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Audit Performance and Practicing Environment Reform:

Audit Practicing Environment in Egypt

DOCTORAL DISSERTATION

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## **Abstract**

This thesis presents a study to identify and measure the interrelationship between proposed audit environment's main factors, in order to present a suggested model for audit fundamentals' reform in Egypt. This model will increase the professional auditors' and practicing regulatory bodies' roles. Due to the globalization of capital markets, the audit environment becomes more complex and includes many interactive relationships between its main fundamental factors. Recent accountability failures in the United States and other countries raised the fact that the accounting and auditing professional practicing environment needs to be reformed, modernized, and expanded.

Despite the increased global attention to the importance of audit practice reforms, there are a limited number of academic researches that discussed the practicing environment changes and their affects on auditors' responsibility and operating process.

An extensive review of the literature revealed a strong relationship between audit practicing and recent financial failures, as well as the subsequent global expansion of practicing reforms.

This thesis makes an important contribution to the audit-practicing global harmonization through developing a theoretical Conceptual Practicing Environment model that has been created and follows a deductive approach, and primary data questionnaires collected from the designated practitioners in different local big audit firms. Data was analyzed according to their descriptive properties and underlying correlation structure. Several principal components were derived from these analyses, which were used in hypothesis testing, in order to examine the interrelationships between the factors associated with audit-practicing environment.

Furthermore, implications for academics and practitioners are drawn that indicate the relevance and applicability of this research to audit practice reforms. Research limitations for possible future research are set out. The thesis is organized into eight chapters, which are entitled in the following order: chapter one introduces the overview and the background of the study, chapter two introduces a review of related literatures, chapter three presents an analysis of the relationship between audit practice and recent financial market failures, chapter four examines different internal and external audit-practicing environment variables, chapter five discusses the current environment of audit practice in Egypt, chapter six proposes the suggested factors that affect the efficiency of the audit-practicing environment, chapter seven analyzes the correlation and multiple regressions based on the questionnaire and empirical tests of the hypothesis, and chapter eight provides suggestions for Egypt's local practice reforms.

The magnitude of each variable in the practicing environment will be differentiated from one country to another based on the local culture and influence power of environment of different variables. The thesis confirmed that the current Egyptian local practice environment is classified as a dormant, complex, and uncertain environment that needs major reforms in order to increase its practice organizations effectiveness. Also, empirical research results raised a consensus between the selected sample answers about the importance of increasing professional accountants' and auditors' technical and judgmental capability, in addition to the necessity of increasing the non-governmental organizations' subscriptions in developing and managing the practicing profession.

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## **1. Introduction**

The emergence of international capital markets requires high cooperation between foreign and local regulators, besides capital providers. This cooperation will support funding growth, invent new ways to manage them, reduce the complexity of the current globalized business environment, and ease the capital flows between borders. In order to increase the efficiency of capital markets, businesses need to unify the processing of international financial transactions through the use of new accounting and assurance methods, such as generally accepted accounting and auditing standards, which simplify the recording of local and foreign economic deals (**ICAA, 1998**). In particular, consider the frequent international spread of companies' financial securities, and the complicated requirements of multi-markets securities listings, which make the companies subject to both local and foreign regulations. Most financial researches present the necessity of markets efficiency, which is essential not only in wealthy countries, but also in undeveloped nations, as markets that work with efficient and transparent systems will be globally recognized.

Current changes in global businesses set a new paradigm for the audit practicing environment, which requires an integrated international harmonization between audit-practicing regulations, taxation rules, corporate laws, and accounting standards. International harmonization represents a strong challenge, as it is hard to establish globally acceptable accounting tools that enable different governments to deal with their local and international unique specifications. This new paradigm led to a more challenging environment for both local and international audit firms, which forced auditors to expand their range of business services beyond the traditional assurance and tax advices (**Epstein & Geiger, 1994**). Additionally, these changes increased the international pressures for imposing professionalism competency, and global strategic professions' mindset that support the creation of global ethical culture, knowledge, skills and social rules for both audit firms and audit-practicing institutions.

## *Introduction*

Recently, accounting and auditing became part of the political lobbying game. Political lobbying can be forced by government, or any of the negatively affected beneficiaries, such as companies' management, executives, investors, regulatory bodies, associations, and any other parties that have the power to influence decision makers. Accordingly, it is essential to create a strong ethical culture in audit-practicing businesses by establishing practice governing rules, policies, and increasing peers to support moral practice and ethical values (**Piotroski & Srinivasan, 2008**). Therefore, professions start to focus more on developing a proper structure of global economies that supporting the International Financial Reporting Standards (IFRS), and International Auditing Standards' (IAS) role in providing high-quality financial information, which is increased due to the recent accounting and financial failures, such as Enron (**Hegarty et al., 2004**).

Definitely, the business world's quick environmental changes and globalization led to a shift in the practicing environment, and impacted the auditors' daily practice operations. The inefficient practicing environmental structure associated with governmental passion to deregulate audit practicing and credit rating services hinders the audit basic role of any financial signaling system, and also turned the practicing environment and audit firms into oligopoly profit seekers that tried their best to cover any crisis indicators and protect their interests. Accordingly audit practicing is quite simply at a truly critical point in the history of professions, which requires an immediate global reform to strengthen, modernize, and promote adherence to high-quality accounting and auditing standards that encourage knowledge exchange, in addition to developing a strong international practicing environment that follows integrated auditing best practices, and putting public interests before personal interests (**Previts, 2005**).

### 2. Problem Identification

Audits have recently become more important than in the past due to the globalization of capital markets. The recent accountability failures in the United States and other countries have led to bankruptcies and restatements that harmed countless shareholders, employees and retirees. This also increased awareness about accounting and auditing professions needing to be reformed, modernized, and expanded. Moreover, the audit environment has become more complex and includes many interactive relationships between its main fundamental factors. There are no specific identifications for these factors that have the main effects on the audit environment efficiency. Many accounting-related theories focus on structuring environmental systematic coherence between accounting as a social concept and its practice. The main theories are represented in Decision Usefulness Theories, Public Interest Theory, Capture Theory, Legitimacy Theory, Stakeholder Theory, and Positive Accounting Theory. **Bogle (2000)** identifies five risks that pressurized audit firms' practicing performance and ethical values. These risks represent the main reasons for the recent financial crisis. Also, they work as warning systems that limit any future audit failures. The five pressurizing risks are summarized as follows:

1. Outdated accounting and auditing standards that do not cope with modern economic changes.
2. Increasing unethical concepts, such as earnings management and accounting creative financial engineering.
3. Unclear new methods of accounting management's incentives, and compensations.
4. The aggressive unethical uses of tax shelter schemes.
5. Audit profession's weak independencies' measurements and increase of auditors' conflict of interests due to new practicing alternative business structures and advisories.

Typically, there are two systems to monitor public companies' performance: the first is internally applied through using accounting standards, while the second is externally managed through the markets' regulators. Market regulators have the essential legally protected tools that enable them to limit organizations' boards and management discretions, monitor companies released significant information, take any necessary actions

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to protect public interests, and impose of specific financial reporting standards (**Gordon, 2003**). The legal system implemented in Egypt is taken from the French legal system, which is basically the Roman law system. A limited liberalization of Egyptian accounting services has been initiated since the last decade. Accounting Practice Law number 133/1951, and its amendments, represent the main law governing professional accountants and auditors. However, the law is considered out of date by most practitioners, which stalled efforts to improve accounting and auditing practices. Egyptian audit-practicing structure only permits local firms to be licensed, however, all of the big international auditing firms are presented in the Egyptian market through partnership with local professions. Currently, small- and medium-size Egyptian audit firms are not obliged to comply with stringent standards, while big firms have to follow rigid standards due to their associations with international audit firms. Also, The Egyptian Stock Exchange does not have the legitimate authority to enforce listed companies to follow International Financial Reporting Standards for their issued financial statements. The Capital Market Authority (CMA) has some limited sanctions authorities and tools. Currently, there is a scarcity of experienced auditors in Egypt because of lack of education and training, the absence of a strong independent counsel (to grant licenses, designations, and enforce training and continuous education), and the lack of competitive advantages in the auditing profession. Egyptian auditors are not required to follow any code of ethics in line with the IFAC codes. This deficiency is accompanied by a prevalence of the closely held companies and the absence of rules associated with appointing, or changing, auditors.

Egyptian audit-practicing function does not totally conform to International Auditing Professional Standards. ESAA (Egyptian Society of Accountants and Auditors) is not functioning as a self-regulating body as per IFAC recommendations. Currently, there are many practicing licensed auditors, non-members of the Egyptian Society of Accountants and Auditors, who lack necessary professional competence for providing high-quality auditing services. Also, the local university's poor educational quality, and outdated accounting and auditing curriculums that mainly focus on preliminary topics and applications without considering the breadth and depth of the studied subjects. Egyptian auditors' independency is dramatically affected by the nature of the closely held companies'



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structure. Most of the Egyptian companies are family business that are controlled by family members through the majority of issued capital shares, which make it difficult for the companies' Board of Directors and key management to separate between auditing and consultancy services provided by auditors

On the other hand, the GLOBE classification of the Egyptian culture, which is summarized in the following table, indicates that the Egyptian culture revolves around the masculine community that believes in groups working with an average degree of capability to change. This community is built on respecting of hierarchy, leadership, and a low degree of potential risk planning.

