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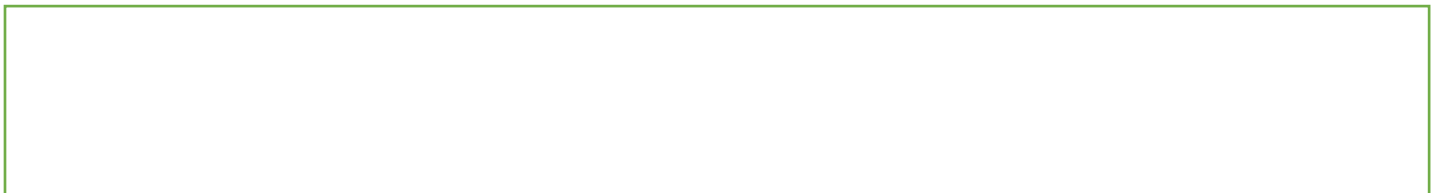
**AUDITOR'S PROFESSIONAL RESPONSIBILITIES AND LEGAL LIABILITY WITH
REGARD TO PRIVATE AUDITORS IN ETHIOPIA**

BY: GEZAHEGN AYELE

**A THESIS SUBMITTED TO DEPARTMENT OF ACCOUNTING AND FINANCE AS A
PARTIAL FULFILMENT OF THE REQUIREMENTS FOR MASTER OF SCIENCE
DEGREE IN ACCOUNTING AND FINANCE**

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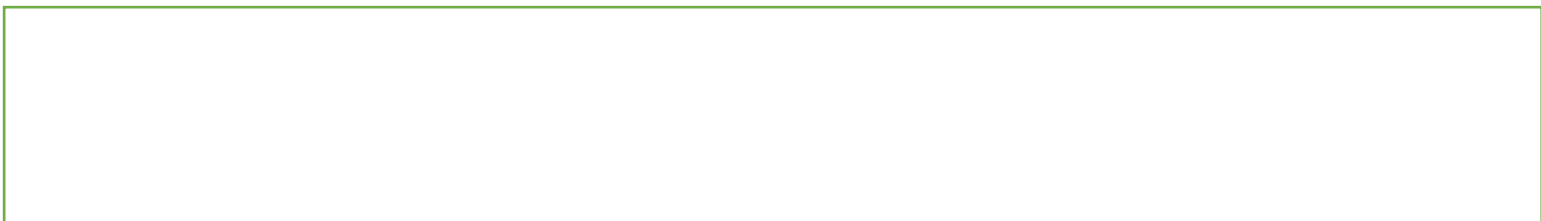
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Statement of Declaration

I, Gezahegn Ayele, declared that this thesis entitled Auditors professional responsibility and legal liability with regard to private auditors in Ethiopia” is my original work, prepared under the guidance of thesis supervisor. All resources used in the thesis have been duly acknowledged. I further confirm that the thesis has not been submitted either in part or in full to any other higher learning institution for the purpose of earning any degree or otherwise.

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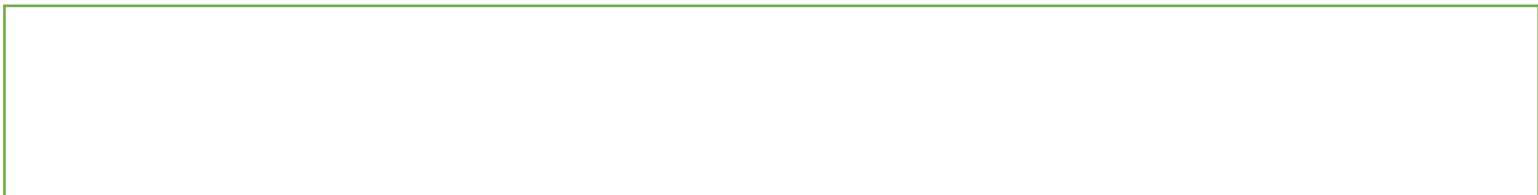
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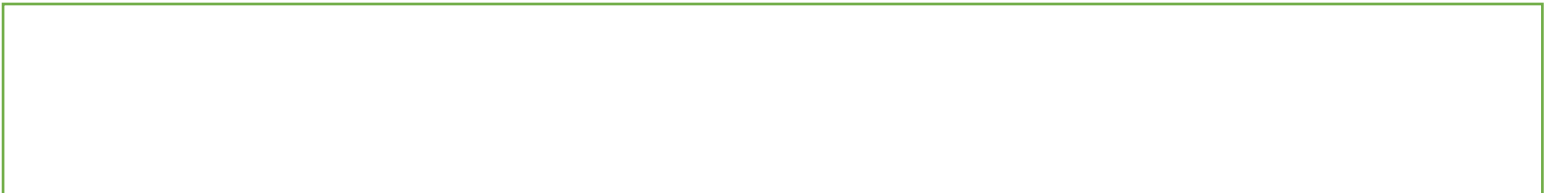
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Abstract

Auditors' professional responsibilities and legal liability with regard to private auditors in Ethiopia

Addis Ababa University 2019

This study examines private auditor's professional responsibilities and legal liability in the context of Ethiopia. The study used descriptive research design and mixed research approach. Furthermore, the study adopts cluster and purposive sampling techniques to collect a data from target population of the study; the target population of the study was classified in to five clusters based on their business type. More specifically, the data were collected from the primary and secondary source. To achieve the objective of the study, the data were collected through questionnaire and interview; the questionnaire was prepared with close-ended and open-ended questions and distributed to 72 professionals from different organizations and audit firms. Interview was made with 6 officials those are combined from Ethiopian accounting and auditing board and as well as Ethiopian revenue and customs authority. The data collected was analyzed through descriptive statements, graphs and figures. The finding of the study reveals that; absence of well-organized professional bodies, selection of auditors based on family or friends relationship, dependence of auditors on their client's for financial and other interest, forwarding of an opinion based on the demand of their clients, and irregularity of laws and regulations are causes auditors not to properly exercise professional and legal responsibilities in Ethiopia. This study recommends concerned bodies to formulate strong professional association of auditors to follow up the activity of private auditors.

Keywords, Professional Responsibility, Legal liability, Private auditors in Ethiopia

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List of Acronyms

AABE:	Accounting and Auditing Board of Ethiopia.
ACCA:	Association of Chartered Certified Accountants.
EPAAA:	Ethiopia Professional Association of Accountants and Auditors
GAAS:	Generally Accepted Auditing Standards
GAAP:	Generally Accepted Accounting Principles
IAS:	International Auditing Standards
IFAC:	International Federation of Accountants
IFRS:	International financial reporting standards
NGO	Non- Governmental Organization
OFAG:	Office of Federal Auditor General.
SAS:	Statements on Auditing Standards
U.S. GAO:	United States Government Accountability Office

CHAPTER ONE

INTRODUCTION

Under this chapter, the study discusses the theoretical ground of the study and followed by the details of statements of the problem that the researcher tried to identify are presented clearly. The intended objectives of the study, research questions, Significance, Scope, and Limitation are also parts included in the chapter and finally, the structure of the study is included.

1.1. Background of the Study

Auditing is generally thought of as practical discipline dealing with control mechanisms and instruments within organizations of different types. The audit profession, its associated bodies, and public firms have played an important role in developing the various standards, rules, and practices in this field. Basically, external auditors are responsible for auditing a given company financial statements (Soltani, 2007).

Actually, it is the responsibility of the management to apply accounting standards when communicating with investors and creditors through financial statements. Another group, auditors serve as an independent intermediary to help ensure that management has in fact appropriately applied the principles followed in preparing the entities financial statements. Auditors examine or audit financial statements to express a professional independent opinion. The opinion reflects the auditors' assessment of the statements "fairness" which is determined by the extent to which they are prepared in compliance with applicable financial auditing and reporting standards.

As per Foulks (2003), assumption generally, the objective of an external audit is to express an opinion on whether the financial statements of an entity are prepared in accordance with Generally Accepted Auditing standards or not. This means that the auditors cannot guarantee that the financial statements are free of fraud or error because of the inherent limitations of the audit. According to C. Knapp (2011); the actions of external auditors and their personal and professional characteristics are being closely scrutinized by interested parties in financial markets that are why External auditors are now faced with greater ethical challenges that were once

addressed through the limited professional code of ethics, Ethical judgments, which are now made in a firmer, more professional way, have a direct and immediate influence on auditors' reputations as a determinant factor in their level of activity in the capital market. This change of perspective places more importance on the development of sound principles and a strong professional code of ethics resulting from higher public expectations of integrity, objectivity and the independence of external auditors (Soltani, 2007).

Regarding external auditor, Messier, Glover, and Prawitt (2008), mention that; the independence of the external auditor has long been a subject of debate, particularly among regulators because it is critical in examining the accounting information in terms of its reliability.

Independence is also the accounting profession's main means of demonstrating that external auditors and audit firms are performing their attestation and monitoring tasks at a level that meets established ethical principles, in particular, those of integrity and objectivity.

To supporting this, auditors examine financial statements and lend credibility to the reports of enterprise by verifying that financial and economic facts do portray the entity's progress and financial position. The quest for developing a means for achieving better and more informative and reliable financial reports is continuous and not static. If financial reports are to be intelligible and of use to different groups, then, there must be a dialogue to shape the basis for accounting "common interest". (Johannes: 1994).

As Meigs et al, (1992) financial statements to be in accordance with generally accepted accounting principles; they must be free from material misstatement. Therefore, the auditors have a responsibility to detect various types of misstatements, including errors, fraud, and those caused by certain illegal acts. GAAS requires the auditors to design their audit procedures to reduce the risk of not detecting a material misstatement resulting from error, unintentional misstatements in financial statements, or fraud, intentional misstatement in financial statements, to an appropriately low level. Accordingly, the auditors must exercise due professional care in planning, performing, and evaluating the results of audit procedures.

They also must exercise the proper degree of professional skepticism by not assuming unquestioned honesty and good faith on part of management; but in the growing economy of the world, the issues of external auditors become more controversy than previous in line with professional responsibility and legal liability of auditors (Soltani, 2007).

As RJ Anderson FCA (1984), auditors' professional responsibilities are governed by the rules of professional conduct whose enforcement is handled exclusively by the recommendations of GAAS (Generally Accepted Auditing Standards). In addition to professional responsibilities, auditors should respect legal responsibility. The auditor's legal responsibility can be statutory, contractual, and tort. Additionally, he pointed out that, ideally legal responsibilities should constitute a minimum standard which professional responsibilities exceed. Occasionally, however, a legal standard may exceed promulgated professional rules.

Some writers conclude that those who fail to fulfill their professional and legal responsibility satisfactory may be faced with legal action. Thus, public and private auditors must be keenly aware of their legal responsibility and liability (Megis et al.1992). Hence, this study is designed to describe the auditors' professional responsibility and legal liability with reference to private auditors in Ethiopia.

1.1.1. Auditing History in Ethiopia.

The main objectives of government auditing are to express an opinion on financial statements and related issues of legality, regularity, and fraud as well as examining whether government institutions are operating economically, efficiently and effectively. To achieve these objectives every country establishes a supreme audit institution (SAI) whose independence is protected by law.

The history of Ethiopia's supreme audit institution (SAI) is related to the 1931 constitution, which stated the importance of the proper collection of the government revenue and the necessity of setting procedures to control expenditures. However, the constitution failed to stipulate the need for government auditing and establishing an SAI. But later, Proclamation No. 69 of 1944 established the first legal audit institution called Audit Commission. Under this proclamation, the commission was responsible for the audit of the accounts of the Ministry of Finance, whereas the financial transactions of other ministries were inspected and controlled by the Ministry of Finance itself. The Comptroller and Auditor General who headed the commission were reporting directly to the Prime Minister. The main functions of the commission were:

- Verification of revenue collection through its inspectors.
- Ensuring appropriate implementations of laws regulations and guidance.

- Identification and detection of irregularities and fraud.
- Initiating legal proceedings against those who were involved in fraudulent activities and irregularities.
- Submitting reports on its findings with recommendations.

Though the proclamation established a sort of the first government audit institution, the commission was not independent of the ministry as far as its professional freedom is concerned. Besides, its audit coverage is limited only to certain government departments. However, these shortcomings were resolved after two years through the amended proclamation No. 79 of 1946. The amended proclamation centralized the audit of all government accounts under one audit department called the Audit and Control Department, under the leadership of the Comptroller and Auditor General reporting to the Prime Minister. Although the power and duties of the commission were substantially increased the commissioner still lacked independence from the executive as he was reporting to the prime minister. The Audit and Control Department continued to operate until it was amalgamated with the Ministry of Finance's control department without any legislative provision in 1952. This was a major setback in the process of developing an independent national audit institution. But after three years, the revised constitution of 1955 established a relatively independent audit institution. Articles 120 and 121 of the revised constitution of 1955 established a separate and independent audit entity accountable to the emperor and to parliament. These articles required the auditor general to report regularly to the emperor and parliament on the financial operations of the government. The articles also empowered the auditor general to access all books and records pertaining to government accounts. However, the constitution did not stipulate the detailed functions and reporting requirements of the Office of the Auditor General until Decree No. 32 of 1958 which articulated the functions of the office including reporting responsibility. Later, amended legislation was issued as proclamation 179/1961. The new proclamation, in addition to defining powers and duties, it laid down the conditions regarding the appointment and independence of the auditor general as well as the reporting procedures. The provision of this legislation was a milestone as the office of auditor general has acquired a higher degree of independence to carry out regularity audits, but the proclamation lacked a mandate for expanding the scope of the office's audit to carry out performance or value for money audits. Accordingly, the office has to wait until

proclamation No. 164/1979. Proclamation NO.164/1979 increased the traditional power and duties of the Office of Auditor General considerably by empowering the office to conduct efficiency and effectiveness (performance) audits. However, the proclamation failed to incorporate the reporting and remuneration aspects of independence which are part and parcel of the basic necessities for the effective operation of an SAI (www.ofag.gov.et).

1.2.Statement of the problem

In the past ten years, the expectation gap in auditing has become much wider and the implications much more complex. Recent corporate crises including corporate collapses and undetected frauds have led to new expectations of and requirements for accountability of external auditors. Users of financial reports and market regulatory agencies expect auditors to provide assurance concerning material fraud, irregularities and the viability of businesses and their management (Arruñada, 2000).

