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The External Auditing and Those Charged with Governance

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Abstract: The purpose of the present study was to identify the communication extent between external auditors and those charged with governance to restrict management and financial corruption depending on ISA260 and ISA265. To achieve the study objective, 21-item questionnaire was developed that addresses different aspects of an enterprise in terms of financial statement reporting, distortions, internal control efficiency, assignment of responsibilities and strategies, etc. Out of 120 questionnaires sent to audit practitioners (111) questionnaires were received representing response rate of 92.5%. The study concluded that communication is well placed between external auditors and those charged with governance as shown by varied mean scores and such communication restricts managerial and financial corruption on all aspects of an enterprise. Researchers recommend greater concentration on communication and enhance the communication process between external auditors and those charged with governance due to its effect in supporting strengths and avoid weaknesses in the internal control process and reduce distortions related to procedures and processes which in turn reduces managerial and financial corruption.

Key words: External auditing, charged with governance, distortions, internal control efficiency, practitioners, communication

INTRODUCTION

Corruption has long been a problem as it is today and has become a source of concern both domestically and globally (Hope, 2014). There are two types of corruption, i.e., financial and managerial like bribe, kickbacks (Begovic, 2005), embezzlement and fraud misstatements and poor internal control that might plague many public and private firms. Although, the aim from corruption practices is to obtain personal gain, the result would be disastrous, i.e., collapse of an organization.

To restrict corruption, organizations should take proper means and procedures and adopt effective mechanisms like governance that refers to the way by which the internal and external relations of an organization are managed (Anonymous, 2016). The internal relations of an organization refer to how functions and procedures are implemented through individuals who take responsibility on workflow, carrying out of duties and timing and relationship among individuals whether horizontal or vertical. The external relations include regulation of the dealings with stakeholders outside the organizations like external audit that aim at demonstrating accuracy and fairness of financial statements.

The concepts discussed earlier have taken a significant part in the business environment considering their impact on business organizations. The present study will address one aspect of governance, i.e., those charged with governance and an external stakeholder (external audit) for purpose of safeguarding organizations from corruption.

Statement of the problem: Governance is considered paramount in restricting managerial and financial corruption (Thawriya, 2017). The procedures and rules emphasized by governance ensure running of work smoothly. The implementation of such procedures and rules is tasked to individuals referred to by ISA260 as those charged with governance and defined as [*Those charged with governance. The person (s) or organization (s) (for example, a corporate trustee) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process. For some entities in some jurisdictions those charged with governance may include management personnel for example, executive members of a governance board of a private or public sector entity or an owner-manager] (ISA., 2017). When these persons implement the entity processes some may inattentively commit mistakes that impact fairness of the financial reporting. So, external auditing becomes important because it plays an objective

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role for controlling processes of the entity and ensures accuracy, thereby enhance trust of financial statement users.

Communication bridges between those charged with governance (governance implementers) and the controllers (external auditing) as mandated by ISA260 and ISA265. From this point, the current study investigates the extent of communication between external auditing and those charged with governance to restrict managerial and financial corruption in light of the ISA260 and ISA265.

Study questions: This study is based on two questions:

- What is the communication extent between external auditing and those charged with governance?
- Does the communication between external auditing and those charged with governance conduits to restricted managerial and financial corruption?

A glance to ISA260 and ISA265 shows close association between external auditing and those charged with governance to restrict managerial and financial corruption. So, both study questions were merged into one main question:

What is the extent of communication between external auditing and those charged with governance to restrict managerial and financial corruption?

Objective of the study: The objective of the current study is to identify the extent of communication between external auditing and those charged with governance to restrict managerial and financial corruption in accordance with ISA260 and ISA265.

Significance of the study: The importance of this study is threefold. First because it addresses external auditing that is significant to improve enterprise processes and increase reliability of fairness of the financial statements. In addition, the significance of the present study stems from the importance of governance in reducing managerial and financial corruption. Finally, this study addresses the negative impacts of managerial and financial corruption on both the firm in particular and community in general.