### Project GLOBE Classification of Egyptians' Societal Cultures

	Low-score	Mid-score	High-score
Gender egalitarianism	Egypt		
In-group collectivism			Egypt
Humane orientation		Egypt	
Uncertainty avoidance	Egypt		
Power distance	Egypt		

**Source:** Javidan et al., 2006, *pp.* 67–90.

In this thesis, we will try to measure the interrelationship, importance, and effect of different proposed main factors on the audit environment, in order to present a suggested model for audit fundamentals reform in Egypt. This was measured through the use of the empirical research and quantitative survey. The concept design tried theoretically to identify the main environmental constructs/variables that may affect the local audit-practicing environment based on the previously discussed literatures and researches. Also, we tried to incorporate in each construct/variable to the expected sub-dimensions that may have a similar effect on the overall practicing environment. The new measures' constructed validity was assessed using perceptual data from professional auditors and

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practitioners. Because neither a single approach to conceptualize the audit practice environment nor to measure it has received widespread acceptance, we have been unable to build comprehensive and coherent literature about the audit practice environment and its impact on the profession's behavior. We conceive our proposed conceptual constructs to be multidimensional, and construct general measures in our empirical research to reflect this approach.

### 3. Research Aims and Objectives

Audit practicing significantly affects both the community and the economy; accordingly, it should be treated as a highly regulated business. It should be properly monitored by governmental regulatory bodies, local government departments, and commissions. After several attempts of accounting and auditing harmonization, many countries still follow two different tiers of accounting systems that consist of a preliminary legalization system for listed public companies, and a domestic legalization system for non-listed companies. From a cost-effective point of view, the two-tier accounting systems may not be convenient for non-listed private companies and public auditors. Also, it creates many obstacles in the road of global accounting.

The growing number of recent financial scandals increased academics demands of applying strong creditable audit model that associated with professional auditors' traits and effective audit environment. This environment has to be based on international standards that designed to support capital market tools, and provide proper measuring of financial reporting quality. Despite implementing of international standards and rigid laws, such as SOX, financial scandals and crisis continued. Typically, the 2008 financial crisis presented the model of financial systemic failure, which encouraged the academic researchers to claim the necessity of financial market regulation. The overconfidence of the financial system, ignoring the market systematic risks by both bankers and regulators, and the complexity of financial markets led to the failure of both credit rating agencies and auditors' warning system.

In general, audit-practicing professions had a very negative role in controlling and prohibiting the recent global financial crisis, which increased the crisis damages' size and the consequences that followed. Also, the 2008's financial crisis presents the importance of auditor's social role in protecting public interests, which represents the main object that underneath audit practicing environment.

The thesis main objective is presenting an environmental model that could be used

## Research Aims and Objectives

to reform the Egyptian audit environmental variables, and increase the professional auditors' and practicing regulatory bodies' roles through the following suggested enhancement:

- 1- Providing institutional structures to permit the auditor to maximize their self-interest in a publicly interested way, which may lead to an explicit covenant to serve the public interests;
- 2- Increasing the local professional body hegemonic role in audit practicing constituted ideologies, as well as, enhancing the coercive and consensual approaches adopted by the government;
- 3- Measuring and increasing the practicing environment fundamental factors interactions based on the type of political, social and cultural setting. This view of the perspective is pivotal to the overall auditing practicing environment efficiency that provides a useful lens to appreciate auditing and non-auditing services;
- 4- Reshaping of audit firms practicing methodologies, as well as the formation of new moral ideologies; and
- 5- Increasing the professional auditors' practicing ability to identify and diagnose problems, through continuous developing training, technical education, and supports that will enhance audit professions' reputation in both and local prospects.

The contingency organizational theory suggests that any organization is consist of number of systems that supported by subsystems and directed by specific boundaries from its surrounding environmental subsystems. The theory analysis helped in understanding the interrelationships between the subsystems, the organization environmental patterns, and other related variable. The theory argued that organization environmental structure is the major source for organization management. Accordingly organizations always trying to interpret their surrounding environment, in order to maximize their advantages, and use the out puts knowledge to reshape their operations (**Richardson, 2009**). Based on the environmental theories we tried to study the environment phenomena and its effect on audit practicing. We proposed a conceptualization of practicing environment that consists of both internal and external environment dimensions. The environmental proposed dimensions are treated as exogenous constructs (independent variables) that affect the audit practicing system; the relationships among the components of those dimensions are not

## Research Aims and Objectives

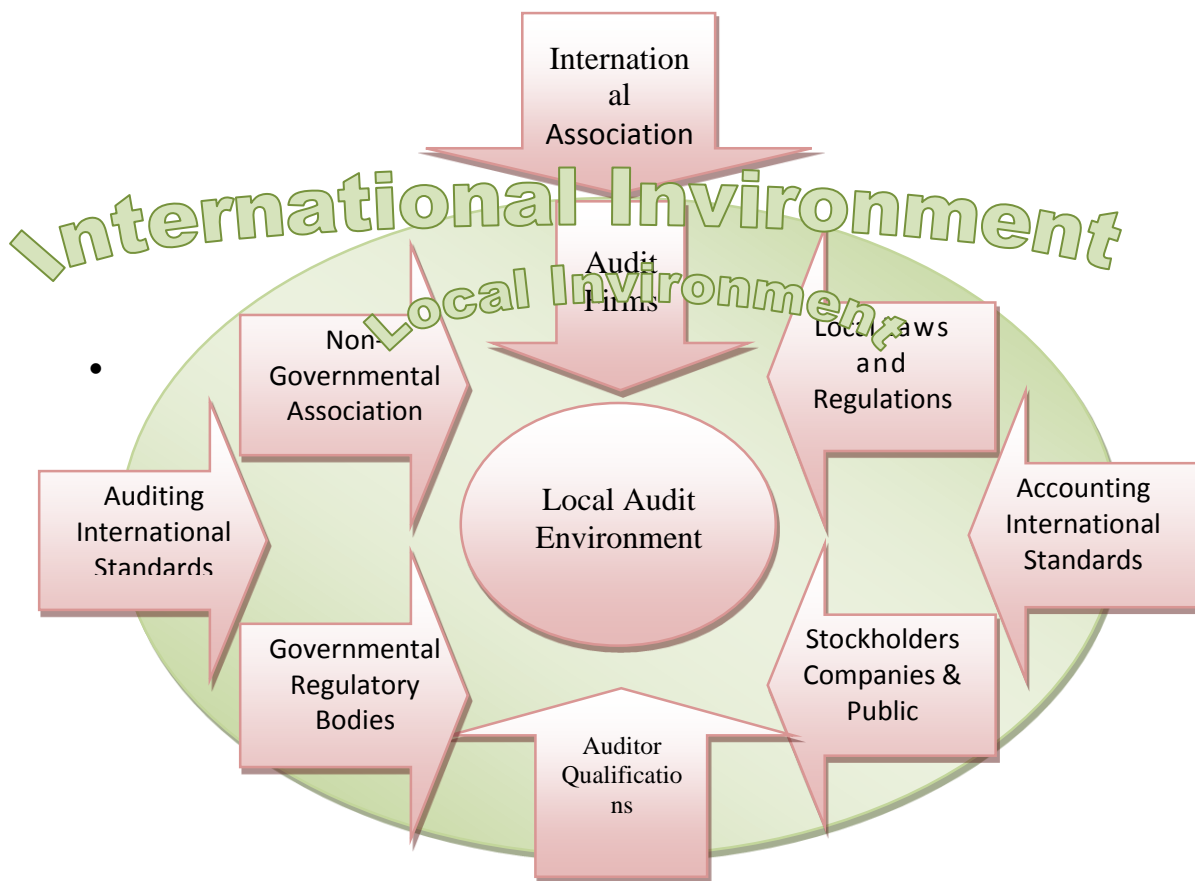
specifically hypothesized. The characteristics of local environmental and weakness points are treated as endogenous constructs (dependent variables). The conceptual model framework is a causal modeling. The concept design tried theoretically to identify the main environmental constructs/variables that may affect the local audit-practicing environment based on the discussed literatures and researches.

The study is an explanatory one. However, we tried to present it in a comprehensive approach. It is important to mention that the study has some limitations. Most of the studies related to the same subject, particularly in audit regulation filed, were mainly focus on audit technical issues. There are a limited number of audit studies that tried to investigate audit environmental variables, or measure their expected effect on the general audit practicing environment. We tried to structure the bases for building a model that can be used by future researchers to construct an initial theory that measure the relationship between audit practicing environmental variables, and their effect on audit services development; accordingly we also recommend that future studies in the same field may focus on developing an integrated theory in the field of practicing environment development.

