Research Journal of Finance and Accounting www.iiste.org
ISSN 2222-1697 (Paper) ISSN 2222-2847 (Online)
Vol.6, No.9, 2015

The Scope of the External Audit and Audit Expectations: A Survey Study

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Abstract
This study examines the expectations among external and internal auditors and investment analysts for increased responsibilities for external auditors of banks to report to the public on the effectiveness of internal controls and risk management systems. The study survey focused on recent changes in audit requirements for the banks in the Republic of Macedonia, and in that respect incorporates analysis of perceptions and attitudes of external and internal auditors and investment analysts. Interviews were conducted with investment analysts in order to identify relevant expectations from modern assurance services. The results of the survey and interviews analysis suggest that external auditors were divided in their attitudes about acceptance of additional responsibilities for a statutory audit engagement, while the majority of internal auditors surveyed thought that external auditors should provide opinion on the effectiveness of internal control system and risk management system in their report. The results of the study provide good insight for statutory audit policy makers in their understanding of the expectations gap among different stakeholders.
Keywords: audit reports, internal control effectiveness, risk management audit, assurance model

1. Introduction

The purpose of statutory audit at its core is to provide an independent opinion to shareholders whether financial statements prepared by the board of directors give true and fair view of company's financial results and position. However, we need to review this definition and confront it with present reality. Nowadays organisations have a variety of stakeholders with various expectations of the audit. In UK, according to the Companies Act 2013 auditors are required to audit the directors' report and compare it with the information provided in financial statements as well to audit the directors' remuneration report. For listed companies in UK, auditors are required to review the Corporate Governance Compliance statement. In USA, Sarbanes-Oxley Act enacted in 2002, for companies listed on domestic stock markets, expects from the appointed auditors to perform integrated audit and report on managements' assessment of the effectiveness of internal control systems as well as the "true and fair view" presentation of financial statements.

In the absence of disclosure of private information about internal control, investors are unlikely to be fully informed about the nature, extent, and quality of internal controls. This makes it difficult for them to observe managers' efforts to manage risks or to provide reliable information by maintaining adequate internal controls. As a result of increased importance of the stakeholder theory and requirements and expectation imposed by different groups influenced by the business, external audit faces contemporary challenges both as regards the subject matter audited and the ways auditors carry out their activities. Corporate financial reporting has enhanced the range of other corporate disclosures-including corporate and social responsibility, corporate governance and risk. Inevitably several questions occupy contemporary audit theory, among these questions I define the research problem. Is it acceptable to conclude that historical financial information is the ultimate and from stakeholders view sufficient subject matter on which audit reports will be issued in the near future? Does the results and added value to the firm net assets expressed in solely financial terms will still satisfy stakeholders needs or the sound internal control environment and systems for effective risk management will be part of the subject matter information provided annually to various interested parties? The research methodology was designed to address the following hypotheses:

1. Assessment of the effectiveness of an internal control system in addition to true and fair presentation of financial statements produces valuable information to stakeholders
2. Appropriateness of risk management and disclosure practices influence the reliability of results and net worth presented in financial statements
3. Suitable criteria frameworks for the subject matter covering risk management and internal control systems could be developed and successfully followed by different companies
4. Integrated audit opinions regarding faithful presentation of financial information, appropriate risk management and disclosure, effectiveness of internal control systems provide higher level of assurance to shareholders and other stakeholders
5. The sole purpose of traditional audits could be enhanced with risk management and internal controls without significant long-term cost burden for large companies

2. Literature review

The external audit function has evolved and developed significantly over the last 100 years. The purpose of auditing developed from strict focus on fraud and errors at the beginning stage of development to providing credibility to external financial reporting process and increase reliability of information provided by the management for various stakeholders. Matthews (2006) suggests that the primary objective of early audits was the detection of fraud with a secondary objective of ensuring the accuracy of reports given by managers. Auditing techniques at this early stage generally consisted of extensive vouching of cash disbursements and a detailed check of bookkeeping records. During the 21 century the idea of accounting systems reliance approach came into light as a mean of reducing extensive tests of details. Chatfield (1977) points out that it was not "until the 1920s that auditors based their examinations on preliminary appraisals of internal control". In the 1960s and 1970s heralded an era when so called "Systems Auditing" dominated. The reasoning behind this approach was apportioned reliance on the accounting system and controls implemented to test system's ability to process data. Auditors looked for assurance regarding the internal control system in order to reduce the extent of substantive work performed.