According to Soltani (2007), Changes in society's expectations and in technology have significantly affected approaches to auditing. These changes have led the audit profession to recognize the need to undertake active measures to help improve the quality of financial reporting to reduce the gap caused by inadequate performance. A series of accounting scandals captured headlines and stimulated most of the regulatory bodies in developed capital markets to adopt laws to enhance the role of auditors in society. Additionally, he mentions out; Despite the efforts made by audit profession to restore confidence among market participants, regulatory agencies and users of financial statements; still attribute the expectation gap to the accounting profession's failure to react and evolve rapidly enough to keep pace with changing business and social environment.

One of the elements regarding the gap between what auditors do and what users expect them to do is directly related to questions such as 'what is the responsibility and legal liability of auditors in the case of material fraud, irregularities, and mismanagement, particularly in publicly held corporations (Knapp, 2011).

Auditors claim that they perform the work required by professional standards, while users of financial information see cases of fraud and irregularities and quickly assume that, because the auditors did not prevent or find the fraud, the audit was a failure and that professional standards must be inappropriate (Meigs and Lam, 1992).

In most cases, the users of financial statements of an entity prefer audited financial statements for making rational decisions. However, in developing countries like Ethiopia, the awareness creation and efficient practices of the auditors has not yet developed very well. But the numbers of private auditors are increasing from time to time in Ethiopia. According to AABE (2018), currently, there are 133 registered private auditors serving society by having a license.

According to Beyene (2007), auditors in Ethiopia are acting illegal or unprofessionally especially when they examine the financial statements of an entity. There are expectations according to Beyene (2007) that private auditors in Ethiopia have been producing misleading audited financial statements because of Reporting assets that do not exist, considering or not disclosing inadequate provision for doubtful debts, reporting stock records disregarding stock inventory counts, Treating capital expenditures as periodic expenses, Not disclosing misapplication of accounting principles and Expressing the audit opinion based on the client's interest and others.

Additionally, In Ethiopia, a number of studies have been conducted related to private auditors but in different perspectives. For example, Fekede (2015) conducted a study on The Current Status of Professional Ethics and Independence of Private Audit Firms Engaged in Ethiopia and Its Overall Impact on Audit Quality. Tsegaw (2017) conducted a study on Auditors Perception of Audit Quality in Ethiopia. Bayou (2016) conducted on threats to professional ethics: among selected authorized accountants and auditors in Ethiopia. Wudu (2014) conducted a study on Auditor responsibility and fraud detection in Ethiopian private firms. So the conducted studies have tried to forward clues to private auditors in Ethiopia in line with professional responsibility but they did not examine the legal liability of auditors. By considering the above research gaps; this study tries to assess the responsibility of private auditors with respect to their legal liability in Ethiopia. Therefore, the purpose of this study is to find out the practice of some private auditor's in exercising professional and legal responsibility. Also, this study is designed to explore whether the consequence of the violation of these responsibilities is exposed and prosecuted at all.

1.3. Research questions

- ✓ To what extent do private auditors exercise their professional and legal responsibilities?
- ✓ To what extent does the client prepare financial statements for easy verification?
- ✓ Are private auditors subject to legal liability for committing illegal audit practices?
- ✓ What constraints exist on private auditors in attempting to exercise their responsibility?
- ✓ What are the major legal concepts that relate auditors' liability to clients and third parties under common law?

1.4. Objective of the Study

1.4.1. General Objective.

The general objective of this study is to investigate the auditor's professional responsibilities and legal liability with regard to private auditors in Ethiopia.

1.4.2. Specific Objective

In light with the above general objective, the following points are set as the specific objectives of the study:

- To identify the magnitude that private auditors exercise their professional and legal responsibilities in conducting audit activities.
- To investigate clients intention in preparing financial statements.
- To examine if private auditors are subject to legal liability for committing illegal audit practices.
- To assess constraints exist on private auditors in attempting to exercise their responsibility
- To identify the major legal concepts those relate auditors' liability to clients and third parties under common law.

1.5. Significance of the Study

The findings and the conclusions drawn from the study will help all concerned bodies in the country to be aware of the existing practice and to address the problem of failure to fulfill the professional and legal responsibility.

Creates awareness on auditor's professional responsibility and legal liability among educators, students, shareholders, and all other concerned bodies and finally,

Contribution to existing literature: In addition, scholars and researchers will find this study useful if they wish to use the findings as a basis for current and further research on the subject.

1.6.Scope and Limitation of the Study

The study was conducted to assess the professional responsibility and legal liability with regard to private auditors in Ethiopia; in doing so, the scope of the study was limited to only private auditors because in most developing countries, like Ethiopia, accounting and auditing profession has not yet developed ; so it is difficult to imagine that; private auditors in Ethiopia can fulfill their professional responsibility and legal liability in the absence of locally developed standards and professions. So this study does not give any consideration to public auditors. The study minimizes its scope to private auditors found in Addis Ababa and some of the profit and non-profit making organizations found in Addis Ababa. In line with this, during the study period, the researcher has faced the following points as a limitation for the study; the first limitation of the study was Lack of internally established accounting and auditing standards found as one limitation of the study. Secondly, Due to the confidentiality nature of information, there was no access to the right data. And finally, Lack of recent publication in relation to study subject, and Lack of past studies relevant to the title was found a limitation for this study.

1.7. Organization of the Paper

The paper has five chapters. Chapter one presents the introduction part containing the background of the study, statements of the problem, research question, and objective of the study, the significance of the study and scope and limitation. Chapter two presents a critical review of the related literature. Chapter three reviews the research methodology and the Ethiopian practice on auditor's professional responsibilities and legal liability. Chapter four contains the data analysis and presentation; finally. The paper ends with major findings, the conclusion that summarizes the main results of the study and gives some recommendations in the fifth chapter.

CHAPTER TWO

REVIEW OF THE RELATED LITERATURE

INTRODUCTION

This chapter focuses on explaining the concept of auditors' professional responsibilities and legal liability with regard to private auditors, in line with their definition, different theories of professional responsibilities and legal liability with regard to auditors are summarized. In addition to this, detailed reviews of empirical studies are discussed.

2.1. Theoretical literature

2.1.1. Evolution of Auditing

The history of auditing started as man's awareness of the need to safeguard state and personal property that has been inferred from the records of a Mesopotamian civilization going back as early as 3500 BC. These records, involving financial transactions displayed various markings, which may be construed as a system of verification, internal controls, and separation of duties. (Gansberghe et al, 2003), Ancient Rome employed the "hearing of accounts", where one official would compare his records with those of another, entails an application of both separations of duties and verification practice, hearing of accounts, which gave rise to the term "audit", from the Latin "Audire", to listen. In the medieval period, the Industrial Revolution in Europe changed the role of auditing that went beyond hearing of accounts to include verification of accounting records and associated supporting documentation

Since the Second World War, internal audit has evolved rapidly from the primary function, which is concerned with financial and accounting matters to the one that addresses the entire range of operational activities. Internal audit profession has advanced primarily as consequences of; the increase size and decentralization of organization, the greater complexity of their operations, and the resulting need for means of monitoring their numerous activities, various government organizations are expected to have an internal auditing function and an audit committee composed of non- management directors (Gliem, 2000)

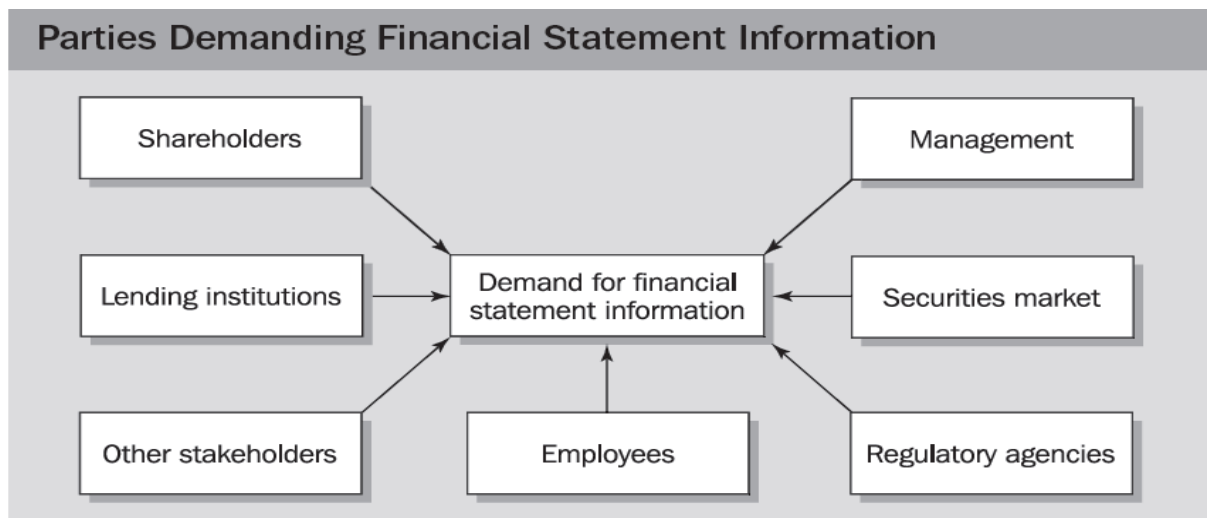
2.2. Demand and supply of audit

Financial statements are the product of a diverse set of demand and supply forces. The role of the auditor in this process is an important element: first as a participant in the process of supplying audited financial statements: and second as an economic agent giving assurance about this information to the parties demanding the corporate financial reports.

A theoretical approach to the demand and supply of audit is helpful in assessing the need for regulation and better functioning of the audit market. This discussion is essential in the sense that the theory of demand for auditing and the incentives this demand creates for the supply of audit are key to clarifying the role and responsibility of external auditors in the capital market (William H. Beaver, 1989)

The current regulations impose constraints and penalties on auditors if they fail to provide high-quality audits. Given recent concerns about the role of auditors in financial markets, there is a need to develop a well-defined theory of the demand for auditing, beginning with the fact that auditing is demanded as a solution to information asymmetry between contracting parties. It is essential to see the following diagram in order to know the main parties involved in the process of supply and demand for information

Figure 2.1: Parties demanding financial statement information



Source: (Soltani, 2007).

2.3. Concepts of Auditing

The policeman theory claims that an auditor is responsible for searching, discovering, and preventing fraud. The focus of the audit, however, has moved towards the verification of the truth and the fairness of the financial statements and the provision of reasonable assurance. The policeman theory is not able to explain fully the role and the purpose of auditing (Gliem, 2000).

According to the lending credibility theory, the primary function of the audit is to add credibility to the financial statements. Audited financial statements increase the financial statement users' confidence in the financial figures and the faith in management's stewardship. The lending credibility does not explain other functions of performing audit services; this theory is limited in explanatory power (Gansberghe, 2003.).

Zerni (2009) explained audit service as unique among other professional services for two major reasons. First, auditors are hired and paid by the client, but their product is really used by the third-parties like investors to whom they owe a standard of care.

Second, the quality of an audit cannot be directly observed prior to contracting and, in general, not even after the audit is conducted. The only observable outcome of the audit process is the issued audit report, which, at least in its standard form, does not contain much information about the audit quality.

Watkins et al. (2004) mention that the process and activities leading up to the production of the audit report such as evidence gathered are an important aspect of the professional conduct which is required of the auditor. An auditor cannot claim to have performed a test of a particular area if he or she cannot show documentation on it.

Brown (1999) argues that to a large extent audit may be a collection of tests and an evidence gathering task. The evidence gathered in the form of documentation is important in order to defend any possible challenge from an authority or defend her or his professional appearance by showing that they were following routines that make sense and have value in the audit society.

Gilo (2010), define external auditor on Ethiopia context on the bulletin on Emerald Journal title "The General Concept of Auditing in Ethiopia "An independent auditor, also known as a

certified public accountant or external auditor, has no connection to the organization being audited. Independent auditor conducts the audit on a fee basis and is primarily responsible to third parties-creditors and shareholders. The type of audit carried out by an independent auditor is a financial statement audit. In Ethiopia, the authorized auditors perform a financial statement audit. In addition, the Audit service corporation a government-owned organization performs financial statement audit.

Therefore, the auditors have been entrusted by the law to conduct statutory audits and that their role is of importance towards a well-functioning business life by enhancing the reliability of the information. This entrustment has been based on the societal roles of an auditor in terms of reducing contractual conflict leading to the so-called agency cost between board of directors of the company who controlled the preparation of accounts and external owners by examining the management's behavior and the economic information provided by the company (Carson and Dowling 2005; Watkins et al. 2004; Chow 1982).

By having, an audit of the company assures that they have quality in the actions of the management and the company due to that the role of the auditor is a role of securing the quality for external users and the company. The claim that the audit has a role of assuring the quality for external users broadens the importance of the audit and shows that it is also performed for more users than the external owners (Carson and Dowling 2005).

2.4. Auditors Rule of Professional Conduct

The fundamental principles in professional conduct involve integrity objectivity, competency, exercising due to professional skills, and behaving with courtesy and consideration. (Foulks lynch: 2004). Members should behave with integrity in all professional, business and personal financial relationships. Objectivity is the state of mind which has regard to all considerations relevant to the task in hand but no other. Auditors should not accept or perform work which they are not competent to undertake unless they obtain such advice and assistance as will enable them competently to carry out the work. Also, they should carry out their professional work with due skill, care, diligence, and courtesy (Foulks, 2004).

The ethical base of auditing has an ethical guide known as the rules of professional conduct (Foulks, 2004). The main areas of these rules are:

2.4.1. Integrity and objectivity

Integrity implies not merely honesty but also fair-dealing and truthfulness. External auditors should be fair and should not allow prejudice or bias, conflict of interest or the influence of others to override their objectivity. Independent auditors serve in many different capacities and need to demonstrate objectivity in diverse circumstances.

The auditor as an economic agent should provide the credibility to accounting and financial information (Auditing Practices Board (UK), Ethical Standard 1, 2004). On the other hand, Objectivity is a state of mind that excludes bias, prejudice, and compromise and that gives fair and impartial consideration to all matters that are relevant to the task in hand, disregarding those that are not. Objectivity requires that the auditors' judgment is not affected by conflicts of interest (Soltani, 2007)

2.4.2. Professional competence and due care

There is a need for auditors to be clearly identified by regulators, clients and other interested parties as professionals in the accountancy field. External auditors should perform attestation and other professional services with due care, competence, and diligence, and have a continuing duty to maintain professional knowledge and skill to ensure that clients receive the advantage of competent professional service based on up-to-date developments in practice, legislation, and techniques. External auditors should not portray themselves as having expertise or experience they do not possess (Foulks, 2004).

2.4.3. Prohibited ethical conflicts in external auditing

Auditor independence and objectivity has been defined in many situations where potential conflicts, while not always certain to affect independence, are nonetheless prohibited in the interests of avoiding the problem entirely. Some observers would describe this strictness as an effort simply to preserve the appearance of independence.