*The Following proposed practicing environmental model and the description of environmental dimensional variables supposed to help in restructuring the local profession, in addition to developing of practicing licensing qualifications, auditors' competence and independence. Also they increase the efficiency of Egypt current local practicing society, and the proposed new board of accountancy.*

# Research Aims and Objectives

## Conceptual Practicing Environment Design: Internal and External Environment Dimensions



• Source: Researcher

*The following table summarizes the definition of environmental dimensional variables*

Environmental variables	Description
<b>Legal regime and associated support of</b>	Legal regime is a vital factor that supports audit credibility. However, legal affects may be varied across different

## Research Aims and Objectives

<p><b>reporting quality standards</b></p>	<p>local cultures, many literatures agree that weak law enforcement will negatively affect accounting and auditing reporting quality.</p>
<p><b>Regulatory bodies influence over maintaining of social and ethical values</b></p>	<p>Regulatory influential power is significantly influencing audit profession. It can support the profession independent social and ethical trust. Also, it may help in positively developing auditors traits</p>
<p><b>Auditors and audit firms specialization</b></p>	<p>Both auditors and audit firms have a significant contribution in weakening the surrounding audit practicing environment. In order to overcome the structured environmental deficiencies we need to set up additional accountability tools, define auditors' duties, qualifications, techniques, as well as, standardized procedures.</p>
<p><b>International and local practicing standards</b></p>	<p>Each country has its own unique practicing characteristics that based on many environmental factors, such as dominated culture, legal system, regulatory body, capital market structure, and other external influences. Both of local regulating systems, and international practicing standards enforce the profession local control matrix.</p>
<p><b>Practicing organizations and profession's culture</b></p>	<p>Culture represents an interaction between human and non-human resources. Therefore, practicing organizations, such as audit firms, professional associations, and governmental regulatory bodies must have a collective unified culture that fit with surrounding local, as well as, international society culture.</p>

## Research Aims and Objectives

<b>Practicing environment characteristics</b>	<p>In general, both contingency and Institutional theories are considered the most convenient environmental theories that suitable for audit profession.</p> <p>Professional practicing organizations have unique and distinct design, therefore researchers classified audit practicing environment as complex structure that requires more individual and grouping control vehicles. Accordingly, integrating audit practicing environment perceptual into a signal framework will enhance its efficiency and effectiveness. In order to structure this single framework there should be a clear identification of audit practicing environmental variables, as well as, specific diagnose of its operating conditions. Such of this approach will help in outlining a unitary stable practicing environment that can be globally uniformed.</p>
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#### 4. Thesis Hypotheses and Model

Capitalism regulations are based on competitive free-market mechanisms rather than relying on the governments (**Windsor & Warming, 2009**). The free market system encourages organizations to focus on competition, efficiency, and creativity rather than equality, fairness, and justice, which led to many financial wrongdoings. On the other hand, the international audit-practicing business typically represents a traditional oligopoly market that is controlled by a limited number of audit firms. Also, the financial risk assessment and valuation business is manipulated by three main international rating agencies. The inefficient financial environment structure that is based on weak laws, accounting standards, and codes of ethics encouraged market players to mask their economic performance and manipulate the facts as they wish, which led the world to the recent financial failures and economic crisis.

Often, audit-practicing ideology serves as a culture starting point for both practicing regulatory organizations and audit firm. The culture of a practicing regulatory organization represents its personality that manages values, norms, and behaviors. It can be described as a system that acts upon feedback from society, professions, and laws. This type of culture should be based on values, such as society service and public interest protection. The accounting and auditing profession environment is based on a mix of “associationism,” “corporatism,” “liberalism,” and “legalism,” which is mainly associated with the three principles of social orders: market, state, and community (**Baker et al., 2005**). The deregulation of financial services represents a key competitive environmental challenge for professions. Deregulation requires shifting of a current stable culture and environment to an adaptable ones that support the organizational society concept. On the other hand, the accounting practicing preventive environment will be more effective if it is based on authoritative compliance systems. This type of environment is always classified as a high-risk environment, which should be associated by general ethical framework that acting as a proactive tool for professions to protect auditors from any

## Thesis Hypotheses and Model

improper actions (**Heninger, 2001**). Also, it supports the reformed role of both governmental and non-governmental regulators in developing an effective audit practicing environment.

Typically, Culture instrumental practicing tools support controls and improve audit-practicing performance therefore, it is essential to understand professions cultural classification that may affect professional environmental dimensions. Academics describe culture as “collective consciousness,” “collective programming,” or “underlying shared assumptions” that identify a group of values (**Sackman, 1991**). Unified culture requires a consensus on a number of norms and values that have to be clearly understandable and approved by the audit-practicing community. The four main characteristics type of professional organizational culture have central tendencies that allow them to be categorized into one of the four culture models, described in following Table

**Culture Models Classification**

Culture Models	Description	Suitability to Audit-Practicing Environment
Competence	-Group contribution is less important than individual contributions; - More focus on the quantitative aspects than the qualitative ones; and - Achievements are driven through organizations.	No
Control	Associated with systems, procedures, and processes that are emphasized on the followed plans.	Yes
Collaboration	-Following of team-focused culture; -Focus on the in-depth knowledge of customers and stakeholders; and - Create strong relationships with other organizations.	Yes
Cultivation	Build on individuals' beliefs that deliver dramatic innovation.	No

**Source: Researcher**

## Thesis Hypotheses and Model

Also, there are four main culture types that should be considered while studying the Audit-Practicing Environment dimensions. Those culture types are classified in the following table

**Culture Types Classification**

Culture Type	Description	Suitability to Audit-Practicing Environment
Clan culture	Applicable for flexible organization that focuses on internal maintenance, and sensitive for people and customers with high degree of commitment. The organization emphasizes human resources development, cohesion, and morale.	Yes
Hierarchical culture	Encourage stability, control enforcement, formal task settings, strict rules, and obedience.	Yes
Adhocracy culture	Focus on dynamic flexible external positioning, and individualism open system. The long-term objective is growth and developing new resources.	No
Marketing culture	Focus on aggressively competing, customers' satisfaction, and product effectiveness.	No

**Source: Researcher**

In this research we tried to present an empirical examination of the validity and correlation between suggested five key constructs (variables) of the general audit practicing environment, and their relationship with our suggested hypotheses. The underlying assumption beyond our argument was mainly that there are some main constructs (variables) that should be seen from the point of their interrelation, and the overall general audit practicing environment. This concept can be considered as a government public management policy that improves the overall performance of both audit practicing and local economy. However, we believe that the correlation and the magnitude of each construct (variable) will be different from one country to the other based on its local fundamentals, such as community culture, structure, and economy sophistication. Accordingly, we suggest that future researches

## Thesis Hypotheses and Model

can study the comparison between these constructs within different countries. Therefore, the thesis studied the following main four hypotheses:

- 1st. Updating of practicing law will partially participate in developing audit environment;
- 2nd. Increasing the efficiency of audit-practicing environment requires structure of all environment fundamental factors / variables at the same time but not with the same degree of importance;
- 3rd. Implementing of practicing firm's quality-control procedures will enhance the efficiency of audit-practicing environment faster than other fundamental factors / variables;
- 4th. International environment fundamental factors / variables will have a positive effect on practicing environment reform; and
- 5th. The primary factors that are expected to have the most important effect in practicing environment reform will be the governmental regulatory bodies and non-governmental associations.

## **5. Structure of the Thesis and Order of Presentation**

Chapter one includes an introduction to the research, problem identification, hypotheses, and research objectives, while Chapter Two introduces a review of related literatures to present a background introduction.

Chapter Three presents an analysis of the relationship between audit practice and recent financial market failures. The chapter considered the effect of creative accounting tools, Enron scandal, and the recent global financial crisis on the governing audit-practicing environment and ethical values.

Chapter Four examines different internal and external audit-practicing environment variables. It describes the effect of internal environment factors on practice organization objectives, structure, and governing culture. Also, it considers the effect of external environmental factors, such as regulators, economic, social, and practicing standards. The chapter also considers the classification of environmental uncertainty.

Chapter Five discusses the Current Environment of Audit Practice in Egypt by reviewing business laws currently in use, different governmental, non-governmental regulatory bodies, and other audit practicing organizations, while Chapter Six proposes the suggested factors that affect the efficiency of the audit-practicing environment. These factors include Non-Governmental local and international organizations, regulatory bodies, audit firms' management, and auditors' characteristics.

Chapter Seven analyses the correlation and multiple regressions based on the questionnaire and empirical tests of the hypothesis. It also discusses the statistical analysis and research results.

Chapter Eight provides suggestions for Egypt's local practice reforms through developing a new conceptual framework and practicing quality measurements. Also, it concludes the end results related to Egypt's local practicing environment.

### **6. Sample Construction**

Increasing the quality of governmental, non-governmental associations, and audit firms cannot be achieved without considering others' environmental factors that may affect their performance. Our research has been built based on studying the pre-described variables that surround both the local and international audit-practicing environment.

In order to empirically examine our hypotheses, we defined the main variables that may have effects on the audit-practicing environment performance and efficiency. A detailed survey questionnaire was designed, comprised of 51 questions, and includes five parts, each of which includes detailed questions that measure different variable implications and their relationship with the Egyptian local audit-practicing environment. These questions are measured through auditors, selected samples, and responses to agreement score of certain statements that discuss the variables effects.