The years after followed the appearance of audit risk model (ARM), directly as a result of series of papers produced on statistical sampling. The earliest versions of the ARM emerged from attempts to quantify the assurance obtained from statistical tests of the system of internal control. This audit risk model describes the interrelation between the overall level of audit risk, and the levels of inherent risk, control and detection risk. Audit procedures, particularly substantive procedures were focused on those account balances given higher risks assessments. However, rather than encouraging reliance on controls, the introduction of the ARM coincided with a move towards substantive testing. The Business Risk Audit was intended to widen the focus of the audit, from audit risk to business risk, where business risk is defined as the risk that an entity will fail to meet its objectives (Eilifsen et al., 2001).The audit methodology correspondently have changed and revolutionised from predominantly substantive audit to business risk auditing as it has been analysed in contemporary times.

Nowadays, auditors provide valuable advice to management by using their expertise to evaluate internal control and identify possible improvements to the clients' internal information systems. Much has been written on the subject of reporting on internal controls before and after introduction of SOX in 2002. Dopuch and Simunic (1980) have stated that in addition to increased credibility of financial statements for external users, audit services are appreciated as a mean to strengthen organisation's control system. Auditors are credited with inventing the term "Internal Control" and their expertise in the matter of control evaluation has traditionally been drawn on by clients. Hermanson (2000) stated that stakeholders considered internal control important for the decision making process and voluntary reporting motivates managers to improve internal control procedures. Further research that extends on the study of Hermanson also tries to determine if mandatory disclosure on internal controls is perceived as valuable. Many researchers have showed results that internal controls disclosures affect investors' perception of earnings quality (Doyle et al., 2007). In the only study to examine lending decisions, Schneider and Church (2008) found that lenders' decisions are negatively impacted by adverse internal control opinions as compared to unqualified ones. Shelton and Whittington (2008) in their study of informative significance of audit reports on effectiveness of internal controls have concluded that these reports provide information about the risk of investment. Their findings supported the view that investors increase company risk assessments where there is adverse audit opinion regarding the effectiveness of internal controls and significant difference in the likelihood of making recommendation for a share to their clients.

Proponents of reporting on effectiveness of internal controls also argue that such requirements will improve internal control systems, i.e. control weaknesses will be identified and remedied sooner and ongoing management involvement will result in improved control systems (Rittenberg & Miller, 2005). Nicolaisen (2004), as a Chief Accountant of the SEC, remarked that "being able to represent that an appropriate control system is in place strengthens public confidence and encourages investment in our nation's industries."

Nevertheless, there are research studies, although less in number, that provide evidence for the opposite. McMullen and O'Reilly-Allen (2002) researched the subject of relevance of assurance on internal controls by giving participants a case study. They wanted to examine whether participants' perceptions of the reliability of financial statements changed when given certain information. The results of the study indicate that users' perceptions do not appear to be affected by the inclusion of an auditor report on firms' internal controls.

Reflection should be given to research papers published by authoritative professional bodies (ICAEW, 2008) concluding in opposite direction, there's no room for enhanced annual audit requirements and statutory audit should retain focused on single purpose. Stakeholders' expectations should be meet by utilizing additional assurance services in conjunction with the relative power of stakeholders determine by the organisation. These requirements for preservation of the current subject matter scope of annual statutory audit limited to fair and truthful presentation of financial statements have been clearly stated by ICAEW researchers.