Hypothesis: The study main hypothesis: "the extent of communication between external auditing and those charged with governance does not conduit to restriction of managerial and financial corruption has emanated from the study questions: what is the extent of communication between external auditing and those charged with governance? How such communication would restrict managerial and financial corruption?

Prior study: The review of the related literature reveals a number of themes related to corporate governance and external auditing. A study by Al-Baidhani (2012) entitled "the nature of a dynamic relationship between audit committee and auditors both internal and external" showed that the auditing committee which viewed as one of internal governance mechanisms can serve as a connection loop that facilitates communication between the board of directors and internal and external auditors. A study by Hafiza (2013). "The role of corporate governance in restricting managerial and financial corruption: field study" found that the cooperation between board of directors as a means of governance and implementation of external auditing restricts financial and managerial corruption. Some of the studies reviewed investigated corporate governance and managerial and financial corruption. Yousef (2015) "Importance of Corporate Governance in enhancing Control and Combating Corruption: Case Study on Jordan Petroleum Company" showed that corporate governance is an effective tool to combat managerial and financial corruption and to reinforce control and resolve problems among different stakeholders.

Entitled "The Role of Governance Mechanisms in Restricting Managerial and Financial Corruption" showed that the application of corporate governance is an effective means to deal with managerial and financial corruption problem. In addition, governance assists in attracting investments and reduces capital flight and related corruption. Al Shawawreh (2009) "Governance Rules and Evaluate its Role in Corruption Combat and Prevention at Jordanian Public Joint-Stock Companies" showed that application of corporate governance rules is an economic and social necessity and commitment to governance rules at public joint-stock companies assists combat corruption and favoritism.

A study by Mariam and Sabrina (2016) "The Role of Corporate Governance Mechanisms in Combating Managerial and Financial Corruption: Case Study Algerian People's Credit Bank (Moghnia Agency)" demonstrated that using the internal auditing as one of governance mechanisms has an effect and promising consequences regarding managerial and financial corruption. A study conducted by Mohammad (2016) "ExternalAudit as a Mechanism to Activate Governance at Companies in Algeria" concluded that as a mechanism of external governance, external audit aims at reducing disputes and problems in the enterprise in terms of fraud and manipulation. Bedard and Compernolle (2014) "The External Auditor and the Audit Committee" revealed that as external governance mechanism, quality assurance of the external audit strengthens trust in the auditor's report thereby eliminating collusive practices that lead tocorruption. The previous discussion supports the purpose from the current study that is to identify the role of external audit and those charged with governance in order to reduce managerial and financial corruption. The present study distinguishes from other studies in that it defines the extent of communication and component parts that contribute to reduce managerial and financial corruption.

External audit and those charged with governance: Before discussing external audit, we need to define audit in general. Suliman (2014) described audit as to scrutinize the internal control system, vouchers, documents and all invoices of an entity carefully in order to obtain a neutral technical opinion about fairness of the financial statements and financial position of the enterprise at the end of certain time period. Audit is also defined as an organized methodological process of objective evaluation of evidences confirming certain economic events to make sure they are consistent with standards (Lutfi, 2007). On the other hand, external auditor was described as a function practiced by an external auditor independent from the entity, ho audits the financial statements, commitment and operation in order to provide confirmation to financial statement users through a neutral technical opinion regarding accuracy and fairness of the financial statements (Thawriya, 2017). From the previous discussion, one may see that the auditing profession in general and external auditing in particular are both aiming at identifying extent of financial statements and whether are reflect reality or not? The external audit will restrict practices that distort financial statements like intentional or unintentional errors, fraud, illicit practices through careful examination of documents, vouchers and control systems. Now, lets move to two issues having to external auditing.