Due to the importance of the study in reforming of the audit practicing environment, and audit law and regulations in Egypt, the survey was based on the highest level of professional auditors in Egypt that mainly represented in the fellows and members of The Egyptian Society of Accountants and Auditors (ESAA). Accordingly the questionnaire were mainly assumed to be distributed through interviews to all the fellows of Egyptian Society of Accountants and Auditors (ESAA); as representative of the most qualified and experienced category of audit professions.

The total sample is represented by the total population of fellows of Egyptian Society of accountants and Auditors, based on data collected from the National Institute of Accountants and Auditors the fellows total numbers was 234, based on 2008 available data. This number was taken as the target population for this study, out of which 105 fellows' auditors approved to share in the research. ESAA Fellows were contacted by telephone and letters to generate interests and obtain approval for interview. Due to the nature of accounting and auditing business filed, it talks a lot of time to fix interview

## Sample Construction

appointments with the selected ESAA's fellows; however most of them asked to receive a copy of the questionnaire before approving on interview appointment. Some of ESAA contacted fellows refused to be interviewed; typically they gave reasons, such as they were too busy or they never participate in surveys.

Most of the interviews (103) have been conducted in auditors' offices while 2 interviews have been done during the international conference organized by the Syndicate of Accountants on the topic "How to Reform Auditing Environment" conducted in Egypt in February 2008 and attended by many Egyptian and Arab key professional accountants and auditors. The questionnaire is also distributed to all the conference attendants as a part of the conference tool kits.

About half of the interviews were conducted in 2 of the biggest audit firms in Egypt:

- KPMG (Hazem Hassan); and
- Price Water House.

As we previously mentioned, the number of questionnaires sent, and fellows targeted to be interviewed were 234, which represents 100% of ESAA Fellows published list during 2008. From this number only 105 fellows approve to cooperate, and interviewed, this sample size of 105 allowed for a confidence level of 95% and confidence interval of + 7.72%.

Study sample demographics included 105 leading auditors' members of ESAA, 23% of them had "CPA", 10% "CIA", 3% "ACCA", 2% "CA" while others had "CIPA, CMA, CFM, and CICA". Currently, 53% of the sample were "Employees in a private auditing office", 24% "Professional Firm Owners", 4% "Governmental Auditors" and 23% work in "others; as Financial Managers or University Professors".

Regarding the work field, 75% of the sample work in "auditing", 34% "general accounting", 29% "taxing", 6% "costing", 5% "insurance" and 8% "others; as training, consultancy, fidelity studies, financial management". 39% of the interviewed auditors

## Sample Construction

evaluated their professional performance as "excellent", 55% "good", 5% "average" and 1% "bad".



## 7. Hypotheses and Analyses

	Hypothesis Description	Empirical Results Summary
First Hypothesis	Updating of practicing law will partially participate in developing audit environment.	<p>Empirical results support the first hypothesis due to the followings :</p> <ul style="list-style-type: none"> <li>-Based on the agreement score analysis updating practicing law ranked as the second in importance comparing to the importance of developing the mutual cooperation between the governmental authorities and professional associations.</li> <li>-However, practicing law is considered as one of most important factors in the practicing environment, it also came in the second level, as "The laws regulating the auditing process and the auditor's role" has a high ranking score of 1.39. It was less in environmental importance than "International auditing standards" that has the highest environmental ranking score of 1.33.</li> <li>- Weak (0.301) positive coefficient correlation between practicing laws and both auditors' responsibilities and all other environment variables.</li> <li>- The correlation between audit clients, and practicing laws that regulate audit was weak (0.251)</li> <li>-The negative relation between both outdated Practicing Law and the government supervision and controlling organizations, which regulate audit practicing, the coefficient correlation results were (-0.653).</li> <li>- Non-governmental local professional organizations, regulating audit practicing, have a positive coefficient correlation with outdated Practicing Law (0.492).</li> <li>- KMO and principle component analysis of general environment variables shows a high score of profession outdated law and rules with score (.720), and the associated lack of auditing standards (.604). While the laws regulating the auditing has a negative value of -.721, which indicate that it is uncorrelated to the general practicing environment. Accordingly it supports our hypothesis</li> </ul>

## Hypotheses and Analyses

		that law partially affect on practicing environment reform.
Second Hypothesis	Increasing of the efficiency of audit practicing environment requires structure of all environment fundamental factors in the same time but not with the same degree of importance.	<p>Empirical results support the second hypothesis due to the followings :</p> <p>- The importance of each environmental factors were indexed as follow :</p> <ul style="list-style-type: none"> <li>• International auditing standards, (ranking score of 1.33).</li> <li>• The laws regulating the auditing process and the auditor's role, (ranking score of 1.39).</li> <li>• The efficiency of the professional audit firms procedures, (ranking score of 1.61).</li> <li>• International financial reports standards, (ranking score of 1.66).</li> <li>• The supervisory governmental organizations controlling auditing quality, (ranking score of 1.75).</li> <li>• Non-governmental professional organizations that regulating the audit practicing, (ranking score of 1.77).</li> <li>• Non-governmental international organizations that regulating the audit general environment, (ranking score of 2.48).</li> </ul> <p>- KMO and principle component analysis of general environment variables shows an importance ranking of environment components as follows:</p> <ul style="list-style-type: none"> <li>• non-governmental international organizations regulating the auditing profession (.844)</li> <li>• non- governmental professional organizations regulating the auditing work (.805)</li> <li>• international financial reporting standards (.804)</li> <li>• The supervisory governmental organizations controlling auditing works (.731).</li> <li>• International Auditing Standards (.581)</li> </ul>

## Hypotheses and Analyses

		<ul style="list-style-type: none"> <li>• Efficiency of professional organization (.510)</li> <li>• -The laws regulating the auditing process and the auditor's law (-.721)</li> </ul>
Third Hypothesis	Increasing of audit practicing firms' quality control procedures will increase the efficiency of audit practicing environment rapidly than other fundamental factors.	<p>Empirical results do not support the third hypothesis due to the followings :</p> <ul style="list-style-type: none"> <li>- The efficiency and quality of the professional audit firms' procedures has ranked as the third variable that affect audit practicing environment, (ranking score of 1.61). Statistical analyses confirm the necessity of developing auditors' competency. Therefore, implementation of both International Auditing Standards and updated of practicing law may have a higher ranking weight, and stronger magnitude in improving the audit practicing environment.</li> <li>- The Pearson correlation result was positive (.158).</li> <li>-The Pearson correlation of developing the clients' audit firms services' procedure presents a positive relation that could enhance practicing environment (.138)</li> <li>- The Pearson correlation of staff periodical update for any new practicing standards' changes was positively correlated to enhancing the professional organization practicing environment (.209)</li> <li>- The Pearson correlation analysis was positive for “the professionalism of the auditor; as one of the factors that affect audit practicing environment” (0.232)</li> <li>- There is a weak positive coefficient correlation of (0.492) between the efficiency of audit firms' followed procedures, and non-governmental professional organizations that regulate audit practicing;</li> <li>- KMO and PCA of general environment variables show a high score of both inconvenience of Egyptian auditing environment (ranking .706), and the</li> </ul>

## Hypotheses and Analyses

		auditors' limited responsibility towards the beneficiary (ranking .740).
Fourth Hypothesis	International environment fundamental factors will have a positive effect in practicing environment reform.	<p>Empirical results partially support the fourth hypothesis due to the followings :</p> <ul style="list-style-type: none"> <li>- "International auditing standards" with ranking score of (1.33), has effect on the auditing environment more than "International financial reports standards", (ranking score of 1.66). While Non-governmental international organizations that regulating the audit practicing general environment have the least effect on practicing environment, (ranking score of 2.48).</li> <li>- Both International Auditing Standards and International Financial Reporting Standards have a strong positive coefficient correlation with the lack of local auditing standards, and the outdated Practicing Law. The results were (0.465, and 0.419), respectively.</li> <li>- There was a strong positive coefficient correlation between International Auditing Standards, International Financial Reporting Standards, and non-governmental international organizations, that regulate audit practicing, with a correlation factor of (0.578, and 0.592)</li> <li>- The coefficient correlation of (.0565) between non-governmental professional organizations that regulate local practicing, and non-governmental international organizations</li> <li>- The KMO and PCA of practicing environment variables shows that both non-governmental international organizations regulating the auditing profession, and International Financial Reporting Standards have a high importance in reforming audit practicing environment with factoring score of (.844 &amp; .804) respectively.</li> </ul>
Fifth Hypothesis	The primary factors that expected to have the most	The importance index may be different based on the country level of development and culture. For example developed country, such as US, UK and