3. Methodology

Considering the specifics of the research problem and presented hypotheses, my decision was to adopt and follow a combination, mixed research design of concurrent type, a questionnaire for the two focus groups of external and internal auditors and concurrently interviews have been conducted with institutional investors in order to explore their views and expectations on the external audit function. Someone will argue that these methods are commonly accepted when it comes to social research work and measuring attitude of selected population. In fact, survey research designs are flexible enough to cause problems defining and putting boundaries to what represents survey research strategy and what does not. The questionnaires were delivered to internal and external auditors through e-mail and were collected in the same way. Interviews were conducted with analysts for institutional investors since it is reasonable to expect that they are not so familiar with the subject of the research, therefore the opportunity for personal and immediate conversation was used in order to provide further explanations on research topics and questions asked. Semi-structured interview allowing interviewee to express additional view and perceptions to those questions preliminary planned was developed and completed.

I've chosen to use mail interviewing through prepared questionnaire for external and internal auditors because it has the advantage of the absence of interviewer which can be considered as less threatening by the interviewee showing willingness to answer sensitive questions. But, the absence of the interviewer means lack of additional explanations regarding the questionnaire or providing assistance to respondents while answering questions and puts high demands on the design of the paper questionnaire.

The design of the questionnaire is crucial and number of issues need to be considered. These include asking relevant and accurate questions, phrasing questions logically, asking questions in sequence and piloting the questionnaire. According to Zikmund (1991), there are two basic criteria that need to be considered in determining the questions that should be asked and included in the questionnaire survey. These two criteria are the relevance of the questionnaire and the accuracy of the questionnaire. Questionnaire relevancy refers to the extent to which the questions address the research questions, and therefore should be included in the questionnaire. Questionnaire accuracy refers to the extent to which the information collected by the designed questionnaire is reliable and valid.

The questions can be open-ended or closed-ended. In case of open-ended questions, the participants are free to give their own answers in their own words. In closed-ended questions, the participants are free to select from a number of possible answers provided. Collis and Hussey (2003) indicated that open-ended questions offer the advantages and disadvantages that the respondents are able to give their opinions as precisely as possible in their own words, but they can be difficult to analyse. However, closed - ended questions are very convenient for collecting data and are usually easy to analyze. They are also answered more easily and quickly and therefore could be expected to help with the overall response rate to questions.

It was necessary to construct a questionnaire of reasonable length and the questionnaire consisted of three pages including the cover page. The questions were grouped together into two main parts, the first one asking about the technical capacity and experience of the firm and the interviewee, the second one contained attitude questions based on Likert scale. The questionnaire used in this research used two different kinds of scales; the nominal scale and the ordinal scale. In the first part of the questionnaire, the nominal scale was used to collect data on the background information about the participants. External auditors were invited to tick a particular classification or characteristic such as number of employees in the audit firm or internal audit department, average years of experience, number of audit engagement undertaken in the last year and past five years, frequency and type of training provided to employees. In the second part of the questionnaire, a five-point Likert scale was used to measure the participants' perceptions regarding the identified auditing issues. The Likert scale was designed to examine the extent to which external auditors agreed or disagreed with several statements. This part of the questionnaire for external auditors contained 21 statements, majority of them segregated in two parts: statements regarding the perceptions about the importance and consequences of effective internal controls and questions in respect of the risk management system (see appendix 1.1). Additional statements were included in order to investigate the perception of the participants regarding the following issues: (a) internal audit function and its contribution towards efficient engagement (b) availability of sufficient guidance for implementation of effective internal control and risk management systems; (c) the role of management recommendation letters; (d) relative importance of control reliance strategy for the overall audit process.

The second part of the questionnaire used to collect data from internal auditors contained 16 questions, aimed to identify internal auditors' perceptions and views on the importance of internal control systems, appropriateness of guidance on internal controls and risk management provided by the Central Bank and the suitability of eventually integrated opinions to be provided by auditors (See appendix 1.1). In addition to the types of questions used for external auditors, this questionnaire was designed to evaluate perceptions regarding the cost/benefit of regular audits performed by external auditors and supervisory bodies for improvements in risk management and internal control systems. The questionnaire involved extra third part with combination of ordinal and nominal scale statements or questions, designed to assess the relationship with the Audit Committee, its structure and expertise, issues of particular interest and frequency and duration of Audit Committee meetings.

