with a significant main effect of high religious adherence of the CFO on auditors' evidence reliability judgments ( $F = 5.786$ ,  $p = 0.018$ ). Additionally, unlike a number of prior audit judgment studies where risk was found to be an important factor, the results show that auditors' perceived level of risk regarding the collectibility of debtors is not a significant factor in this case ( $F = 0.786$ ,  $p = 0.378$ ). This is likely due to the doubtful debt judgment scenario considered by the auditors in this study to be "moderate" and "not very high". Auditors' general audit experience ( $F = 3.176$ ,  $p = 0.078$ ) and task-specific experience ( $F = 0.767$ ,  $p = 0.384$ ) are also insignificant with the only significant

control variable being auditors' familiarity with ISAs ( $F = 6.796$ ,  $p = 0.011$ ). Auditors who scored high on the ISAs familiarity scale rate the reliability of the CFO to be low. The results suggest that auditors who scored higher on the ISA familiarity scale are more compliant with ISAs.

<b>Table 3.7: 2x2 ANCOVA with control variables</b>				
Dependent variable: Auditors' evidence reliability judgment				
<b>Source</b>	<b>df</b>	<b>Mean square</b>	<b>F</b>	<b>Sig.</b>
Religious adherence of CFO	1	6.512	5.786	.018
Gender of CFO	1	2.802	2.489	.118
Religious adherence of CFO * Gender of CFO	1	.393	.349	.556
<b>Control variables</b>				
Perceived level of risk about the collectability of debtors	1	.885	.786	.378
Total audit experience	1	3.574	3.176	.078
Task-specific experience	1	.863	.767	.384
Familiarity with ISAs	1	7.649	6.796	.011
Error	86	1.125		
Total	97			
Corrected total	96			
a. R-squared = .212 (Adjusted R-squared = .121)				

### 3.5 Discussion and conclusions

This study contributes to the audit judgment literature by examining the influence of clients' religious adherence and gender on auditors' evidence reliability judgments in Pakistan. The study adopted a 2x2 between-subjects experimental design and manipulated the religious adherence of the client (high vs low) and the client's gender (male vs female). Previous literature in the Anglo-American context documents how religious adherence is likely to influence corporate behaviour (Hilary & Hui, 2009; McGuire et al., 2011; Leventis et al., 2018) and auditors' judgments (Omer et al., 2016). This study, however, investigated the influence of religious adherence on auditors' evidence reliability judgments.

Pakistan was selected as an appropriate context for this research because religious adherence is an important cultural variable in Pakistani society and higher religious adherence is associated with increased social acceptance and trust. Specifically, this study hypothesized that audit evidence received from a client with high religious adherence is considered by auditors to be more reliable. Additionally, given the patriarchal nature of Pakistani society and its persistent gender discrimination, the study also hypothesized that information received from a male client will be assessed by auditors to be more reliable than information received from a female client. Further, based on the expected interaction between religious adherence and gender in an Islamic cultural context this study also examined the

influence of a possible interaction between the client's religious adherence and gender on auditors' evidence reliability judgments.

The results of the study provide support for the hypothesis that audit evidence received from a client with high religious adherence is considered by auditors to be more reliable. Additionally, the results do not support clients' gender to be significant factor auditors' evidence reliability judgments. This finding contradicts some earlier studies that indicated the existence of gender inequality, discrimination, and organizational gender imbalance in representation in public accounting firms (Abidin, Rashid, & Jusoff, 2009; Kamla, 2012, 2014; Dalton et al., 2014). However, in most of these studies, the primary investigation concerned the gender of the accountant and auditor. This study examined the gender variable in an entirely different context, that is, the gender of the client.

Further, the results of the interaction hypothesis suggest that the gender of the client is a significant factor in audit judgments only under certain circumstances. The results indicate that when the client exhibits low religious adherence, auditors take into account the influence of gender and consider the audit evidence received by the male client to be more reliable than that received from the female client. Overall the results suggest that despite the emphasis Big 4 firms place on professional training and "acculturation" (Jenkins, Deis, Bedard, & Curtis, 2008) increased professionalism and targeted training programs for auditors in Islamic countries may be necessary. This study indicates that it may be important to mitigate potential judgment biases related to culture-specific characteristics of the client, such as religious adherence and gender.

Additional analysis suggests that although the level of clients' religious adherence is a significant factor in auditors' evidence reliability judgments, it does not significantly impact auditors' follow-up judgments regarding the likelihood of an adjustment to clients' provision for doubtful debt. However, overall, auditors recommended material reduction (on average PKR 490 (AUD 5.76) million) to the provision for doubtful debts, which is of concern. The results suggest that auditors not only trust the information provided by the client but more importantly are willing to materially<sup>39</sup> reduce the provision for doubtful debt judgment based on insufficient evidence of very low reliability (i.e., internal

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<sup>39</sup> Materiality specified for the client in the research instrument is PKR 500 (AUD 5.6) million.

verbal evidence without any corroborating evidence). According to ISA 500, auditors need to evaluate the relevance and reliability of the information to be used as audit evidence objectively if the source is management-provided (IAASB, 2012d). The results of this study suggest that auditors were non-compliant in following ISAs and failed to demonstrate the appropriate level of professional scepticism by relying on verbal evidence of the client, regarding revision for doubtful debt. The results indicate that auditors exhibit an inappropriately low level of professional scepticism and conservatism in their judgments and are not complying with the specific principles of ISA 500, resulting in reduced audit quality and potentially materially misstated financial statements. Therefore, auditors' professional scepticism and conservatism in an Islamic context is an area worth investigating in future research.

This study contributes to the literature in a number of ways. First, the findings extend the literature on auditors' information source reliability judgments by investigating the impact of clients' religious adherence and gender in an Islamic cultural context. While prior research on audit evidence reliability has focused on client- and audit firm-related factors (Bamber, 1983; Rebele et al., 1988; Hirst, 1994; Bhattacharjee et al., 2012; Cefaratti & Bhattacharjee, 2013), this study shows that auditors' evidence reliability judgments are significantly driven by an external cultural factor that lies beyond managerial control of the auditing firm and the client. Second, the results of the study provide evidence that in the cultural context of Islamic countries clients' religious adherence is likely to influence the level of trust that auditors place on the evidence received. As the religious adherence level of clients increases, auditors place a higher level of trust (i.e., reliance) on the evidence received from the client. Third, the study also provides evidence of the differential impact of clients' gender in different religious adherence conditions and suggests that it may be an important area for future audit judgment research in an Islamic context.

The implications of this study are important for global audit firms, standard setters, and audit managers in Islamic countries. The study suggests that religious adherence constitutes an essential element of the clients' environment in Islamic countries and this factor requires consideration when designing relevant policies and procedures to mitigate the influence of religious culture biases. Moreover, audit managers in Islamic countries should place more emphasis on the application of professional scepticism and compliance of ISAs within their auditing realms.

The research does, however, have some limitations. This research used clients' religious adherence as a manipulated variable. Future research could adopt a different perspective by measuring clients' and auditors' religious adherence with more sophisticated and validated measures. Further investigation is thus required and could employ alternative tools such as (electronic or mail) surveys and interviews to measure aspects of individual religiosity, that is, beliefs, practices, formal membership, informal affiliation, or rituals. Such approaches might provide additional insights into the relationship between religious adherence and auditors' judgments. Moreover, since this study is restricted to one country, the findings are limited to specific geographical borders and therefore may not be generalizable to other countries. Future researchers could employ cross-country samples to investigate the influence of religious adherence and gender on auditors' judgments.

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## Chapter 4

### **Study 3: The influence of auditors' Islamic religiosity and clients' religious adherence on conservatism in auditors' judgments<sup>40</sup>**

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<sup>40</sup> An earlier version of this paper was accepted for presentation at the 29<sup>th</sup> Asian-Pacific Conference (APC) on International Accounting Issues held on 5–8 November 2017 in Kuala Lumpur, Malaysia.

- The paper will be submitted to *Auditing: A Journal of Practice and Theory* (an American Accounting Association journal ranked A\* by the ABCD).

## **Influence of auditors' Islamic religiosity and clients' religious adherence on the level of conservatism in auditors' judgments**

### **Abstract**

This paper investigates the influence of auditors' Islamic religiosity and clients' religious adherence on the level of conservatism in auditors' judgments. Conservatism in auditors' judgments is defined as auditors' preference for income-decreasing accounting choices and is selected for examination in this research because it is a core cultural value in Islamic societies. Pakistan, this study's proxy for Islamic countries, provides an appropriate national setting because conservatism influences almost all aspects of personal and professional conduct in that country. Islamic religiosity is selected for examination because evidence shows that it is an indicator of increased conservatism in both an accounting and non-accounting context. A valid and reliable Islamic religiosity framework, the Muslim Religiosity Personality Inventory (MRPI), is adopted to measure auditors' Islamic religiosity level. Based on the MRPI framework, Islamic religiosity is categorized into Islamic worldview and religious personality. Islamic worldview encompasses deeply held, core, and enduring Islamic values and beliefs, whereas religious personality represents the external manifestations of religion such as prayer and worship. Islamic influence is operationalized by measuring auditors' Islamic religiosity and manipulating the religious adherence level of the client as high versus low in a 2x2 between-subjects experiment. The results provide support for the hypotheses that high scores on the overall Islamic religiosity scale and the Islamic worldview scale are likely to increase the level of conservatism in auditors' judgments. The results also suggest that auditors' religious personality and clients' religious adherence does not have a significant impact on the level of conservatism in auditors' judgments. The results of the interaction hypothesis show that when auditors' Islamic religiosity is high, the level of conservatism in their judgments is also high, irrespective of the religious adherence of the client. However, when auditors' Islamic religiosity is low, conservatism in their judgment decreases in the presence of a client with high religious adherence. The results of this study contribute to the literature on auditors' conservatism judgments in an Islamic cultural context and are also relevant for auditing firms operating in Islamic countries.

**Keywords:** ISAs, Islamic religiosity, conservatism in auditors' judgments, client's religious adherence

#### **4.1 Introduction**

This paper contributes to the literature on auditing judgments by investigating the influence of an important cultural variable, namely, Islamic religiosity, on the level of conservatism in auditors' judgments. Conservatism in auditors' judgments is important with respect to both audit research and practice (Kim et al., 2003, p. 60) and has been extensively examined in the literature (Devine, 1963; Antle & Nalebuff, 1991; Chen et al., 2015; Chen et al., 2016). Auditors' conservatism refers to a tendency to require a higher degree of verification to recognize good news as gains than to recognize bad news as losses (Basu, 1997, p. 7). Similarly, Kim et al. (2003, p. 327) suggest that auditors' conservatism is a preference for income-decreasing accounting choices. They argue that external auditing acts as an effective deterrent to opportunistic earnings management only when auditors' preferences over accrual choices conflict with managers' preferences. A key point underlying this argument is that auditors' concerns over potential litigation costs motivate them to prefer conservative (or income-decreasing) accounting choices (DeFond & Jiambalvo, 1993; Lys & Watts, 1994). Desai and Chang (2016) suggest that conservatism in auditors' judgments stems from two sources. First, conservatism results from various accounting practices and disclosures which, in general, promote inappropriate recognition of losses and expenses and being more conservative with the timing of recognition of gains and income. Second, auditors continuously face increased litigation risk if they fail to detect incorrect income-increasing items compared to incorrect income-decreasing choices. Desai and Chang (2016) indicate auditors' conservatism judgments are associated with income-increasing items and increase significantly when management is under pressure to inflate earnings.

Conservatism is particularly relevant to Islamic countries and has been identified as a core cultural value that influences all aspects of personal and professional conduct (Hanafi, 2002; Norris & Inglehart, 2012; Tlaiss, 2015). Conservatism is one of the basic foundations of Islamic society, and most religious, anthropological, and political literature supports the notion that Islamic doctrines are based on conservatism (McIntosh & Islam, 2010). Additionally, evidence from studies on Christianity (Chen & Lind, 2005) and Islam (Tanuwidjaja, 2010) shows that higher religiosity is linked to increased conservatism.

Many prior studies have identified culture as an explanatory variable in auditors' judgments and decision making, specifically with reference to the recent convergence of ISAs (Nolder & Riley, 2013;

Heinz, Patel, & Hellmann, 2013; Ying & Patel, 2016; Bik & Hooghiemstra, 2016). However, very few studies have “unpacked the black box of culture” to identify its various components and dimensions, which are likely to influence judgments (Patel, 2006, p. 13). To “unpack” the concept of culture in an Islamic context in this paper, Islamic religiosity is selected as a variable because religiosity provides a sharper focus for auditors’ conservatism compared to the broader cultural variables that have dominated previous research on auditors’ conservatism (Mohamed Yunus et al., 2012; Chen et al., 2015).

Islamic religiosity represents a commitment to the empirical and theoretical fundamentals of Islam through which Muslims fulfil the right of God, protect the rights of others, adhere to the divine decrees, abstain from wrong deeds, and worship (Al-Goaib, 2003). It also refers to the extent of one’s beliefs and level of agreement with Islamic religious doctrines and actual practices, such as prayer and worship (Krauss et al., 2005). Islamic religiosity can be broadly classified into two significant theoretical constructs: “Islamic values” and “Islamic rituals” (Krauss et al., 2005; Ji & Ibrahim, 2007b; Tiliouine & Belgoumidi, 2009; Abou-Youssef et al., 2011). The Muslim Religiosity Personality Inventory (MRPI), a well-validated and extensively used Islamic religiosity framework, is used to measure these constructs (Krauss et al., 2007; Rehman & Shahbaz Shabbir, 2010; Annalakshmi & Abeer, 2011; Othman & Hariri, 2012; El-Bassiouny, 2014). Based on Krauss et al. (2005) framework, “Islamic values” are Islamic worldview and “Islamic rituals” are religious personality. This study suggests that Islamic worldview, which represents deeply held, enduring, stable, core Islamic values, is likely to influence auditors’ judgments while the religious personality construct, which exemplifies rituals, dress code, and appearance, and differs from the core values embedded in Islamic worldview, is not likely to influence auditors’ judgments.

While the literature has acknowledged the role of religiosity in the corporate governance environment (Parboteeah et al., 2008; Hilary & Hui, 2009; Callen et al., 2011; Gundolf & Filser, 2013; Du et al., 2015), very few studies have addressed this issue in the auditing domain (Sunder, 2005; Alteer et al., 2013; Jha & Chen, 2014; Omer et al., 2016; Jaggi & Lewis, 2017; Leventis et al., 2018). The limited research conducted so far provides evidence of the influential role of religiosity on auditing judgments, including ethical judgments (Walker et al., 2012; Hickman, 2013; Saat et al., 2016), going



concern judgments (Omer et al., 2016), and audit pricing decisions (Jha & Chen, 2014; Leventis et al., 2015; Jaggi & Lewis, 2017).

Prior research has operationalized religiosity in two major ways. First, a number of studies have examined religiosity in the context of beliefs, rituals, practices, church membership, and religious affiliation (Weaver & Agle, 2002; Muhamad, 2009; Hickman, 2013; Saat et al., 2016; Haron, 2016; Alshehri et al., 2016; Sauerwein, 2017). Second, studies that have examined religious adherence at the audit firm level adopted simplistic variables, such as number of sites for religious activities (e.g., churches), the religiosity of the population in an area (Boone et al., 2013), the extent of religious participation in the area in which the firm is located (Dyreng et al., 2012; Callen & Fang, 2015), the geographical proximity of audit offices to religious areas (McGuire et al., 2011; Omer et al., 2016), and a single-item measure of religiosity based on church attendance (Walker et al., 2012).

This study extends this prior research by adopting a more nuanced approach and for the first time combines the measured and manipulated independent variables of religiosity in an experimental setting. The current study measures the level of Islamic religiosity (and its two components, Islamic worldview and religious personality) of the auditor and manipulates the religious adherence level<sup>41</sup> of the client in the experimental setting.

“Religious adherence”, which plays a major role in individual decision making, is defined as the degree to which an individual complies with the values, beliefs, and practices promulgated by religion (Weaver & Agle, 2002; Vitell & Paolillo, 2003; Shukor & Jamal, 2013; Leventis et al., 2018). It differs significantly from religiosity, which entails a multidimensional conceptualization including religious beliefs and religious practices. A number of studies provide evidence on the impact of religious adherence on auditors’ judgments in an Anglo-American context (Walker et al., 2012; Omer et al., 2016; Leventis et al., 2018).

Religious adherence is an integral part of Islamic cultures (Esposito, 2016). Prior research shows that individuals who have high religious adherence are likely to receive more social acceptance and

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<sup>41</sup> Clients’ religious adherence was manipulated because research evidence in Chapter 3 of this thesis indicates that clients’ religious adherence has a significant influence on auditors’ audit evidence reliability judgments. Religious adherence relates to compliance with Islamic rituals and is associated with the religious personality construct of the overall Islamic religiosity framework adopted in this research. Specifically, a client’s attendance at daily prayer, which is an important ritual, is used to manipulate clients’ religious adherence as high (client attends daily prayer) versus low (client does not attend daily prayer).

credibility within an Islamic cultural context (Johansson-Stenman et al., 2009; Jamshidi & Hussin, 2016). Furthermore, views expressed by religious individuals are considered to be more reliable in an Islamic context (Maron, 1957; Baqai, 1975; Delavande & Zafar, 2011; Sohaib & Kang, 2014). Thus this research provides a holistic examination of auditors' level of conservatism by incorporating both auditors' Islamic religiosity as well as clients' religious adherence.

Given this thesis has already shown that auditors are inclined to trust information provided by a client who exhibits high religious adherence, this chapter extends the possible influence of a client's religious adherence in a high-risk scenario involving inventory valuation. Also, given the importance of conservatism in the socio-religious context of Pakistan, this study expects an interaction between auditors' Islamic religiosity, clients' religious adherence, and auditors' conservatism. This study is also motivated by the recent findings of the International Forum of Independent Auditor Regulators across some jurisdictions that raise concerns over non-compliance of ISAs and auditors' assessments of audit evidence concerning management-provided information (IFIAR, 2018, p. 10). This study responds to these concerns and further investigates these issues in an Islamic cultural context.