## Hypotheses and Analyses

	<p>important effect in practicing environment reform will be the governmental regulatory bodies and non-governmental associations.</p>	<p>Canada, have non-governmental practicing regulators that manipulating the practicing environment more than any other environmental factor. This was supported by the KMO and PCA of general environment variables that show a high score for non-governmental international organizations regulating the auditing profession (score .844), and both of non-governmental professional organizations regulating the auditing work (score .805) and the supervisory governmental organizations controlling auditing works (score .731).</p> <p>Even though, Empirical results of Egyptian local practicing environment do not support the fifth hypothesis due to the followings :</p> <ul style="list-style-type: none"> <li>-Both governmental regulatory bodies and non-governmental associations were locally ranked less important in their effect on local audit practicing environment than other variables, (ranking score of 1.75, and 1.77) respectively.</li> <li>-Correlation analysis presented a weak relationship between the efficiency of audit firms' internal practicing procedures and both of local non-governmental and governmental organizations, those responsible of regulating the audit practicing. The correlation factors were (0.312, and 0.042) respectively</li> <li>- Correlation between staff of audit practicing firms, and both of local non-governmental, and governmental organizations that regulate practicing was weak, (0.337, and 0.060) respectively</li> <li>- The correlations between audit clients and both of local non-governmental and governmental organizations, which regulating practicing, were positively weak, (0.435, and 0.294) respectively</li> <li>- Non-governmental international organizations that organize audit practicing have a positive regression factor of (0.469), which is higher than the positive (0.387) regression factor of local non-governmental professional organizations. This is due to weakness and the ineffective role of local non-governmental organizations.</li> </ul>
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## Hypotheses and Analyses

		<p>- The government supervision and controlling organizations, which regulate audit practicing, have a positive regression of (0.539). However, their coefficient correlation indicates a negative relation with both outdated Practicing Law and lack of auditing standards. Also, it indicates a positive relation with the easiness of obtaining practicing license. The coefficient correlation results were (-0.653, -0.447, and 0.553), respectively.</p>
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## **8. Empirical Analysis Discussion and Results**

Researchers in accounting literatures have tried to study individually each of our proposed practicing environment constructs (variables). Many researchers studied the process of auditors' ethical decision while others studied the effect of laws and regulations on audit practicing, but none of them have measured the correlations, and the effect of those overall variables on the overall audit environment.

Based on our proposed conceptualization of practicing environment that consists of both internal and external environment dimensions, the following table presents a summary of internal environment correlation and regression analysis:

## Empirical Analysis Discussion and Results

Pearson correlation	Correlation	
Q 10.1	q9_6	Q10.1
	f- Inconvenience of auditing environment	1- The efficiency of the professional organization procedures
<b><u>The effect of the professional organisations practicing auditing on the auditing environment</u></b>		
1- The mutual understanding between the customers and the professional organisations on the provided services helps improving the performance of audit practicing environment.	0.138	0.165
2- The availability of a system for evaluating the efficiency and quality of the relation with the customer has a limited effect on the auditing job environment.	0.115	0.02
3- The planning for the control arrangements of applying the professional quality in a way that meets the organisational requirements and technical standards helps improving the performance of	0.176	0.158
4- The auditor's awareness of the customer's work field and activities has a limited effect on the	0.218	0.04
5- Keeping the auditors up to date with the changes of the professional requirements (accounting standards, independency, objectivity, policies and procedures) helps activate the auditing job	0.066	0.209
6- The availability of internal rules at the professional organisations guarantying the regular rotation of auditors will help in improving the audit profession environment.	0.041	0.091
7- The organisations' use of an effective mechanism to face the failure in the application of quality procedures and policies helps improve the auditing job environment.	0.017	0.135
8- Do you think the professional organisations practicing in the auditing field are one of the factors that influencing the auditing practicing environment?	0.002	0.026
<b><u>The effect of the auditors' qualification on the auditing work environment</u></b>		
1- Do you think that the application of continuing vocational education will be more effective if carried out through obligatory instructions from the professional associations regulating the auditing	0.141	0.097
2- Do you think that the professionalism of the auditor is one of the factors affecting the audit	0.232	0.066
3- Assigning the professional associations to supervise the auditor's commitment to the continuing education requirements will have more effect on the audit practicing environment rather than	0.036	0.166
4- Determining the auditor's annual duties should be based on the vocational training previously	0.178	0.07
5- The commitment to Code of Ethics plays a more effective role in improving the audit practicing environment than the laws regulating profession practice and companies work.	0.029	0.12
<b><u>The effect of the Stakeholders on the audit practicing environment</u></b>		
1- Do you think that the interested parties and beneficiaries (Stock companies managements, banks, governmental and supervisory authorities) are one of the factors affecting the audit practicing	0.073	0.03
2- Do you think that the main interest of the beneficiaries is to obtain the financial statements, information summary and the financial policies rather than obtaining efficient recommendations or realizing the scope of work and procedures applied by the professional authorities?	0.105	0.175
3- Do you think that the companies' managements growing awareness of their social responsibilities helps increasing the performance and efficiency of the audit practicing environment?	0.221	0.036
4- The meeting of the beneficiaries' unusual requirements is one of the auditing priorities.	0.086	0.132
5- The beneficiaries' continuing interest in following up the audit notes and recommendations provided by the professional audit firms and the verification of these recommendations will help	0.105	0.016
6- The management philosophy and operating way may affect the audit practicing environment.	0.163	0.019
7- Obliging the commercial organisations by the governmental supervisory authorities to apply the code of ethics through the business ethics laws and the auditing committees' duties strongly affects	0.079	0.177



The study classified the main internal environmental variables that may affect the audit firms into three:

**1<sup>st</sup> Practicing internal procedures;**

**2<sup>nd</sup> Practicing recourses (auditors' qualification); and**

**3<sup>rd</sup> Stakeholders / audit firms clients.**

SPSS software was used in analyzing both of correlation and regression analysis for these variables that related to local audit practicing firms. Following is a summary of analysis main results:

### **1st Practicing internal procedures**

Analysis results confirmed that local audit firms are not implementing any procedures to agree with their clients about the expected services. This weakness is affecting negatively the audit firms practicing with a Pearson correlation (.165). However, the Pearson correlation of this procedure presents a positive relation that could enhance practicing environment (.138), which propose that local audit firms are neither focusing on the types of services they provide to their clients, nor following the pre-engagement evaluation procedures that are required by international auditing standards.

Regarding audit firms implemented internal quality procedures and their effect on the practicing environment, the Pearson correlation result was positive (.158). However, the result was (.176) in relation to actual implementation of these procedures by local practicing audit firms, which lead us to conclude that most of local audit firms do not follow any internal quality procedures

Regarding following of internal procedures for developing audit staff knowledge and skills, the Pearson correlation was (.218), which confirms the none following of these procedures. The Pearson correlation result was positively weak (.040) in relation to the effect of these procedures on enhancing practicing environment. On the other edge, the periodical update of staff for any new practicing standards' changes was positively correlated to enhancing the professional organization practicing environment with Pearson correlation (.209)

## **2nd Practicing recourses (auditors' qualifications)**

The Pearson correlation analyses shows a positive relationship between auditors following of both code of conducts, auditing standards requirements to monitor continuous education, and enhancing audit firms internal practicing environment (0.120, and 0.166), respectively. On the other hand, the Pearson correlation analysis was positive for “the professionalism of the auditor; as one of the factors that affect audit practicing environment” (0.232), which confirms the importance of developing staff professionalism, and their strong relation to enhance practicing environment.

## **3rd Stakeholders / audit firms clients**

Pearson correlation results related to clients' internal control procedures was negative (-0.177), which indicates a weak relationship between clients implementation of code of ethics and internal control procedures, and enhancing of audit practicing environment.

In relation to increasing of clients' understanding of their social responsibilities, and enhancing of audit practicing environment, the Pearson correlation was positive (0.222).

Also, we tried to analyze the relationship between both of audit firms internal environment variables, and audit practicing environmental variables through measuring the correlation between both of these variables, the analysis results are summarized as follows:

### **1st Practicing Internal Procedures**

Correlation analysis presented a weak relationship between the efficiency of audit firms internal practicing procedures and both of local non-governmental, and governmental organizations, those responsible of regulating the audit practicing. The correlation factors were (0.312, and 0.042) respectively, which indicates the limited role that those organizations play for regulating, monitoring, and control local audit practicing firms. Those organizations' role is critique, and needs to be more active to comply with international auditing standards requirements, mainly, if we considered the key role of audit practicing firms and professional organization in both of economy and society.

## **2nd Practicing recourses (auditors' qualifications)**

Correlation between staff of audit practicing firms, and both of local non-governmental, and governmental organizations that regulate practicing was weak, (0.337, and 0.060) respectively, which indicates that both of local non-governmental and governmental organizations have no effect on enhancing audit practicing professions or the practitioners.

## **3rd Stakeholders / audit firms' clients**

The correlations between audit clients and both of local non-governmental and governmental organizations, which regulating practicing, were positively weak, (0.435, and 0.294) respectively. Also the correlation between clients, and practicing laws that regulate audit was weak (0.251). These weak correlations' results confirmed that internal local practicing environment is Stale / Dormant and need major reforms in order to increase its operating organizations effectiveness.