Appearances matter because visible conflicts of interest are all that there is to go on. The rules forbidding audit partners from owning stock in the clients they audit and the rules tightly restricting the eligibility of corporate directors to serve on audit committees are only two examples of rules based not on the proven, but rather on the presumed, dangers of conflicting interests (William H. Beaver, 1989)

2.4.5. Confidentiality

An external auditor usually has access to highly confidential information, not otherwise disclosed to the public, about the client's affairs. Users of the services of external auditors should be able to feel confident that there is a framework of professional ethics governing the provision of these services. This requires that auditors respect the confidentiality of information acquired during the course of performing the audit and should not use or disclose any such information without proper and specific authority or unless there is a legal or professional right or duty to disclose. This does not apply to disclosure to properly discharge the independent auditor's responsibility in accordance with the profession's standards (Carson and Dowling 2005).

2.5.6. Professional behavior

Professional accountants should carry out assurance services of the highest quality. An external auditor should act in a manner consistent with the good reputation of the profession and refrain from any conduct that might discredit it. This requires audit firms and/or professional bodies to consider, when developing ethical requirements, the responsibilities of an external auditor to audit clients, investors, third parties, and the other members of the audit profession, staff, employers and the general public (Carson and Dowling 2005; Watkins et al. 2004; Chow 1982).

2.5.7. Basic requirements for compliance with ethical standards

Ethical professional standards are applicable to the audit of financial statements in different countries, particularly those with developed capital markets. These standards are also issued by international bodies such as IFAC. Compliance with these requirements of integrity, objectivity, and independence is the responsibility of the audit firm, individual partners and professional staff.

The audit firm should establish policies and procedures, appropriately documented and communicated, to ensure that the audit firm and all those who are in a position to influence the conduct and outcome of the audit respect the fundamental ethical principles.

In carrying their duty auditors should be independent of the client; such independence is in terms of fees, family relationship, and other interests. For instance, it is recognized that a dependence on income from a particular client or group of clients may impair objectivity. So that, a firm which derives most of its income from one client may find it difficult to make a stand on a particular issue, as a loss of that client would have a disastrous effect on the firm's financial position (Foulks lynch: 2004).

Auditors' working papers are their own property and any request for their production should be refused. However, if the taxation authority requests the production working papers relating to a particular client whose affairs are under investigation, auditors should ensure their response is in the best possible interests of the client. (Foulks lynch: 2004). As per Arens and Loebbecke, the AICPA code of professional conduct consists of general statements of ideal conduct or specific rules that define unacceptable behavior. (Arens and Loebbecke: 1991). Thus, the code consists of four parts; principles, rules of conduct, interpretations, and ethical rulings; which are listed in order of increasing specificity. (Arens and Loebbecke: 1991). The ethical principles are ideal standards of ethical conduct stated in philosophical terms but are not enforceable.

These principles include that; Members should exercise sensitive professional and moral judgments in all their activities; Members should accept the obligation to act in a way that will serve the public interest; honor the public trust, and demonstrate a commitment to professionalism; Members should perform all professional responsibilities with the highest sense of integrity; Member should maintain objectivity and be free of conflicts of interest in discharging professional responsibilities; Member in public practice should be independent in fact and appearance when providing auditing and attestation services; and Member should observe the professional's technical and ethical standards or simply exercise due professional care.

The rules of conduct are minimum standards of ethical conduct stated as specific rules which are also enforceable. This part of the code includes the explicit rules that must be followed by every CPA in the practice of public accounting. The need for published interpretations of the rules of conduct arises when there are frequent questions from practitioners about a particular rule, for this reason, these parts are not enforceable. The ethical rulings, which are highly specific, are explanations by the executive committee of AICPA to questions about the rules of conduct. (Arens and Loebbecke: 1991). Also, Meigs, Whittington, Pany, Megis, and Lam pointed out that the rules of professional conduct of various provincial institutes consist of three parts;

Fundamental principles; such as members responsibility to the public and the profession; integrity, due care, and competence; objectivity; and responsibilities to clients and colleagues, Applicable and enforceable rules of conduct and Interpretations of rules of professional conduct (Meigs, Whittington, Pany, Megis, and Lam: 1992). Therefore, from many writers' explanations, one can conclude that the rules of professional conduct adopted by public accountants in most countries are similar in principles but differ in their specification and enforceable by the profession.

2.6. Auditor's Professional Responsibilities

The U.S. Government Accountability Office (U.S.GAO) publicized through the internet that preparation of financial reports is the responsibilities of the audited entity, not the auditor. Thus, Officials of the audited entity entrusted with handling public and private resources and auditors of government programs or entity fulfill essential roles and responsibilities in ensuring that public resources are used efficiently, economically, effectively, and legally. Audit organizations also have the important responsibility of ensuring that auditors can meet their responsibilities. These unique roles involve using sound management practices and providing professional audits and attestation engagements. (Internet sources: U.S GAO) .The management of the audited entity (for example, managers of a state or local governmental entity or a nonprofit entity that receives federal awards) are responsible for Applying those resources efficiently, economically, effectively, and legally to achieve the purposes for which the resources were furnished or the program was established;

Complying with applicable laws and regulations, including identifying the requirements with which the entity and the official must comply and implementing systems designed to achieve that compliance; establishing and maintaining effective internal control to help ensure that appropriate goals and objectives are met; resources are used efficiently, economically, and effectively, and are safeguarded; laws and regulations are followed; and reliable data are obtained, maintained, and fairly disclosed; Providing appropriate reports to those who oversee their actions and to the public in order to be accountable for the resources used to carry out government programs and the results of these programs; Addressing the findings and recommendations of auditors and for establishing and maintaining a process to track the status of such findings and recommendations; Following sound procurement practices when contracting for audits and attestation engagements, including ensuring procedures are in place for monitoring contract performance. The objectives and scope of the auditor attestation engagement need to be made clear. In addition to price, other factors that may be considered in evaluating bid proposals include the responsiveness of the bidder to the request for proposal; the prior performance and experience of the bidder; the availability of the bidder's staff who have the appropriate professional qualifications and technical abilities; and the results of the bidder's peer reviews. (Internet source: U.S GAO) .Also as explained by the U.S Government Accountability Office, the following is the auditors' Responsibilities:

In discharging their professional responsibilities, auditors need to observe the principles of serving the public interest and maintaining the highest degree of integrity, objectivity, and independence. The public interest is defined as the collective well-being of the community of people and entities the auditors serve. Auditors should act in a way that will serve the public interest, honor the public trust, and uphold their professionalism. A distinguishing mark of a profession is acceptance of its responsibility to the public. This responsibility is critical when auditing in the government environment. GAAS embodies the concept of accountability, which is fundamental to serving the public interest. Auditors need to make decisions that are consistent with the public interest in the program or activity under audit. In discharging their professional responsibilities, auditors may encounter conflicting pressures from the management of the audited entity, various levels of government, and others who rely on the objectivity and

independence of the auditors. In resolving those conflicts, auditors are responsible for acting with integrity, guided by the precept that when auditors fulfill their responsibilities to the public, these individuals' and organizations' interests are best served. To maintain and broaden public confidence, auditors need to perform all professional responsibilities with the highest degree of integrity.

Auditors need to be professional, objective, fact-based, nonpartisan, and non-ideological in their relationships with audited entities and users of the auditors' reports. Auditors should be honest and candid with the audited entity and users of the auditors' work in the conduct of their work, within the constraints of the audited entity's confidentiality laws, rules, or policies. Auditors need to be prudent in the use of information acquired in the course of their duties. They should not use such information for any personal gain or in any manner that would be detrimental to the legitimate and ethical objectives of the audited entity.

Service and public trust should not be subordinated to personal gain or advantage. Integrity can accommodate the inadvertent error and the honest difference of opinion; it cannot accommodate deceit or subordination of principle. Integrity requires auditors to observe both the form and the spirit of technical and ethical standards; circumvention of those standards constitutes subordination of judgment. Integrity also requires auditors to observe the principles of objectivity and independence.

Auditors should be objective and free of conflicts of interest in discharging their professional responsibilities. Auditors are also responsible for being independent in fact and appearance when providing audit and attestation services. Objectivity is a state of mind that requires auditors to be impartial, intellectually honest, and free of conflicts of interest. Independence precludes relationships that may in fact or appearance impair auditors' objectivity in performing the audit or attestation engagement. In applying GAAS, auditors are responsible for using professional judgment when establishing scope and methodologies for their work, determining the tests and procedures to be performed, conducting the work, and reporting the results. Auditors need to maintain integrity and objectivity when doing their work to make decisions that are consistent with the broader public interest in the program or activity under review.

When reporting on the results of their work, auditors are responsible for disclosing all material or significant facts known to them which, if not disclosed, could mislead knowledgeable users, misrepresent the results, or conceal improper or unlawful practices.

Auditors are responsible for helping management and other report users understand the auditors' responsibilities under GAAS and other auditor attestation coverage required by law or regulation. To help managers and other report users understand an engagement's objectives, time frames, and data needs, auditors need to communicate information concerning planning, conduct, and reporting of the engagement to the parties involved during the planning stages of the auditor attestation engagement. (Internet source: U.S GAO). On the other hand, as per U.S Government Accountability Office internet source audit organizations'(auditors) have responsibility for ensuring that (1) independence and objectivity are maintained in all phases of the assignment, (2) professional judgment is used in planning and performing the work and in reporting the results, (3) the work is performed by personnel who are professionally competent and collectively have the necessary skills and knowledge, and (4) an independent peer review is periodically performed resulting in an opinion issued as to whether an audit organization's system of quality control is designed and being complied with to provide reasonable assurance of conforming with professional standards. While management is responsible for addressing audit and attestation engagement findings and recommendations and tracking their status of the resolution, audit organizations are responsible for establishing policies and procedures for the follow-up to determine whether previous significant findings and recommendations are addressed and are considered in planning future engagements. (Internet sources: U.S GAO)

Also RJ Anderson pointed out that, auditors' professional responsibilities are governed by the rules of professional conduct whose enforcement is handled exclusively by the local standards. Most of these rules, however, refer to the accounting and Auditing standards of the profession, which in turn influenced by the recommendations in local standards. Among the auditing recommendations, the most fundamental is GAAS. (R.J.Anderson FCA, 1984).

Generally Accepted Auditing Standards are authoritative rules for measuring the quality of performance. Also as per Arens and Loebbecke, the existence of GAAS is evidence that auditors are very concerned with the maintenance of the uniformly high quality of audit work by all independent public accountants. If every public accountant has adequate technical training and performs audits with skill, care, and professional judgment, the prestige of the profession will rise, and the public will attribute more and more significance to the auditors' opinion attached to financial statements. (Arens and Loebbecke: 1991).

As per the United states GAAS, the 1972 Statements on Auditing Standards No 1 (SAS-1) issued by AICPA, the auditors' professional responsibilities are based on three broad standards (Arens and Loebbecke: 1991) No.1). These are:

1. General standards:

The examinations are to be performed by a person or group of persons having adequate technical training and proficiency as an auditor.

In all matters relating to the assignment, independence in mental attitude is to be maintained by the auditors (s).

Due professional care is to be exercised in the performance of the examination and the preparation of the report.

2. Standards of fieldwork:

The work is to be adequately planned and assistants, if any, are to be properly supervised.

There is to be a proper study and evaluation of the existing internal control as a basis for reliance thereon and for the determination of the resultant extent of the tests to which auditing procedures are to be restricted.

Sufficient competent evidential matter is to be obtained through inspection, observation, inquiries, and confirmations to afford a reasonable basis for an opinion regarding the financial statements under examination.

3. Standards of reporting:

The report shall state whether the financial statements are presented in accordance with generally accepted accounting principles.

The report shall state whether such principles have been consistently observed in the current period in relation to the preceding period.

Informative disclosures in the financial statements are to be regarded as reasonably adequate unless otherwise stated in the report.

The report shall either contain an expression of opinion regarding the financial statements, taken as a whole, or an assertion to the effect that an opinion cannot be expressed. When an overall opinion cannot be expressed, the reason, therefore, should be stated. In all cases where an auditor's name is associated with financial statements, the report should contain a clear cut indication of the character of the auditor's examination, if any, and the degree of responsibility he is taking. Moreover, FTC Foulks Lynch, ACCA paper 3.1 (Audit and Assurance service), discusses that the auditor has no responsibility for the prevention and detection of fraud and error. As a responsibility, auditor's should design audit procedures to obtain reasonable assurance that those frauds and errors which are material and might impair the truth and fairness have not occurred, or that if they have occurred they have either been corrected or properly disclosed in the financial statements.

The auditor should have a responsibility to report to the management and those charged with governance of an enterprise when the audit has brought to light any irregularities or errors. When the matter is material he/ she should ensure the management are informed promptly and that, where appropriate, a report is made to the board of directors or the audit committee auditors should report to the users of the audit report to the extent that in their opinion, the "true and fair view" or "fair presentation", is affected. (Foulks lynch, ACCA paper 3.1: 2004).

Therefore, from the above writers' discussion, it is wise to summarize that management of an entity is responsible for the efficient, economic and effective utilization of the entity's resources.

Besides, it is the responsibility of the management preparing financial statement for easy verification. On the other hand, it is the responsibility of auditors to form an independent opinion based on audit examination and to report the findings to the users of audited financial statements. Accordingly, the auditor should base on standards or principles formulated by the professional and /or regulatory body to which they are members or by which they have been regulated.

2.7. Auditors Legal Responsibilities

As some writers say, the auditor's legal responsibility can be statutory, contractual or both. Statutory responsibility which is based on the mandatory audit requirement in the federal and local businesses Contractual responsibility drives from an agreement mutually decided upon by the auditor and the client. Both may also agree to certain functions in addition to the statutory requirements; in such case, the auditor will be responsible to the client for both the statutory and the additional contractual requirements. Besides the auditors must be familiar with the specific act applicable to each of their clients (Megs, Whittington, Meigs, and Lam: 1987)

The auditors' statutory responsibilities and the company or national legislation consist of the general duty that auditors have to report to users on whether the financial statements of the company show a 'true and fair view' or 'present fairly' the financial position and results of its operations. Specific duties such as to consider whether the information in the management report is consistent with the financial statements and whether proper accounting records have been kept by the company were also considered as stippled in statutory requirements. (Foulks Lynch: 2004). As per RJ Anderson, (RJ Anderson FCA, 1984), legal responsibilities of the external auditor arise from one or more of statues, as interpreted by common law; contract, as governed by common law; and tort, as governed by common law. From the above discussions, the researcher concludes that auditor is legally responsible for both contractual agreement made between the auditor and the client; and statutory audit requirements.