A 2x2 between-subjects experiment involving an inventory write-down scenario was administered to 105 professional auditors<sup>42</sup> working in the Big 4 auditing firms. Pakistan is considered an appropriate context for this study because Islam is the national religion and conservatism is regarded as a core cultural value both in religion and society (Ahmad, 1965; Yeganeh & May 2011). Additionally, a higher religiosity level is linked to a higher level of conservatism in social and political settings (Hassan, 2007).

The MRPI framework was adopted to measure auditors' overall Islamic religiosity, Islamic worldview, and religious personality. Clients' religious adherence was manipulated as high versus low.<sup>43</sup> Three control variables and dependent variables concerned with the write-down of inventory were measured. The hypothesis only predicts a relationship between a high Islamic religiosity score and a

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<sup>42</sup> Professional auditors in Pakistan are members of the Institute of Chartered Accountants of Pakistan (ICAP), have practiced as an Associate accountant for five years or a non-practicing Associate for 10 years, and have completed all requirements of Chartered Accountancy in addition to three years of professional experience (ICAP, 2014).

<sup>43</sup> Clients' religious adherence was manipulated as high versus low because earlier evidence indicates that clients' religiosity significantly influences auditors' audit evidence reliability judgments. Please refer to the Results section of Chapter 3 of this thesis (p. 127) for details.

higher level of conservatism in auditors' judgments. Whether auditors exhibit an appropriate or inappropriate level of conservatism is not addressed by this hypothesis.

The results support the hypothesis that auditors with high overall Islamic religiosity and Islamic worldview exhibit a higher level of conservatism. However, the results do not support the significant influence of auditors' religious personality on the level of conservatism in their judgments. The results of the interaction hypothesis show that when auditors' Islamic religiosity level is high, conservatism in their judgments is also high, irrespective of the religious adherence level of the client. However, when auditors' Islamic religiosity level is low, the level of conservatism in their judgments is decreased in the presence of a client with high religious adherence. Further, the results show that auditors' risk assessments of the inventory write-down issue also significantly influences the level of conservatism in their judgments.

Although the results of this study suggest that auditors who score high on the Islamic religiosity and Islamic worldview scale exhibit a higher level of conservatism in their judgment, the results show that the level of conservatism is inappropriately low, with the resulting inventory balance being, on average, materially overstated for all auditors.

The remainder of the paper is organized as follows. Section 4.2 presents the literature review and background. Section 4.3 discusses the hypotheses development and section 4.4 details the research methodology. Section 4.5 presents the results and section 4.6 concludes the study.

## **4.2 Literature review and background**

This section provides a brief overview of prior research on auditors' conservatism followed by a discussion on reasons for selecting Pakistan as an appropriate context for this study. Additionally, this section also provides further discussion on religiosity, Islamic religiosity, Islamic worldview, and religious personality.

### ***4.2.1 Conservatism in auditors' judgments***

A number of studies have examined conservatism in auditors' judgments in an Anglo-American context (Kim et al., 2003; Lee et al., 2006; DeZoort et al., 2006; Firth et al., 2014; Boyle et al., 2015; Chen et al., 2015; Lennox & Kausar, 2015; Desai & Chang, 2016; Illueca Muñoz et al., 2016). However, most previous research has focused on examining conservatism in auditors' judgments in relation to the firm's

financial information, including timeliness of earnings (Basu, 1997; Basu et al., 2002), earnings forecasts (Lee et al., 2006), financial information quality (Pae, 2010), and earnings management (Kim *et al.*, 2003). Auditors' conservatism in judgments is increased by stronger regulatory sanctions specifically with regard to risky clients (Firth et al., 2014), a high estimated risk of clients' bankruptcy (Lennox & Kausar, 2015), and more accountability pressure (DeZoort et al., 2006). A number of studies have also investigated audit engagement and firm-related factors, including issues in auditor–client negotiations (Antle & Nalebuff, 1991), decreased auditor independence (Lin et al., 2014), and reduced auditor legal liability (Liao & Radhakrishnan, 2015), and found that these variables increase the level of conservatism in auditors' judgments. An increase in auditors' conservatism after specific events, such as prior audit failure in Big 4 firms (Fafatas, 2010), the global financial crisis (Chen et al., 2016), and the collapse of Enron (Cahan & Zhang, 2006; Feldmann & Read, 2010) have also been documented.

A number of studies have investigated the influence of cultural variables on the level of conservatism in auditors' judgments (Askary, 2006; Mohamed Yunos et al., 2012; Kanagaretnam et al., 2013; Salter et al., 2013; Chen et al., 2015; AlAbbad, 2016). Most of these studies uncritically adopt cultural frameworks provided by Hofstede (2001) and Gray (1988) to examine conservatism practices. Chen et al. (2015) provide evidence from China that clients located in high-trust regions are less likely to receive a modified audit opinion, suggesting that client trustworthiness lowers auditors' reporting conservatism. Kanagaretnam et al. (2013) investigated cultural dimensions of individualism and uncertainty avoidance in an international banking industry sample and provide evidence that individualism is negatively related to conservatism and uncertainty avoidance is positively related to conservatism. Additionally, there is also evidence of a positive influence of social and family values on accounting conservatism in family-based firms (Ferramosca & Ghio, 2018). Salter et al. (2013) compared social and accounting values in 22 countries and provide evidence that accounting conservatism is greater in countries with more conservative societal and accounting values. This suggests that social and religious variables are likely to predict conservatism in accounting practices.

Prior research, which has mostly focused on Anglo-American countries, suggests that social norms and local values are likely to increase the level of conservatism in auditors' judgments. However, there is little evidence of this influence within an Islamic cultural context. An exception is Mohamed

Yunos *et al.* (2012), who investigated the influence of two ethnic groups in Malaysia on accounting conservatism.

Most studies conducted in Islamic countries have focused on investigating conservatism in the Islamic banking and finance industry (Awan & Shahzad Bukhari, 2011; Souiden & Rani, 2015; AlAbbad, 2016; Abdelsalam *et al.*, 2016). Islamic banks have strong religious norms and moral accountability constraints and thus adopt more conservative accounting policies (Abdelsalam *et al.*, 2016). Most of these studies provide evidence that consumers who score higher on the Islamic religiosity scales exhibit higher conservatism in their decisions and are more likely to prefer an Islamic bank over a conventional bank.

The current research provides additional insights for understanding auditors' conservatism in an Islamic cultural context by invoking the concept of Islamic religiosity as an independent measured variable. In this regard, it differs from Mohamed Yunos *et al.* (2012) and suggests that the measured Islamic religiosity variable is a sharper variable than ethnicity for examining auditors' judgments.

### ***The selection of Pakistan***

Pakistan came into existence in 1947 on the foundations of an Islamic ideology (Nadvi, 2009). Muslim politicians, scholars, and researchers hold the view that the only rationale behind the formation of Pakistan was to practice a social, economic, and political system based on Islam (Ali, 1988). The preamble of the 1973 Constitution declares Pakistan an Islamic Republic, Islam as the state religion, and states "that all laws will be brought into accordance with the injunctions of Islam as laid down in the holy book (*Quran*) and the Prophetic tradition (*Sunnah*)"<sup>44</sup> (Munir & Saeed, 1975, p. 3; GOP, 2017). The Constitution also upholds that "Muslims shall be enabled to order their lives in the individual and collective spheres by the teaching and requirements of Islam as set out in the Holy book (*Quran*) and the Prophetic tradition (*Sunnah*) (Munir & Saeed, 1975, p. 3)". It is not surprising then that Islam occupies a powerful position in Pakistani society.

Pakistan has seen an ever-increasing rise in the level of individual Islamic religiosity (Rana, 2015). Islamic religiosity not only pervades individuals' personal lives but also impacts organizational and professional conduct (Nadvi, 2009). The wave of Islamization that occurred in the 1980s has

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<sup>44</sup> *Sunnah* are the sayings and deeds of the Prophet Muhammad and are a primary source of Islamic *Shariah*.

embedded several controversial and mandatory Islamic injunctions into the professional and personal lives of the people of Pakistan (Haque & Gardezi, 1991). A number of conservative legal rulings and authoritative opinions regarding personal conduct have been issued by the Council of Islamic Ideology, which reviews laws under Islamic injunctions and advises the legislature on personal, social, and economic matters (CII, 2017).

Some of the manifestations of conservative ideology within Islam include strictly following *Shariah* Law<sup>45</sup> and abiding by the injunctions of the *Quran* and *Sunnah* (Anjum, 2011). Additionally, Muslims have a stern belief in the “day of judgment”, which results in a higher level of conservatism in both social and professional settings (Syed, 2008).

Prior literature in Pakistan provides evidence that Islamic religiosity is a core and prominent cultural value and is likely to influence individual judgments in a variety of contexts (Awan & Shahzad Bukhari, 2011). For example, a higher level of Islamic religiosity is an indicator of Muslim consumers’ halal<sup>46</sup> choices (Ilyas et al., 2011; Yousaf & Malik, 2013; Baig & Baig, 2013), conservative choices in marketing (Baig & Baig, 2013; Yousaf & Malik, 2013), and banking practices (Khattak, 2010; Awan & Shahzad Bukhari, 2011; Butt et al., 2011; Awan & Azhar, 2014). There is also a positive relationship between the level of Islamic religiosity on ethical behaviour in educational organizations (Zafar, 2011), on psychological health (Khan et al., 2013), and on the subjective well-being of patients (Gull & Dawood, 2013).

Recent reports on religiosity levels in Pakistan show that there is an increase in the number of women wearing headscarves in professional settings (Afzal-Khan, 2007; Burke, 2012). There is also evidence of a new wave of Pakistani women belonging to the elite class who are increasingly being drawn to the conservative ideologies of Islam (Burke, 2012). Similarly, Siddiq (2010) investigated the reasons for conservative views and radicalization in youth studying in three elite universities and provided evidence of easily observable multiple layers of conservatism in social, religious, political, and geopolitical arenas. Additionally, views held by religious leaders in rural areas of Pakistan have been

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<sup>45</sup> *Shariah* is Islamic Law and the *Quran* (Holy Scripture) is another source of Islamic Law.

<sup>46</sup> Certain restrictions on diet and consumable goods are prescribed according to Islamic law. Halal refers to permissible items according to Islamic *Shariah*. For example, pork and alcoholic drinks are strictly forbidden and not halal for Muslim consumption. According to the *Quran*, Muslims can only eat the meat of an animal which is halal and has been slaughtered in the prescribed manner as taught by the Prophet.

found to be conservative with regard to reproductive health issues (Ali & Ushijima, 2005). Thus, given the growing influence of Islam and conservatism on personal, professional, and business conduct in Pakistan, the country is considered an appropriate context for this study.

A rapidly growing and emerging market in South Asia, Pakistan adopted ISAs in 2005 (ICAP, 2015). Since then, both national regulators<sup>47</sup> and auditing standard setters<sup>48</sup> have focused on improving audit quality in Pakistan (SECP, 2013; ICAP, 2016b; Ghorri, 2017). The recent adoption of Islamic accounting, auditing, and *Shariah* standards by the ICAP is evidence of the growing influence of Islam on auditing, accounting, and the business environment (GIFR, 2017).<sup>49</sup>

#### **4.2.2 Religiosity**

Religiosity is the degree to which beliefs in specific religious values and ideals are held and practiced by an individual (Minton, 2013). Religiosity is a major cohesive force because its value system is accepted unquestioningly by many members of society (Mokhlis, 2009).

Prior research shows that religious beliefs and practice are related to attitudes towards risk (Noussair, Trautmann, van de Kuilen, & Vellekoop, 2013). A consistent finding of religiosity studies is that individuals who score high on the religiosity scale measure tend to hold traditional or conservative views (Gundolf & Filser, 2013). Therefore, a positive relationship between religiosity is associated with greater levels of risk aversion (Kanagaretnam, Lobo, Wang, & Whalen, 2015). A number of studies show how the level of religiosity and perceptions of risk are likely to influence accounting and auditors' judgments. For example, Hilary and Hui (2009) provide evidence that firms in religious areas have lower risk exposure, lower investment rates, and less growth. Miller and Hoffmann (1995) establish a negative association between religiosity and self-reported attitudes towards risk, and Osoba (2004) reports that individuals characterized by less risky behaviour tend to be more religious.

A number of studies have investigated the influence of religiosity in accounting and auditing in the Anglo-American context (Hilary & Hui, 2009; McGuire et al., 2011; Walker et al., 2012; Hickman, 2013; Jaggi & Xin, 2014; Walker et al., 2015; Omer et al., 2016; Jaggi & Lewis, 2017; Sauerwein, 2017;

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<sup>47</sup> The Securities and Exchange Commission of Pakistan and the State Bank of Pakistan (SBP) are the key regulators of accounting, auditing, and corporate governance mechanisms in Pakistan.

<sup>48</sup> The ICAP is the main body for auditing standard setting and adoption in Pakistan.

<sup>49</sup> For example, a *Shariah*-compliant banking system under the SBP has been created, and facilitates the development of the Islamic banking industry through enabling a legal, regulatory, and *Shariah*-compliant framework and promoting Islamic finance (SBP, 2014).

Bik & Hooghiemstra, 2018), but most of these have used simplistic proxies for measuring religiosity. For example, Hilary and Hui (2009), McGuire et al. (2011), and Jaggi and Lewis (2017) examine religiosity according to the geographical location of audit offices in religious or non-religious areas. In addition, categorization of high and low religiosity areas in most of these studies is based on a single measure of church attendance (Walker et al. (2012) Hilary and Hui (2009). Evidence suggests that an individual measure of religiosity is a better measure and can provide sharper insights into judgments (Tarakeshwar et al., 2003).

### ***Islamic religiosity***

To provide a holistic and comprehensive insight into the influence of Islamic religiosity on auditors' judgments, this section draws on the literature on Islamic religiosity to complement cultural studies in organizational behaviour in accounting, which largely focus on quantified and dimensional approaches (e.g., Hofstede and Bond (1988). Islamic religiosity is the belief that Islam should direct one's social, political, personal, and professional life (Fuller & Kurpershoek, 2013). It also refers to the extent of one's beliefs and level of agreement with Islamic religious doctrines and adherence to actual practices, such as prayer and worship (Krauss et al., 2005). Islamic religiosity is defined as a commitment to the empirical and theoretical fundamentals of the religion (Islam) through which Muslims fulfil the rights of God, protect the rights of others, adhere to the divine decrees, abstain from wrong deeds, and worship (Al-Goaib, 2003).

Islamic religiosity has been used to theoretically examine religious influence in Islamic cultural contexts in previous research (Muhamad, 2009; Souiden & Rani, 2015; Usman, 2016). A number of Islamic scholars have developed similar multidimensional theoretical constructs that comprise Islamic religiosity (Krauss et al., 2005; Ji & Ibrahim, 2007b; Olufadi, 2017). This study uses a different framework of Islamic religiosity, the Muslim Religiosity Personality Inventory (MRPI), adopted from Krauss (2005), which involves examination of a multidimensional measure of religiosity at both the worldview and religious personality levels. It is important to note here that almost all Islamic scholars have divided Islamic religiosity into Islamic values and Islamic rituals, which is consistent with the MRPI framework adopted in this research.

Islamic values and rituals are based on the *Quran*, Islam's holy book, and *Sunnah*, which represents the sayings of the Prophet as reported by others, the deeds of the Prophet as reported by



others, and the opinions of early jurists based on their interpretation of the sources of Islamic law mentioned above (Alsharif et al., 2011). Islamic values and rituals are strongly interrelated since devout Muslims' day-to-day practices and behaviour are guided by the existence of internally held core values; the deeper the belief in these values, the stronger the practice (Koenig & Shohaib, 2014). Thus, by measuring these two separate constructs, this study adds insights into the religiosity measurement in audit judgment research.

### ***Islamic worldview (values)***

Values are the ideological dimensions of religiosity and are constituted by expectations that the religion will hold to certain beliefs (Glock et al., 1965). Values, which are based on experience, are established throughout one's life and tend to be relatively stable (Schwartz & Bilsky, 1987). Values have long been considered an important antecedent of individual behaviour (Glew, 2009). They are a central part of any culture; while the external behavioural part of the culture (symbols and rituals) may change, the "software" of the culture, deep-seated values, remains constant.

Islamic worldview is a "comprehensive conception of the universe and man's relation to it from the Islamic perspective and serves as one's philosophy or outlook of life" (Abdullah & Nadvi, 2011, p. 271). Islamic worldview is a particular philosophy of life, and a specific concept of the world held by individuals who follow the Islamic faith (Abdullah & Nadvi, 2011). Regarded as a central cognitive orientation, Islamic worldview reflects the doctrine of the divine unity of God and ascertains one's level of agreement with basic Islamic values, beliefs, and creed (Krauss et al., 2005, p. 138). Islamic worldview is based on Islamic values and creed,<sup>50</sup> and is focused on the absolute oneness of God and maintaining "God-consciousness" in all aspects of life (Krauss et al., 2005, p. 137). In addition, the concept of the unity of God (*Tawhid*) is the basis upon which Islamic worldview is established (Siddiqi, 1981; Ahmad, 1979; Al-Buraey, 1990; Chapra, 1992).

Prior literature suggests that Islamic worldview is an important religiosity construct and is likely to influence individual judgment and behaviour in almost all areas of inquiry, including historical development (Badawi, 2002), ethical business practices (Rahman, 2003; Choudhury, 2015), and

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<sup>50</sup> The two main sources of Islamic belief and creed are the *Quran* and the authentic prophetic traditions based upon messengers who were sent to guide humanity (including Abraham, Moses, Jesus, and Muhammad). The core Islamic beliefs are based on the six articles of faith and include belief in one God, the angels, the prophets of God, the revealed books of God, the Day of Judgment, and belief in the divine decree (Krauss et al., 2005).

consumer decision making (Arham, 2010; Ilyas et al., 2011; El-Bassiouny, 2014; Ahmad et al., 2015a) as well as corporate governance principles (Asri & Fahmi, 2004; Alam Choudhury & Nurul Alam, 2013).