First: Those charged with governance the person (s) or organizations (s) (for example, a corporate trustee) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process. For some entities in some jurisdictions, those charged with governance may include management personnel, for example, executive members of a governance board of a private or public sector entity or an owner manager (ISA., 2017).

Second: Corruption which is defined by transparency International. Anonymous (2018) as "The abuse of entrusted power for private gain". Further, Begovic (2005) defined corruption as the "intentional non-compliance with the arm's-length principle aimed at deriving some advantage for oneself or for related individuals from this behavior". The definition of corruption outlines that both parties of corruption act for their own advantage independently and are not subject to coerce from the other party and there is no collusion between parties (like buyer and purchaser). However, Ozsahin and Ucler (2017) demonstrated that corruption also includes such crimes as embezzlement, dishonesty and favoritism and has longer been confined to public or national organization but expanded to include different parties (Liu, 2016).

The relation between auditing and corruption comes from the fact that auditing scrutinizes different operations of the entity thereby restricting misuse of authority and ensuring compliance of individuals and the enterprise with the principles and rules which help restrict collusive practices, embezzlement, bribery, etc.

Communication is the means by which external audit, auditor and those charged with governance are connected in a relationship in that communication assists those charged with governance to understand the entity and surrounding environment and help them fulfill their commitments of overseeing financial reporting process. On the other hand, communication reduces substantial mistakes in the financial data (ISA., 2016) and requires from auditor understand the internal audit, so that, to assess risks related with substantial errors and identify shortcomings in order to design appropriate auditing procedures and report them to those charged with governance and managers (ISA., 2010).

As a result (ISA., 2010) held auditor accountable regarding communicating such issues and other practices emphasized by ISA (2010). In addition, management is also takes responsibility on communicating issues related to governance management to those charged with governance. This means that communication by auditor does not disclaim managers from that responsibility. Similarly, the communication by management with those charged with governance regarding issues required from auditors to report does not disclaim auditor from communicating such issues (ISA., 2009).

In light of earlier discussion of the concepts of corruption, external auditing and those charged with governance when the auditor performs the auditing job and communicates with those charged with governance to assess errors and identify shortcomings in the internal control process by this way the auditor restricts corruption whether financial such as embezzlement or managerial like doing illicit practices related to financial statements reporting.

Table 1: Validity and reliability tests

Participants	Distributed questionnaires	Returned back	Response rate
Practitioner auditors	120	111	92.50 %

MATERIALS AND METHODS

This study adopts the field analytical descriptive approach. This study is descriptive because it introduces precise definition of the external auditing, corruption and those charged with governance and outlines the relationship between the three concepts. The field part of the study collects data from audit practitioners at their workplace using a questionnaire designed based on a review of the ISA260 and ISA265. The present study analyzes the preliminary data to identify the communication extent between the external auditing and those charged with governance for purpose of defining the aspects in which managerial and financial corruption is restricted.

Population and sample: Population (n = 404) consisted of external audit practitioners (Anonymous, 2018). A sample of (120) external auditors was randomly selected. Among the questionnaires distributed, (111) were returned back with response rate (92.50%) and were usable for analysis as shown by Table 1.

The questionnaire was sent to a number of faculties in order to identify its ability to measure the purpose for which it was developed, i.e., extent of communication between external auditing and those charged with governance to restrict managerial and financial corruption. Cronbach's alpha test was used to test for reliability of the study instrument and related results are shown in the table.

RESULTS AND DISCUSSION

First; demographic characteristics: The previous Table 2 shows that the demographic characteristics of participants were primarily limited to experience and professional certification and results were as follows.

Experience: As shown by Table 3, experience had three levels where the majority of participants (45%) had high experience level with tenure more than 6 years. The remaining participants were placed in the two levels which increases confidence in results from this study.