The central focus point of the research was covered by Likert scale type of statements aimed at identification and summarization of attitudes and beliefs. Since, the research problem is oriented on exploring the potential for enhanced responsibility of external auditors, opinions and attitudes regarding the subject matter information have been accepted as proper object of measurement for the study. Likert scales (originally devised by R. Likert in 1932) of the kind used in these questionnaires are devices to discover strength of feeling or attitude towards a given statement or series of statements and the implication here is that the higher the category chosen, the greater the strength of disagreement, but care has to be taken not to read too much in these ranked scales. Similar to nearly all psychometric scale measures, the Likert scale consists of multiple items that typically are summed or averaged to produce a more reliable measure than could be obtained by use of a single item. They are usually, though not always, on a three, five or seven-point range and ask respondents to indicate rank order of agreement or disagreement by circling the appropriate number. They certainly arrange individuals or objects from the highest to the lowest, but the intervals between each may not be the same. We cannot say that the highest rating 5, is five times higher than the lowest (which is 1). All that can be said is that they indicate order. In spite of these limitations, Likert scales can be useful, as long as the wording is clear. I've been sufficiently careful while constructing the statements and questions in order to avoid duplicate questions, which can produce confusion among respondents and often neutral non-determinable responses. Typical wording labels for five categories were used and these are: Strongly Agree (1), Agree (2), Neither Agree Nor Disagree (3) , Disagree (4) and Strongly Disagree (5).

Although Likert scales have been used in social research to often, Likert items and their corresponding Likert scales are subject to response distortions. Central tendency bias may result from respondent reluctance to select extreme response categories (Nicholls, 2010). Acquiescence bias can result when respondents choose to agree with statements because of a desire to choose what they believe is the ''correct'' or otherwise most appropriate answer. Similarly, social desirability bias may result when respondents attempt to portray themselves or an organization to which they belong in a favourable light (Fisher & Tellis, 1998). These effects can be minimised by varying attitude statements so that some are expressed in a positive form while others are expressed in the negative. Therefore, some of the statements requested level of agreement with a positive causality and relationship with investigated items, others asked for expression of level of agreement on identified negative relationship or causality among investigated items.

For the **face-to-face interviews** with investment analysts, at the start of the interviewing process I've introduced the respondents to the subject, research question, and a list of topics that we would like to discuss with them. The interviews were planned to last a maximum of 45 minutes with the agreement of the 12 respondents with considerable experience as investment advisors. My principal intention was to identify the importance of internal control or risk management information for assessment of potential investment performed by investment advisors. Thus I started my interviews asking the respondents to briefly introduce themselves and provide information on their practice. At times during the interviews we tried to reformulate what the respondents said to confirm understanding of what they were telling. Questions were also added if there was a need for clarification of issues the respondents brought to my attention during the interviews. Interviewees were asked to provide information on their views and perceptions regarding the purpose of statutory audit of financial statements of banks, whether auditors responsibilities and reporting requirements in respect of annual audit exercise should be enhanced, eventual changes of audit report format, additional requirements for disclosures related to risk and internal controls, extent of relying to risk information and internal controls in the decision making process etc (see Appendix 1.2 for interview contents). The summaries of the interviews are the base of my empirical findings.

4. Sample description and results of the survey and interview analysis

Questionnaires were sent to 32 respondents currently holding the position of head of internal audit department or senior internal auditor in all banks in the Republic of Macedonia. Also the study covered external auditors specialized in auditing and assurance services within the banking industry and therefore questionnaires were sent to 19 external auditors working with local offices of international audit firms usually engaged to perform statutory audit in the banking industry. Out of 32 planned 27 internal auditors provided response to our invitation to comment on assurance services related to effectiveness of internal control and risk management systems. Fourteen out of 19 external auditors surveyed have successfully returned completed questionnaire and their answers were subject of further analysis.

First, responses from external auditors were analysed through the use of descriptive statistics. The analysis of responses provided by external auditors has showed that the average experience of auditors involved in the financial sector is between 6-10 years, all surveyed audit firms have been engaged in more than 20 audit engagements for the past five years and more than 5 audit engagements in the banking industry for 2013. The respondents have replied that usually they receive general type of training related to planning and executing audit engagements with occasionally specific training in financial industry auditing. Training sessions are organized internally with duration of few days and delivered usually once a year.