### ***Religious personality (rituals)***

Rituals are an important form of human expression (Turner, 1973). A ritual is defined as “a sequence of activities involving gestures, words, and objects, performed in a sequestered place, and performed according to set sequence” (Turner, 1973, p. 123). Rituals play a significant role in an individual's emotional well-being, communal harmony, and social integration (Irani & Funk, 1998). Since rituals stem from certain religious frameworks, and can be conventional or socially prescribed, the emphasis on structure, detailed instructions, and guidelines is more evident in ritual practices than it is in other forms of human behaviour (Bloch, 2004; Turner, 2017).

In the present study, Islamic rituals are represented by religious personality, which measures a person's level of commitment to ritualistic behaviour.<sup>51</sup> Religious personality is the means through which an individual expresses his or her religious beliefs and performs rituals and worship motivated by God consciousness. Religious personality is divided into two kinds of worship: special worship (*ibadat*), which is the rituals that reflect one's direct relationship with God (e.g., prayers, fasting, and pilgrimage); and general worship (*muuamlat*), which is religiously guided behaviour towards one's family, fellow human beings, colleagues, animals, the environment, and nature (Krauss et al., 2005). Based on the above discussion, specific hypotheses are developed in the following section.

### **4.3 Hypothesis development**

This section details the five hypotheses examined in this study. Hypothesis 1 examines the influence of auditors' overall Islamic religiosity and its two components, Islamic worldview (Hypothesis 1a) and religious personality (Hypothesis 1b) on the level of conservatism in auditors' judgments. Hypothesis 2 investigates the influence of clients' religious adherence on the level of conservatism in auditors' judgments. Hypothesis 3 examines the possible interaction between clients' religious adherence and auditors' overall Islamic religiosity on the level of conservatism in auditors' judgments.

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<sup>51</sup> A number of Muslim scholars argue that ritualistic behaviour is not a superficial expression of one's prayers and worship, but in fact represents a far deeper and experiential connection with God (Hassan, 2007; Ahmad et al., 2015b). The present research does not contest the importance of rituals in Islamic societies, but suggests that, compared to the Islamic worldview, Islamic rituals (religious personality) are less likely to influence judgments.

#### 4.3.1 *Islamic religiosity and auditors' conservatism*

The development of the hypotheses in this study is based on two strands of literature, namely, Islamic religiosity and conservatism in auditors' judgments.

A consistent finding of religiosity-related studies in Islamic countries shows that individuals who score high on measures of religiosity tend to hold traditional or conservative views (Ji & Ibrahim, 2007a; Hamid, 2013; Gesink, 2014). Evidence shows that in Islamic countries, a higher score on Islamic religiosity results in increased ethical sensitivity among accounting professionals (Muhamad & Ghani, 2006; Abuznaid, 2009; Muhamad, 2009; Alshehri et al., 2016), has a positive influence on accountants' ethical judgments (Abdul-Baki et al., 2013), and has a positive relationship with social responsibility and entrepreneurial judgments in Islamic organizations (Adamu et al., 2011).

There are a number of reasons why high Islamic religiosity is likely to increase the level of conservatism in an Islamic society. First, Islam is rigorously monotheistic, and it provides clear guidelines for the personal, social, and professional lives of followers (Lewis, 2001). Second, there is specific emphasis on strict adherence to the basic pillars of Islam, for example, submitting to the *Quran* and abiding by *Sunnah* (Newman, 2013). Therefore, a prominent religious tradition in Islam is one of "submission" or to "submit completely" (Lewis, 2001) and conservative attitudes towards strictly following Islamic injunctions are evident in Islamic societies (Lapidus, 2002).

This study examines auditors' conservatism in the context of their inventory write-down judgments. Research evidence suggests that conservatism in Islam restricts over-optimistic write-downs and distribution of unearned profits (Khan, 1994; Lewis, 2001; Hameed, Ibrahim, & Rizal, 2005; Napier, 2007). For example, over-optimistic write-downs can lead to an understatement of assets that could be subject to religious levy or *zakat*,<sup>52</sup> and thus Islamic injunctions are likely to restrict and encourage conservatism. Ahmed (1990) considers that by restricting overoptimistic valuations, conservatism in Islamic financial reporting helps to maintain public welfare. Therefore it is expected that auditors with high overall Islamic religiosity scores will take a more conservative approach by recommending a higher write-down of inventory. The hypothesis in this study predicts a relationship between the level of Islamic

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<sup>52</sup> *Zakat* is a form of alms-giving which is one of the five pillars of Islam. *Zakat* is a religious obligation for all Muslims who meet the necessary criteria of wealth. *Zakat* is based on total income, which also includes the value of all of one's possessions. It is customarily 2.5% (or 1/40th) of a Muslim's total savings and wealth above a minimum amount known as *nisab*.

religiosity and the level of conservatism in auditors' judgments regardless of whether such judgments are or are not appropriately conservative. The first hypothesis is:

**H1:** Auditors scoring high (low) on the Islamic religiosity scale will exhibit a higher (lower) level of conservatism in their judgments.

### ***Islamic worldview and auditors' conservatism***

Islamic worldview refers to enduring, fundamental, and internally developed core Islamic values and beliefs. As individual judgments are driven by values (Torelli & Kaikati, 2009), Islamic worldview, grounded as it is in core Islamic values, is likely to be a dominant factor in influencing judgments in a business context.

Prior literature in history, ethics, and marketing provides evidence of a positive influence of Islamic worldview on ethical practices and judgments (Badawi, 2002; Asri & Fahmi, 2004; Choudhury, 2015) and consumer judgments (Arham, 2010; Ilyas et al., 2011; El-Bassiouny, 2014; Ahmad et al., 2015a). A number of studies suggest that conservative Islamic values embedded in the Islamic worldview hold an important position in the conduct of business and professional activities, such as banking, accounting, and auditing (Rahman, 2000; Lewis, 2001; Rahman, 2003), for example, the development and interpretation of *Shariah*-based accounting and auditing standards (AlAbbad, 2016) and the prohibition of interest (*Riba*), which is one of the basic Islamic values of Islamic jurisprudence (Usmani, 2004). Also, *zakat* on both individuals and institutions is an example of how conservative Islamic values are incorporated into accounting, auditing, and financial management practices in Islamic financial institutions (Lewis, 2005). Given the emphasis on *zakat* and the responsibility of auditors for providing a true and fair view of the financial statement of the organization to shareholders, they are also likely to be more conservative in an Islamic cultural context. A higher level of conservatism is also expected to ensure public interest.

Hypothesis 1 predicts that auditors who score high on the Islamic religiosity scale will prefer income-decreasing choices, and therefore a higher score on Islamic worldview, which is the integral part of Islamic religiosity, is also likely to increase the level of conservatism in their judgments. This hypothesis does not suggest that a higher level of conservatism is more appropriate or complies more

with ISAs but only suggests that the level of conservatism will be determined by the level of the Islamic worldview. Thus, the second hypothesis is:

**H1a:** Auditors scoring high (low) on the Islamic worldview scale will exhibit a higher (lower) level of conservatism in their judgments.

### ***Religious personality and level of conservatism in auditors' judgments***

Prior research provides evidence that Islamic rituals are an important part of the social, personal, professional, and organizational landscape in Islamic countries (Ali & Weir, 2005). Islamic rituals are detailed, structured, and predominantly rules- and compliance-based. Scholars have labelled these ritual aspects of Islam “legalistic” (Trimingham, 1998; Farooq, 2011) and “mechanical” (Bennett (2009). “Islamic legalism” refers to the interpretation of aspects of Islam without human intellect or judgment playing a vital role (Farooq, 2011).<sup>53</sup>

Religious personality represents external forms of worship (Krauss et al., 2005, p. 140). It reflects an individual’s direct relationship with God through ritualistic acts such as prayer, fasting, reading the holy scriptures, and obedience to the external Islamic discipline, such as dress code and appearance, as well as items specific to Islamic legal rulings (Krauss et al., 2005, p. 179). Religious personality measures one’s level of commitment to ritualistic behaviour and reflects a variety of external behaviours to assess the extent to which they reflect Islamic teachings.

Since most of these forms of worship follow a strict pattern and are associated with compliance with rules, religious personality in Islam is often regarded as “mechanically ritualistic and ethically superficial” (Powers, 2004, p. 426). Since conservatism in Islam also refers to the strict and unwavering interpretation of religious doctrines and traditions (Huq, 2010), it is expected that following fundamental Islamic rituals as determined by the *Quran* and *Sunnah* are also manifestations of conservatism in Islam (Atacan, 2005). It is expected that those who score high on the religious personality scale are likely to follow the rules and comply with ISAs (i.e., in this context, writing off a higher amount of inventory)

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<sup>53</sup> “Islamic legalism” refers to the historical emergence of a dominant mode of thinking in some Islamic communities from the 18<sup>th</sup> to the 21<sup>st</sup> century. The legalistic interpretation of Islam suggests that form should override substance and treats *Shariah* as a stagnant resource of rules and rigid guidelines. There are some aspects of *Shariah* that do not require interpretation, for example, rituals and worship. However, scholars warn that this approach in other areas of inquiry leads to substantive degeneration that reduces Islam to a shell of codes rather than a dynamic and value-oriented religion (Farooq, 2011). However, Islamic accounting standard setters suggest that application of Islamic *Shariah* to financial banking and contracts emphasizes form *as well as* substance.

and are likely to exhibit a higher level of conservatism in their judgments compared to those who score low on the religious personality scale. The third hypothesis is:

**H1b:** Auditors scoring high (low) on the religious personality scale exhibit a higher (lower) level of conservatism in their judgments.

#### ***4.3.2 Clients' religious adherence and the level of conservatism in auditors' judgments***

The second hypothesis of this study investigates the influence of clients' religious adherence (manipulated as high or low) on the level of conservatism in auditors' judgments. Prior research provides evidence that religious adherence is an important aspect in the organizational context and is likely to influence auditors' judgments in a variety of ways. It is generally acknowledged that religious adherence mostly manifests itself as rituals and performs important group functions. Scholars of religion, including Durkheim (1915), Rappaport (1979), and Weber (1993) assume that religion promotes intragroup trust among its adherents (Sosis, 2005). Several studies have argued that exhibitions of religious adherence such as prayer and worship enable the expression and reaffirmation of shared beliefs, norms, and values and are thus essential for maintaining communal stability and group harmony (Fischer et al., 2013). Thus it is expected that religious adherence is likely to generate trust and intergroup dependence for adherents of a particular religion.

With its rigid and hierarchical cultural structure, Islamic society is cohesive and is characterized by a strong sense of intergroup unity (Verkuyten, 2007). In Islam, religious rituals are an important aspect of social and cultural integration (Lapidus, 2014). Triandis (1992) points out that in Islamic cultures one either is or is not a member of the in-group. In Islamic culture, group identification is not a matter of degree, and one cannot be more or less identified with a group; rather orientation and commitment to the in-group are normative and compulsory (Verkuyten, 2007). Islamic individuals thus show more of a sense of duty and obligation in the interests of the religion (Basabe & Ros, 2005).

Given Islamic society places a great deal of emphasis on the importance of religious adherence in both a personal and professional context, it is expected that religious adherence within Islamic culture is positively related to the tendency to favour the in-group over other groups (Verkuyten, 2007). More specifically, intergroup trust within social and religious groups in Pakistan is evident and impacts corporate governance practices (Mirza & Azfa, 2010). Additionally, previous experimental evidence in the Pakistani educational context suggests that highly religious individuals are considered more

trustworthy (Delavande & Zafar, 2011). It is suggested therefore that individuals who exhibit a high level of religious adherence are likely to be more trusted in society.

Regarding auditor–client interaction, it is expected that auditors are more likely to trust a client who exhibits a high level of religious adherence (as expressed in the regularity of prayer in the experiment) and are more likely to trust the information provided by the client, decreasing the amount of inventory write-down and the associated level of conservatism in their judgments. In contrast, when the client exhibits low religious adherence (i.e., non-attendance at prayer), auditors are less likely to trust the information provided by the client regarding the resale of inventory and are likely to increase conservatism in their judgments. This hypothesis predicts that a client’s higher religious adherence is likely to decrease the level of conservatism in auditors’ judgments. Thus the fourth hypothesis is:

**H2:** A high (low) level of clients’ religious adherence is likely to decrease (increase) the level of conservatism in auditors’ judgments.

#### ***4.3.3 Interaction between clients’ religious adherence and auditors’ Islamic religiosity level***

Hypothesis 1 predicts that auditors’ overall Islamic religiosity score will increase the level of conservatism in their judgments. However, given there are two manipulations of clients’ religious adherence level, high versus low, there is a possibility that clients’ religious adherence will interact with auditors’ Islamic religiosity and the level of conservatism in their judgments.

Based on Hypothesis 2, it is expected that auditors are likely to trust the information provided by a client with high religious adherence and this level of trust will increase if auditors themselves have a high score on the Islamic religiosity scale, as auditors’ Islamic religiosity and clients religious adherence will reinforce each other. It is expected that a client’s high religious adherence level will interact with auditors’ religiosity and is likely to decrease the level of conservatism in their judgments. Thus the interaction hypothesis proposed is:

**H3:** Client’s religious adherence level (high versus low) will interact with auditors’ overall Islamic religiosity level (high versus low) to decrease (increase) the level of conservatism in auditors’ judgments.

## **4.4 Research method**

### **4.4.1 Participants**

Professional auditors working in the Big 4 auditing firms in Pakistan participated in the experiment. Big 4 auditing firms were selected for examination in this research because audit methodologies adopted in Big 4 firms are in line with ISAs. Given they have a similar organization culture, the Big 4 firms provided a homogenous sample for the experiment. A total of 105 usable responses were received from 250 distributed questionnaires, resulting in a response rate of 58%.<sup>54</sup> The majority of the sample consisted of audit seniors (40%) and assistants (38%) aged between 20 and 30 years (62%), and between 30 and 40 years (30%). On average, the audit experience of partners was approximately 13 years; managers had an average of nine years' audit experience and audit seniors had an average of five years' audit experience. Approximately 90.5% of the participants were active members of the ICAP.

Additionally, 86.7% of the participants reported being “somewhat familiar” with ISAs (a mean score of 5.6 on a Likert scale of 1–7, where 1 = very unfamiliar and 7 = very familiar). The overall mean score on task-specific experience with inventory write-downs was 4.95 on a Likert scale of 1–7, where 1 = no prior experience and 7 = dealt with very often. Importantly both the familiarity with the ISAs score and the task-specific experience indicate that the participants possessed the requisite knowledge and experience to complete the experimental task and make an informed judgment on inventory valuation.

The sample consisted of 86% males and 14% females, which is consistent with Pakistan's ranking on the Global Gender Gap Index (WEF, 2017). Pakistan has witnessed persistent gender inequality in representation specifically in the accounting and business professions, and this sample is representative of the existing gender gap in workforce participation (ADB, 2016, p. 70). A summary of the demographic information for the respondents is provided in Table 4.1.

### **4.4.2 Research design and procedure**

A 2x2 between-subjects experiment was designed and administered to test the hypotheses with manipulated and measured independent variables. The experimental design was selected to provide a

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<sup>54</sup> The response rate of 58% is considerably higher than recently published examples from audit judgment research, which shows low response rates, for example, a response rate of 20.7% in Abbott et al. (2016) and 26% in Mohd Sanusi et al. (2017).



strong cause–effect relationship between the variables of interest with higher reliability and internal validity.

The Big 4 auditing firms were contacted via email to obtain permission to conduct the experiment in their respective firms. The firms were informed about the ethical approvals and the voluntary nature of the research. Both the firms’ and individual participants’ confidentiality were assured. After the firms agreed to participate and provided an estimate of the number of potential participants, the sealed questionnaire packs were distributed to the assigned contact person at each of the firms.

<b>Table 4.1: Demographics</b>					
<b>Item</b>	<b>N (105)</b>	<b>%</b>			
Gender					
Male	91	86.7			
Female	14	13.3			
Age					
20–30	65	61.9			
30–40	32	30.4			
40–50	6	5.7			
50–60	2	1.9			
Membership					
ICAP (CA/ICAP)	95	90.5			
Other professional bodies	10	9.5			
<b>Item</b>	<b>Current position in firm</b>	<b>Total audit experience</b>	<b>Experience at current level</b>	<b>Task-specific experience (1–7)* Mean</b>	<b>Familiarity with ISAs (1–7)**</b>
	N (%)	Range (mean)			
Audit trainee	8 (7.6)	1–2 (1.44)	1–2 (1.44)	3.0	5.03
Assistants	40 (38.1)	1–5 (3.08)	1–5 (2.63)	5.6	5.60
Audit senior	42 (40.0)	2–12 (4.54)	1–8 (4.26)	5.8	5.83
Manager	9 (8.6)	4–15 (7.89)	1–15 (6.22)	5.8	5.56
Partner	6 (5.7)	9–25 (12.17)	2–25 (11.50)	6.0	6.0
Total	105 (100)	1–25 (4.47)	1–25 (4.0)	4.95	5.59
* where 1 = no prior experience and 7 = dealt with very often					
** where 1 = very unfamiliar and 7 = very familiar					

Each questionnaire pack included a cover letter,<sup>55</sup> instructions to participants, and the research instrument (see Appendix D for details). The experiment was conducted during training sessions held at the respective auditing firms. As instructed in the questionnaire pack, the participants placed and sealed the completed questionnaires in the envelopes provided. The questionnaire packs were then

<sup>55</sup> The cover letter included information about the researchers, institutional affiliations, general aim of the research, information on ethical approvals, and the voluntary nature of the study.

collected from the contact person at each of the firms by the researcher.<sup>56</sup> The research instrument was administered in English<sup>57</sup> and was extensively pilot-tested<sup>58</sup> to ensure readability and relevance to the Pakistani audit context.

#### ***4.4.2 Research instrument and variables***

The research instrument consisted of three sections. The first section contained an inventory valuation scenario and dependent variable measures. The second section collected participants' demographic information and also included a manipulation check question and a number of control variables. The third section consisted of an Islamic religiosity scale, which measures auditors' overall Islamic religiosity,<sup>59</sup> and its two components, Islamic worldview and religious personality (refer to research instrument in Appendix D for details).