The following table presents a summary of external practicing environment correlation, and regression analysis:

Regression & Coefficients Analysis for local Practicing Environmental Weakness	q9_1	q9_2	q9_3	q9_4	q9_5	q9_6	q9_7	Q10.1
<b>a- Laws and Procedures:</b>								
1- The efficiency of the professional organizations procedures	0.081	-0.174	0.161	-0.183	-0.066	-0.361	0.084	0.000
2- The laws regulating the auditing process and the auditor's role	-0.061	0.016	-0.187	-0.148	0.285	-0.129	0.067	-0.114
<b>b- Organisations:</b>								
1- Non governmental professional organisations regulating the auditing work	-0.140	0.057	-0.452	0.244	-0.306	-0.174	0.306	-0.355
2- The supervisory governmental organisations controlling auditing works	-0.447	-0.097	-0.653	0.203	-0.553	0.163	0.541	0.206
3- Non governmental international organisations regulating the auditing profession	-0.556	0.114	-0.475	0.021	-0.349	0.081	0.361	0.011
<b>c- Standards:</b>								
1- International auditing standards	-0.086	-0.160	-0.466	-0.104	-0.160	-0.123	0.121	-0.139
2- International financial reporting standards	-0.419	-0.024	-0.140	-0.099	-0.281	-0.279	0.438	-0.127

We have empirically analyzed the regression analysis for both current weakness elements in the Egyptian practicing environment, and their effect on the audit-practicing

environment. The results proposed the major environmental variables that have a strong impact on those weakness elements. The following is a summary discussion of these variables:

- A. The government supervision and controlling organizations, which regulate audit practicing, have a positive regression of (0.539). However, their coefficient correlation indicates a negative relation with both outdated Practicing Law and lack of auditing standards. Also, it indicates a positive relation with the easiness of obtaining practicing license. The coefficient correlation results were (-0.653, -0.447, and 0.553), respectively. This confirms the necessity of increasing the role that government professional organizations play in developing the local practicing environment, which can be achieved through using the government regulatory authorities in order to reorganize the weight of local environmental variables.
- B. Non-governmental international organizations that organize audit practicing have a positive regression factor of (0.469), which is higher than the positive (0.387) regression factor of local non-governmental professional organizations. This result represents a deviation from the actual practicing model in developed countries, as local non-governmental professional organizations always play the key role in profession regulating. Accordingly, we assume that the current statistical analysis results are due to weakness and the ineffective role of local non-governmental organizations.
- C. Non-governmental local professional organizations, regulating audit practicing, have a positive coefficient correlation with both outdated Practicing Law and audit firms' practicing procedures (0.492, and 0.354). This indicates the need to have a stronger role of non-governmental local professional organizations to support practicing environment reform procedures.
- D. Both International auditing standards and International financial reporting standards have a strong positive coefficient correlation with the lack of local auditing standards, and the outdated Practicing Law. The results were (0.465, and 0.419), respectively, which confirms the important role that both auditing and accounting reporting standards can play a part in developing the practicing local environment. The results also indicate the necessity of considering those standards as an integrated part of any practicing law reforming procedure.

## Empirical Analysis Discussion and Results

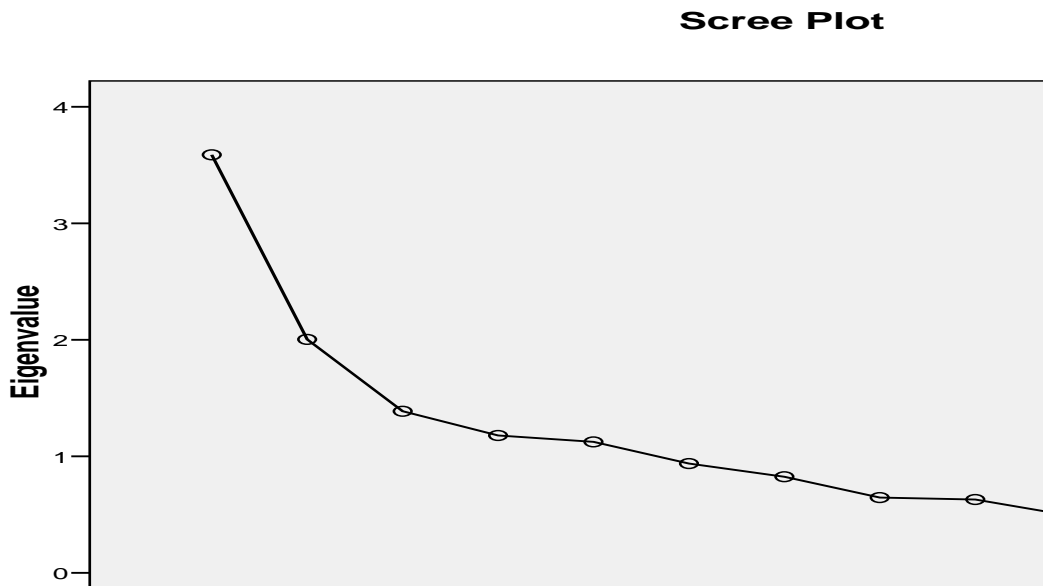
We also used the SPSS to prepare KMO (Kaiser-Mayer-Oklin) and PCA (Principle Component Analysis) for the two general type tested questions about the expected weighted average and importance of the practicing environmental main three factors (laws, practicing related organizations, and practicing related standards), as well as, the currently expected deficiencies in the Egyptian practicing environment. These analysis are used to support the other used statistical techniques during the data empirical study. The following table presents the Total Variance Explained

### Total Variance Explained

Component	Initial Eigen values			Extraction Sums of Square Loadings			Rotation Sums Squared Loadings(a) Total
	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %	
1	3.588	25.628	25.628	3.588	25.628	25.628	3.522
2	2.004	14.312	39.940	2.004	14.312	39.940	1.901
3	1.387	9.908	49.848	1.387	9.908	49.848	1.524
4	1.179	8.421	58.269	1.179	8.421	58.269	1.306
5	1.124	8.029	66.297	1.124	8.029	66.297	1.309
6	.938	6.701	72.998				

However, the tested sampling size is not that big, only 105 sample units tested, the factoring analysis technique is still visible due to the tested variables linear correlation. The KMO value is more than 0.6. Also, the Bartlett test significant value is less than .05, which indicates that factor analysis is appropriate for the tested data. The tested data plot shape is systematic and taking a horizontal trend as presented in the following Scree Plot figure.

**Scree Plot figure**



The Eigen values test, Eigen values  $>1$ , resulted in generate five main components that represents 66% of cumulative variances. In order to increase the confidence degree in the generated components we used different software, Monte Carlo PCA, in order to computes a random parallel analysis criteria for SPSS generated Eigen values. Based on this test we decided to discuss the components that have SPSS generated Eigen values more than those randomly generate by Monte Carlo PCA. Accordingly, we discussed only the first three components. The following table of Pattern Matrix presents the comparison between SPSS and Monte Carlo PCA Eigen values.

**Pattern Matrix**

	Component				
	1	2	3	4	5
q10_b3	.844				
q10_b1	.805				

## Empirical Analysis Discussion and Results

q10_c2	.804				
q10_b2	.731				
q10_c1	.536				
q10_a1	.510	.396	-.372		
q9_4		.740			
q9_6		.706			
q9_3			.720		-.361
q9_1		-.503	.604		
q9_7	-.334	.301	.508		
q9_5	.311			.776	
q10_a2				-.721	
q9_2					.879

Extraction Method: Principal Component Analysis.

Rotation Method: Oblimin with Kaiser Normalization.

a Rotation converged in 19 iterations.

Also, the following table presents component correlation matrix, which shows a low degree of correlation between the different factors results, therefore the factors rotation test was not necessary.

### Component Correlation Matrix

Component	1	2	3	4	5
1	1.000	.049	.122	-.087	-.023
2	.049	1.000	-.005	-.065	.152
3	.122	-.005	1.000	.070	.008



## Empirical Analysis Discussion and Results

4	-.087	-.065	.070	1.000	.033
5	-.023	.152	.008	.033	1.000

Extraction Method: Principal Component Analysis.

Rotation Method: Oblimin with Kaiser Normalization.

We analyze KMO and PCA Results based on the following structure matrix table:

### Structure Matrix

	Component				
	1	2	3	4	5
q10_b3	.849				
q10_b1	.809				
q10_c2	.784				
q10_b2	.730				
q10_c1	.581				
q10_a1	.481	.468	-.312		.325
q9_6		.725			
q9_4		.725			
q9_3	.325		.731		-.336
q9_1		-.453	.642		
q9_7		.313	.481		.343
q9_5				.741	
q10_a2				-.738	

## Empirical Analysis Discussion and Results

q9_2					.870
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Extraction Method: Principal Component Analysis.

Rotation Method: Oblimin with Kaiser Normalization.

### The First Component

The first component includes the different types of practicing organizations that monitoring and control the audit profession. The highest loading value is associated with non-governmental international organizations that influencing the audit practicing with a weighted score of 0.844. While the second loading highest value, with weighted score of 0.805 is in favor of the local supervisory non-governmental organization that monitoring and control the audit profession. International reporting standards have the third ranking within the first factor with weighted loading score of 0.804. While the lowest loading ranking is associated with the local governmental organizations that regulating audit practicing with a score of 0.731.