2.8. Auditors Legal Liability

Professions such as a lawyer, financial analyst, accountant and auditor have historically attached to themselves responsibility and care beyond that of the providers of other services. As a consequence, they face liability for the outcomes of their professional advice and business activities beyond that generally imposed on the businessperson. Professionals have always been responsible for providing a reasonable level of care while performing work for those they serve. These consequences have mainly resulted from specific features of the relationship between members of such professions with their clients and the importance of the services to the client, who often required special protection. Legal liability and its consequences for the audit profession have great importance and are critical issues in a changing business environment influenced by technological developments. As is the case with many professions, the issue of legal responsibility for malpractice has been an overriding concern of auditors. In performing their duties, there will always be some risk that auditors will fail to detect a material misstatement in financial information.

In the business environment, auditors are accountable in law for their professional conduct. This responsibility may arise under common law or under statute law. However, in recent years, practitioners in high-risk fields such as auditors have found the liability regime under which they operate to be increasingly expensive and onerous. This is mainly related to the fact that the legal environment within which auditors work is one that evolves and develops due to changes related to information users' expectations and perceptions.

2.9. Types of audit professional liability

Professional liability lies on three levels (Canadian Bar Association, 1996: 8): Personal liability of individual partners who actually performed or supervised the act or omission under consideration; Joint and several liabilities among co-defendants; Joint and several liabilities among professional partners, exposing the firm's assets and individual partner assets to the liability of the firm; Before discussing auditor liability and to clarify the arguments for and against limited liability for auditors, it is essential to define the terms in this area: limited liability; joint and several liabilities; proportionate liability; and statutory capping.

In our environment, investors and creditors who suffer from financial reversals find auditors, as well as lawyers and corporate directors, tempting targets for lawsuits alleging professional malpractice. Auditors must approach every engagement with the prospect that they may be required to defend their work in court.

Even if the court finds in favor of auditors, the cost of defending a legal action can be very substantial. As a result, the cost of professional liability insurance has escalated greatly. (Meigs, Whittington, Meigs, and Lam: 1987). Accordingly, costs are not the only concern, lawsuits can be extremely damaging to a professional's reputation. In extreme cases, the auditors may even be tried criminally for malpractice. Hence, auditors are legally liable to their clients and to third parties who rely upon audited financial statements.

As Foulks lynch (Foulks lynch: 2004) says, statutory responsibilities impose liabilities if things go wrong. Auditor liability in most countries can be categorized as liability under legislation either civil or criminal in those countries with civil code legal traditions and liability arising from negligence under common law in those countries with common law legal traditions. The civil code of many countries makes director or others responsible for a company liable for fines and other penalties for:

Failing to properly prepare and deliver financial statements to the relevant authorities within the given time period.

Failing to provide auditors with access to the books, records and necessary information and explanation for the purpose of the audit

Failing to keep proper books account

Failing to appoint auditors. On the other hand, auditors may be liable in the following circumstances; to third parties suffering loss as a result of relying on a negligently prepared audit report,

Under insolvency legislation to creditors,

Under fiscal legislation (such as tax fraud)

Under financial services legislation to investors,

Under stock exchange legislation and/or rules; Criminal liability can arise in the following circumstances;

It is always an offense to accept an appointment as an auditor when ineligible to do so or to continue in office after becoming ineligible.

It may be a criminal offense to misappropriate others property, obtain a financial advantage by deception, falsify accounting records or documents, publish a misleading statement intended to deceive members or creditors.

(Foulks Lynch) also stated that the company has a contract with the auditors, and hence can sue the auditor for breach of contract if the auditor simply fails to deliver an audit report, or delivers a negligently prepared audit report. In countries with common law legal traditions, the auditor may be liable to shareholders and others who have relied on the financial statement upon which he expressed an opinion, under the general principle of owing a duty of care to those parties and being liable in the tort of negligence if he fails in that duty. A third party (i.e. a person who has no contractual relationship with the auditor) may also sue the auditor for damages', i.e. a financial award- which is a liability in the tort. Writers also pointed out (Meigs Whittington, Meigs and Lam 1987) auditors are liable to their clients when failed to exercise due professional care. This obligation exists whether or not it is specifically set forth in the written contract with the client. Thus, private auditors are liable to their clients under common law for any losses proximately caused by the auditors' failure to exercise due professional care. That is, to cover its loss an injured client need only prove that the auditors were guilty of negligence and that the auditor's negligence has the proximate cause of the client's losses.

The liability of private auditing firms to third parties not in practice has developed under the common law. The responsibility of auditors to third parties who may rely on the auditor's report has evolved through several significant court cases. These cases involve the auditors' liability to third parties for negligence, gross negligence, and fraud. Negligence is a failure to perform an audit in accordance with applicable professional standards. Substantial failures on the part of an auditor to comply with generally accepted auditing standards might be interpreted as gross

negligence. Fraud is misrepresentation by a person of a material fact, known by that person to be untrue or made with reckless indifference as to whether the fact is true, with the intention of deceiving the other party and with the result that the other party is injured (Meigs, Whittington, Meigs And Lam: 1987).

As per RJ Anderson (RJ Anderson FCA 1984), private auditors become legally liable to certain parties if they fail to discharge statutory responsibilities, contractual responsibilities, and responsibilities in tort.

The majority of errors which expose a private auditor to legal liability fall under the law of torts and specifically the tort of negligent misrepresentation. Negligence results from the failure to perform a legal duty or the failure to perform that duty with the requisite standard of care. Whether the duty is statutory, contractual or one in tort may affect the technical nature of the action brought against the auditor. An action for negligence brought by third parties we generally are action in tort whereas one brought by the auditor's client will generally be for breach of contract (RJ Anderson FCA: 1984).

Some writers argued that litigation has had a significant impact on the public accounting profession and it seems reasonable to expect that it will continue to do so in the foreseeable future. To avoid litigation, it is vital that the auditor complies fully with professional pronouncements in completing each audit engagement and use sound professional judgment during the audit and at the time of issuing the audit report. The issue of auditor liability is very much an unresolved matter. Auditors are liable under the statute to their clients for breach of duty under corporations' law. However, the interpretation of the law has been largely dependent on court cases. (Gill, Cosserat, Leung & Coram: 1999)

As per Grant Gay & Roger Simnett, the auditor duty of care to a client arises both in the contract and in the tort of negligence. If the auditor has been negligent, the clients may sue the auditor for breach of the implicit term of the contract, and recover any consequential loss suffered. Alternatively, the client may sue the auditor in the tort of negligence to obtain damages sufficient to restore the client to its original position. Moreover, the situation of the auditor's liability in relation to persons other than the immediate client has been the subject of much litigation.

Third parties who rely on an auditor's opinion, and suffer a loss caused by the negligence of the auditor, have no contractual claim for recovery of losses. An injured third party can, however, bring an action in tort, which is a civil wrong compensated by an award for damages. A right of action tort depends on whether an interest protected by law has been injured (Grant Gay & Roger Simnett). Therefore, the researcher summarizes the above writers' discussions, as that auditor should be legally liable for the violation of contractual, statutory and/or both. Thus, an auditor should be liable to the client for violation of both contractual agreement and statutory audit requirements. Moreover, the auditor should be liable to the third party who suffers a financial loss as a result of miss stated audit report, which is a liability in tort.

2.10. Legal Liability of Auditors

Concerns about the legal liability of auditors continue to grow every day. Auditors are highly important people because, ultimately, they are responsible for enhancing the reliability of financial statements for all kinds of external users.

Like other professionals, they can face civil and criminal liability in the performance of their duties. Without independent and competent auditors, many fraud cases worldwide would've gone unnoticed, notwithstanding all the other cases that are still undiscovered. In fact, the code of professional conduct states that auditors must go about their business with due care. Due care is the "prudent person" concept.

Due care generally implies four things:

1. The auditor must possess the requisite skills
2. The auditor has a duty to employ such skill with reasonable care and diligence
3. The auditor undertakes good faith and integrity but is not infallible
4. The auditor may be liable for negligence, bad faith, or dishonesty, but not for pure errors in judgment

2.10.1. Sources of Legal Liability for an Auditor

Let us consider the possible entities that may sue an auditor and the possible reason for a lawsuit.

The Legal Liability of Auditors to Third Parties

By reading this article, one question that might arise is who exactly are auditors responsible to? Can any third party sue an auditor? Or is there a certain class of parties? It is generally known that auditors are responsible to two groups of third parties: 1) Known users of the financial statements, and 2) A limited class of foreseeable users who will rely on the financial statements. Known users of the financial statements consist of the actual shareholders and creditors of the company. Usually, the company maintains a full list of all these individuals by name. The second group pertaining to foreseeable users requires a bit of judgment. For example, if the company is trying to issue new equity or get a loan from a bank, these potential investors and the potential creditor (i.e., a bank) will fall under the class of foreseeable users. Therefore, even though the auditor does not know the specific user, the auditor is aware that the client will be using the financial statements to raise bank financing or issue new shares and hence, knows the type of user.

Unjustified Lawsuits

Despite all the potential for lawsuits against auditors, many lawsuits by third parties are unjustified. For example, if a third party sues the auditor because the client (i.e., the company being audited) is no longer a viable company that is not justified because the auditor is not responsible for making sure that the company is viable and can continue operating in the long-term. The auditor is solely responsible for making sure that the financial statements are presented fairly against the appropriate evaluation criteria. In addition, unjustified lawsuits also may involve the phenomenon of audit risk. Audit risk is the risk that an auditor does everything correctly/to the best of his/her ability, however, will express an inappropriate audit opinion on the financial statements. Essentially, the situation deals with errors in financial statements that remain even after the auditor has followed the auditing rules provided by the governing body. There are simply bad luck situations when an auditor, for example, decides to pick a sample to

audit which is not representative of the entire population of data. The errors originate from unfortunate situations and are not the auditor's responsibility. If, however, an auditor were not to comply with the general auditing standards outlined by the governing accounting body, that would be a justified reason for a lawsuit, which is a situation called audit failure.

2.11. Empirical Review

There are arguments regarding the impacts of extended audit tenure on auditors' professional responsibility and legal liability. Since the aim of this study is to assess Auditors Professional Responsibilities and Legal Liability with Regard to Private Auditors in Ethiopia, it's difficult to get empirical studies directly about this study topic. So the researcher tries to incorporate some arguments by reviewing empirical studies related to professional behavior, auditor's quality, auditor's responsibility, and auditor's professional ethics.

Christopher Akpotu (2013) conducted study on "External Auditors' Unethical Behavior and Corporate Business Failure in Public Owned Organizations in Nigeria, The main objective of the research was to ascertain whether unethical practices of external auditors like Concealment of Fraud Collusion with Management Team Certification of Untrue and Unfair Account Lack of Professional Skills, Care & Diligence Tardiness in Discharging Duties have influenced corporate business failures. The study was conducted by using a survey on eighteen (18) companies listed in the Stock Exchange of Nigeria and State Centre for Alternative Investment was carried out through a self-administered structured questionnaire which was administered on strategically positioned personnel both in the top and middle-level positions of the firms.

The finding of the study indicates that external auditors have shown a lack of concern for ethical practices when engaged in public organizations and this had, in turn, resulted in corporate failures. The researcher stated that some of the auditors engaged to undertake to audit do not necessarily have to focus the general expectation of agency theory that expects utility maximization and commitment to rules of the relationship. In addition, the lack of commitment is expressed in the level of tardiness in discharging their duties to the public organization. Finally the study concludes that the correlation analysis showed the existence of external auditor's unethical practices concealment of fraud, collusion with management, certification of

untrue and unfair accounts, lack of professional skills, care and diligence and tardiness in discharging duties are major unethical behavior all significantly reflected on external auditors these practices' also results corporate business failure among public owned organizations.

Oseni, Abubakar Idris (2011), conduct a study on unethical behavior by a professional accountant in an organization, as per (Oseni, 2011). The ethical issues faced daily by organizations and their employees are neither always straightforward nor easy to resolve.

The study focus on what factors influence the likelihood that an individual will act ethically or less than ethical, and what this means to management, the organization, and internal controls in general.

The researcher covers the fundamental principles of professional ethics, issues on ethical behavior, issue related to human rights, the challenge of ethical behavior in organizations, types of unethical behaviors by financial reporters, reasons for behaving unethically, the reason why unethical behavior occurs in organizations monitoring unethical behavior and imposing penalty and how can promoting an ethical climate. Based on his research the ethical problems in organizations and the business environment is a great concern for the public, organizations, and individuals itself. (Oseni, 2011) recommend, accountant should be realistic in setting values and goals regarding employment relationships and do not promise what the organization cannot deliver, encourage input throughout the organization regarding appropriate ethical values and practices for (Etienne Chia-Ah and Joel Karlsson, 2010) implementing the cultures, use a whistle-blowing and/or ethical concerns procedure is established for internal problem solving and Provide ethics training programs for all employees.

Semiu Babatunde and Temitope Olamide (2013), conducted study on “The perception of ethics in auditing profession in Nigeria” The purpose of the study was to provide evidence on ethics, legitimacy of auditing profession and the future outlook of the profession in Nigeria by obtaining responses from external auditors, industry and academic accountants as well as auditing students which help to improve the auditing profession in Nigeria from the perspectives of ethics. In order to achieve this aim, the researcher includes three specific objectives which are investigating the credibility of the auditing profession, investigate the implication of accounting scandals on the auditing profession and finally examine whether any significant relationship exists among the perceptions of the respondent groups in their research.

Babatunde and Olamide (2011): a conducted a study on the need for auditors to abide by high ethical standard and the need to shape the views of new entrants to the profession. The finding of the research as per the analysis of data shows that there is no significant difference in the perception of respondent groups on the need for auditors to abide by high ethical standard and the need to shape the views of new entrants to the profession. However, respondents have a different perception of the decline of core values which attracted them to the profession. The study suggests that there is a need for the profession to gear its effort towards shaping the views of new entrants to the profession in Nigeria, ensure adherence and enforcement of the high ethical standard. Regulation of the profession should be targeted towards restoring the confidence of users of financial statements in financial reporting in Nigeria.

Bayou (2016), conducted a study on threats to professional ethics in Ethiopia, the objective of the research was to identify the threats that impede adherence to professional ethics among selected Authorized Accountants and Authorized Auditors in Ethiopia.