##### ***The scenario***

This study utilized an audit judgment scenario with an inventory valuation task. Prior studies provide evidence that auditors' inventory valuation judgments are appropriate for examining the level of conservatism in auditors' judgments (Nöteberg & Hunton, 2005; Chung, Cohen, & Monroe, 2008; Knechel, Salterio, & Kochetova-Kozloski, 2010; Bhattacharjee et al., 2012). The inventory valuation scenario was adopted from Yamamura, Frakes, Sanders, and Ahn (1996), and has been extensively tested for reliability and validity in prior research (Goodwin, 1999; Nöteberg & Hunton, 2005).<sup>60</sup>

The participants assumed the role of a senior auditor working on the audit of a hypothetical client, Nature-Pakistan Limited (Nature). Participants were provided with relevant company background and audit-related company information, including additional client-provided information to support client-preferred treatment, including valuation write-downs. Participants evaluated an inventory write-down scenario involving Nature and made a series of related judgments.

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<sup>56</sup> According to the ethical approvals and requirements of the research, and in order to minimize coercion, the researcher was not allowed to come into direct contact with the participants during data collection; thus the management of the auditing firms administered the survey.

<sup>57</sup> Audit professionals contacted during pilot-testing commented that auditors in Pakistan would have no problem in understanding and responding to the case in English because English is the official language in auditing firms in Pakistan.

<sup>58</sup> Extensive pilot-testing to ensure readability, comprehension, and practical relevance was conducted. Feedback was sought from 13 professional accountants, two accounting professors, and two accounting regulators from Pakistan and their comments were incorporated as appropriate.

<sup>59</sup> Overall Islamic religiosity score refers to the combined religiosity score for both Islamic worldview and religious personality.

<sup>60</sup> According to ISA 330 *Auditors' response to assessed risk* and ISA 501 *Audit evidence*, there are specific requirements for auditors to obtain sufficient appropriate audit evidence concerning certain aspects of inventory (IAASB, 2012e) and thus this particular issue was selected for examination in this research.

### ***Independent variables***

Auditors' Islamic religiosity level is a measured independent variable, while clients' religious adherence is a manipulated independent variable.

#### **Client's religious adherence: Manipulated independent variable**

The experiment manipulated the religious adherence level (high vs low) of the client, that is, the Sales Director.<sup>61</sup> In the high religious adherence treatment, participants were informed that the Sales Director "prays in the company's prayer room".<sup>62</sup> In the low religious adherence version, the participants were informed that the Sales Director "does not pray in the company's prayer room". Daily prayer is an important socio-religious ritual in Pakistan, and both local and international enterprises in the country provide designated prayer rooms for employees (Khib'i, 2004). Attendance at the prayer room indicates a high level of religious adherence (i.e., regularity of prayer is an expression of high adherence to Islamic rituals and worships). Thus this study adopted attendance at the prayer room as a proxy for clients' religious adherence.

#### **Auditors' Islamic religiosity level: Measured independent variable**

Auditors' Islamic religiosity level is the measured independent variable in this study. In the third section of the research instrument, the MRPI, an Islamic religiosity scale, was used to measure auditors' overall Islamic religiosity level and its two components, Islamic worldview and religious personality. For each participant, overall Islamic religiosity score, Islamic worldview score, and religious personality scores were calculated. Based on participants' scores on each of these scales, the participants were classified into high and low categories of Islamic religiosity, Islamic worldview, and religious personality.<sup>63</sup>

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<sup>61</sup> Clients' religiosity level was manipulated because earlier evidence in this thesis indicates that clients' religiosity level is an important consideration and significantly influences auditors' evidence reliability judgments. Please refer to the Results section of Chapter 3 of this thesis for details.

<sup>62</sup> Krauss et al. (2005) provide a number of items that exhibit the level of one's religious adherence; this study uses regularity of daily prayer as an indication of high religious adherence of the Sales Director in the scenario.

<sup>63</sup> Individual religiosity scores were determined according to the MRPI scoring manual, with each scale summed and divided by the number of items in that scale. For example, for the Islamic worldview scale, which has 20 items, if the total score was 86, 86 was divided by 20 which is 4.3, the scaled score for that participant. This score was then categorized based on the threshold values of high and low religiosity (Krauss, 2011). The threshold value for Islamic worldview is 4.19 (Krauss, 2011, p. 2). All auditors who scored higher or equal to 4.19 were categorized as having a high Islamic worldview score and those who scored less than 4.19 were categorized as scoring low on the Islamic worldview scale. For religious personality, the threshold value was 3.55. Subjects who scored higher or equal to 3.55 were categorized as having a high score on the religious personality construct, and those who scored less than 3.55 were categorized as low (Krauss, 2011, p. 2). For overall Islamic religiosity, the threshold value for each participant was determined based on the mean of the combined scores for Islamic worldview and religious personality. Subjects who scored higher or equal to 8.44 were categorized as high, and those who scored less than 8.44 were categorized as low.

### **Manipulation check**

To assess the effectiveness of the experimental manipulation of clients' religious adherence, a manipulation check was added in the second part of the research instrument. Participants were asked to indicate "how religious they perceived the Sales Director to be" on a Likert scale from 1–7, where 1 = not at all religious and 7 = very religious. The results from this item were used to assess whether the experimental manipulation was successful or not.

### ***Control variables***

In an experimental setting, factors other than the main independent variables that could affect the outcome of the experiment should be controlled. Control variables help to eliminate alternative explanations for the results. Three control variables were measured in this study: (i) auditors' perceived level of risk about the inventory valuation issue; (ii) auditors' experience (general audit experience and task-specific experience); and (iii) auditors' familiarity with ISAs.

First, auditors' perceived level of risk in relation to inventory valuation was measured as a control variable because previous evidence shows that auditors' risk perceptions of an audit issue influence their judgments in a variety of contexts (Chen et al., 2007; Hogan & Wilkins, 2008; Johnson et al., 2012). Thus auditors' perceived risk assessment was measured to enable analysis of its influence on the level of conservatism in auditors' judgments.

Second, prior research provides evidence that auditors' experience is an important factor in their judgment and decision making (Choo & Trotman, 1991; Moroney & Carey, 2011). This study measures auditors' total audit experience (in years) as well as auditors' task-specific experience with inventory write-downs (i.e., the number of times they have been exposed to a judgment task), to enable analysis of the impact of experience upon auditors' judgments (Martinov-Bennie & Pflugrath, 2009). Participants rated their experience with the inventory write-down task on a Likert scale from 1–7 (ranging from 1 = no prior experience to 7 = dealt with very often).

Auditors' familiarity with ISAs was the third control variable measured. Prior studies have shown that auditors' familiarity with ISAs is an important factor and is likely to influence auditors' judgments and decision making (Chand et al., 2010). This study measures auditors' familiarity with ISAs on a Likert scale from 1–7 (where 1 = very unfamiliar and 7 = very familiar). A number of

demographic variables were also included in the second section of the research instrument, including participants' age, gender, professional membership, and current position in their auditing firm.

### ***Dependent variables***

After participants read the company background information provided in the audit scenario, they were required to make a series of audit judgments, including the likelihood of recommending an inventory write-down and the likelihood of agreeing with the clients' assessment of no write-down of inventory; both judgments were made on a Likert scale from 1–7 (where 1 = very unlikely and 7 = very likely). In addition, auditors were asked to make a final recommendation for the actual inventory write-down amount. This measure (i.e., the Pakistani rupee (PKR)<sup>64</sup> amount) is the proxy for the level of conservatism in auditors' judgments and represents the primary dependent variable used throughout the analysis. Participants responded on a seven-point scale ranging from PKR 0–1500 (AUD 0–16.9) million, with the scale points increasing in PKR 250 (AUD 2.82) million increments.

## **4.5 Results**

### ***4.5.1 Data reliability analysis and descriptive statistics***

#### ***Data reliability analysis for independent variables***

In this section, results of tests conducted to ascertain the validity and reliability of the data are reported. Table 4.2 provides the reliability scores for the independent variables. The Cronbach's alpha for overall Islamic religiosity scale is 0.72, for Islamic worldview it is 0.73, and for religious personality it is 0.76. Importantly, for all three scales, the alpha value is above the acceptability level of 0.70 (Nunnally, 1978, p. 245).

To ensure that the assumptions about the nature of the two constructs, Islamic worldview and religious personality, hold true, a correlation analysis was conducted. The results of the Pearson correlation coefficient provided in Table 4.2 show that although both of these constructs are significantly correlated with overall Islamic religiosity ( $p = 0.000$ ), they are not significantly correlated with each other ( $p = 0.163$ ). The results verify that Islamic worldview and religious personality are two distinct and separate constructs of religiosity and support the validity of the Krauss et al. (2005) Islamic religiosity framework adopted in this study.

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<sup>64</sup> All number values in the questionnaire are reported in PKR (Pakistan rupee) (PKR 80 = AUD 1).

Prior research posits that religiosity data are based on self-reported responses and thus are subject to social desirability response (SDR) bias.<sup>65</sup> To address the potential SDR bias in this study, the MRPI framework has an embedded “lie scale” in the religious personality component. There are five items in the scale. It is suggested that with regard to these five items, respondents who score a total exceeding 20 (>80%) be removed from the analysis (Krauss, 2011, p. 6). Eleven participants scoring higher than the threshold value for SDR were removed from the original sample. Removal of these participants from the sample does not qualitatively change the significance of the statistical tests. However, the results reported are those following the removal of the participants from the sample.

**Table 4.2: Data reliability and validity tests for independent variables**

Panel A: Cronbach's alpha				
Variable		Cronbach's alpha		
Islamic religiosity (48 items)		0.72		
Islamic worldview (20 items <sup>66</sup> )		0.73		
Religious personality (28 items)		0.76		
Panel B: Pearson correlation between independent variables				
		Islamic worldview	Religious personality	Overall Islamic religiosity
Continuous values of scale				
Islamic Worldview	Pearson correlation	1		
	Sig. (two-tailed)			
	N	105		
Religious personality	Pearson correlation	.137	1	
	Sig. (two-tailed)	.163		
	N	105	105	
Overall Islamic religiosity	Pearson correlation	.704**	.800**	1
	Sig. (two-tailed)	.000	.000	
	N	105	105	105
** Correlation is significant at the 0.01 level (two-tailed).				

\*\* Correlation is significant at the 0.01 level (two-tailed).

### ***Descriptive statistics for independent, control, and dependent variables***

Gender, age, professional membership, current position, general audit experience, and task-specific experience were tested for significance, and no significant results for level of conservatism in auditors' judgments were identified ( $p > 0.000$ ). The descriptive statistics summary is presented in Table 4.3.

<sup>65</sup> SDR bias is the tendency of individuals to deny socially undesirable traits and behaviours and to admit to socially desirable ones (Zerbe & Paulhus, 1987). Individuals often report inaccurate behaviour by answering the questions according to what they think they should be doing not to what they actually do (Smith et al., 2007).

<sup>66</sup> According to the MRPI scoring manual, 13 are reverse-scored in the Islamic worldview scale. For the normal score, 1 = strongly disagree and 5 = strongly agree. For the reverse-scored items, values on the Likert scale are reversed (1 = strongly agree and 5 = strongly disagree (Krauss, 2011, p. 7).

Based on the actual MRPI scores, the participants were divided into high and low categories.<sup>67</sup> Panel A, Table 4.3 shows that 57 participants scored high on the overall Islamic religiosity scale and 48 scored low with a mean score of 8.41 (range = 6.49–9.73). Sixty-one participants scored high on Islamic worldview and 44 scored low, with a mean score of (3.10–4.95), and for religious personality, the mean was 4.22 and the range was 3.14–5.00. However, only 38 participants scored low on religious personality, and 67 scored high.

The descriptive statistics for the control variables in Panel B, Table 4.3 show that auditors perceived a relatively high level of risk in relation to inventory write-downs (mean = 5.28 on a Likert scale of 1–7 where 1 = very low and 7 = very high). Auditors, on average, were highly likely to recommend an inventory write-down (mean = 4.99 on a Likert scale of 1–7) and were less likely to agree with clients' recommendation of no write-down of inventory (mean = 3.13 on a Likert scale of 1–7).

The average inventory write-down amount recommended by auditors was PKR 1129.05 (AUD 12.7) million, a material amount.<sup>68</sup> Based on the information provided in the scenario, the maximum (and expected) write-down value from the auditors was PKR 1500 (AUD 16.9) million.<sup>69</sup>

### ***Manipulation check***

To assess the effectiveness of the experimental manipulation of clients' religious adherence, a manipulation check was included in the second part of the research instrument. The participants were asked to rate how religious they perceived the client (i.e., the Sales Director) to be, on a Likert scale of 1–7 (where 1 = not at all religious and 7 = highly religious). The results show that 94% of the participants responded correctly to the experimental condition.<sup>70</sup>

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<sup>67</sup> The threshold value for Islamic worldview is 4.19 (Krauss, 2011, p. 2). All those auditors who scored higher or equal to 4.19 were categorized as having a high Islamic worldview score and those who scored less than 4.19 were categorized as scoring low on the Islamic worldview scale. For religious personality, the threshold value was 3.55. Subjects who scored higher or equal to 3.55 were categorized as having a high score on the religious personality construct, and those who scored less than 3.55 were categorized as low (Krauss, 2011, p. 2). For overall Islamic religiosity, the threshold value for each participant was determined based on the mean of the combined scores for Islamic worldview and religious personality. Subjects who scored higher or equal to 8.44 were categorized as high, and those who scored less than 8.44 were categorized as low.

<sup>68</sup> Planning materiality for this client was set at PKR 500 million (AUD 5.6 million).

<sup>69</sup> According to the scenario, the inventory was valued at PKR 7800 million and NRV was PKR 6300 million. The difference between these two values is the expected write-down value, which should be approximately PKR 1500 million. To ensure that the inventory was valued near to equal to the NRV (in accordance with IAS *Inventories*), auditors were required to revise the write-down to this benchmark. A lower inventory write-down is likely to increase the net assets and will materially overstate the profit.

<sup>70</sup> The analysis was repeated by excluding the participants who failed the manipulation test; the results were consistent with the main results. Thus overall results that include all participants are reported in this paper.

**Table 4.3: Descriptive statistics for independent, dependent, and control variables**

<b>Panel A: Descriptive statistics for independent variables</b>			
<b>Measured independent variables</b>	<b>Mean score (range)</b>	<b>Percentage</b>	
Auditor's Islamic religiosity (48 items)	8.41 (6.49–9.73)	58 high	55%
		47 low	45%
Auditor's Islamic worldview (20 items)	4.19 (3.10–4.95)	61 high	58%
		44 low	42%
Auditor's religious personality (28 items)	4.22 (3.14–5.00)	67 high	64%
		38 low	36%
<b>Manipulated independent variable</b>			
Client's religious adherence level			
High (client prays in the prayer room)		54	56%
Low (client does not pray in the prayer room)		51	54%
<b>Panel B: Descriptive statistics for control variables</b>		<b>Mean</b>	<b>(SD)</b>
Perceived level of risk for inventory write-down, 1–7 (1 = very low and 7 = very high)		5.28	(1.105)
Familiarity with ISAs (1 = very unfamiliar and 7 = very familiar)		5.6	(1.089)
General audit experience (number of years)		4.47	(3.472)
Task-specific experience (1 = no prior experience and 7 = dealt with very often)		4.95	(1.555)
<b>Panel C: Descriptive statistics for auditors' intermediate judgment and dependent variable</b>			
Likelihood of recommendation an inventory write-down, 1–7 (1 = very low and 7 = very high)		4.99	(1.362)
Likelihood of agreement with the client, 1–7 (1 = very low and 7 = very high)		3.13	(1.363)
Amount of inventory write-down (PKR 0–1500 million) (AUD 0–16.9 million)		PKR 1129.05 million AUD 12.7 million	(448.704)

The mean score for the condition in which clients' religious adherence was manipulated as low was 3.62 (SD = 1.63,  $n = 54$ ), which is significantly lower ( $p = .001$ ) than the mean score of 5.01 (SD = 1.47,  $n = 51$ ) for the treatment in which clients' religious adherence was manipulated as high. The results indicate that manipulation of clients' religious adherence was successful.

#### 4.5.2 Hypotheses testing

##### *Auditors' overall Islamic religiosity and the level of conservatism in auditors' judgments*

Hypothesis 1 predicts that a high score on auditors' overall Islamic religiosity is likely to increase the level of conservatism in auditors' judgments. It is expected that auditors with high Islamic religiosity will recommend a higher value for inventory write-downs as compared to those who scored low.

One-way ANOVA results in Panel A, Table 4.4 report a significant main effect for auditors' Islamic religiosity score on the amount of inventory write-down recommended ( $F = 6.324$ ,  $p = 0.013$ ). Specifically, the mean value for the inventory write-down amount (in millions) for auditors ( $n = 58$ ) who scored high on the Islamic religiosity scale is PKR 1195.39 (AUD 13.4) million, which is greater than the mean of PKR 955.17 (AUD 10.7) million for those who scored low ( $n = 47$ ). The results support Hypothesis 1.



#### ***Auditors' Islamic worldview and the level of conservatism in auditors' judgments***

Hypothesis 1a predicts that a high Islamic worldview on the part of auditors is likely to increase the level of conservatism in their judgments. One-way ANOVA results from Panel A, Table 4.4 show a significant main effect of auditors' Islamic worldview scores on the inventory write-down amount ( $F = 15.352, p = 0.000$ ). Specifically, the mean inventory write-down amount (in millions) for auditors who scored high ( $n = 61$ ) on the Islamic worldview is PKR 1268.33 (AUD 14.2) million) which is greater than PKR 943.33 (AUD 10.6) million), the mean for those auditors who scored low ( $n = 44$ ) on the Islamic worldview. These results support Hypothesis 1a.