The component structure reflects the importance of governing audit practicing organizations in shaping of an idle professional environment. In contrary, the Egyptian local practicing environment is ranking these governing organizations in a lower environmental value due to the inconvenience of the local environment. Both of the Egyptian governmental regulatory bodies and non-governmental organizations are ranked as lower variables that may help in enhancing the efficiency of practicing audit environment, ranking score is 1, 75 and 1.77 respectively. Also, the non-governmental international organizations that influencing the audit practicing are classified as the lowest environmental variable in Egyptian practicing environment with a ranking score of (2.48).

### The Second Component

The second component presents the loading of the Egyptian audit practicing environmental deficiencies and its associated inconvenience of audit environment that has the highest component loading score of 0.706, as well as, the auditor's limited responsibilities towards the audit services beneficiaries that ranked as the lowest loading score with 0.604.

### The Third component

Third component presents the loading of the Egyptian audit practicing regulating deficiencies, such as outdated practicing law and regulations that has the highest component loading score of 0.720. While the lack of associated audit standards has the lowest loading score (0.604).

## Empirical Analysis Discussion and Results

Regarding the External General Environment Correlation Analysis We analyzed the correlation between all of the suggested external environment variables in order to confirm our understanding of their interrelation effects. The following is a summary of analysis results:

- Weak positive coefficient correlation (0.492) between the efficiency of audit firms' followed procedures and non-governmental professional organizations that regulate audit practicing;
- Weak (0.301) positive coefficient correlation between practicing laws and both auditors' responsibilities and all other environment variables. The weakest coefficient correlation was for non-governmental professional organizations that regulate practicing;
- In relation to organizations that regulate and monitor audit practice, there was a strong positive correlation between the three main regulatory organizations. The coefficient correlation between non-governmental professional organizations that regulate local practicing, and both governmental regulatory bodies and non-governmental international organizations were (.0606, and .0565), respectively, which indicates the importance of integrating these organizations' efforts during development of the practicing environment; typically, this can be achieved by increasing the role, authorities, and responsibilities of non-governmental professional organizations.
- There was a strong positive coefficient correlation between International Auditing Standards, International Financial Reporting Standards, and non-governmental international organizations, that regulate audit practicing, with a correlation factor of (0.578, and 0592), respectively, which confirms the strong integration between all of these variables, the importance of their parallel implementation, and the necessity of increasing cooperation between local and international professional non-governmental organizations.

## 9. Summary of Findings and Conclusion

Any organization is an open system that continuously interacts with its surrounding environmental variables; accordingly, congruence is required to harmonize the environmental internal and external variables and the dominant behaviors of the organization. Environmental changes do not usually require cultural changes. Culture changes involve a total restructuring of the environment, through changing the societal expectations (including regulation or deregulation). Due to the unique fundamentals and inefficiency of the Egyptian practicing local environment, and based on the empirical analysis results that were previously discussed, we may conclude that the Egyptian practicing local environment requires a deep culture change.

Some researchers in the field of management environment, such as **Gordon (1991)**, suggests that changing the environment through imposing government actions does not always lead to the targeted outcomes. This assumption is not applicable for audit-practicing professions, as audit practicing is a key function in servicing society and protecting its interests, and accordingly it should be properly regulated.

Also, some environment early researches argued that close controls centralization through tightening laws and regulations will increase both governmental and non-governmental organizations' roles. Furthermore, this will decrease environmental uncertainty, and enhance the efficiency of the practicing environment.

In general, many organizational environments' researches concluded that organizations usually perform well, and properly understand customers' expectations, if they are working in a friendly, simple, and stable environment that offer substantial resources (**Child, 1972; Cameron & Quinn, 2006**). These high-performance organizations always have minimum environmental changes to deal with, thus they will be more focused on improving efficiency (**Porter, 1985; Patrick & Maister, 2001**). Based on the previously discussed literatures, we may conclude that the audit-practicing environment, in general, can be classified as a stable and complex environment, since there are many elements and variables included in this type of environment. However, these elements and variables are usually constant and change slowly. The recent financial scandals dramatically shifted the practicing environment's designation to be more complex, unstable, and uncertain. This shift resulted in many changes of law and regulations that govern practicing.

## Summary of Findings and Conclusion

**Pfeffer and Salancik (1978) and Brickley et al. (2003)** argue that greater uncertainty increases efforts to more centralization and coordination, which encourage formalizing of larger organizations through merger and acquisitions in order to face the increasing environment regulating steps and political control. The following Table presents the main characteristics of the Egyptian practicing local environment:

### Characteristics of Egypt Practicing Local Environment

Environment Dimension	Reasons of Classification	Local Environmental variables that Support the Classification
Complex/ State	Degree to which the environment variables remain basically the same over time, or without continual change; -Ineffective role of the variables; -Inefficient performance of the variables; -Non-active interrelation between the variables	<ul style="list-style-type: none"> <li>- Practicing environment has many variables that affect it;</li> <li>-Weak governing rules and regulatory bodies;</li> <li>-Unorganized and inefficient interrelationship between governmental and nongovernmental organizations that regulate and control the practicing decisions environment; including unavailability of clear vision, mission or strategy for these organizations;</li> <li>-Poor practicing qualifications and rarity of human resources;</li> <li>-Outdated practicing law;</li> <li>-Inefficient relationship with international professional organizations;</li> <li>-Improper development of local accounting and auditing standards, which are not in line with similarly used international standards;</li> <li>-Unavailability of local code of ethics or independency roles;</li> <li>-Improper interrelation between business industry laws and practicing regulations;</li> <li>-Unclear responsibilities of audit firms against stakeholders and community;</li> <li>-Unclear strategic goals or mission statement for audit-practicing firms.</li> </ul>
Uncertainty	The trait of the environment resulting from the two powerful	<ul style="list-style-type: none"> <li>-No available clear structure of organizations that regulates professional practicing;</li> <li>-No available authorized institutions to monitor quality of services provided by practicing audit firms;</li> </ul>

## Summary of Findings and Conclusion

	forces of complexity and state	<ul style="list-style-type: none"> <li>-No clear structures, or working procedures in most local practicing firms;</li> <li>-Weak organizational culture of the most practicing audit firms;</li> <li>-Local professional practicing organizations are not generally following the global pattern or speed of development.</li> </ul>
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On the other hand, any environment changes require two levels (assumptions level and value level), therefore, empowering practicing organizations is necessary to meet both external and internal environment challenges. The successful implementations of these changes require modernizing of laws and regulations that organize audit practicing. They also require increasing the supported government and non-governmental governing bodies that regulate the practicing environment, in addition to creating proper strategic plans that provide effective communication between all environment key players through integrating their efforts to achieve the targeted overall development of the practicing environment.

In general, we extended our study research to understand the relationship between both the external and internal practicing environmental. We connected our measures to previous works in the field of the organizational environment, which provide us with the base to identify five practicing environmental constructs (variables) that consist of Non-Governmental Associations (Organizations), Audit Firms/Professional Organization, Governmental Regulatory Bodies (Organizations), Practicing Laws Auditors Characteristics, and International Associations. We identified the classification of Egypt's current practicing environment as dormant, complex, and uncertain. Also, we proposed that the local audit practicing environment is neither working efficiently nor effectively.

Based on our empirical analyses results and findings, there are a number of interesting observations related to the audit-practicing environment, services quality, and controls that may affect audit practicing in Egypt. The following table summarizes these observations, which are closely related to Egypt's local practicing environment's main weaknesses:

## Summary of Findings and Conclusion

### Empirical Analyses Observations Summary

	Exists	Does not exist	To a certain extent
<b>a-</b> Lack of auditing standards.	<b>29%</b>	<b>41%</b>	<b>30%</b>
<b>b-</b> Defects in some of the applied auditing standards.	<b>33%</b>	<b>30%</b>	<b>37%</b>
<b>c-</b> Outdated Audit Practicing Law and regulations.	<b>61%</b>	<b>13%</b>	<b>26%</b>
<b>d-</b> Auditor's limited responsibilities toward the beneficiaries.	<b>42%</b>	<b>22%</b>	<b>37%</b>
<b>e-</b> Easiness of obtaining practicing license.	<b>56%</b>	<b>21%</b>	<b>24%</b>
<b>f-</b> Inconvenience of auditing environment.	<b>52%</b>	<b>12%</b>	<b>36%</b>
<b>g-</b> The limited role of authorities regulating accounting and auditing.	<b>64%</b>	<b>9%</b>	<b>27%</b>

Also, the following table indexes, in a ranking base, the different environment variables based on their magnitude on the audit-practicing environment:

### Ranking Base of Practicing Environmental Variables

	Ranking Score
<b>a- Laws and Procedures:</b>	
1- The efficiency of the professional organization's procedures.	1.61
2- The law regulating audit practicing and the auditor's role.	1.39
<b>b- Organizations:</b>	
1- Non-governmental professional organizations that regulate auditing practice.	1.77
2- Monitoring governmental organizations that control audit practicing.	1.75
3- Non-governmental international organizations regulating audit practicing.	2.48
<b>c- Standards:</b>	
1- International auditing standards.	1.33
2- International financial reporting standards.	1.66

## Summary of Findings and Conclusion

In summary, the empirical analyses results reveals that both local non-governmental and governmental organizations play a limited role in regulating Egypt's local practicing organizations compared to what is supposed to be as per international practicing standards. This limited role resulted in an inefficient and ineffective correlation between both the local practicing environment and practice professions, which is contrary to what is expected in a fully regulated practicing business. Local law regulating practicing does not present any interrelation, neither through regression nor correlation analysis, with any of the current weakness problems indicated in the local practicing environment, except for those related to the easiness of obtaining practicing licenses. These indicate the weakness and ineffectiveness of currently used practicing law, and confirm the immediate necessity of law reform procedures. The negative factors that are currently presented in the Egyptian local practicing environment led us to classify it as a complex and dormant environment with a limited degree of uncertainty. These types of environment need major reform procedures, mainly through increasing the role of both governmental and non-governmental professional organizations.