Professional certification: The previous Table 4 shows that the vast majority of participants (90%) were holders of at least one professional certification, i.e., the JCPA whereas the remaining participants (5.40%) had more professional certification than the JCPA. The reason is that in Jordan to practice as external auditor, one should be holding the Jordan Certified Public Accountant JCPA even if had other certifications like the Arab Certified Public Accountant ACPA.

Table 2: Cronbach's alpha test

Item	Cronbach's alpha
21	91.90 (%)

Table 3: Frequencies and percentages of demographics (experience, professional certifications)

Demographics/levels	Frequency	Percentage	Cumulative (%)
Experience			
3 years or less	27	24.30	24.30
3-6 years	34	30.60	55.00
More than 6 years	50	45.00	100.00
Total	111	100.00	
Professional certification			
"JCPA"	105	94.60	94.60
More than certificate	6	5.40	100.00
Total	111	100.00	

Second: Communication between external auditing and those charged with governance related to restriction of managerial and financial corruption. To measure respondent's estimates to the study instrument, Liker-5-point scale was adopted.

Table 5 shows that the mean score for all instrument items was (M = 3) which represents the cutoff score between agreement and disagreement to an item in that the mean score >3 indicates agreement and mean scores <3 indicates disagreement.

Table 4 shows the overall mean score for all questionnaire items (21) was (M = 3.610) meaning that the respondents agreed with setting up communication between the external auditing and those charged with governance. However, the responses varied among items as shown above where the communication was placed very low (M = 3.210) for item 7 "The external auditor discusses with those charged with governance issues considered of special concern during the audit" whereas the highest rating (M = 3.940) for communication was for item 9 "The external auditor discusses with those charged with governance any issues impacting financial statement auditing". The communication between external audit and those charged with governance affects different aspects of an entity as shown by the following three groups.

First group: Communications related to financial reporting and distortions (items: 1, 2, 9, 19, 20).

Second group: Communications related to efficiency and effectiveness of the internal control system (items: 13, 14, 16, 17, 18).

Table 4: Means and standard deviations of items related to communication between external auditing and those charged with governance regarding to restriction of managerial and financial corruption

Item	M	SD
The external auditing helps those charged with governance in fulfillment of responsibilities regarding overseeing financial reporting	3.440	0.857
Assisting those charged with the governance in the financial reporting by external auditing reduces substantial distortion risks in the financial statement	3.590	0.932
Once a fraud or distortion has been identified by external auditing those charged with governance are communicated as early as possible for notification	3.610	0.621
The external auditor discusses with those charged with governance assignment of responsibilities between management and those charged with governance	3.260	0.893
The external auditor discusses with those charged with governance strategic goals of the entity	3.500	0.543
The external auditor discusses with those charged with governance risks that would result in substantial distortions	3.820	0.907
The external auditor discusses with those charged with governance issues considered of special concern during the audit	3.210	0.845
The external auditor discusses with those charged with governance all the fields that might require additional measure to control work	3.790	0.637
The external auditor discusses with those charged with governance any issues impacting financial statement auditing	3.940	0.956
The external auditor discusses with those charged with governance conditions of the customers that may affect the entity, work plans and strategies that affect the substantial distortion risks	3.870	0.845
The external auditor explains any significant doubts related to the entity's continuity with those charged with governance	3.440	0.657
The external auditor proposes suggestions to those charged with governance to deal with significant risks of substantial distortions	3.400	0.422
The external auditor informs those charged with governance about any indication of transactions that are of concern to the management not properly scrutinized by the internal control system	3.470	0.374
The external auditor informs those charged with governance about fraudulent practices by the managers whether it was substantial in order to restrict it using the entity's internal control system	3.910	0.848
The external auditor informs those charged with governance about failure of the managers in taking the appropriate action regarding any faults reported	3.450	0.552
The external auditor informs those charged with governance about efficacy of internal control system	3.810	0.920
The external auditor informs those charged with governance about effectiveness of the internal control system	3.660	0.958
The external auditor informs those charged with governance of any distortion or mistake found out by auditing to prevent or correct it from the internal control system	3.680	0.579
The external auditor informs those charged with governance redisplay the financial statements issued by management, so that, to reflect a substantial distortion committed due to fraud or error	3.690	0.668
The external auditor informs those charged with governance about any evidence that the entity is unable to oversee financial statements reporting	3.610	0.0451
The external auditor shows to those charged with governance what procedures are there to encourage employees comply with regulations and values to perform job appropriately	3.580	0.364
Overall mean score	3.610	0.711