#### ***Auditors' religious personality and the level of conservatism in auditors' judgments***

Hypothesis 1b predicts that a high level of auditors' religious personality is likely to increase the level of conservatism in auditors' judgments. One-way ANOVA results from Panel A, Table 4.4 report a non-significant main effect of auditors' religious personality on the inventory write-down amount ( $F = 1.831, p = 0.179$ ). The mean of the inventory write-down value (in millions) for auditors who scored high ( $n = 67$ ) on religious personality is PKR 1152.20 (AUD 12.9) million, and the mean is PKR 978.57 (AUD 11) million for those who scored low ( $n = 38$ ). These results do not support Hypothesis 1b.

#### ***Client's religious adherence and the level of conservatism in auditors' judgments***

Hypothesis 2 predicts that a high level of client religious adherence is likely to decrease the level of conservatism in auditors' judgments. Although, as per Table 4.4, the mean inventory write-down amount of PKR 1050.00 (AUD 11.8) million for auditors ( $n = 54$ ) who received a high level of clients' religious adherence is lower than the mean of PKR 1212.75 (AUD 13.6) million for those who received a low manipulation of clients' religious adherence. The difference is not significant ( $F = 3.534, p = 0.063$ ) and thus Hypothesis 2 is not supported.

**Table 4.4: One-way ANOVA results for Hypotheses 1, 1a, 1b, and 2**

<b>Panel A: One-way ANOVA for auditors' overall Islamic religiosity, Islamic worldview, religious personality, and clients' religious personality</b>				
<b>Independent variable IV</b>	<b>df</b>	<b>Mean square</b>	<b>F</b>	<b>P</b>
Islamic religiosity (H1)				
Between groups	1	1211292.466	6.324	0.013
Within groups	103	191530.217		
Islamic worldview (H1a)				
Between groups	1	2716071.429	15.352	0.000
Within groups	103	176920.712		
Religious personality (H1b)				
Between groups	1	365772.894	1.831	0.179
Within groups	103	199739.144		
Clients' religious adherence (H2)				
Between groups	1	694689.076	3.534	0.063
Within groups	103	196545.783		
<b>Panel B: Dependent variable amount of write-down PKR (0–1500 million)</b>				
<b>Independent variable</b>	<b>N</b>	<b>Mean PKR (AUD) in millions</b>	<b>SD</b>	<b>Standard error</b>
Islamic religiosity				
Low	47	955.17 (10.7)	505.566	93.881
High	58	1195.39 (13.4)	409.404	46.962
Islamic worldview				
Low	44	943.33 (10.6)	474.417	80.191
High	61	1268.33 (14.2)	423.798	50.654
Religious personality				
Low	38	978.57 (11)	566.288	170.742
High	67	1152.20 (12.9)	432.942	44.655
Client's religious adherence				
Low	51	1212.75 (13.6)	428.117	59.948
High	54	1050.00 (11.8)	457.227	62.221

### ***Interaction between clients' religious adherence and auditors' Islamic religiosity level***

Hypothesis 3 predicts that a high level of client religious adherence is likely to interact with a higher level of auditors' Islamic religiosity and both the variables are likely to reinforce each other, thus decreasing the level of conservatism in auditors' judgments. A 2x2 ANOVA from Panel A, Table 4.5 does not report a significant interaction between clients' religious adherence and auditors' Islamic religiosity in relation to the level of conservatism in auditors' judgments ( $F = 0.278$ ,  $p = 0.599$ ). The results do not support Hypothesis 3.

Table 4.5: 2x2 ANOVA results for Hypothesis 3: Interaction between clients' religious adherence and auditors' overall Islamic religiosity				
Dependent variable: Amount of inventory write-down				
Source	df	Mean square	F	Sig.
Client's religious adherence level	1	579668.756	3.061	0.083
Auditor's Islamic religiosity level	1	992177.692	5.238	0.024
Client's religious adherence level * Auditor's Islamic religiosity level	1	52565.828	0.278	0.599
a. R-squared = .086 (adjusted R-squared = .059)				

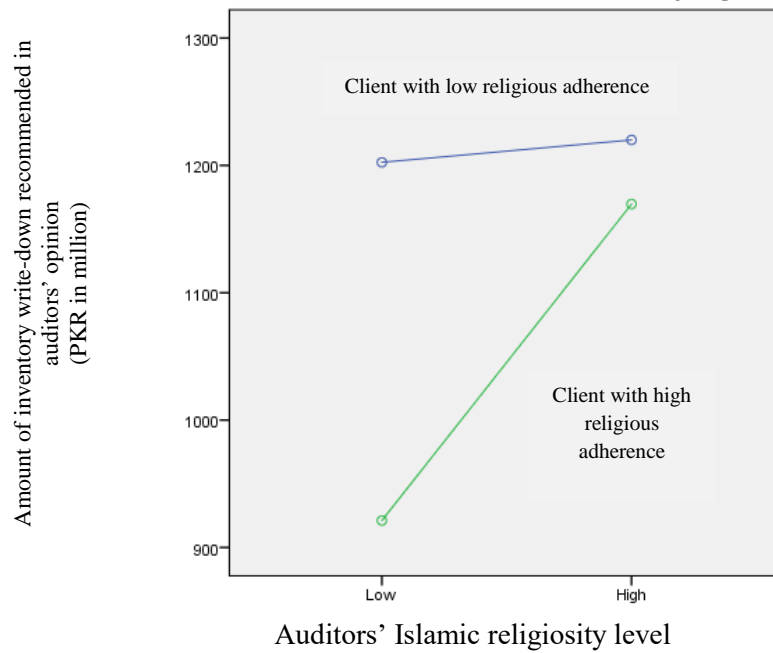
However, the results of a 2x2 ANOVA plot in Figure 4.1 depict a possible interaction between the two independent variables, namely, clients' religious adherence (a manipulated independent variable) and auditors' Islamic religiosity level (a measured independent variable). The interaction is significant if the effect of the variation in one independent variable differs as a function of the level of the other independent variable (Trotman, 1996). In this particular context, the interaction hypothesis suggests that the level of conservatism in auditors' judgments is not only influenced by auditors' Islamic religiosity level but also for each level of clients' religious adherence. The graph shows that the interaction between clients' religious adherence and auditors' Islamic religiosity level is "ordinal". An interaction graph in which the lines do not cross and the slope of the lines is not parallel (such as in Figure 4.1) are "ordinal" interactions (Field, 2013).

<b>Table 4.6: Interaction between clients' religious adherence and auditors' overall Islamic religiosity (mean inventory write-down value for each treatment)</b>			
Auditors' overall Islamic religiosity	Religious adherence of client	Total n = 105	Mean amount of write-down of inventory PKR (AUD) in millions
High	High	28	1169.64 (13.1)
	Low	30	1220.00 (13.7)
Low	High	26	921.15 (10.35)
	Low	21	1202.38 (13.5)

Hypothesis 3 suggests that a higher level of clients' religious adherence is likely to interact with auditors' high Islamic religiosity level and will decrease the level of conservatism in auditors' judgments. From Table 4.6 and Figure 4.1, it is seen that auditors who score high on the Islamic religiosity scale, irrespective of the religious adherence level of the client, recommend a higher value for the write-down of inventory and thus exhibit a higher level of conservatism in their judgments. However, when auditors' overall Islamic religiosity score is low, clients' religious adherence becomes important. Auditors who score low on the overall Islamic religiosity scale exhibit a lower level of conservatism in their judgments when clients' religiosity adherence is high (mean of write-down = 921.15) compared to when clients' religious adherence level is low (mean of write-down = 1202.38) with similar write-down amounts to auditors' high religiosity levels under both conditions.

These results suggest that auditors' Islamic religiosity level has a different impact on each level of clients' religious adherence concerning the level of conservatism in auditors' judgments depending upon auditors' religiosity. When auditors' Islamic religiosity level is high, the level of conservatism is similar irrespective of the religious adherence level of the client. However, when auditors' Islamic religiosity level is low, the level of conservatism in their judgment decreases in the presence of a client with a high religious adherence condition.

**Figure 4.1: Estimated marginal means for the amount of inventory write-down exhibiting the level of conservatism in auditors' judgments**



#### 4.5.4 Additional analysis

Prior audit judgment research provides evidence that auditors' risk assessments are important in examining auditors' judgments (Hogan & Wilkins, 2008), they can provide an alternative explanation for auditors' judgments, and should be controlled for in an experimental setting (Brazel & Agoglia, 2007; Hogan & Wilkins, 2008).

To assess the possible influence of perceived audit risk assessment on the level of conservatism in their judgments, a correlation test between the dependent variables and auditors' perceived risk assessment was conducted. Results in Table 4.7 show that all three dependent variables are not only significantly correlated with each other but also with the control variable, that is, inventory write-down audit risk assessment. Auditors' assessments of perceived risk in relation to inventory write-downs is significantly correlated with auditors' likelihood of recommending an inventory write-down ( $p = 0.002$ ), auditors' likelihood of agreement with the Sales Director ( $p = 0.020$ ), and the amount of the inventory write-down recommended by auditors ( $p = 0.000$ ). The results suggest that auditors' perceived audit risk significantly impacts the level of conservatism in their judgments.

**Table 4.7: Pearson correlations between dependent variables and control variable**

		Perceived level of risk in relation to inventory write- down	Likelihood of recommending an inventory write-down	Likelihood of agreement with the Sales Director	Amount of inventory write-down recommended
Perceived level of risk in relation to inventory write- down	Pearson correlation	1	.		
	Sig. (two-tailed)				
	N	105			
Likelihood of recommending an inventory write-down	Pearson correlation	.302**	1		
	Sig. (two-tailed)	.002			
	N	105	105		
Likelihood of agreement with the Sales Director	Pearson correlation	-.229*	-.207*	1	
	Sig. (two-tailed)	.020	.035		
	N	104	104	104	
Amount of inventory write- down recommended	Pearson correlation	.451**	.297**	-.356**	1
	Sig. (two-tailed)	.000	.002	.000	
	N	105	105	104	105

\*\* Correlation is significant at the 0.01 level (two-tailed)

\* Correlation is significant at the 0.05 level (two-tailed)

Based on these results, further ANCOVA analysis was conducted to examine the influence of the three measured control variables, that is, auditors' perceived risk assessment, auditors' experience (general audit experience and task-specific experience), and auditors' familiarity with ISAs on the level of conservatism in auditors' judgments. The results of 2x2 ANCOVA are presented in Table 4.8.

Panel A, Table 4.8 reports that the influence of auditors' overall Islamic religiosity is non-significant ( $F = 1.314$ ,  $p = 0.254$ ). However, the influence of auditors' Islamic worldview remains statistically significant ( $F = 12.169$ ,  $p = 0.001$ ), after controlling for auditors' perceived audit risk assessment, auditors' general and task-specific experience, and auditors' familiarity with ISAs.

Further, Table 4.8 reports that auditors' perceived level of audit risk in relation to inventory write-downs is significant for all four main effect hypotheses: for Hypothesis 1, auditors' overall Islamic religiosity level ( $F = 19.752$ ,  $p = 0.000$ ); for Hypothesis 1a, auditors' Islamic worldview ( $F = 18.734$ ,  $p = 0.000$ ); for Hypothesis 1b, auditors' religious personality ( $F = 20.302$ ,  $p = 0.000$ ); and for Hypothesis 2, clients' religious adherence level ( $F = 20.881$ ,  $p = 0.000$ ). The results suggest that auditors' perceived audit risk has a significant influence on the level of conservatism in auditors' judgments.

**Table 4.8: One-way ANCOVA for Hypotheses 1, 1a, 1b, and 2**

Dependent variable: Amount of inventory write-down				
<b>Panel A: H1 Influence of auditors' overall Islamic religiosity on the level of conservatism in auditors' judgments with control variables</b>				
Source	df	Mean square	F	Sig.
Overall Islamic religiosity	1	206501.008	1.314	0.254
Perceived level of risk in relation to inventory write-down	1	31033509.089	19.752	0.000
Total audit experience	1	106398.815	0.677	0.413
Task-specific experience with inventory write-down	1	13943.010	0.089	0.766
Familiarity with ISAs	1	1005981.642	6.402	0.013
<b>Panel B: H1a Influence of auditors' Islamic worldview on the level of conservatism in auditors' judgments with control variables</b>				
Islamic worldview level	1	1723651.593	12.169	0.001
Perceived level of risk in relation to inventory write-down	1	2653534.501	18.734	0.000
Total audit experience	1	43435.955	0.581	0.581
Task-specific experience with inventory write-down	1	235.238	0.002	0.968
Familiarity with ISAs	1	865711.854	6.112	0.015
<b>Panel C: H1b Influence of auditors' religious personality on the level of conservatism in auditors' judgments with control variables</b>				
Religious personality level	1	10004.132	0.063	0.803
Perceived level of risk in relation to inventory write-down	1	3230716.342	20.302	0.000
Total audit experience	1	77586.589	0.488	0.487
Task-specific experience with inventory write-down	1	8561.773	0.054	0.817
Familiarity with ISAs	1			
<b>Panel C: H2 Influence of clients' religious adherence on the level of conservatism in auditors' judgments with control variables</b>				
Clients' religious adherence level	1	295557.457	1.892	0.172
Perceived level of risk in relation to inventory write-down	1	3262001.824	20.881	0.000
Total audit experience	1	113138.117	0.724	0.397
Task-specific experience with inventory write-down	1	5158.160	0.033	0.856
Familiarity with ISAs	1	827703.240	5.298	0.023

This relationship is particularly evident from the descriptive statistics, with 16 auditors who perceived the inventory valuation to be “very high risk” (an average score of 7 on the Likert scale) and on average recommended the highest inventory write-down values (PKR 1402 (AUD 15.8) million).

The results suggest that auditors' perceived risk assessments provide an alternative explanation for an increase in the level of conservatism in auditors' judgments. In conclusion, the results of this study suggest that auditors' Islamic religiosity, Islamic worldview, as well as their perceived risk assessments, determine the level of conservatism in their judgments.

## 4.6 Conclusion

This study contributes to the literature on auditors' judgment and decision making by examining the influence of Islamic culture, more specifically auditors' Islamic religiosity and clients' religious adherence, on the level of conservatism in auditors' judgments. Auditors' exercise of conservatism in their judgments is important for audit practice and has been extensively examined in prior research (e.g., Firth et al. (2014) Lara, Osma, and Penalva (2016) Chen et al. (2016) but not in an Islamic context. Conservatism, however, is considered in Islamic countries to be an important cultural factor with

evidence of its pervasiveness in most social and professional settings (McIntosh & Islam, 2010). In Pakistan, this study's proxy for Islamic countries, a higher religiosity level is associated with a higher level of conservatism in social and political settings (Hassan, 2007). As such, this study contributes to and extends previous research into cultural influences on auditors' judgments generally and auditors' conservatism judgments specifically in an Islamic context.

This study used a 2x2 between-subjects experimental design to investigate the influence of auditors' Islamic religiosity and clients' religious adherence on the level of conservatism in auditors' judgments. The results support the hypotheses that auditors who score high on the Islamic religiosity and Islamic worldview scales make more conservative judgments. Results, however, do not support the influence of auditors' religious personality and clients' religious adherence on the level of conservatism in auditors' judgments. Further, the results of the interaction between auditors' religiosity and clients' religious adherence show that when auditors' Islamic religiosity level is high, conservatism in their judgments is also high, irrespective of the religious adherence level of the client (i.e., auditors' religiosity is the key factor). However, when auditors' Islamic religiosity level is low, the level of conservatism in their judgments is decreased in the presence of a client with high religious adherence (clients' religious adherence is a significant factor). Additional analysis indicates that auditors' perceived risk assessment of audit issues as "high" also significantly increases the level of conservatism in their judgments.

This study extends the research conducted in Chapters 2 and 3 by providing auditors with a relatively high-risk audit scenario (i.e., a required material write-down of PKR 1500 (AUD 17.1) million of near-expiry infant formula inventory to its net realizable value (NRV)). In addition, the scenario also included contradictory evidence (actual sales forecasts for the infant formula had not been met in the past) to the verbal audit evidence provided by the client (i.e., Sales Director) who believed that the inventory in question would be sold (as per forecast), with no write-down required. Given the high-risk audit issue and the client's aggressive proposed accounting treatment only supported by insufficient and low-reliability evidence (i.e., internal verbal evidence not supported by past sales evidence), it was expected that auditors would be highly conservative in their judgments and fully write down the inventory in question to its NRV.



Although the results of this study suggest that auditors who score high on the Islamic religiosity and Islamic worldview scales exhibit a higher level of conservatism in their judgments, auditors did not write down the inventory to its full NRV (a write-down of PKR 1500 (AUD 16.6) million) in accordance with accounting standard IAS 2 *Inventories* (IFRS, 2018). Auditors, on average, recommended an inventory write-down between PKR 900–1250 (AUD 10.1–14.06) million resulting in both the inventory balance and profit being materially overstated (client materiality = PKR 500 (AUD 5.6) million). These results suggest non-compliance with not only the accounting standards but also with ISAs (i.e., reliance on insufficient and unreliable evidence in a high audit risk scenario) and exercise of an inappropriately low level of professional scepticism leading to material misstatement. Thus the results of this study further support the concerns, already raised in Chapters 2 and 3 of this thesis, about auditors in an Islamic context exhibiting non-compliance with ISAs and demonstrating inappropriately low levels of conservatism and professional scepticism resulting in reduced audit quality and materially misstated financial information.

The results of this study have a number of implications. First, the findings are likely to interest global standard setters such as the International Federation of Accountants (IFAC) and more specifically the International Auditing and Assurance Standards Board (IAASB), who have called for more research to investigate the influence of culture on the convergence and operationalization of ISAs in an Islamic context. The evidence in this study shows the significance of Islamic religiosity and, more specifically, Islamic worldview on bias in auditors' judgments with negative consequences for audit quality. Global and Islamic standard setters need to consider developing strategies for auditors to recognize and mitigate the influence of religious–cultural bias on their judgments.