The empirical findings, in general, confirmed that the Egyptian audit practicing law and professional regulatory bodies need to be reformed. Also, local professional auditors need to integrate their best practices in order to enhance their audit firms' practicing quality, and use procedures that monitor and evaluate the professional practicing process.

However, the magnitude of each variable in the practicing environment will be differentiated from one country to another based on the local culture and influence power of environment different variables. Accordingly, categorizing of environmental factors into groups for similar countries will be more efficient and save efforts during the study phase and implementation of audit harmonization.

Since Egypt is applying the Roman law system, any proposed practicing reforms require detailed laws to be issued by parliament to codify each type of accounting transactions, mainly if we consider the Egyptian basic values culture classification that has a low score of uncertainty avoidance and power distance.

Since the current Egyptian local practice environment is classified as a dormant,



## Summary of Findings and Conclusion

complex, and uncertain environment that needs major reforms in order to increase its practice organizations' effectiveness. The Egyptian practice environment encourages the reduction of accounting and auditing profession's judgment role.

Also, empirical research results raised a consensus between the selected sample answers about the importance of increasing professional accountants and auditors' technical and judgmental capability, in addition to the necessity of increasing the non-governmental organizations' subscriptions in developing and managing the practicing profession.

### **10. Thesis Contribution and Motivation**

The causes beyond the research results may be associated with the increase of globalization phenomena, and the influence of international audit-practicing environment on the way that the local Egyptian practice environment interacts. The main law governing the Egyptian professional accountants and auditors, particularly in the private sector, is the Accounting Practice Law 133/1951 and its amendments, which are considered out of date by most practitioners. The Company Law does not cover accounting and auditing standards, but requires that external audits be conducted in compliance with the Accounting Practice Law 133/1951. There is a gap between the Egyptian's law and the practice's compliance with accounting and auditing standards. Egyptian professional standards for accountants and auditors need to be improved by raising the quality of public university education and by introducing a professional qualifications examination.

The basic ground rules of the Egyptian political system have prevented necessary legislative reform. As such, this faulty legislative system has institutionalized a corrupt set of structures that led to biased decisions and occasionally outright corruption. Moreover, current local laws created an inefficient, unethical, and wasteful system. The auditor's independence in Egypt is strongly affected, which is aggravated by the lack of separation between audit and consultancy services provided by the auditor.

The thesis helps to develop the local audit practicing environment, which is expected to result in significant effects on the public auditing profession and practicing role. Also, it may create new balance for political forces, and increase the creditability of public audit services.

In general, profession reforms will support the auditor's position in the country's policy making through establishing a governmental relations module that enables the local standard-setting bodies to have a voice in issues affecting the local accounting professions. This can be achieved through the followings suggested Practicing General Reform Conceptual Framework:

## **Practicing General Reform Conceptual Framework**

This framework focus on individual auditors development in order to support their professional judgment skills and capabilities to protect shareholders' interests through the fair presentation of financial information. Therefore, Egyptian regulators should also recognize the importance of applying IFAC Code of Ethics as the base for national independency codes of conduct.

### **Practicing General Reform Procedures**

Developing of practicing performance quality involves changing the accounting and auditing statutory framework. to protect public interests through:

- Establishing of an accounting and auditing oversight body that focus on:
  - Preparing auditing standards for legislation;
  - Formulating auditing and assurance standards' guidance; and
  - Representing the local professions internationally.

#### **The oversight body powers of authorities can be extended to:**

- Engaging staff and consultants;
  - Establishing committees and consultative groups; and
  - Receiving money contributions to compensate its operating costs.
- Apply International Auditing and Accounting standards as a law.
  - Develop proper monitoring and reporting mechanisms, including peer-review programs.
  - Establish Competency Standards Committee to monitor the adequacy of professional and business ethics.
  - Monitor auditors' annual independency declaration, and perform periodic independency tests to confirm that both practicing auditors and audit firms have the proper independency mechanism.

## Thesis Contribution and Motivation

- Prohibit any kind of employment or financial relationships between auditors and their clients.
- Legalize the establishment of mandatory audit committees for listed companies
- Apply compulsory audit partners' rotation program,.
- Impose all publically listed companies to report their auditor's change to the Egyptian Stock Exchange
- Impose a Professional Code of Ethics for all auditors
- Apply licensing system that meets IFAC requirements
- Implement maximum civil penalty for audit misleading or fraud.
- Oblige chief executive officer and chief financial officer of audited companies to sign the company's audited financial statements.
- Impose auditors to form an opinion on the company's corporate governance standards.
- Prohibit auditors from providing their audited clients with non-audit services, mainly for joint stock companies, except in cases approved by the clients' audit committee.
- Enhancing the Role of Other Regulatory Agencies/Ministry of Finance, as the ministry of finance (MOF) should have more powerful controlling and monitoring authorities in order to properly act on behalf of the government, therefore, it should have the right to:
  - Give a professional accounting body ESAA, "Egyptian Society for Accountants and Auditors," a written notice to request a copy of the society's code of professional conduct, and any related amendments.
  - Request any local audit firm or individual auditor to provide information about any completed audit assignment,
  - Punish and penalize any audit firm, or individual auditor, that commits any non co-piling auditing or accounting standards offence.
- Developing the Quality of Audit-Practicing Organizations through :

## Thesis Contribution and Motivation

- Developing the Role of Egyptian Society of Accountants and Auditors (ESAA) to include :
  - Regularly examine the appropriateness of overseeing public interests mechanism, supporting continuous education, and training quality of accountants and auditors
  - Monitor the recent changes on the international accounting and auditing standards, and evaluate their effects on the local profession.
  - Review of both auditors and audit firms' compliance standards, and impose actions against violators.
  - Assess the effectiveness of local audit firms' operating systems to ensure their independency compliance. Measure the adequacy of auditors' local independency rules, Audit Practicing Act, and Codes of Professional Conduct.
  - Perform periodic quality-assurance reviews for the local audit firms.
  - Monitor companies' compliance procedures in relation to disclosures' arrangement rules and regulations.
  - Provide its members with a future clear vision of the professions that help them to shape their practicing development plan throughout their careers.
  - Provide guidance of expected competencies for newly qualified professional auditors.
  - Support Ministry of Finance activities through providing it with a yearly report that discusses the society performance, and any actions taken against any individual auditor or audit firm.
- Improving Audit Firms' Quality Management Through enhancing :
  - Internal Leadership Responsibilities for Quality Within the Firm
  - Applying of Ethical Requirements

## Thesis Contribution and Motivation

- Acceptance and Continuation of Clients' Relationships and Specific Engagements
- Human Resources Management Procedures
- Monitoring and control procedures

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## List of Publications

### List of Publications

#### Published Researches Details

**Research Title: Canadian Monetary Policy.**

Magazine Name: Management Academic Researches Magazine

Magazine Type: Academic Periodical Magazine

Researches Types: Academically Accredited Researches

Publisher: Sadat Academy for Management Science

Periodic Numbers: Volume 23, Number 3

**Research Title: University Role in Research and Economic Setting:  
Canadian Universities Innovations.**

Magazine Name: Management Academic Researches Magazine

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Publisher: Sadat Academy for Management Science

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#### Current Researches in Publishing Process

**Research Title: Audit Practicing and Financial Market Failures**

Magazine Name: ESAA Professional Researches Magazine

Magazine Type: National Profession Periodical Magazine

Researches Types: Paper Researches

Publisher: Egyptian Society of Accountants and Auditors (ESAA)

**Research Title: "Audit Professions and Enron Failure"**

Magazine Name: ESAA Professional Researches Magazine

Magazine Type: National Profession Periodical Magazine

Researches Types: Paper Researches

Publisher: Egyptian Society of Accountants and Auditors (ESAA)

#### Subscription in Published Book

**Book Name: Interpretations of International Financial Reporting Standards.**

Authors: Nasim Awad, Salah Al- Alami, and Khaled Omar

Publisher: Department of Publishing, State of Kuwait. 2007

#### Seminars

**Seminar Title: GAAP & GAAS Review & Update**

Seminar Date: 2/10/2014

Seminar Administrators: CGA Ontario Professional Developments