Through the questionnaire used for internal auditors we had the opportunity to explore the experience of internal auditors employed in the banking industry and the historical background of their departments, areas of professional work including years of successful establishment and functioning. Internal audit departments have been effectively functioning for the past 14 years on average with actual reported years ranging from 8 to 19. Regarding the capacity, heads of internal audit departments have stated that the number of internal auditors engaged varied, but, the majority of banks (78%) had between one and five employees. The average experience of internal auditors was 12 years. Most of respondents (55%) have replied that their department on average had above 20 engagements annually.

More than 75% of respondents have identified their agreement or strong agreement that internal controls are essential for the survival of organisations. Also, surveyed external auditors had clear perceptions that effective internal control system results in reduced risk of material misstatements due to fraud. Auditors were consistent in their views of the inverse relationship between poor internal controls and organisations' ability to achieve their strategic and operational goals. However, different views were expressed for the relationship between poor internal controls and poor financial condition of an organisation, responses ranging equally from strong agreement to neutral perception with mean of 1.88 which represents tendency towards agreement with the surveyed statement on average. All respondents either agreed or strongly agreed that their use of management recommendation letters have contributed to improvement of internal control systems. Similarly, our investigation of external auditors' perceptions in respect of the relationship between poor internal controls and the quality of financial reporting process have highlighted relative inconsistence in perceptions although all respondents except one have either agreed or strongly agreed that poor internal controls result in poor quality of financial reporting. The variability of provided answers was significant with calculated standard deviation of 0.78 on provided scale responses.

External auditors were asked to give their insights and experienced views whether effective internal controls contribute significantly for increased efficiency in completion of the audit engagement. Precisely half of the respondents have strongly agreed that effective design and functioning of internal controls contributes to increased efficiency of their work, the other half expressed just agreement with such statement. Greater variability in responses was observed when auditors were required to state whether they believe that high level of gained control assurance means greater probability for reduced risk of material misstatements in financial statements than just high level of substantive assurance. Although 63% of respondents have expressed strong agreement with the suggested relationship, 25% of them have stated neutral views on the relationship between combined assurances gained through the engagement and decreased risk of material misstatements incorporated in financial statements. The variability of views is confirmed by the standard deviation of scale responses in this case being 0.86.

Interesting perceptions the respondents showed when they were asked to express their beliefs regarding anticipated greater probability for expressing unqualified audit opinion when control reliance strategy is accepted and control assurance gained. Although the majority of respondents agreed that control assurance will certainly lead to greater probability for unqualified audit opinion to be issued, considerable portion of respondents were neutral (38%). One of the questions observed perceptions of external auditors in respect of the relative appropriateness of developed frameworks for assessing internal controls effectiveness compared to frameworks used to form opinions as to the objectivity and fair view provided by financial statements. It can be observed that responses were equally distributed in the range of agreement to disagreement with mean value of 2.88 and standard deviation of 0.78. It can be concluded that external auditors' had dissimilar views on the state of development of the yardstick when it comes to effective design and implementation of internal controls, which can be interpreted as potential obstacle for complete adoption of further requirements auditors' to report on effectiveness of internal control systems as their regular statutory responsibility. Almost same responses were received when auditors provided insight and evaluated the quality of guidance prescribed by the Central bank related to the implementation of sound risk management systems, when the mean calculated amounted to 2.75 and standard deviation 0.66.

Noteworthy results were obtained when external auditors were asked to provide their views and perceptions whether they should have the responsibility to report annually as part of statutory audit engagements to the general public on fair presentation and objectivity of financial statements, effectiveness of implemented risk management and internal control systems with formulated integrated opinions. Approximately 50% of respondents agreed with such requirements to be imposed to external auditors, 38% disagreed with the possibility additional responsibilities to be accepted on regular annual basis by external auditors, while 12% where neutral on this issue. The mean that was calculated on scale responses was again 2.88 close to neutral response on average with standard deviation of 0.93.