The pillars of ethical values rest on integrity, objectivity, professional competence and due care, confidentiality and professional behavior. Observance of these pillars of ethics was evaluated in light of threats and safeguards. The research approach employed for the study was mixed research augmented with simple statistical analysis. The findings indicate that there are lapses in the observance of professional ethics.

Wudu (2014) conducted a study on Auditor responsibility and fraud detection in Ethiopian Private Audit firms. The study was conducted to examine the roles and responsibilities of external auditors in fraud detection in Ethiopia including the factors that influence external auditors' responsibility and expert performance in detecting fraud. The study adopts a mixed methods research approach by combining data gathering instruments of research questions, in-depth interviews, and document analysis. The findings of the study show that auditors are responsible for detection and uncovering fraud, and are legally liable for subsequently discovered misstatement in audited financial statements. Reporting intentions of an auditor to the concerned body depends upon the type of fraudulent act basically if it is an investigative audit than financial statement audit. Fraud, in general, was not perceived to be a major problem in Ethiopian. Unwillingness to look for fraud because of fear of spoiling a good relationship with clients, too much trust placed on the auditees, management and employees, auditor not giving

enough emphasis to audit quality, management not having fraud policy; and, failure to focus on high-risk fraud areas. Fraudsters collusion, Absence of clear interpretation of tax law /proclamation, absence of the well-organized professional body in Ethiopia is listed among the most important challenges of auditors fail to detect fraud. The study also finds that the five variables which are certification, practical experience, training, audit fee, and independence significantly influence the auditor's expert performance to fraud detection.

The study suggests that Auditors need to “audit smarter which can be accomplished by the need for auditors to be more aware in a context which the audit occurs and the fact that the nature and concentration of fraud vary by industry and auditors should be aware of the development of their profession.

Fekede (2015) conducted a study on The Current Status of Professional Ethics and Independence of Private Audit Firms Engaged in Ethiopia and Its Overall Impact on Audit Quality. The main objective of the study was to examine the current status of private audit firms' professional ethics and independence and its overall impact on the quality of audit service provided to the public on 20 private audit firms selected based on stratified random sampling technique. The study used descriptive statistics to analyze the collected primary and secondary data using SPSS. The results of the study indicate that most of the private audit firms do not comply with professional ethics and lack independence from their client. This non-compliance came from self-interest, self-review and familiarity threats which result from lower audit fee, poor client assessment before accepting new engagements, having a family, financial and personal relationship with their clients. Moreover inactive and dormant contribution of the regulatory and professional association respectively also are other factors that contribute to unethical practice, lack of independence and lower audit quality provided by the private audit firm. The study recommends private audit firms should provide their professional services to the public in compliance with the rules and regulations stated by the regulatory bodies, Accounting, and Auditing Board of Ethiopia should prepare a well-organized code of professional conduct and ethics that strictly applied by all private audit, regulatory and professional bodies should set strong audit quality control, high standard audit practices and enforce all audit and other constructive recommendation stated under researcher paper.

Tsegaw (2017) conducted a study on Auditors Perception of Audit Quality in Ethiopia. The study examines the perception of auditors on audit quality and carried out by survey as a strategy of inquiry. The survey covers 88 external auditors who have a senior auditor and above positions Bayou (2016), have conducted on threats to professional ethics: among selected authorized accountants and auditors in Ethiopia. The objective of the research was to identify the threats that impede adherence to professional ethics among selected Authorized Accountants and Authorized Auditors in Ethiopia. The pillars of ethical values identified were rested on integrity, objectivity, professional competence and due care, confidentiality, and professional behavior. Observance of these pillars of ethics was evaluated in light of threats and safeguards

2.12. Conclusion and Knowledge Gap

In previous studies, the issue of professional ethics, behavior, auditor's quality and professional responsibility has been highly discussed and reviewed by many papers. Particularly in the case of Ethiopia so many studies have been conducted on the private auditors in Ethiopia but from a different perspective. For example, the study conducted by Fekede (2015), Bayou (2016), tsegaw(2017) and wudu(2014), was tried to show what kind of professional ethics that the auditors should have to follow but all researchers do not assess the legal liability with regard to private auditors; by considering the above literature gap, this study was conducted to assess the professional responsibility and legal liability with regard to private auditors in Ethiopia.

CHAPTER-THREE

RESEARCH METHODOLOGY

Introduction

This chapter consists of a research approach that the researcher was applied while conducting this study. The research methodology, research design, sampling and study period, data sources and types are given in detail. It also comprises the data analysis and the techniques used to achieve the objective of the study.

3.1. RESEARCH APPROACH AND DESIGN

There are three types of research approach, namely qualitative, quantitative and mixed approach. Qualitative approach used mostly when the researcher needs to develop a complex, holistic picture, analyzes words, reports, detailed view of informants, and conducts the study in a natural setting and involves studies that do not attempt to quantify their results through statistical summary or analysis (Creswell, 2009). The rational reason for the adoption of quantitative approach includes: to develop knowledge of cause and effect thinking, reduction to specific variables and hypotheses and questions, use of measurement and observation, and the test of theories, employee strategies of inquiry such as experiments and surveys (Creswell, 2009). The quantitative approach uses surveys of cross-sectional or longitudinal using self-administered semi-structured questionnaires with the intent of generalizing from a sample to a population. So well designed and implemented quantitative research approach has the advantage of making a generalization to a wider population from the sample. The mixed research approach is a means to collect both qualitative and quantitative data and analyses together to answer the research questions. In other words, it involves the collecting and “mixing” or integration of both quantitative and qualitative data in a study. A mixed methods approach is one in which the researcher tends to base knowledge claims on pragmatic (Creswell, 2009). Even though, each approach has its own objective and application time, in the selection process one should take into account the nature of the research problem or issues being addressed. Consequently, by considering this, the study in hand adopted a mixed research approach.

3.2. Research Design

According to Creswell (2009) research design is a plan or proposal to conduct research. It involves the intersection of philosophy, strategies of inquiry and specific methods. The researcher should define and evaluate research design before conducting the research since it is a blueprint for the collection, measurement, and analysis of data or conceptual structure which research is conducted (Kothari, 2004). For this study, the descriptive research design was adopted to assess the professional responsibility and legal liability of private auditors in Ethiopia.

3.3. Target Population

The target population of the study was all private auditors which are legally registered as an auditor with AABE and auditee (organization to be audited) located in Addis Ababa.

3.4. Sampling technique and Sample Size

The sampling technique used in this study was a multi-stage sampling technique, in which it includes Purposive sampling and cluster sampling technique. Cluster sampling was used to categorize the auditee (organization to be audited) into different groups based on their business type. While, purposive sampling was used to select the auditee (organization to be audited) from each cluster in order to represent that cluster, and additionally purposive sampling was used to select a sample of private auditors from a total population of the auditors as well as to make an interview with key personnel selected from a different organization. In doing so, the study classified the total population (clients) of study into five (5) clusters; which consists of the financial sector, construction sector, manufacturing sector, service sector and not for profit organizations. In the first cluster, a number of financial sectors are classified and includes; banks, microfinance institutions, and insurance companies. In this case, the researcher was set different criteria to select sample representative of organizations from the clusters; the criteria set by the researcher was like a year of establishment, profit, a number of branches and overall activity of the companies are taken to account to select from the cluster. So the researcher has selected each two (2) organizations from banks, microfinance institutions, and insurance companies respectively. The total sample representative of the first cluster is 6 organizations. In the second, third and fourth cluster those companies which are involved in construction, manufacturing and service sector are included respectively.

In this case, the researcher has included two companies for each of them; so the total sample representative of cluster two, three and four are totally 6 companies. And finally, the fifth clusters include not for profit organizations. Under the fifth cluster, the researcher was included 2 not for profit organizations. In this way the researcher has conducted data from each organization through questionnaires, the questionnaire was distributed to top management, assistant manager and internal control of the companies. Based on this fact it was useful for this study to analyze the professional responsibility and legal liability of private auditors in Ethiopia; by gathering data from different parties. In addition to this, the researcher was purposely included a number of Audit firm as target respondents for this study.

The sample size of the study was 78 personnel's, which are combined from different organizations; 42 of them are from different sectors, which includes 18 from the financial sector, 6 from the construction sector, 6 from manufacturing, 6 from the service sector and 6 from not for profit organizations. Additionally, the researcher was included 10 audit firms of private auditors found in Addis Ababa and the total respondents of the audit firms were 30 personnel. The auditors were included to fill the questionnaires' with subject to the study area. The questionnaires' was distributed to 72 personnel and collected from different organizations; while the interview was made with the general manager of Ethiopian accounting and auditing board, legal officers and three tax officers of Ethiopian revenues and customs authorities. in doing so, the researcher was distributed the questionnaires' based on personal judgment by considering that; those selected companies, as well as audit firms, have enough knowledge with regard to professional responsibility and legal liability regarding private auditors in Ethiopia.

Table 3.1: a sample size of the study

Category	Sample Size	Remarks
Financial sector	18	Located in Addis Ababa
Construction sector	6	Located in Addis Ababa
Manufacturing sector	6	Located in Addis Ababa
Not for profit organ	6	Located in Addis Ababa
Service sector	6	Located in Addis Ababa
Audit firms	30	Located in Addis Ababa
Key Informant Interview	6	3 from AABE, 3from ERCA
Total	78	

Source: researcher own selection

Table 3.2: classification of the cluster for the study

Cluster	Sectors	Selected companies	Selected Respondents
1	Financial sector	Awash International bank	3
		Commercial bank of Ethiopia	3
		Addis macro-finance institution	3
		Gasha macro-finance institution	3
		Nyala insurance company	3
		Nile insurance company	3
2	Construction	Tilahun General contractor	3
		Theodors Tsegaye Consulting Architects & Engineers	3
3	Manufacturing sector	Pioneer Hi-Bred Seeds Ethiopia	3
		PP bags Factory	3
4	Service sector	Accounting and Auditing Board of Ethiopia	3
		Ethiopia Revenue and Customs authority	3
5	Not for profit organizations	World Vision Ethiopia	3
		World Food Program	3

Source: researcher own selection

3.5. Source of Data and Data Collection.

To make analysis the researcher was used both primary and secondary data's. The primary data was collected through questionnaire, direct observation and, an interview. to gather the necessary information, Primary data was collected from respondents through a Survey questionnaire and Self-administered questionnaires usually completed by the respondents and administered electronically using the Internet (through respondent's e-mails) and delivered by hand to each respondent and collected later (delivery and collection questionnaires). The Questionnaires was prepared with open-ended and close-ended types of question that are relevant to the subject of the study. On the other hand, to get detail information about auditor's responsibility and legal liability the researcher was made face to face and telephone interview with the head of audit firms. Finally, the researcher was used as a secondary source of data which was obtained through review and selected materials such as

The Office of Federal Auditors-General (OFAG), in order to identify the sources of and audit requirement mandated by the international and local organizations, and to infer the auditor's professional and legal responsibilities and rationale, therefore;

The EPAAA in order to explore that to what extent do private auditors exercise their professional and legal responsibilities

Commercial code of Ethiopia, in terms of the major legal concepts that relate auditors' liability to clients and third parties under common law, and Other publications such as newspaper, magazines, Journals, and others, in terms of some, violated professional and legal responsibilities, and legal action taken at all.

3.6. Data Analysis Method

Data analysis is the coming task following the data collection in which the application of the statistical technique to evaluate data through inspecting, transforming and modeling data to draw useful information or decision making. "The term analysis refers to the computation of certain measures along with searching for patterns of relationship that exist among data-groups" (Kothari, 2004). To be useful the collected data was analyzed and interpreted in a meaning full manner, in doing so, descriptive statements, tabulation, charts, and percentages were used.

CHAPTER FOUR

DATA ANALYSIS AND PRESENTATION

Introduction

This Chapter deals with result and discussion of the study; In order to address the extent to which private auditors exercise their professional and legal responsibilities, and the extent to which the client prepare financial statements for easy verification. Moreover, it designed to explore the responsibility of directors (management) and auditors with regard to financial statements and subsequent to the discovery of misstatements to the audited financial statement. Additionally, this chapter also tries to examine the extent to which private auditors are subject to legal liability for committing illegal audit practices and the constraints that exist on private auditors in attempting to exercise their responsibility.

4.1. Descriptive analysis of the study

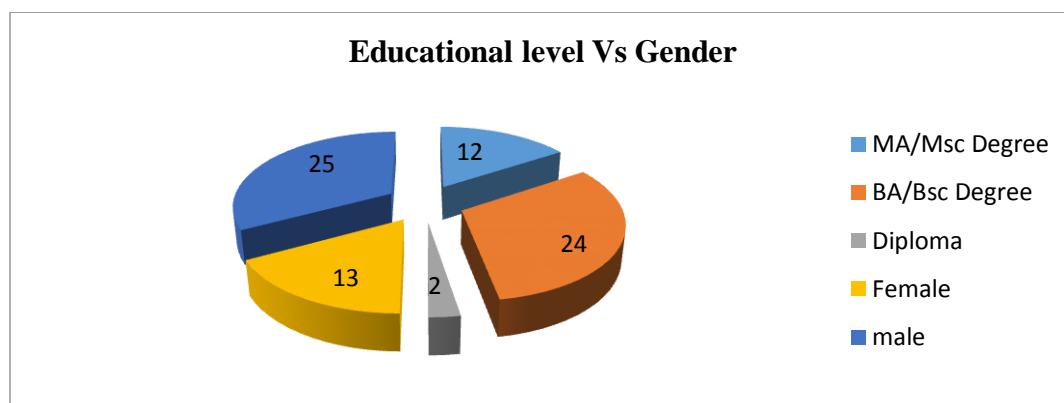
In order to achieve the objective of the study; the researcher was used both cluster and purposive sampling; cluster sampling was used to classify different organizations which are operating in the same sector as a group; while purposive sampling was used to select a sample of organizations from each cluster in order to represent the total population; additionally interview was conducted from the general manager of Ethiopian board of accounting and auditing, legal officers and a number of tax officers in Ethiopian revenue and customs authority. So the data collected through a questionnaire distributed to respondents and interview made with some authorized personnel were analyzed and discussed. At the same time information obtained from secondary sources such as reports and related forms, action has been analyzed by using different tools like simple tabulation percentage, graph, charts, and simple statement. The researcher has distributed 72 questionnaires to respondents but only 62 questionnaires were returned and the rest of respondents did not return the questionnaire. As it can be discussed in the following subsections of the chapter; the study was targeted two groups as a population, the first group was a client which are combined from different sectors; in this case, 42 respondents were included as a sample size, questionnaire was distributed to them and only 38 of respondents were give their responses.