Second, the results of this study also support the recent findings of the International Forum of Independent Audit Regulators' (IFIAR) global annual audit inspection survey, with many instances of auditors' failure to assess the reasonableness of assumptions, including consideration of contrary or inconsistent evidence regarding accounting estimates (IFIAR, 2018, p. 10), and calls by regulators worldwide for the audit profession to implement strategies for auditors to exercise an appropriate level of professional scepticism and to increase audit quality.

Third, the recently published Framework for Audit Quality issued by the IAASB specifically highlights the direct impact of “national culture” on the judgments of accountants and auditors involved in financial reporting (IFAC, 2014b, p. 60). By “unpacking” culture into a stronger and sharper variable, namely, Islamic religiosity, this study shows the importance of this cultural variable on auditors’ judgments. More specifically, the results contribute to a better understanding of conservatism in auditors’ judgments, particularly in an Islamic context, and the potential consequences for audit quality. Additionally, the findings may also interest auditing standard setters and regulators in Pakistan, such as the ICAP and the Securities and Exchange Commission of Pakistan, in developing relevant training and audit tools to detect and prevent the impact of potential Islamic cultural bias on auditors’ conservatism and professional scepticism with consequential impact on judgments and resulting audit quality.

Finally, the findings are particularly relevant for multinational accounting firms operating in Islamic countries and firms that employ a significant number of Muslims. Global and multinational accounting firms are under increasing pressure to include measurable cultural diversity and gender-based targets regarding firm composition (Durkin, 2017). In response to demands from major clients, who will not engage with firms that do not present a diverse management team, global accounting firms are re-structuring to improve their diversity (Taurian, 2017). Thus, the current focus on increasing cultural diversity within accounting firms and in the profession makes our findings even more relevant. The findings suggest that understanding the Islamic cultural context will assist multinational auditing firms in considering the potential implications of cultural variables such as Islamic religiosity on auditors’ judgments, and assist them in developing relevant policies, procedures, and training to overcome potential consequential culturally induced bias with a negative impact on audit quality.

The findings of this study should also be considered in the light of its limitations. First, the study investigates two constructs of Islamic religiosity. However, the nature of Islamic religiosity is complex, and future research could examine the influence of other multidimensional theoretical constructs of religiosity to provide further insights into auditors’ conservatism judgments. Second, as with most single-country studies, caution needs to be exercised in generalizing the findings to other countries. Third, an issue in any religiosity study is a reliance on the self-reported responses of the participants and challenges with endogeneity and SDR bias. In this study, a “lie scale” embedded in the MRPI was used

to mitigate SDR bias (Krauss, 2011). Finally, the scenario used in this study may not fully invoke real-world pressures and contexts faced by auditors.

Overall, the results of this study suggest that future research may benefit from a further examination of auditor judgment-related issues in Islamic countries, such as those identified in this study, namely non-compliance with ISAs, inappropriately low level of professional scepticism, and conservatism leading to materially misstated financial statements. Future research should examine these and other relevant issues to provide further evidence to equip standard setters and audit professionals with further evidence to improve audit practice and audit quality.

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## Chapter 5

### Conclusions

#### 5.1 Summary of main findings

Motivated by recent investigations into the impact of culture on accounting and auditing in both Anglo-American and Islamic cultural contexts, the aim of this thesis was to investigate the influence of Islam on auditors' professional judgments. Specifically, the research was motivated by an existing gap in the literature on the impact of Islamic culture on international auditing standards convergence, including potential consequences for auditors' judgments and audit quality. This thesis selected Pakistan as a proxy for Islamic countries that have adopted ISAs. Given the significant influence of Islam on the personal and professional spheres in Pakistan, the country provides an ideal setting for this study. The thesis consists of three individual research studies that empirically examine the influence of Islam, as either a measured (auditors' Islamic religiosity level) and/or manipulated (clients' religious adherence) independent variable on auditors' professional judgments. Specifically, the objectives of the three studies are to investigate the influence of:

1. Islamic religiosity on auditors' preference for more or less judgment.
2. Clients' Islamic religious adherence and gender on auditors' judgments in an Islamic context.
3. Auditors' Islamic religiosity and clients' religious adherence on conservatism in auditors' judgments.

The three independent studies were designed to achieve the above-mentioned research objectives. To address the first research objective a survey was conducted with auditors from medium-tier auditing firms in Pakistan. To address the second and third research objectives, 2x2 between-subjects experiments were conducted with auditors in Big 4 auditing firms in Pakistan. A summary of results from the three independent studies is provided below.

##### ***5.1.1 Study 1 (Chapter 2): The influence of Islamic religiosity on auditors' preference for more or less judgment***

Study 1 (Chapter 2) addressed the first objective by investigating the following research hypotheses:

- Auditors with a high (low) Islamic religiosity score have a preference for more (less) judgment.
- Auditors with a high (low) Islamic worldview score have a preference for more (less) judgment.

- Auditors with a high (low) religious personality score have a preference for less (more) judgment.

The results provide empirical evidence that auditors' level of Islamic religiosity, on average, has a significant impact on auditors' preference for more or less judgment. Specifically, the results support the hypotheses that, on average, auditors who score high on the overall Islamic religiosity and Islamic worldview scales have a preference for more judgment. However, the results do not support the significant influence of religious personality on auditors' preference for more or less judgment.

The results contribute to the literature on auditors' judgment and decision making by providing evidence of the importance of Islamic religiosity as a cultural variable. However, the results of this study also identified a number of judgment related issues. First, a majority of the participants based their final judgment (adjustment to the provision for doubtful debt) on unverified verbal information provided by the client. This result suggests non-compliance with ISAs, in particular, ISA 500 *Audit Evidence* (IAASB, 2012f). The results also highlight issues with auditors' inappropriate evidence reliability assessments and the resulting negative consequences on audit judgment and audit quality. Additionally, the results show an inappropriately low level of professional scepticism and *conservatism exhibited by auditors in their judgments*.

#### ***5.1.2 Study 2: The influence of clients' religious adherence and client's gender on auditors' evidence reliability judgments in an Islamic context***

Study 1's findings highlighted auditors' judgment bias, non-compliance with ISAs when relying on client-provided information, and the potential consequential audit quality concerns. Study 2 extends Study 1 by examining the influence of clients' Islamic religious adherence (high vs low) and gender (male vs female) on audit evidence reliability judgments in a 2x2 between-subjects experiment. Three hypotheses were investigated in Study 2:

- Audit evidence provided by a client with high (low) religious adherence is considered by auditors to be more (less) reliable.
- Audit evidence provided by a male (female) client is considered by auditors to be more (less) reliable.

- Client's religious adherence (high vs low) will interact with the gender (male vs female) of the client and will increase (decrease) the reliability assessment score.

The results suggest that information received from a client with high religious adherence is assessed by auditors, on average, to be more reliable than information received from a client with low religious adherence. However, the gender of the client has no significant influence on auditors' audit evidence reliability judgments. The results of the interaction hypothesis show that when a client's religious adherence level is high, auditors assess the reliability of the information received from the client as "high" irrespective of their gender. However, when a client's religious adherence level is low, the gender effect becomes significant, and audit evidence received from a male source is assessed by auditors to be more reliable than that received from a female client.

Additional analysis suggests that although the level of client's Islamic religious adherence is a significant factor in auditors' evidence reliability judgments, it, however, does not significantly impact auditors' follow-up judgments of the likelihood of an adjustment or their final monetary adjustment of the client's provision for doubtful debt. However, overall, auditors recommended a relatively high reduction in the provision for doubtful debt, which is of concern. The results suggest that auditors not only trust the information provided by the client but more importantly are willing to materially reduce the provision for doubtful debt balance based on insufficient evidence of very low reliability (i.e., verbal internal evidence without any corroborating evidence in a moderate risk audit scenario). The results further confirm the findings from Study 1 and suggest that auditors exhibit an inappropriately low level of professional scepticism and conservatism in their judgments and are not complying with the specific principles of ISA 500. The results of this study suggest that auditors' professional scepticism and conservatism in an Islamic context are worth examining in further investigations.

### ***5.1.3 Study 3: The influence of auditors' Islamic religiosity level and clients' religious adherence on the level of conservatism in auditors' judgments***

Given the results of Studies 1 and 2 regarding auditors' non-compliance with ISAs, exercise of an inappropriately low level of professional scepticism, and conservatism, Study 3 (Chapter 4) extends these papers by investigating the influence of auditors' Islamic religiosity and clients' Islamic religious adherence on the level of conservatism in auditors' judgments. Prior research provides evidence that Islamic religiosity is an indicator of increased conservatism in both accounting and non-accounting

contexts. Auditors' Islamic religiosity level was measured by adopting an Islamic religiosity framework, the Muslim Religiosity Personality Inventory (MRPI), which categorizes Islamic religiosity into Islamic worldview and religious personality. Clients' religious adherence was manipulated as high versus low in a 2x2 between-subjects experiment conducted with 105 professional Chartered Accountants from the Big 4 auditing firms in Pakistan.

This study extended the research conducted in Studies 2 and 3 by providing auditors with a relatively more risky scenario (i.e., inventory write-down of near expiry infant formula inventory). The scenario also included contradictory evidence (actual sales forecast for the infant formula had not been met in the past) to the verbal audit evidence provided by the client (i.e., Sales Director) who believed that the inventory in question would be sold, with no write-down necessary. The hypotheses examined included:

- Auditors scoring high (low) on the Islamic religiosity scale will exhibit a higher (lower) level of conservatism in their judgments.
- Auditors scoring high (low) on the Islamic worldview scale will exhibit a higher (lower) level of conservatism in their judgments.
- Auditors scoring high (low) on the religious personality scale exhibit a higher (lower) level of conservatism in their judgments.
- A high (low) level of clients' religious adherence is likely to decrease (increase) the level of conservatism in auditors' judgments.
- Clients' religious adherence level (high vs low) will interact with auditors' overall Islamic religiosity level (high vs low) to decrease (increase) the level of conservatism in auditors' judgments.

The results support the hypotheses that auditors with a high score on Islamic religiosity and Islamic worldview scales exhibit a higher level of conservatism in their judgments. However, auditors' religious personality scores and clients' religious adherence do not significantly impact the level of conservatism in auditors' judgments. Further, the results of the interaction between auditors' religiosity level and clients' level of religious adherence show that when auditors' Islamic religiosity level is high, conservatism in their judgments is also high irrespective of the religious adherence level of the client

(i.e., auditors' religiosity is the key factor). However, when auditors' Islamic religiosity level is low, the level of conservatism in their judgments is decreased in the presence of a client with high religious adherence (the client's religious adherence is a significant factor). Additional analysis indicates that the auditor's perceived risk assessment of the audit issue as "high" also significantly increases the level of conservatism in their judgments.

Although the results of this study suggest that auditors who score high on the Islamic religiosity and Islamic worldview scales exhibit a higher level of conservatism in their judgments, we found that the level of conservatism is inappropriate with the resulting inventory balance being, on average, materially overstated, for all auditors. Given that auditors were provided with a relatively high-risk judgment scenario involving a near to expiry inventory, it was expected that auditors would provide a highly conservative judgment. In addition, auditors were provided with "internal verbal evidence" about the expected resale of inventory from the client (i.e., the Sales Director argued that almost all the inventory would be sold based on the projected sales forecast and no write-down would be necessary) as well as "additional contradictory evidence" concerning the accuracy of sales forecasts, with the inventory in question not achieving its sales forecast in the past. Auditors failed, on average, to write-down the inventory to its full net realizable value (i.e., non-compliance with IAS 2 *Inventories* (IFRS, 2018)). Auditors, on average, recommended an inventory write-down of between PKR 900–1250 (AUD 10.1–14.06) million. Given the planning materiality of PKR 500 (AUD 5.6) million, auditors' adjustments were materially understated with the resulting inventory and profit both materially overstated. The results further support the concerns raised by the results of Chapters 2 and 3 of this thesis about the lack of compliance with ISAs and the inappropriately low level of professional scepticism resulting in reduced audit quality and materially misstated financial information. In summary, the results indicate non-compliance with ISAs (i.e., reliance on insufficient and unreliable evidence in high audit risk scenario) and an inappropriately low level of professional scepticism leading to material misstatement, a significant concern for audit quality.

## **5.2 Contributions and implications**

By addressing and examining the objectives mentioned in the previous section through the three related research papers, this thesis aims to make a number of original and significant contributions to the international auditing literature and specifically to auditors' professional judgment research to date.



First, the findings are likely to interest global standard setters such as the International Federation of Accountants (IFAC) and, in particular, the International Auditing and Assurance Standards Board (IAASB), and their calls for more research to investigate the influence of cultural variables on auditing judgments in Islamic countries (IFAC, 2014a). Additionally, the findings are relevant for regional standard-setting bodies such as the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) and the Asian-Oceanian Standard-Setters Group (AOSSG) and their aim of facilitating the emerging Islamic convergence (AOSSG, 2011, 2014), that is, efforts by global and Islamic standard setters to identify and address the potential influence of Islamic values on the convergence of IFRS and ISAs in Islamic countries (Askari et al., 2010).

Second, the results of this thesis also support the recent findings of the International Forum of Independent Audit Regulators' (IFIAR) global annual audit inspection survey (IFIAR, 2018), which found many instances of auditors' failure to assess the reasonableness of assumptions, including consideration of contrary or inconsistent evidence regarding accounting estimates (IFIAR, 2018, p. 10). In addition, the recently published Framework for Audit Quality (IFAC, 2014b) by the IAASB highlights that "national culture" is likely to have a direct effect on the judgments of accountants and auditors involved in financial reporting (IFAC, 2014b, p. 60). By "unpacking culture" into a stronger and sharper variable, namely, Islamic religiosity, this thesis makes an original contribution to the literature and provides evidence of the importance of Islamic religiosity in understanding auditors' judgments in Islamic countries.

Third, the findings of this thesis are particularly relevant for multinational auditing firms operating in Islamic countries and also for those firms that employ a significant number of Muslims. Given the global convergence of auditing standards and the emphasis on the exercise of judgments in the principles-based ISAs, the findings in Study 1 of this thesis are particularly relevant for global audit firms. Internationally operating audit firms rely heavily on global firm policies and audit methodologies to ensure the consistency of audits across jurisdictions (Bik & Hooghiemstra, 2016). The risk-based audit methodologies embodied in the ISAs and practiced by international auditing firms require auditors to oversee or avoid certain biases in judgment and decision making. The results of the three studies collectively suggest that judgment biases can exist due to cultural (i.e., religious) influences and auditing firms should consider developing specialized training programs to eradicate such potential biases.

Fourth, global and multinational accounting firms are under increasing pressure to include measurable cultural diversity and gender-based targets in firm composition (Durkin, 2017). In response to the demands of major clients who will not engage with firms that do not present a culturally diverse management team, global accounting firms are re-structuring to improve their diversity (Taurian, 2017). Thus, the current focus on increasing cultural diversity within accounting firms and the profession makes the findings of this thesis even more relevant. In other words, the findings of this thesis suggest that understanding Islamic culture will assist multinational auditing firms in considering the potential implications of Islamic religiosity on auditors' judgments and assist them in developing relevant policies and procedures to identify such influences.

Fifth, given the incorporation of Islamic *Shariah* accounting and auditing standards within accounting and auditing domains in Islamic countries, the results of this thesis are relevant. The findings suggest that further examination of accounting and auditing judgments within Islamic countries and Islamic financial institutions is required. Finally, the findings may also interest auditing standard setters and regulators in Pakistan, such as the Institute of Chartered Accountants of Pakistan (ICAP) and the Securities and Exchange Commission of Pakistan in developing relevant training methodologies and tools to understand and eradicate any possible influence of religious or cultural biases on auditors' judgments.

### **5.3 Limitations and suggestions for future research**

The findings of this thesis should be considered in the light of its limitations.

First, and as with most single-country studies, caution needs to be exercised in generalizing the findings to other Islamic cultural contexts.

Second, Studies 1 and 3 in this thesis examined Islamic religiosity as the main independent variable and adopted a validated and reliable Islamic religiosity scale, the MRPI. An issue in any religiosity study is a reliance on the self-reported responses of the participants and challenges with endogeneity and SDR bias. In this thesis, a "lie scale" embedded in the MRPI was used to mitigate SDR bias (Krauss, 2011). However, it is still likely that the research is subject to SDR bias and endogeneity bias.

Third, the thesis investigates two constructs of Islamic religiosity, namely, Islamic worldview and religious personality. However, the nature of Islamic religiosity is very complex, and future research

should examine the influence of other multidimensional theoretical constructs of religiosity to provide further insights into auditors' judgments and decision making.

Fourth, although a thorough pilot testing of the research instrument was conducted to ensure its similarity with real-life auditing contexts, the scenarios used in this thesis may not fully invoke the pressures and contexts faced by auditors in the real world.

Fifth, the results of this thesis suggest that future research may benefit from an examination of auditor judgment-related issues identified herein. The most concerning issues with respect to auditors' professional judgments, highlighted from the results of all three studies, are auditors' non-compliance with ISAs. Given Pakistan converged to ISAs in 2005, the issues with non-compliance highlighted in this thesis are of concern. Specifically, almost all the results provided evidence that, overall, the auditors based their judgments (adjustment to provision for doubtful debts in Studies 1 and 2 and the write-down amount of inventory in Study 3) on unverified verbal information provided by the client. Given ISAs provide detailed guidelines for assessing the reliability of audit evidence, auditors' non-compliance with ISAs, specifically with regard to audit evidence assessments in an Islamic cultural context, requires additional investigation.

Additionally, a consistent finding from the three studies suggests an inappropriately low level of professional scepticism and conservatism in auditors' judgments. Given these issues are under-researched in an Islamic cultural context, future research may examine the influence of Islamic religiosity on auditors' professional scepticism and conservatism in more detail.

## Appendix A: Macquarie University ethics approval letter

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**MACQUARIE**  
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SYDNEY · AUSTRALIA

18 November 2015

Professor Martinov-Bennie  
International Governance and Performance Research Centre  
Faculty of Business and Economics  
Macquarie University  
NSW 2109

Dear Professor Martinov-Bennie

**Reference No:** 5201400804

**Title:** *Influence of Islam on auditors' professional judgement in Pakistan*

Thank you for submitting the above application for ethical and scientific review. Your application was considered by the Macquarie University Human Research Ethics Committee (HREC (Human Sciences & Humanities)) at its meeting on 30 October 2015 at which further information was requested.