Again questionable perceptions were identified among external auditors regarding their opinion whether engaging specialists is necessary for the purpose of evaluation and assessment of risk management systems and results in costs in excess of benefits from regular annual assessment. Although the majority of surveyed auditors disagreed with this statement, 38% of them shared the same viewpoint as suggested by the question. External auditors were hesitant when evaluated the possibility for conflict goals set for the annual audit rising from integrated opinions and consequently imposing limitation to audit procedures related to financial statements accuracy, objective presentation and disclosure. Approximately one third of respondents thought that there is danger with the multipurpose audit to sacrifice the extent and depth of audit procedures related to appropriate presentation of financial statements. One third was neutral towards such relationship and the rest of respondents didn't support such possibility for reduced quality of audit work related directly to the financial statements. One of the questions explored the level of reliance that external auditors place on the work of internal auditors in respect of testing effectiveness of internal controls and risk management systems. Except one respondent who actually strongly agreed that the work of internal auditors reduces extent of external auditors' testing, the rest of respondents expressed neutral views. It can be inferred that external auditors believe the work of internal auditors neither reduces nor increases the volume of their activities, i.e. there is poor interest for the results of the internal auditors' work.

All internal auditors have either agreed or strongly agreed that internal controls are essential for the survival of organisations and effective internal control systems reduce the risk of fraud. Similarly all except one surveyed internal auditor have shared the view that poor internal controls decrease the quality of financial reporting process. When asked to evaluate the contribution of management recommendation letters for improvement of internal control system majority of internal auditors agreed or strongly agreed that recommendation letters improve internal controls, however there was considerable variety of opinions received ranging from disagree (11%) to strongly agree (11%) where 22% of respondents were neutral. The standard deviation determined in this case was 0.82. Significant variety of opinions were identified when internal auditors were asked to provide their beliefs whether external auditors should be charged with increased responsibilities and be held responsible for conducting integrated audit engagements. Although considerable number (67%) agreed or strongly agreed with such extended requirements 22% disagreed and 11% were neutral. On average the mean calculated in this case was 2.11 with standard deviation of 1.2 which represents significant fluctuation in scale responses. Interesting results were obtained when internal auditors' were asked to evaluate and match costs and benefits from increased responsibilities imposed on external auditors' as a result of increased regulatory requirements by the Central bank, where 66% have decided to express neutral standpoint, which can be interpreted as lack of understanding or assessment of potential benefits from multipurpose audit. Certainly, poor information on benefits can be explained with the limitations and absence of considerable past experience since the requirements are newly introduced and have been in place for no more than 18 months.

Internal auditors had divided views on the relative appropriateness of guidance and regulations imposed by the Central Bank in respect of implementation of both, effective internal control and risk management systems, were approximately half respondents agreed that banks are provided with sufficient and adequate guidance and the others expressed neutral thoughts.

When asked to evaluate external auditors' reliance on work performed by internal auditors related to assessment of effectiveness of internal controls, on scale from 1 to 10 (10 meaning complete reliance and utilization of results) respondents provided variety of assessments ranging from 2 to 8 with the mean value of 4.33 meaning limited reliance.

Part C of the questionnaire contained questions on cooperation and relationship between internal auditors and members of Audit Committees. Internal auditors believe that the Audit Committee is more interested in issues related to the adequacy and effectiveness of procedures for minimization of financial risks and control procedures in place for securing efficient, effective and economic operations than effective internal control procedures related to the process of preparing reliable and accurate information and the security of the information systems. On scale from 1 to 10 (10 meaning to distant relationship) internal auditors have evaluated their current relationships and closeness, arriving at mean value of 5, meaning not to distant nor close relationship with members of the Audit Committee. Such results obviously hold room for future improvement and more close cooperation between internal auditors and members of the Audit Committee.

As mentioned before, interview instrument has been used to collect primary data from investor advisors. Such approach have been seen as appropriate one, enabling interviewer help interviewees closely understand questions important for the research and collect precise answers related to the subject researched. First, respondents were asked to consider what they believe is the purpose of an audit of financial statements of banks. Knowledge of audit objectives might be an important factor in understanding the nature of auditing and scope of annual statutory audit services provided by external auditors. Interviewees have provided similar opinions stating that the statutory audit of financial statements of banks is conducted with the purpose of providing reasonable assurance whether financial statements give true and fair view, and are free of material misstatements and errors.