Table 5: Mean score of the instrument and measurement of responses to items by Likert scale

Strongly agree	Agree	Neutral	Disagree disagree	Strongly	Mean of the overal instrument
5	4	3	2	1	((1+2+3+4+5)/5) = 3

Table 6: Testing hypothesis

Computed T	Tabulated t	Sig.	M	Result
9.802	1.99	0.000	3.610	Rejection

Third group: Communications related to miscellaneous issues like assignment of responsibilities, strategies, business risks, sustainability, substantial distortion risks etc. (items: 3, 4, 5, 6, 7, 8, 10, 11, 12, 15, 21). Such communication results in control of the financial and managerial processes and procedures of the entity which reflects on the performance of the entity in terms of effective control, reduced substantial errors and restricted corruption in the financial and managerial fields (Table 6).

Third; testing hypothesis: "Communication between external auditing and those charged with governance does not restrict managerial and financial corruption". The previous table shows rejection of the null hypothesis and to accept the alternate hypothesis stating "communication between the external auditing and those charged with governance restricts managerial ad financial corruption". The previous table shows that all items had general mean score (M = 3.610) which is higher than the mean score of the overall instrument (M = 3) and computed T was higher than tabulated T with significance level <0.05. The earlier discussion of results reveals the following practical inferences:

There is communication between the external auditing and those charged with governance which varied among items as shown by Table 4. The communication between external auditing and those charged with governance restricts managerial and financial corruption at the Jordanian companies through: assisting those charged with governance to commit with governance responsibilities related to overseeing financial reporting which has reflections represented by reduced risks of substantial distortion in the financial statements.

When a fraud or manipulation is identified, the external auditor would communicate with those charged with governance as early as possible for notification. Discussion between external auditing and those charged with governance regarding distribution of responsibilities among those charged with governance and management.

Discussion between external auditing and those charged with governance regarding entity goals and strategies and relevant risks that might result in substantial distortions. Discussion between external auditing and those charged with governance regarding issues considered by those charged with governance as requiring section concern during audit and any other fields require further procedures.

Discussion between external auditing and those charged with governance any issued considered by those charged with governance affecting audit of the financial statements. Discussion between external auditing and those charged with governance work conditions that impact the entity and research plans and strategies and risks of substantial distortion.

Propose suggestions to those charged with governance to deal with significance risks related to substantial distortions resulting from mistakes or fraud. Informing those charged with governance any meaningful indications of a transaction of concern for the management and not sufficiently considered by the internal control system.

Inform those charged with governance about fraud practice by management in order to curb it through the internal control system. To inform those charged with governance about efficiency and effectiveness of the internal control system. To notify those charged with governance with any distortions detected by the auditing procedures in order to prevent or correct it through the internal control system of the entity.

CONCLUSION

To notify those charged with governance with redisplay of the financial statements issued by the management, so as to reflect correction of the substantial distortions due to fraud or error. To notify those charged with governance any evidence of the entity's ability to oversee financial statement reporting process. To communicate to those charged with governance with procedures encouraging employees comply with laws and values enhancing good performance.

RECOMMENDATIONS

To concentrate on communication between external auditing and those charged with governance due to its effect in boosting strengths and avoiding weaknesses in the internal control system. To enhance communication between external auditing and those charged with governance due to its effect in controlling distortion related to procedures and processes which conduits to restricted managerial and financial corruption.

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