The requested information was received with correspondence on 13 November 2015. The HREC (Human Sciences and Humanities) Executive considered your responses at its meeting held on 17 November 2015.

I am pleased to advise that ethical and scientific approval has been granted for this project to be conducted at:

- Macquarie University

This research meets the requirements set out in the *National Statement on Ethical Conduct in Human Research* (2007 – Updated March 2014) (the *National Statement*).

This letter constitutes ethical and scientific approval only.

### **Standard Conditions of Approval:**

1. Continuing compliance with the requirements of the *National Statement*, which is available at the following website:

<http://www.nhmrc.gov.au/book/national-statement-ethical-conduct-human-research>

2. This approval is valid for five (5) years, subject to the submission of annual reports. Please submit your reports on the anniversary of the approval for this protocol.

3. All adverse events, including events which might affect the continued ethical and scientific acceptability of the project, must be reported to the HREC within 72 hours.
4. Proposed changes to the protocol must be submitted to the Committee for approval before implementation.

It is the responsibility of the Chief investigator to retain a copy of all documentation related to this project and to forward a copy of this approval letter to all personnel listed on the project.

Should you have any queries regarding your project, please contact the Ethics Secretariat on 9850 4194 or by email [ethics.secretariat@mq.edu.au](mailto:ethics.secretariat@mq.edu.au)

The HREC (Human Sciences and Humanities) Terms of Reference and Standard Operating Procedures are available from the Research Office website at:

[http://www.research.mq.edu.au/for/researchers/how\\_to\\_obtain\\_ethics\\_approval/human\\_research\\_ethics](http://www.research.mq.edu.au/for/researchers/how_to_obtain_ethics_approval/human_research_ethics)

The HREC (Human Sciences and Humanities) wishes you every success in your research.

Yours sincerely



**Dr Karolyn White**

Director, Research Ethics & Integrity,  
Chair, Human Research Ethics Committee (Human Sciences and Humanities)

This HREC is constituted and operates in accordance with the National Health and Medical Research Council's (NHMRC) *National Statement on Ethical Conduct in Human Research* (2007) and the *CPMP/ICH Note for Guidance on Good Clinical Practice*.

## Appendix B: Research instrument for Study 1



**MACQUARIE**  
University

Dear Participant,

My name is Nazia Adeel, and I invite you to participate in this research, which is being conducted to meet the requirements of the Ph.D. thesis at Macquarie University. As you are aware, auditors' professional judgment is a key aspect of the audit process. However, relatively little is known about professional judgment in Pakistani audit context. The purpose of my Ph.D. and this study is to address auditors' professional judgments in Pakistan.

The thesis is supervised by Professor Nonna Martinov-Bennie [International Governance and Performance Research Centre (IGAP), nonna.martinov-bennie@mq.edu.au, Ph +61 2 9850 1926] and Professor Chris Patel [Department of Accounting and Corporate Governance, chris.patel@mq.edu.au, Ph +61 2 9850 7825] at the Faculty of Business and Economics, Macquarie University, Australia.

If you decide to participate in this study, kindly complete the attached questionnaire. The questionnaire has three parts: **Part-I** provides an audit scenario about a company with a specific audit issue (doubtful debts) that requires your assessment; **Part-II** asks for some demographic and other information; and **Part-III** contains a scale that measures personal values. It will take approximately 25-30 minutes to complete the questionnaire.

The questionnaire is anonymous, and any information or personal details gathered in the course of the study are confidential. No individuals or their firms will be identified in any publication of the results. Data will be analyzed in aggregate form, held solely by the researchers, Professor Nonna Martinov-Bennie, Professor Chris Patel, and Mrs. Nazia Adeel, and will not be used for any other purpose. The results of this study will be published as part of a Ph.D. thesis, which will be available at Department of Accounting and Corporate Governance, Macquarie University. The results may further be published in the form of a journal article(s) and conference paper(s). You may also request a summary of the results directly from the researchers.

Participation in this study is voluntary; you are not obliged to participate and required information is provided to help you make an informed decision about your participation. The return of the questionnaire will be regarded as consent to use the information for research purposes. Thank you so much for assisting with this research.

Kindly feel free to contact us for further information. Your cooperation is highly appreciated.

Nazia Adeel

[nazia.adeel@students.mq.edu.au](mailto:nazia.adeel@students.mq.edu.au) Ph+61 0 469843157

Department of Accounting and Corporate Governance

Faculty of Business and Economics

Macquarie University

Australia

Macquarie University Human Research Ethics Committee has approved the ethical aspects of this study. If you have any complaints regarding ethical aspects of your participation in this research, you may contact the committee through the Director Research Ethics & Integrity at (+61 02 9850 7854 or [ethics@mq.edu.au](mailto:ethics@mq.edu.au)). For further information about this project, you can also contact the project's local focal person Mr. Khawar Ali Sher at ([khawar.ali@khi.iba.edu.pk](mailto:khawar.ali@khi.iba.edu.pk) # +923215113643) in Pakistan.

### Instructions to participants

This questionnaire examines auditors' exercise of professional judgment in Pakistan using an audit case scenario. It has the following parts:

**Part-I** provides relevant background information in relation to a specific audit issue (doubtful debts) and requires a series of assessments in relation to this issues based on the information provided.

**Part-II** collects brief demographic information and some additional assessments.

**Part-III** consists of a personal values scale, which requires your responses.

Your assessments should consider the practicalities of the situation and reflect the real world considerations and compromises which auditors face. Please make your assessments reflective of practice, and if possible, take into consideration actual actions and behaviours in similar situations.

The questionnaire is completely anonymous, and no person or their firm will be identified during the data collection, analysis, or in publications. The results will be reported in aggregate form.

There are **no right or wrong answers** to **Part-I** and **Part-III** of the questionnaire.

Once you complete **Part-I**, place it in the smaller envelope and seal it.

Please immediately proceed to **Part-II**. Please do not go back and change responses to prior parts of the questionnaire that have already been completed.

After completing **Part-II** and **Part-III**, place these and the smaller envelope in the larger envelope provided.

Thank you for your assistance and valuable input to this research.

## Part-I

## Background information

Assume that you are currently working on the annual audit of one of your firm's largest clients, Nature Pakistan Limited (Nature). Nature is a leading food company, and its shares are listed on the Karachi and Lahore stock exchanges. The principal activity of the company is manufacturing and wholesale of food products (dairy, confectionary, infant nutrition and drinking water). You are an audit senior on Nature's audit engagement for the year ended 30<sup>th</sup> June 2015. This is your third consecutive audit of Nature. The planning materiality for the current audit has been set at Rs 500 million. Profit before tax (PBT) for the year ended 30<sup>th</sup> June 2015 is Rs 7140 million. The information from previous year audit file suggests that accounting estimates on the prior audits have been reasonable and not materially misstated.

It is now mid-August 2015, and you are reviewing the adequacy of Nature's provision for doubtful debts, which is the only material issue remaining. The following accounts receivable aging schedule summarized the actual balances and predicted provision for doubtful debts based on the average percentages (%) of the balances not collected in prior years. A staff auditor has correctly calculated the total estimated amount of doubtful debt in Table 1 below:

Table 1: Calculation for the provision for doubtful debt as at 30<sup>th</sup> June 2015:

Age category of outstanding debtor balances	Balance of debtors for each category (Rupees in million)	% History of doubtful debts not collected	Predicted provision for doubtful debt (Rupees in million)
Under 60 days	3500	1	35
61-90 days	3000	3	90
91-120 days	900	15	135
Over 120 days	2000	50	1000
Totals	9400		1260

While finalizing your review, the Chief Financial Officer (CFO) provides the audit team with some relevant additional information. According to the CFO, the two accounts, which make up Rs 2000 million of debt over for more than 120 days, will be paid in full by each debtor. In both cases, the delay in payment has been caused because to the seasonal payment cycle of the two customers, and the payment will be made within a few weeks.

## Audit Assessments

Using the background information given in the case, please complete the following series of assessments by placing a cross(x) at the appropriate number on the scale:

- 1 What method would you prefer for assessing the client's provision for doubtful debts?  
Please tick only one of the below:
- ☐ Percentage method based on history of previous years' amounts not collected
- ☐ Judgment based on the aged balances of each individual overdue debtor together with the review of the analysis of their sales and past history of payments
- 2 What is your perceived level of risk in relation to the collectability of debtors?
- | 1        | 2 | 3 | 4        | 5 | 6 | 7         |
|----------|---|---|----------|---|---|-----------|
| very low |   |   | moderate |   |   | very high |
- 3 Please indicate the amount by which you believe that the provision for doubtful debt should be reduced by (Rs in million):
- |   |     |     |     |     |      |      |
|---|-----|-----|-----|-----|------|------|
| 0 | 200 | 400 | 600 | 800 | 1000 | 1200 |
|---|-----|-----|-----|-----|------|------|

Please fold and seal your completed responses to **Part-I** with the information sheet and instructions in the smaller envelope provided prior to completing Part-II and Part-III



## Part-II

### Demographic and other information

- 1 Your age (years)  
☐ 20-30      ☐ 30-40      ☐ 40-50      ☐ 50-60      ☐ 60-70
- 2 Your gender:    ☐ Male              ☐ Female
- 3 Your nationality      ☐ Pakistani      ☐ Other, please specify:
- 4 In which country you were born (if different from nationality)? Please specify:
- 5 What is your professional qualification:  
☐ a practicing member of the Institute of Chartered Accountants of Pakistan (ICAP)  
☐ a practicing member of The Institute of Cost & Management Accountants of Pakistan (ICMAP)  
☐ a practicing member of Pakistan Institute of Public Finance Accountants (PIPFA)  
☐ a practicing member of any other body, please specify:
- 6 Which of the following best describes the current position in your audit firm:  
☐ Junior/Assistant      ☐ Senior      ☐ Manager      ☐ Partner      ☐ Senior/Managing Partner  
☐ Executive Director/Country Partner      ☐ Other (please specify)
- 7 Number of years of audit experience you have:
- 8 How many years of audit experience do you have at current level:
- 9 Your firm is:  
☐ Big 4                      ☐ Non-Big 4 (International)      ☐ Other (please specify)
- 1 Please indicate by placing a cross(x) on the appropriate number on the scale for following series of  
0 questions:
- a How familiar are you with International Standards on Auditing (ISAs) issued by the International Auditing and Assurance Standards Board (IAASB), as implemented by Institute of Chartered Accountants of Pakistan (ICAP):  

1	2	3	4	5	6	7
very unfamiliar			neither familiar nor unfamiliar			very familiar
- b Your experience with the treatment of provision of doubtful debts:  

1	2	3	4	5	6	7
no prior experience			moderate experience			dealt with very often
- c Please indicate which type of auditing standards are more relevant to Pakistan:  

1	2	3	4	5	6	7
rule-based standards			mix of & principles			principle-based standards
- d Please indicate your level of preference for applying judgment during an audit process:  

1	2	3	4	5	6	7
very low			neither low nor high			very high
- e Please indicate your level of preference for applying specific rules during an audit process:  

1	2	3	4	5	6	7
very low			neither low nor high			very high

### Part-III

#### Personal values scale:

Based on the statements below, please identify the view that most accurately reflects your own by marking (✓) the appropriate box

	Item	Strongly Agree	Somewhat Agree	Undecided	Somewhat Disagree	Strongly Disagree
1	A man should leave his job when told by the doctor that he will die within a short time.					
2	Allah will not forgive people who commit sins intentionally.					
3	Damage and destruction that occur in the world are the negative results of non-believers' actions.					
4	Allah is knowledgeable of the movements of the sand particles at the bottom of the ocean.					
5	Prophets (PBUH) teachings are for the advantage and well-being of Muslims only					
6	All Islamic laws can be modified to fulfil contemporary needs					
7	In emergency situations, Islam allows Muslims to abandon obligatory prayer (Namaz)					
8	To fully develop their nations, Muslims cannot completely follow Islamic teachings.					
9	If Allah wills to destroy a place, both Muslims and non-Muslims living there may be affected.					
10	People who impart beneficial knowledge to others will be rewarded for it in this world only.					
11	Islamic values are applicable only in certain situations, places and times.					
12	All deeds (Sunnah) performed by Prophet are guided by revelation.					
13	Prophet (PBUH) created laws that were not given to him by Allah					
14	If a person is raised as a Muslim they will not necessarily die as a Muslim					
15	All human activities must be done for the sake of Allah					
16	Allah teachings fulfill all of His creatures' needs					
17	Islamic teachings do not fulfill the needs of human beings' natural state					
18	Worldly life cannot be separated from the afterlife					
19	Allah will not test a person who internalizes and practices religion					
20	Certain orders ordained by Allah can be violated to achieve success in worldly life					

Based on the statements below, please identify the practices that most accurately reflect your own by marking (✓) the appropriate box

	Item	Strongly Agree	Somewhat Agree	Undecided	Somewhat Disagree	Strongly Disagree
1	I encourage my family members to follow the teachings of the Prophet (PBUH)					
2	I try to understand the meaning of Quranic words/verses					
3	I make effort to have ablution (Wuzu') at all times					
4	I make an ongoing effort to increase the frequency of my non-obligatory (Nafil) prayers					
5	I make effort to understand Islamic law					
6	I take advantage of opportunities to understand Islam with my family					
7	I invite others to perform obligatory prayer (Namaz)					
8	I discuss religious issues with my friends					
9	I find time to recite the Quran even if I am busy					
10	I make effort to internalize the Prophet's ethical conduct in my daily life					
11	I feel sad when Ramazan ends					
12	I set aside money every year for charity					
13	I feel at peace when I hear the Quran recited					
14	I love my brothers and sisters in Islam as I love myself					

Based on the statements below, please identify the practices that most accurately reflect your own by marking (✓) the appropriate box

	Item	Strongly Agree	Somewhat Agree	Undecided	Somewhat Disagree	Strongly Disagree
1	I do not enter a person's house until I am invited					
2	I respect other people's opinions					
3	I feel worried when I hurt my parents					
4	I do not expose the shortcomings of others					
5	I do not neglect my friends' dignity					
6	I make effort to make my guests feel as comfortable as possible					
7	I make effort not to display my personal good deeds					
8	I use public buses, walkways, etc. with care/respect					
9	I feel happy when someone says something good about one of my friends					
10	I will keep a person's identity hidden when I talk about them and they are not present					
11	I prefer to work than to beg					
12	I refer to the people who know when I feel uncertain about Islamic rulings					
13	I like to help the poor without anyone knowing					
14	I work/study hard to achieve my goals in the specified time					

Thank you so much for your time and participation. If you are interested in receiving a summary of the results from the researcher. Please indicate if your consent and provide your email address:

☐ I am interested in receiving the results of this research and my email address is:

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The return of the questionnaire will be regarded as consent to use the information for research purposes. If you need further information, do not hesitate to contact us. Thank you very much for providing input to this project.

**Nazia Adeel (PhD candidate)**

Macquarie University  
Australia

Please fold and seal your completed responses to Part-I & Part-II in the larger envelope provided

## Appendix C: Research Instrument for Study 2



Dear Participant,

My name is Nazia Adeel, and I invite you to participate in this research, which is being conducted to meet the requirements of the Ph.D. thesis at Macquarie University. As you are aware, auditors' professional judgment is a key aspect of the audit process. However, relatively little is known about professional judgment in Pakistani audit context. The purpose of my Ph.D. and this study is to address auditors' professional judgment in Pakistan.

The thesis is supervised by Professor Nonna Martinov-Bennie [International Governance and Performance Research Centre (IGAP), nonna.martinov-bennie@mq.edu.au, Ph +61 2 98501926] and Professor Chris Patel [Department of Accounting and Corporate Governance, chris.patel@mq.edu.au, Ph +61 2 98507825] at the Faculty of Business and Economics, Macquarie University, Australia.

If you decide to participate in this study, kindly complete the attached questionnaire. The questionnaire has two parts; **Part-I** provides an audit scenario about a company with a specific audit issue (doubtful debts) that requires your assessment and **Part-II** asks for some demographic and other information. It will take approximately 25-30 minutes to complete the questionnaire.

The questionnaire is anonymous, and any information or personal details gathered in the course of the study are confidential. No individuals or their firms will be identified in any publication of the results. Data will be analyzed in aggregate form, held solely by the researchers, Professor Nonna Martinov-Bennie, Professor Chris Patel, and Mrs. Nazia Adeel, and will not be used for any other purpose. The results of this study will be published as part of a Ph.D. thesis, which will be available at Department of Accounting and Corporate Governance, Macquarie University. The results may further be published in form of a journal article(s) and conference paper(s). You may also request a summary of the results directly from the researchers.

Participation in this study is voluntary; you are not obliged to participate and required information is provided to help you make an informed decision about your participation. The return of the questionnaire will be regarded as consent to use the information for research purposes. Thank you so much for assisting with this research.

Kindly feel free to contact us for further information. Your cooperation is highly appreciated.

Nazia Adeel  
[nazia.adeel@students.mq.edu.au](mailto:nazia.adeel@students.mq.edu.au) Ph+61 0 469843157  
Department of Accounting and Corporate Governance  
Faculty of Business and Economics  
Macquarie University  
Australia

Macquarie University Human Research Ethics Committee has approved the ethical aspects of this study. If you have any complaints regarding ethical aspects of your participation in this research, you may contact the committee through the Director Research Ethics & Integrity at (+61 02 9850 7854 or [ethics@mq.edu.au](mailto:ethics@mq.edu.au)). For further information about this project, you can also contact the project's local focal person Mr. Khawar Ali Sher at ([khawar.ali@khi.iba.edu.pk](mailto:khawar.ali@khi.iba.edu.pk) # +923215113643) in Pakistan

### Instructions to participants

This questionnaire examines auditors' exercise of professional judgment in Pakistan using an audit case scenario. It has the following parts:

**Part-I** provides relevant background information in relation to a specific audit issue (doubtful debts) and requires a series of assessments in relation to the issue based on the information provided.