The interview further explored whether investment advisors seek for modifications in the format of audit report as currently prescribed and requested by International Standards on Auditing. 58% of the interviewees expressed satisfaction of the current format which is strict and structured, and users should be able to draw conclusions based on their prior understanding of modified audit reports and circumstances requiring the issuance. The rest of the respondents shared their own view that auditors should offer their opinion as regard the bank performance and highlight areas that need to be improved.

In order to evaluate information needs of investment advisors, our interviewees were first asked to state which are the three most important contents of the financial statements. Their views were that income (revenues), operating results and their analysis as well as equity structure are the most important contents of financial statements they need for analysis purposes. Then the interviewees were invited to evaluate the relevance of audited information on effectiveness of risk management and internal controls (financial and operating) system for the investment analysis process. Most of the interviewees (83%) have declared that audited information on effectiveness of internal controls and risk managements systems could increase the level of confidence that potential investors have in the eventual decision to invest their money.

Finally, interviewees were required to assess whether the scope of annual statutory audit should be extended and incorporate other additional information except financial statements on which auditors will express independent opinion. Two thirds of the respondents were satisfied with the level of disclosures provided by bank management and credibility provided by external auditors and one third of them recognized that separate disclosures of compliance with relevant bank laws and regulations are necessary.

5. Conclusions

This paper examines the expectations of stakeholders of statutory audit in respect of the importance of internal control and risk management assurance and prospects for possible increased scope of the statutory audit in the banking industry. As detailed through the survey study and interview analysis, internal and external auditors including investments advisors, have different perspectives on the importance of internal controls and risk management for the results, financial stability and operation of banks.

Although internal auditors would like to impose increased liability to their external fellows, investment advisors and external auditors have shown certain degree of caution or limited level of importance of audited information in respect of effectiveness of internal control and risk management systems. General users' needs for audited information are still attached to financial statements solely, and credible information on effectiveness of internal control or risk management systems should be subject to incident or exceptional assurance services not part of regular statutory audit. However, as long as listed companies or large banking holding companies are concerned, increased disclosure practices and assurance requirements are expected trends.

This paper contributes to the extensive literature covering the subject matter of the statutory audit and contents of the audit report. It provides evidence on the perceptions and expectations of external auditors, internal auditors and investors from the audit. However, these perceptions can be influenced and shaped by variety of factors and variables outside the objective and scope of the research, such as a different risk appetites, control supportive or contrary attitudes, ownership and management structure and interactions etc.

The findings of this study is limited only to Republic of Macedonia because it only reflects the views of the respondents employed as external, internal auditors and investors in Macedonia. These views may be influenced by the culture, regulations and the system of the country. Thus, the findings of this study may not be capable of being extended to other countries.

Consideration should be given to the fact that the research covered only external auditors engaged in the banking industry, also internal auditors employed in the banking sector. Auditors both external and internal engaged and employed in manufacturing and other service lines were not taken into consideration for the research since they were short of experience associated with the costs and benefits of multipurpose annual audit.