While the second group was private auditors found in Addis Ababa, the sample size of this group was 30, but only 24 of them gave responses to the questionnaire distributed. Additionally, an interview was conducted with 6 personnel combined from different offices.

4.2. Demographic characters of respondents (Clients)

To start the basic part of the study it is appropriate to know the characteristics such as educational background and gender of respondents; in line with the data collected from the clients; the following figure shows the distribution related to educational level and gender of respondents.

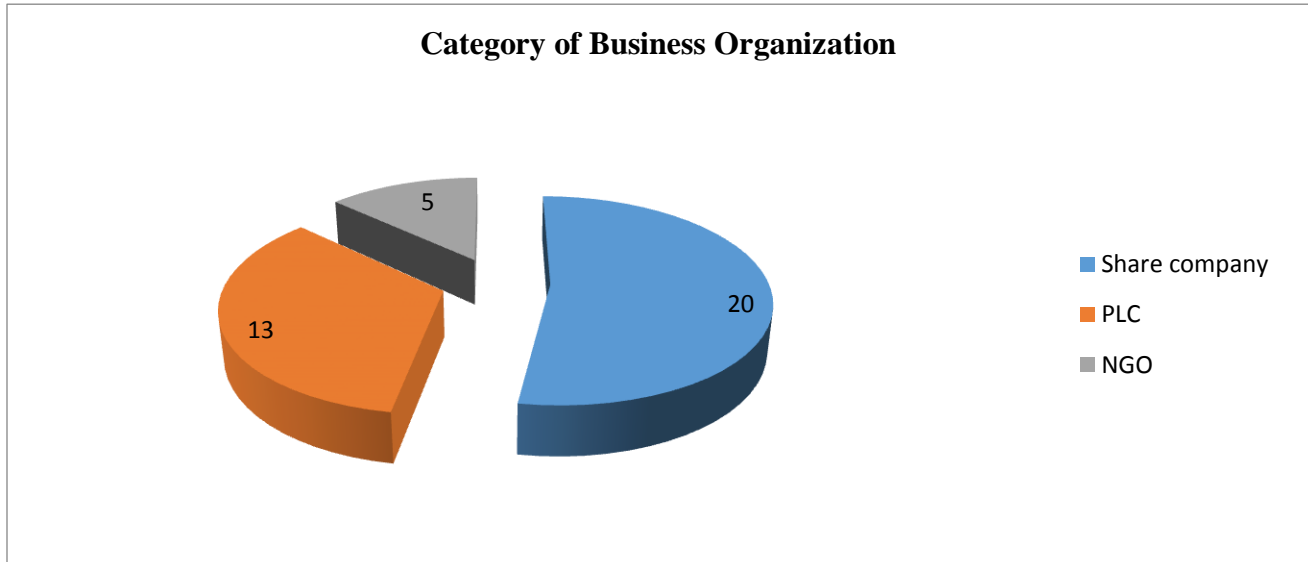
Figure 4.1: Educational level and Gender Distribution of the Respondents



Source: researcher own computation

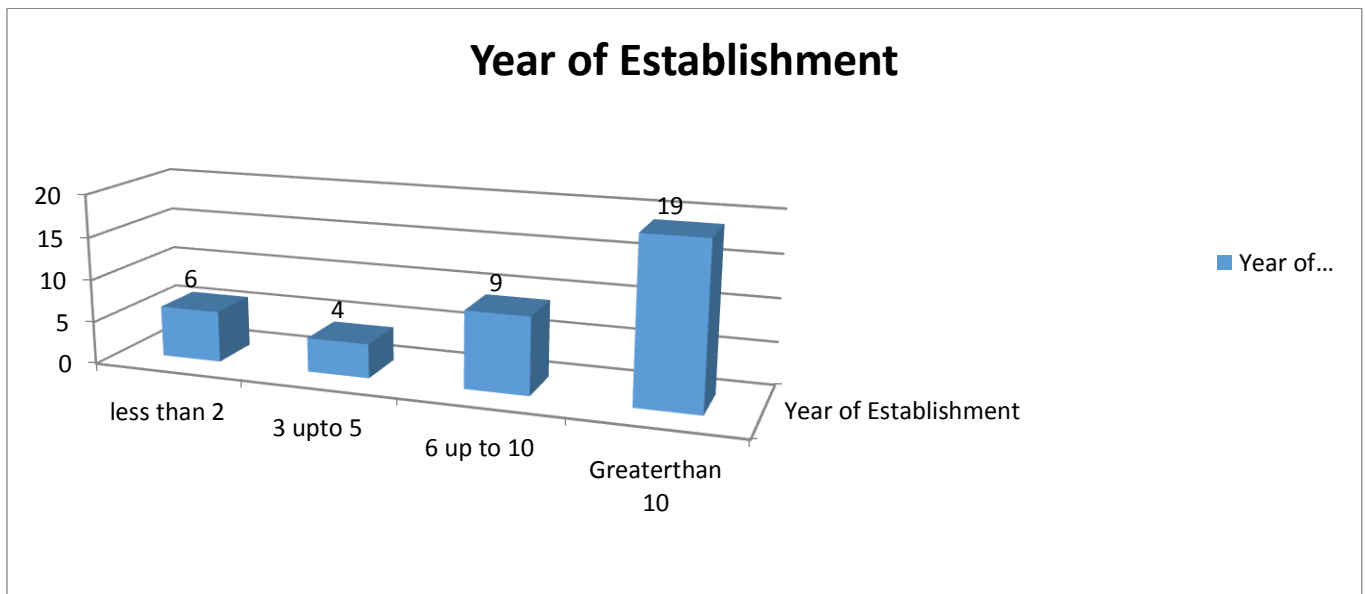
As it can be observed from the above figure 4.1; responses were obtained in majority from male respondents, which means, from the total 38 respondents clients, 25(65.79 %,) of them was male respondents. While the remaining 13(34.21%) of respondents were females. While regarding to their educational level of respondents; most of the respondents, 24 (63.16%) was first degree holders and 12(31.58%) was MA (master' degree) holders; finally, the remaining respondents which are (5.2%) 2 in numbers are a college diploma holders.. On the other hand, with regard to the respondent's gender; most of the respondents participated in this study was male respondents and this can be evidenced from the above data collected. From this it is possible to understand that, most respondents have educational level of first degree and above which is interesting for the quality of the studies. Because, it is assumed that; the more educated the respondent, the more the accurate answer they will provide when compared to uneducated (See appendix number 3).

Figure 4.2: Respondents/ companies category of business organization



Source: researcher own computation

Graph 4.1: Targeted companies/ Respondents year of establishment



Source: Researcher own computation

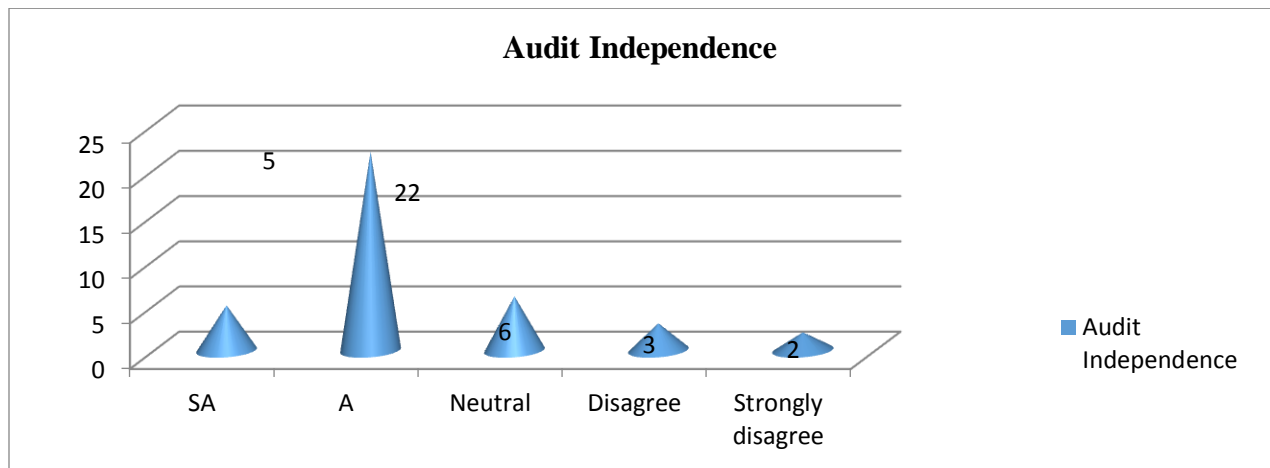
As it can be seen in the above graph 4.1 and figure 4.2 respectively, the question was provided to respondents/clients in order to know; on average how many years their current employer was operating its activities after its first establishment. The data collected with regard to this question revealed that; from the total responding organizations, the majorities are characterized as share companies, which is supported by 20(52.63%) of respondents. the reason behind is, most of the financial sectors in Ethiopia are share companies, which means since financial sectors are included in this study as a targeted population of the study; the researcher was included six financial institutions which are purposively selected as a target respondent of the study. so this is the real fact for increasing in a number of share companies. Additionally, a number of manufacturing companies were also found as share companies during data collection. While on the other hand, 13(34.21%) of respondents included in this study was from private limited companies. And finally, the remaining 5 (13.15%) of respondents are from nongovernmental organizations (NGOs). In this case, it is possible to understand that the data collected for this study are from different business sectors which are profit-seeking as well as nonprofit seeking organizations; and this increases the value of the study since the study is conducted by including different organizations. Furthermore, with regard to the year of the establishment; Most of the companies were aged more than 10 years on average, 19(50%). While 6 (15.79%) are aged less than two years. On the other hand, from a number of organizations participated in this study, 4(10.5%) are aged between three and five years. Finally, the remaining 9(23.69%) is between 5 and 10 years after establishment. This is a good indication for the reality of data collected, since; the companies which are participated in this study are a combination of the oldest, young and child one. Especially, those companies which have greater than five years' experience in doing business are engaged with different audit firms for more than five years on average; so it is not difficult for the clients to evaluate the professional responsibility and legal liability of the auditors (see appendix number 4).

4.3. Responses from Clients concerning as to what Extent Ethiopian Private Auditors are Exercising Professional and Legal Responsibilities

4.3.1. Independence

The survey was conducted in order to assess the auditor's independence in exercising professional responsibilities. Thus, in all matters relating to the audit work, the audit organization and the individual auditors, whether government or public should have an adequate degree of independence from the legislature and should be free from the executive and audited entity and should maintain an independent attitude in fact and appearance. The survey result concerning independence is as follows:

Graph 4.2: Respondents response to auditor's independence



Source: researcher own computation

As it can be shown in the above graph 4.2; the respondents' response with regard to a question that shows the independence of auditors from their clients in all matters is provided. According to the data collected from respondents, the following finding arrived during the study period. Most respondents, 27(71%) agreed (responded) that private auditors in Ethiopia were independent in all aspects from the influence of audit organization in relation to the audit activity they have performed. However, a considerable number of 5 (13.15%), confirmed that private auditors in Ethiopia were not independent in all matters. Furthermore, the other respondents 6(15.78%) were responded as neutral. Since some number of respondents shows straight forward disagreement about private auditor's independence; anyone can understand that; there is a

problem related to private auditors in Ethiopia with respect to protecting professional independence of auditors (see appendix number 5). On the other hand, the interview was conducted with some personals of Ethiopian accounting and auditing board and number of tax officers of Ethiopian revenue and customs authority in order to get detail information about independence of auditors from their clients. The majority of the respondents responded as saying that; in all aspects, private auditors were independent of their clients. But, one tax officer of the Ethiopian revenue and customs authority does not agree on this, by giving an indication of that; most of the case, private auditors loss independence in terms of soliciting clients, negotiating audit fee, and giving an opinion. The data collected through the questionnaire as well as interview shows there is a disagreement by some respondents regarding the independence of the auditors; so it's an indication for further assessment on the study area. In line with this, as stated in the article of Tesfaye Mengasha, on the capital weekly newsletter, " bidding/tendering cited on muluneh (2007). The following points were discussed by the writer in order to show how the independence of the private auditors can be affected in Ethiopia and the issue was related to audit fee.

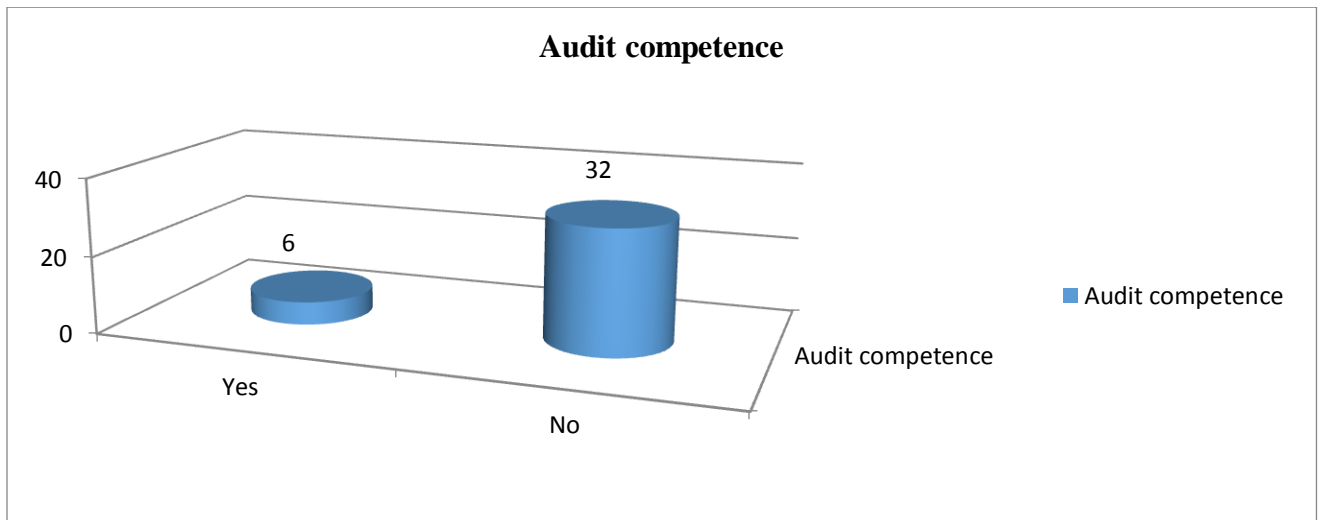
Audit fee levels were recovered to be the lowest even by African standards before the tendering/bidding systems came about. What if such reductions in fees are achieved at the expense of the quality/effectiveness of the independent audit, which is the "raison-d'etre" of the entire exercise?