**Part-II** collects brief demographic information and some additional assessments.

Your assessments should consider the practicalities of the situation and reflect the real world considerations and compromises which auditors face. Please make your assessments reflective of practice, and if possible, take into consideration actual actions and behavior in similar situations.

The questionnaire is completely anonymous, and no person or their firm will be identified during the data collection, analysis or in publications. The results will be reported in aggregate form.

There are **no right or wrong answers** to **Part-I** of the questionnaire.

Once you complete **Part-I**, place it in the smaller envelope and seal it.

Please immediately proceed to **Part-II**. Please do not go back and change responses to prior parts of the questionnaire that have already been completed.

After completing **Part-II**, place this and the smaller envelope in the larger envelope provided.

Thank you for your assistance and valuable input to this research

## Part-II

### Background Information

Assume that you are currently working on the annual audit of one of your firm's largest client, Nature Pakistan Limited (Nature). Nature is a leading food company, and its shares are listed on the Karachi and Lahore stock exchanges. The principal activity of the company is manufacturing and wholesale of food products (dairy, confectionary, infant nutrition and drinking water). You are an audit senior on Nature's audit engagement for the year ended 30<sup>th</sup> June 2015. This is your third consecutive audit of Nature. The planning materiality for the current audit has been set at Rs 500 million. Profit before tax (PBT) for the year ended 30<sup>th</sup> June 2015 is Rs 7140 million. The information from previous year audit file suggests that accounting estimates on the prior audits have been reasonable and not materially misstated. It is now mid-August 2015, and you are reviewing the adequacy of Nature's provision for doubtful debts, which is the only material issue remaining. The following accounts receivable aging schedule summarized the actual balances and predicted provision for doubtful debts based on the average percentages (%) of the balances not collected in prior years. A staff auditor has correctly calculated the total estimated amount of doubtful debt in Table 1 below:

Table 1: Calculation for the provision for doubtful debt as at 30<sup>th</sup> June 2015:

Age category of outstanding debtor balances	Balance of debtors for each category (Rupees in million)	% History of doubtful debts not collected	Predicted provision for doubtful debt (Rupees in million)
Under 60 days	3500	1	35
61-90 days	3000	3	90
91-120 days	900	15	135
Over 120 days	2000	50	1000
Totals	9400		1260

While finalizing your review, the Chief Financial Officer (CFO), Mr (Mrs) Khan provides the audit team with some relevant additional information. According to the CFO, the two accounts which make up Rs 2000 million of debt overdue for more than 120 days, will be paid in full by each debtor. In both cases, the delay in payment has been caused because the seasonal payment cycle of the two customers, and the payment will be made within a few weeks.

Mr (Mrs) Khan is a member of the Institute of Chartered Accountants of Pakistan (ICAP). He (She) has 15 years of accounting experience and has been the CFO of Nature for the last five years.

You have been on the audit team for the last 3 years and are aware that Mr (Mrs) Khan strictly follows the Quran and Sunnah in matters pertaining to personal and professional life [Mr (Mrs) Khan prefers to follow her own judgment rather than the Quran and Sunnah in matters pertaining to personal and professional life].

Using the background information given in the case, please complete the following series of assessments by placing a cross(x) at the appropriate number on the scale:

- Please fold and seal your completed responses to **Part-I** along with information sheet and instructions in the smaller envelope provided prior to completing **Part-II**.



## Part-II

### Demographic and other information

- 1 Your age (years)  
☐ 20-30      ☐ 30-40      ☐ 40-50      ☐ 50-60      ☐ 60-70
- 2 Your gender:    ☐ Male      ☐ Female
- 3 Your nationality      ☐ Pakistani      ☐ Other, please specify:
- 4 In which country you were born (if different from nationality)? Please specify:
- 5 What is your professional qualification:  
☐ a practicing member of the Institute of Chartered Accountants of Pakistan (ICAP)  
☐ a practicing member of The Institute of Cost & Management Accountants of Pakistan (ICMAP)  
☐ a practicing member of Pakistan Institute of Public Finance Accountants (PIPFA)  
☐ a practicing member of any other body, please specify:
- 6 Which of the following best describes the current position in your audit firm:  
☐ Junior/Assistant      ☐ Senior      ☐ Manager      ☐ Partner      ☐ Senior/Managing Partner  
☐ Executive Director/Country Partner      ☐ Other (please specify)
- 7 Number of years of audit experience you have:
- 8 How many years of audit experience do you have at current level:
- 9 Your firm is:  
☐ Big 4      ☐ Non-Big 4 (International)      ☐ Other (please specify)
- 10 Please indicate by placing a cross(x) on the appropriate number on the scale for following series of questions:
- a How familiar are you with International Standards on Auditing (ISAs) issued by the International Auditing and Assurance Standards Board (IAASB), as implemented by Institute of Chartered Accountants of Pakistan (ICAP):  

1	2	3	4	5	6	7
very unfamiliar			neither familiar nor unfamiliar			very familiar
- b Your experience with the treatment of provision of doubtful debts:  

1	2	3	4	5	6	7
no prior experience			moderate experience			dealt with very often
- c Please indicate how religious you perceive the CFO to be  

1	2	3	4	5	6	7
not at all religious			neither high nor low			very religious

Thank you so much for your time and participation. If you are interested in receiving a summary of the results from the researcher please provide your consent and email address below:

☐ I am interested in receiving the results of this research and my email address is:

---

The return of the questionnaire will be regarded as consent to use the information for research purposes. If you need further information, do not hesitate to contact us. Thank you very much for providing input to this project.

**Nazia Adeel (PhD candidate)**  
Macquarie University  
Australia

## Appendix D: Research Instrument for Study 3



**MACQUARIE**  
University

Dear Participant,

My name is Nazia Adeel and I invite you to participate in this research, which is being conducted to meet the requirements of PhD thesis at Macquarie University. As you are aware, auditors' professional judgement is a key aspect of the audit process. However, relatively little is known about professional judgement in Pakistani audit context. The purpose of my PhD and this study is to address auditors' professional judgement in Pakistan.

The thesis is supervised by Professor Nonna Martinov-Bennie [International Governance and Performance Research Centre (IGAP), nonna.martinov-bennie@mq.edu.au, Ph +61 2 98501926] and Professor Chris Patel [Department of Accounting and Corporate Governance, chris.patel@mq.edu.au, Ph +61 2 98507825] at the Faculty of Business and Economics, Macquarie University, Australia.

If you decide to participate in this study, kindly complete the attached questionnaire. Questionnaire has three parts; **Part-I** provides an audit scenario about a company with a specific audit issues (inventory valuation) that requires your assessment, **Part-II** asks for some demographic and other information & **Part-III** contains a scale that measures personal values. It will take approximately 25-30 minutes to complete the questionnaire.

The questionnaire is anonymous and any information or personal details gathered in the course of the study are confidential. No individuals or their firms will be identified in any publication of the results. Data will be analysed in aggregate form, held solely by the researchers, Professor Nonna Martinov-Bennie, Professor Chris Patel, and Mrs. Nazia Adeel, and will not be used for any other purpose. The results of this study will be published as part of a PhD thesis, which will be available at Department of Accounting and Corporate Governance, Macquarie University. The results may further be published in form of a journal article(s) and conference paper(s). You may also request a summary of the results directly from the researchers.

Participation in this study is voluntary; you are not obliged to participate and required information is provided to help you make an informed decision about your participation. The return of the questionnaire will be regarded as consent to use the information for research purposes. Thank you so much for providing assistance to this research.

Kindly feel free to contact us for further information. Your cooperation is highly appreciated.

Nazia Adeel

[Nazia.adeel@students.mq.edu.au](mailto:Nazia.adeel@students.mq.edu.au) Ph+61 0 469843157

Department of Accounting and Corporate Governance

Faculty of Business and Economics

Macquarie University

Australia

Macquarie University Human Research Ethics Committee has approved the ethical aspects of this study. If you have any complaints regarding ethical aspects of your participation in this research, you may contact the committee through the Director Research Ethics & Integrity at (+61 02 9850 7854 or [ethics@mq.edu.au](mailto:ethics@mq.edu.au)). For further information about this project, you can also contact the project's local focal person Mr Khawar Ali Sher at ([khawar.ali@khi.iba.edu.pk](mailto:khawar.ali@khi.iba.edu.pk) # +923215113643) in Pakistan

### **Instructions to Participants**

This questionnaire examines auditors' exercise of professional judgement in Pakistan using an audit case scenario. It has the following parts:

**Part-I** provides relevant background information in relation to two specific audit issues (inventory valuation) and requires a series of assessments in relation to each of the two issues based on the information provided.

**Part-II** collects brief demographic information and some additional assessments.

**Part-III** consists of personal values scale, which requires your responses.

Your assessments should consider the practicalities of the situation and reflect the real world considerations and compromises which auditors face. Please make your assessments reflective of practice, and if possible, take into consideration actual actions and behaviour in similar situations.

The questionnaire is completely anonymous and no person or their firm will be identified during the data collection, analysis or in publications. The results will be reported in aggregate form.

There are **no right or wrong answers** to **Part-I** and **Part-III** of the questionnaire.

Once you complete **Part-I**, place it in the smaller envelope and seal it.

Please immediately proceed to **Part-II**. Please do not go back and change responses to prior parts of the questionnaire that have already been completed.

After completing **Part-II** and **Part-III**, place these and the smaller envelope in the larger envelope provided.

Thank you for your assistance and valuable input to this research.

## Part-I

### Scenario

#### Background information:

Nature Pakistan Limited (Nature) is one of your audit firm's largest clients. The annual audit for the year ending 30<sup>th</sup> June 2015 is almost complete except for one item related to the valuation of specialized inventory which is the only material issue remaining. The issue that has arisen is a potential material write-down of infant formula inventory valued at Rs 7800 million. This is a significant portion of the total inventory and will expire in December 2015. The planning materiality for the audit engagement has been set at Rs 500 million and the estimated gross Profit before Tax (PBT) for the year is Rs 7140 million. In the past, inventory problems were immaterial, but there are concerns that the amount will be material this year if infant formula inventory is written-down to its Net Realisable Value (NRV) that is approximately Rs 6300 million. It is late-August 2015 and you just had a meeting with the Sales Director about the inventory write-down issue. The Sales Director argued that almost all of the inventory will be sold based on the projected sales forecast and no write-down is needed, "if sales forecasts are accurate, we can easily sell this inventory in targeted area (Alipur town and adjoining areas) before the expiry date". Although the company has achieved its overall targeted sales forecasts for previous years, this has not always been the case for the infant formula inventory.

The Sales Director holds a Master in Business Administration from one of the top universities in Pakistan and has held similar positions in other companies and has been with Nature for the last 4 years. You have been on the audit team of Nature for the last 3 years and you know that Sales Director does (not) pray at the company's prayer room.

#### Audit Assessments:

Using the background information given in the case, please complete the following series of assessments by placing a cross(x) at the appropriate number on the scale:

- 1 What is your perceived level of risk in relation to the inventory valuation:

1	2	3	4	5	6	7
very low			moderate			very high

- 2 In the light of the additional information provided by the Sales Director regarding sales forecast of infant formula inventory, what is the likelihood of you recommending an inventory write-down:

1	2	3	4	5	6	7
very unlikely			neither likely nor unlikely			very likely

- 3 If you do recommend an inventory write-down based on the additional information, what is the likelihood that you would agree with Sales Directors' assessment of no write-down of inventory:

1	2	3	4	5	6	7
very unlikely			neither likely nor unlikely			very likely

- 4 Please indicate the amount of inventory write-down required in your opinion (Rs in million):

0	250	500	750	1000	1250	1500
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Please fold and seal your completed responses to

**Part-I** along with information sheet and instructions in the smaller envelope provided  
prior to completing **Part-II**

## Part-II

### Demographics and other information:

- 1 Your age (years)  
☐ 20-30      ☐ 30-40      ☐ 40-50      ☐ 50-60      ☐ 60-70
- 2 Your gender:    ☐ Male      ☐ Female
- 3 Your nationality      ☐ Pakistani      ☐ Other, please specify:
- 4 In which country you were born (if different from nationality)? Please specify:
- 5 What is your professional qualification:  
☐ a practicing member of the Institute of Chartered Accountants of Pakistan (ICAP)  
☐ a practicing member of The Institute of Cost & Management Accountants of Pakistan (ICMAP)  
☐ a practicing member of Pakistan Institute of Public Finance Accountants (PIPFA)  
☐ a practicing member of any other body, please specify:
- 6 Which of the following best describes the current position in your audit firm:  
☐ Junior/Assistant      ☐ Senior      ☐ Manager      ☐ Partner      ☐ Senior/Managing Partner  
☐ Executive Director/Country Partner      ☐ Other (please specify)
- 7 Number of years of audit experience you have:
- 8 How many years of audit experience do you have at current level:
- 9 Your firm is:  
☐ Big 4      ☐ Non-Big 4 (International)      ☐ Other (please specify)
- 10 Please indicate by placing a cross(x) on the appropriate number on the scale for following series of questions:
- a How familiar are you with International Standards on Auditing (ISASs) issued by the International Auditing and Assurance Standards Board (IAASB), as implemented by Institute of Chartered Accountants of Pakistan (ICAP):
- |                 |   |   |                                 |   |   |               |
|-----------------|---|---|---------------------------------|---|---|---------------|
| 1               | 2 | 3 | 4                               | 5 | 6 | 7             |
| very unfamiliar |   |   | neither familiar nor unfamiliar |   |   | very familiar |
- b Your experience with the treatment of inventory write-down:
- |                     |   |   |                     |   |   |                       |
|---------------------|---|---|---------------------|---|---|-----------------------|
| 1                   | 2 | 3 | 4                   | 5 | 6 | 7                     |
| no prior experience |   |   | moderate experience |   |   | dealt with very often |
- c Please indicate how religious you perceive the Sales Director to be:
- |                      |   |   |                      |   |   |                |
|----------------------|---|---|----------------------|---|---|----------------|
| 1                    | 2 | 3 | 4                    | 5 | 6 | 7              |
| not at all religious |   |   | neither high nor low |   |   | very religious |

### Part-III

#### Personal values scale:

Based on the statements below, please identify the view that most accurately reflects your own by marking (✓) the appropriate box

	Item	Strongly Agree	Somewhat Agree	Undecided	Somewhat Disagree	Strongly Disagree
1	A man should leave his job when told by the doctor that he will die within a short time.					
2	Allah will not forgive people who commit sins intentionally.					
3	Damage and destruction that occur in the world are the negative results of non-believers' actions.					
4	Allah is knowledgeable of the movements of the sand particles at the bottom of the ocean.					
5	Prophets (PBUH) teachings are for the advantage and well-being of Muslims only.					
6	All Islamic laws can be modified to fulfil contemporary needs.					
7	In emergency situations, Islam allows Muslims to abandon obligatory prayer (Namaz)					
8	To fully develop their nations, Muslims cannot completely follow Islamic teachings.					
9	If Allah wills to destroy a place, both Muslims and non-Muslims living there may be affected.					
10	People who impart beneficial knowledge to others will be rewarded for it in this world only.					
11	Islamic values are applicable only in certain situations, places and times.					
12	All deeds (Sunnah) performed by Prophet are guided by revelation.					
13	Prophet (PBUH) created laws that were not given to him by Allah					
14	If a person is raised as a Muslim they will not necessarily die as a Muslim					
15	All human activities must be done for the sake of Allah					
16	Allah teachings fulfil all of His creatures' needs					
17	Islamic teachings do not fulfil the needs of human beings' natural state					
18	Worldly life cannot be separated from the afterlife					
19	Allah will not test a person who internalizes and practices religion					
20	Certain orders ordained by Allah can be violated to achieve success in worldly life					

Based on the statements below, please identify the practices that most accurately reflect your own by marking (✓) the appropriate box

	Item	Strongly Agree	Somewhat Agree	Undecided	Somewhat Disagree	Strongly Disagree
1	I encourage my family members to follow the teachings of the Prophet (PBUH)					
2	I try to understand the meaning of Quranic words/verses					
3	I make effort to have ablution (Wuzu') at all times					
4	I make an ongoing effort to increase the frequency of my non-obligatory (Nafil) prayers					
5	I make effort to understand Islamic law					
6	I take advantage of opportunities to understand Islam with my family					
7	I invite others to perform obligatory prayer (Namaz)					
8	I discuss religious issues with my friends					
9	I find time to recite the Quran even if I am busy					
10	I make effort to internalize the Prophet's ethical conduct in my daily life					
11	I feel sad when Ramazan ends					
12	I set aside money every year for charity					
13	I feel at peace when I hear the Quran recited					
14	I love my brothers and sisters in Islam as I love myself					

Based on the statements below, please identify the practices that most accurately reflect your own by marking (✓) the appropriate box

	Item	Strongly Agree	Somewhat Agree	Undecided	Somewhat Disagree	Strongly Disagree
1	I do not enter a person's house until I am invited					
2	I respect other people's opinions					
3	I feel worried when I hurt my parents					
4	I do not expose the shortcomings of others					
5	I do not neglect my friends' dignity					
6	I make effort to make my guests feel as comfortable as possible					
7	I make effort not to display my personal good deeds					
8	I use public buses, walkways, etc. with care/respect					
9	I feel happy when someone says something good about one of my friends					
10	I will keep a person's identity hidden when I talk about them and they are not present					
11	I prefer to work than to beg					
12	I refer to the people who know when I feel uncertain about Islamic rulings					
13	I like to help the poor without anyone knowing					
14	I work/study hard to achieve my goals in the specified time					

Thank you so much for your time and participation. If you are interested in receiving a summary of the results from the researcher, please indicate your consent and provide your email address:

☐ I am interested in receiving the results of this research and my email address is:

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The return of the questionnaire will be regarded as consent to use the information for research purposes. If you need further information, do not hesitate to contact us. Thank you very much for providing input to this project.

**Nazia Adeel (PhD candidate)**  
Macquarie University  
Australia

Please fold and seal your completed responses to **Part-I & Part-II** in the larger envelope provided



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