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Appendix 1.1 Part B Questions of External and Internal Auditors' Survey Questionnaire
B. Perceptions regarding the internal control and risk management systems
External auditors
1. Internal controls are essential for the survival of organisation.
2. Effective internal control system reduces the risk of fraud.
3. Poor internal controls can significantly impair organisation's financial condition.
4. Poor internal controls reduce the quality of financial reporting.
5. Poor internal controls decrease the ability of an organisation to achieve its strategic and operating goals.
6. Management recommendation letters significantly contribute the improvement of internal controls system.
7. Effective design and functioning of internal controls system contributes for improved audit efficiency.
8. High level of control assurance means lower risk of material misstatements in financial statements than substantive assurance only.
9. Effective internal controls system significantly reduces the assessment of entity's business risk.
10. For you, control assurance gained from effective and efficient internal control system means greater security in formulating unqualified opinion for the audit of financial statements.
11. Frameworks available to you for assessment of internal control system effectiveness are more weakly defined and developed than the framework for preparation and formulating opinion to the financial statements.
12. External auditors engaged for regular statutory audit should report to the general public integrally for: the effectiveness of internal control system, adequacy of risk management system and true and fair presentation of financial statements.
13. National Bank of Republic of Macedonia provides sufficient regulation, additional guidance and supervisory memos which can be used as framework (criteria) if opinion is requested on the effectiveness of risk management systems.
14. The assessment of effectiveness of internal control system over financial reporting has effect on the assessment of risk management system effectiveness and opposite.
15. Effective risk management system reduces the risk of material misstatements incorporated in financial statements.
16. Banks characterized with absence of significant weaknesses related to internal control and risk management systems are less risky for acceptance or continuance of audit engagements.
17. Time required for completion of an audit of financial statements decreases when internal control and risk management systems are adequate.
18. Activities for assessment of risk management systems require engagement of specialists who significantly increase costs above benefits of regular assessment.
19. If the purpose of regular statutory audit is extended to expression opinion in respect of internal control and risk management system effectiveness, there is significant threat auditors to reduce the debth of procedures related to financial statements testing.

20. The adequacy of relationship between business risk and quality of financial reporting of an entity are equally important in decision making.
21. Internal audit contributes for a reduction in tests performed on internal control and risk management systems.

Internal auditors

1. Internal controls are essential for the survival of organisation.
2. Effective internal control system reduces the risk of fraud.
3. Poor internal controls can significantly impair organisation's financial condition.
4. Poor internal controls reduce the quality of financial reporting.
5. Management recommendation letter prepared by external auditors significantly contributes the improvement of internal controls system.
6. Poor internal controls decrease the ability of an organisation to achieve its strategic and operating goals.
7. External auditors engaged for regular statutory audit should report to the general public integrally for: the effectiveness of internal control system, adequacy of risk management system and true and fair presentation of financial statements.
8. Effective risk management system reduces the risk of material misstatements incorporated in financial statements.
9. Regular annual assessment of risk management systems requires engagement of specialists who significantly increase costs above benefits of regular assessment.
10. Regular external audits and controls by relevant supervisory bodies performed on internal control and risk management systems contribute for improvement of internal audit function and achievement of organisational goals.
11. From your experience, considering the requirements of the National Bank from the external audit of banks, external auditors with their recommendations are capable for significant contribution to the improvement of internal control and risk management systems.
12. External auditors' work reduces the volume of your activities related to the system of internal controls.
13. Increased external audit costs (as a result of increased requirements with the National Bank's Decision on contents of audit of performance and annual financial statements of banks) are lower than the benefits of such audit for the bank.
14. To which extent do you think external auditors are using the results of your tests performed over internal controls?
15. National Bank of Republic of Macedonia provides sufficient regulation, additional guidance and supervisory memos for implementation of adequate internal controls system.
16. National Bank of Republic of Macedonia provides sufficient regulation, additional guidance and supervisory memos for implementation of adequate risk management system.

Appendix 1.2 Interview for investigation of perceptions and attitudes of investors related to the audit of banks

PART A

Personal data

1) Name and surname:
2) Firm:
3) Industry:
4) Position:
5) Contact information:
   - Phone:
   - E-mail:

PART B

Interview – Questions

1. From your point of view, what is the purpose of financial statements audit in commercial banks?
2. Do you think that the current format of audit report could be modified to fit interests of users of audited financial statements?
3. Do you think that auditors should guarantee the accuracy of financial statements?
4. Do you think that auditors should provide early warnings related the possibility for clients' bankruptcy?
5. Which are the three most important things for you from audited financial statements?
6. Do you need and how relevant for your analysis are audited information related to the effectiveness of internal controls (financial and operating) and effectiveness of the risk management system?
7. Do you think that the scope of annual statutory audit of banks should be extended to include other additional information except financial statements for which the auditor should prepare and express opinion (describe what kind of information and if banks are already disclosing such information in public)?