When the tax collection role of the government is considered, the quality of the audit, as a reliable source of information, becomes even more important, relative to the required audit fees. This is because of; any audit has its own startup costs to the auditor concerned and government shall consider these costs to protect independence of auditors. From the above overall analysis of the data; the researcher concluded that private auditors in Ethiopia were independent in their audit activity but there could be an occasion where private auditors by force or interest can violate the principle of auditor's independence from their clients in conducting an audit activity.

4.3.2 Competence

The audit organization needs to command the range of skills and experience necessary for the effective discharge of the audit mandate. Whatever the nature of the audit to be undertaken under that mandate, persons whose education and experience is commensurate with the nature, scope, and complexities of the audit task should carry out the audit activity. The survey result is shown in this regard as follows:

Graph 4.3: Respondents response to auditor's competence



Source: researcher own computation

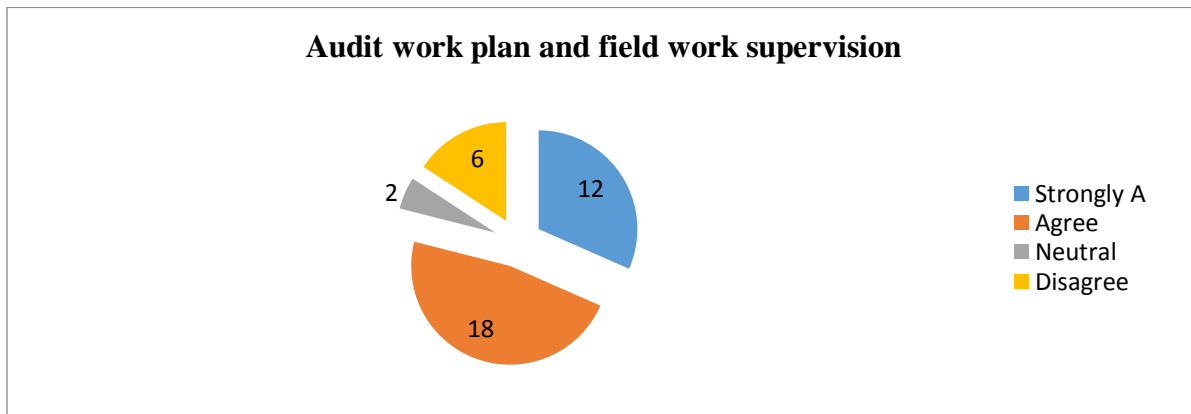
The above graph 4.3 shows the respondents response with regard to a question that shows a competency of auditors in performing audit activity. As the result indicates, 32(84.20%) of the respondents showed that auditors were professionally skilled, trained and competent in order to carry out their professional responsibilities. While 6(15.80%) of respondents were not agreed with the professional competence of the auditors and they have responded by saying that we have faced professionally not trained auditors. On the other hand; the question was provided for the respondents what kind of decision they have taken when incompetent auditors faced them; most of them responded as saying; the number of auditors which incompetent are BA degree holders, in this case, we inform the audit firms and directly change that person with other experienced auditors. Additionally, the result of interview responses revealed that; most of the time individual auditors hold B.A degree and above in accounting profession in order to perform audit work is incompetent and this makes the level of audit practice danger. Thus, in accordance

with the data collected and interview results, the researcher concluded that most private auditors in Ethiopia are professionally trained and competent except on some occasions (see appendix number 6).

4.3.3 Audit Work Plan and Supervision

The auditor should plan the audit work in a manner which ensures that an audit of high quality is carried out in on time, an economic, efficient and effective way. On top of this, proper supervision and control are therefore necessary in all cases regardless of the competence of individual auditors. The data collected with regard to the audit work plan and supervision is shown in the table below:

Figure 4.3: Respondents response to the audit work plan and fieldwork supervision



Source: researcher own computation

Figure 4.3 shows the respondents response with regard to; if the auditors make audit work plan and mandatory supervision was made by audit firms; As it can be observed in the above figure 4.3; the majority of the respondents 30(78.90 %) agreed that private auditors in Ethiopia are properly planned their work and the senior auditors frequently supervise field auditors. While 6(15.78%) of respondents responded as saying; the private auditors in Ethiopia are not properly planning their work and also the senior auditors do not give any supervision.

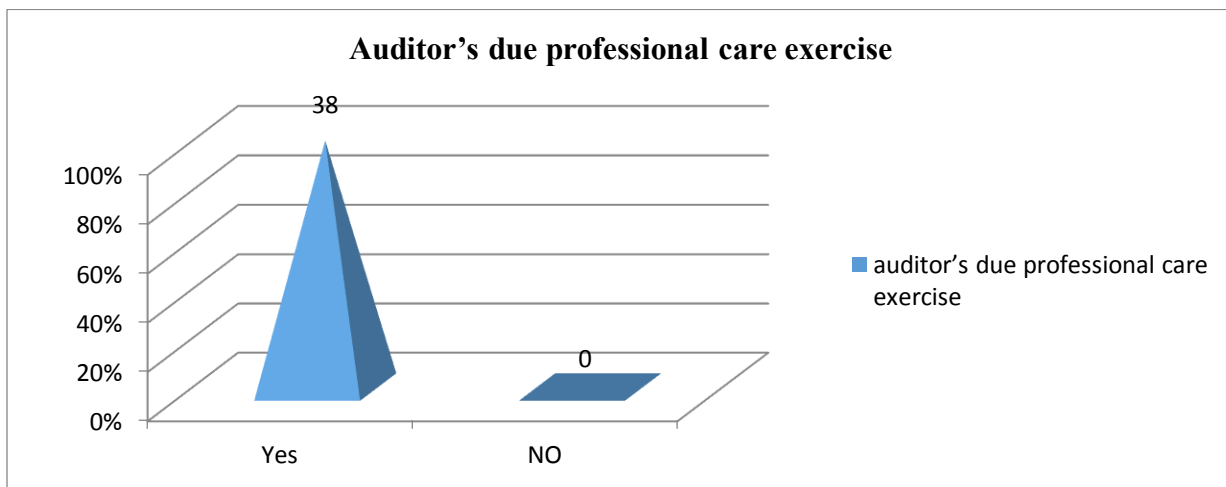
On the other hand, the remaining respondents 2(5.26%) responded as neutral. Which indicates, they have no information about the question provided to them with regard to auditors work plan and mandatory supervision. Furthermore, the entire interviewee responses depicted the same conclusion; which shows that; the auditors have properly planned their work and the senior

auditors frequently supervise the field of auditors. Hence, the analysis of the overall data shows that private auditors adequately plan their audit work and frequently supervise the work of field auditors (see appendix number 7).

4.3.4: Due Professional Care

The researcher also tried to identify whether the auditor exercise due professional care or not. Thus, the auditor and the audit organization must exercise due care and concern in complying with the auditing standards. This embraces due care in specifying, gathering and evaluating evidence, and in reporting findings, conclusions, and recommendations. In this regard, the data collected from the respondents summarized hereunder.

Graph 4.4: Respondents response to auditor's due professional care exercise



Source: researcher own computation

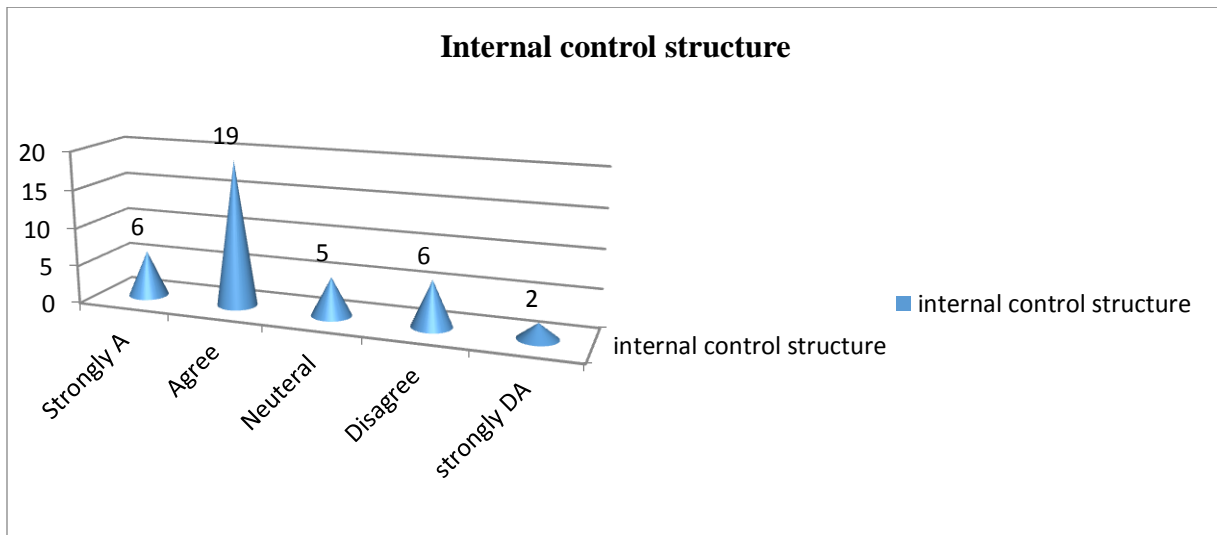
Accordingly, as it is shown in the above graph 4.4; all respondents have indicated the same answer for the question related to if they're all audit process needs due to professional care in audit activity. As a result, the interview conducted from the respondents indicates the same conclusion about the importance of due professional care in processing audit work.

Thus, both preparation of financial statements, which is the responsibility of the management of the client; and examination of the financial statements, which is the responsibility of the auditor's need exercising due professional care (see appendix number 8).

4.3.5 Internal Control Structure

The study also tried to clarify whether private auditors examine the internal control structure of an audited entity. Thus, as it was obtained from the respondent's responses, most of them agreed that; auditors examine the internal control structure of an audit organization. The survey with regard to internal control structure is summarized as follows.

Graph 4.5: Respondent's response to the internal control structure



Source: researcher own computation

As we can observe from the above graph 4.5, most of the respondents (65.79%) agreed that; private auditors in Ethiopia examine the internal control structure of an audit organization. While on the other hand, 21% of respondent responded as saying no; which means, the private auditors in Ethiopia do not examine the internal control structure of an audit organization. On the other hand, a number of considerable respondents responded as saying neutral about the issue. Similarly, the result of the interview shows that; examining the internal control structure of an organization under audit helps to evaluate the extent of sampling, tests of the documents in order to gather sufficient evidential matter to express an opinion.

Based on this fact, the researcher concludes that; examination or evaluation of client internal control system helps the auditor in gathering the important information for the expression of an opinion. From the data collected with this regard, it is possible to understand that; most of the private auditors in Ethiopia conduct or examine the internal control structure of the companies,

but, since there are a number of respondents those do not agree with this, it needs further investigation on the issue (see appendix number 9).

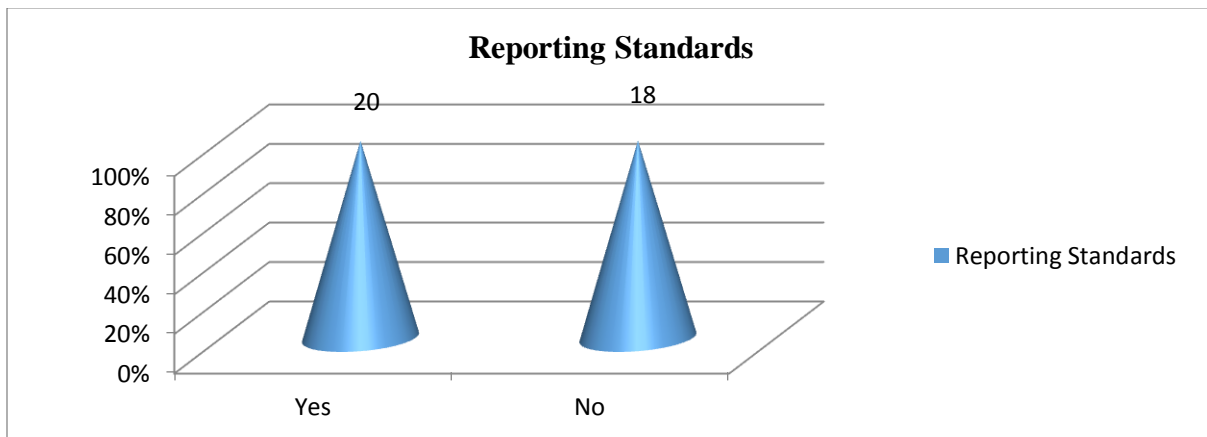
4.3.6 Evidence

The researcher also administers an interview in order to obtain data to identify how the auditors obtain sufficient evidential matters in order to express an opinion. Accordingly, the majority of the respondents responded that such information was obtained through inspection, observation, inquiries, and circulating confirmations to serve as a reasonable basis for an opinion.

4.3.7 Reporting Standards

The auditors should follow reporting standards while preparing a report for the users. The reporting standards demand that the report shall state whether financial statements are presented in accordance with applicable financial auditing and reporting standards; whether such principles have been consistently applied in the current period in relation to the previous period; adequate information disclosure to the users of the report; and an expression of an opinion regarding the financial statements, taken as a whole, or an assertion to the effect that an opinion cannot express.

Graph 4.6: Respondent’s response to principles followed by auditors



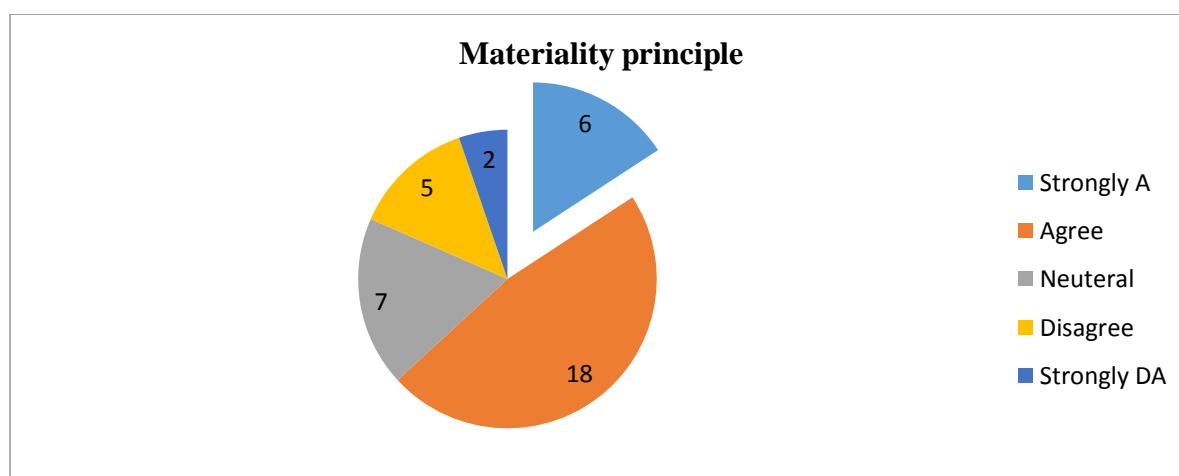
Source: researcher own computation

Accordingly, the result of the survey revealed that some of the respondents, 20(52.63%) responded that, the generally accepted auditing standards are applied in the preparation of the financial statements and auditors also follow that principle in examining audit activity. While on the other hand, a number of respondents, 18(47.37%) responded that other principles were

followed than generally accepted auditing standards in their organization. Regarding to open-ended question, the respondents were asked to specify other principles followed by auditors in conducting audit activity in their companies if not GAAS; and almost all respondents responded as saying, in current situation after international financial reporting standards become a mandatory principle that should have to be followed in preparing financial statements; also, international auditing standards are followed in line IFRS for the sake of financial auditing.

So, they have started to use international auditing standards as a principle in auditing financial statements; which is, in line with the new financial proclamation of 2016; which commands all companies found in Ethiopia to prepare their financial statement in accordance with international financial accounting standards. In this case, the auditors conduct their audit examination based on international audit standards. The result of the interview also showed a mixed justification on the principles used in preparing financial statements and examining audit. According to the interviewee, the reason behind for mixed answer is in that; most companies in Ethiopia do not start to use international financial accounting standard as a base in preparing financial statements, and this is because of the length of time it takes to convert all data to IFRS. From the above finding, it is possible to conclude that; the private auditors in Ethiopia have previously followed the principle that was based on generally accepted but because of change in financial proclamation; presently they base their principle on international audit standards (see appendix number 10).

Figure 4.4: Respondents response on materiality principle



Source: researcher own computation

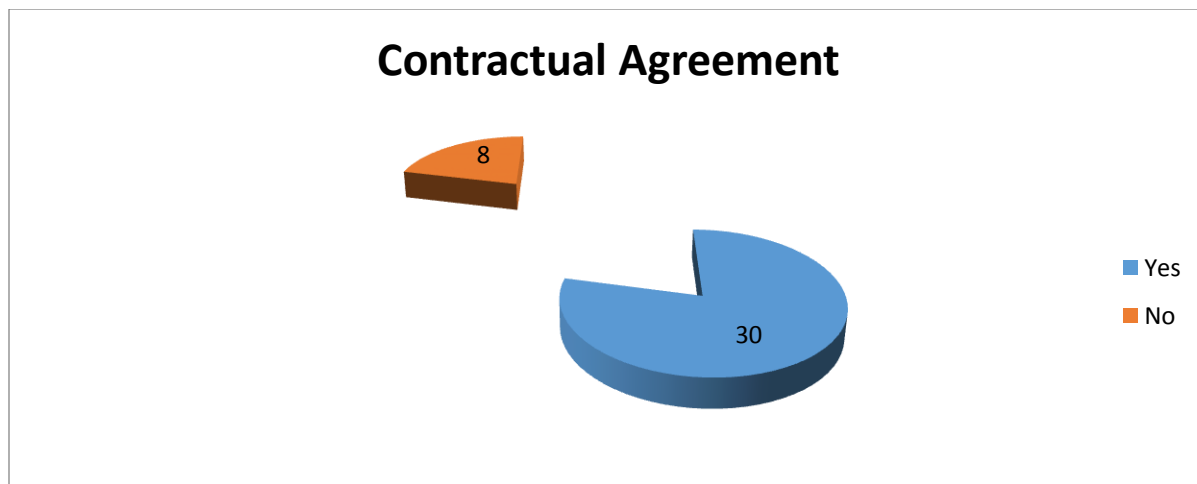
The survey result showed that; 63.15% of the respondents confirmed that; auditors follow the materiality of information in disclosing to the users of the report. However, 18.42 % of respondents disagree with auditors were disclosing all information obtained, regardless of its materiality to the users of audited financial statements. Furthermore, 18.42% of respondents responded to the issue related to disclosing materiality as a neutral.

On the other hand, the interview response showed that even though the error obtained was immaterial, the long run effect of the information on the going concern was taken in to account to disclose in the report. Additionally, they added that such immaterial information was reported on the management letter for internal control purpose and in order to eliminate the long run effect of it. From this, the researcher concludes that; private auditors in Ethiopia were properly planning and performing the audit so as to obtain sufficient evidence to give reasonable assurance that the financial statements of the client are free from material misstatements (see appendix number 11).

4.3.8 Contractual Agreement

The second part of this section deals with the auditors legal responsibilities with regard to the examination of the financial statements of the audit client's from the point of view of both clients and auditors. In this regard the researcher attempted to assess the issues as follows:

Figure 4.5: Respondents response on a contractual agreement



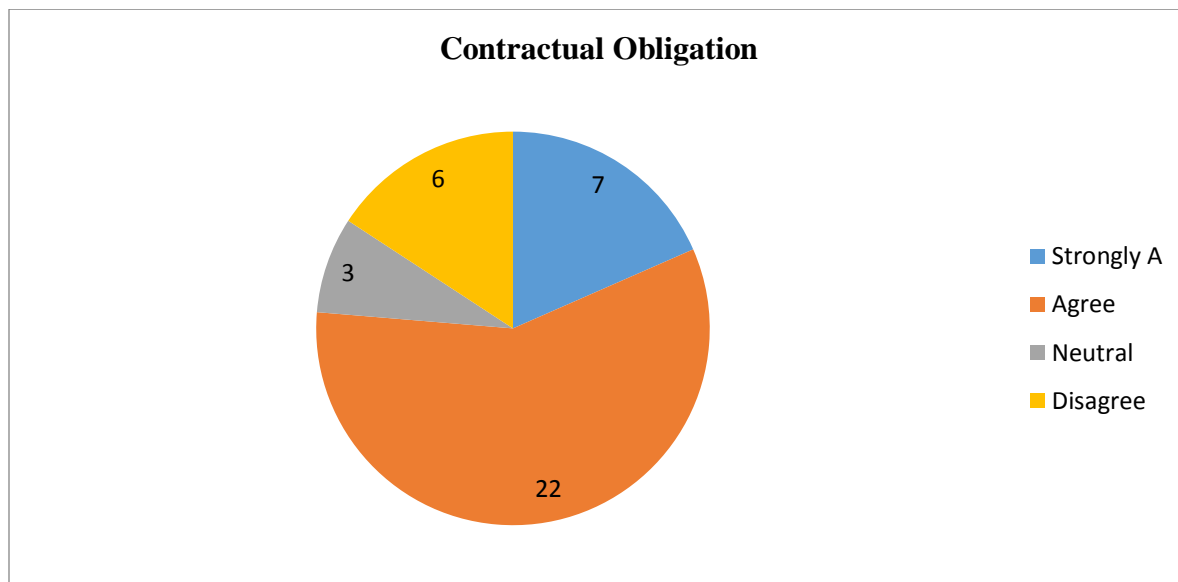
Source: researcher own computation

As indicated in table 4.9, of the total respondents, 79%, replied that once the auditor is assigned or selected, the next step is signing contractual agreement consisting of the scope of the audit, the qualification of the auditor’s staff to be involved in the audit task, duration of the audit work, responsibility of the management and the auditors, audit fee and others. Similarly, all the interviewed auditors responded that it is mandatory to sign contractual agreement consisting of the scope of the audit, the qualification of the auditor staff to be involved in the audit task, duration of the audit work, the responsibility of the management and the auditors, audit fee and others before starting the audit. From these, the researcher can conclude that; businesses sign a contractual agreement with auditors before starting auditing the books of accounts (see appendix number 12)

4.3.9 Contractual Obligation

A contractual obligation is something that you are required to do because you have agreed to it by way of a legally binding contract (whether in writing or verbal). So once, the auditor signs a contractual agreement with its clients. The auditor has the obligation to perform that activates. With regard to a contractual obligation, the following figure shows the responses of respondents.

Figure 4.6: Respondents response to auditor’s contractual responsibility



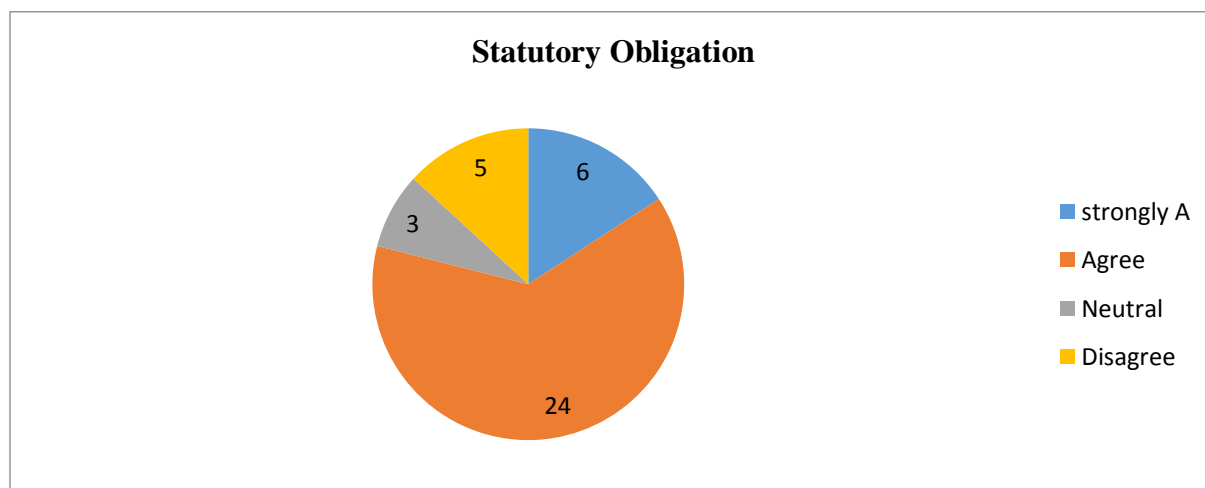
Source: researcher own computation

As it is depicted in the above figure 4.6; all the respondents, 76.3% of respondents confirmed that; auditors are responsible for contractual agreements made between the client and the auditor. Moreover, the respondents confirmed that auditors who violate a contractual agreement are made legally liable to the client and the law of the land. On the other hand, a considerable number of respondents do not agree with the contractual obligation of the auditors. And this can be evidenced from the above data collected as 6 (15.79%) of respondents responded as saying disagree. Furthermore, as determined from the interview result, private auditors have the responsibility to follow the contractual agreement signed between the two parties in conducting audit work. Thus, from the analysis of data on auditor’s contractual responsibility, it is possible to infer that private auditors are made liable for the violation of contractual responsibility (see appendix number 13).

4.3.10 Statutory Obligation

As stated in Art. 380 of the commercial code of Ethiopia, auditors shall be civilly liable to the company and third parties for any fault in the exercise of their duties which occasioned loss. Besides, an auditor who knowingly gives, or confirms an untrue report concerning the position of a company or fails to inform the public prosecutor of an offense which he was known to have been committed shall be punished under Art. 438 or Art.664 of the penal code as the case may be. The survey result in this regard is as follow:

Figure 4.7: Respondents response to auditor’s statutory responsibility



Source: researcher own computation

As it is depicted in the above figure 4.7, (78.90%) of respondents confessed that; auditors are responsible for statutory audit requirements. Moreover, the respondents confirmed that auditors who violate statutory responsibility are legally liable for both to their client and a third party. While on the other hand, (13.15%) of respondents disagreed with this question; Furthermore, as examined from the interview result, private auditors have the responsibility to follow statutory audit requirements when conducting audit work and made liable for the violation of those responsibilities. In general, from the overall analysis of the data, it is possible to conclude that private auditors are liable for the violation of statutory responsibility (see appendix number 14).

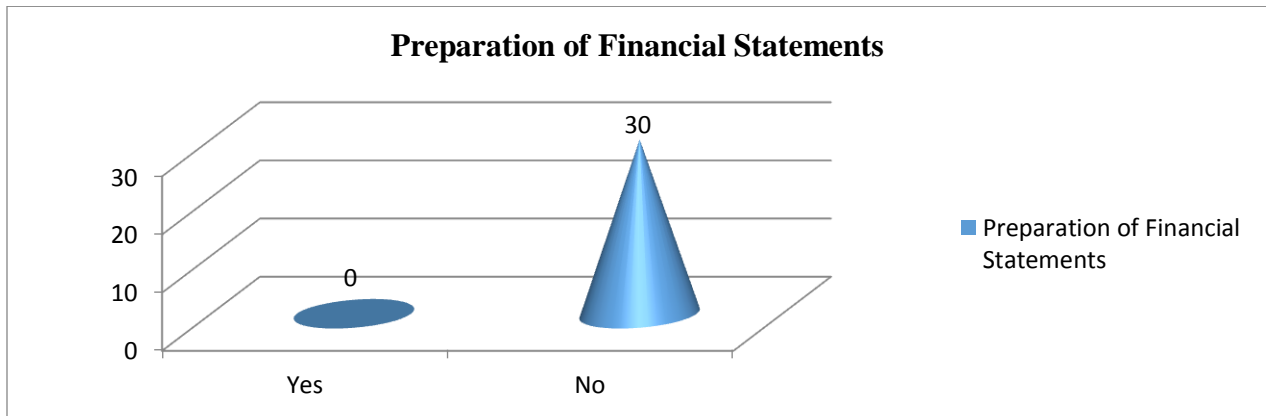
4.4. The responsibilities of management and auditors with regard to the financial statements and subsequent to the discovery of misstatements to the financial statements

In any corporate organizations, the responsibility of management is different from the responsibility of auditors. In order to identify the responsibilities of the management from the auditor with regard to the preparation of financial statements and subsequent discovery of misstatements to the audited financial statements the researcher explores the following results:

4.4.1 Preparation of Financial Statements:

Preparing general-purpose financial statements; including the balance sheet, income statement, statement of retained earnings, and statement of cash flows; is the most important step in the accounting cycle because it represents the purpose of financial accounting. Preparation of such like statement is mainly the responsibility of management than external auditors. The survey with regard to the party prepare financial statements is summarized hereunder.

Graph 4.7: Respondent's response to the preparation of financial statements

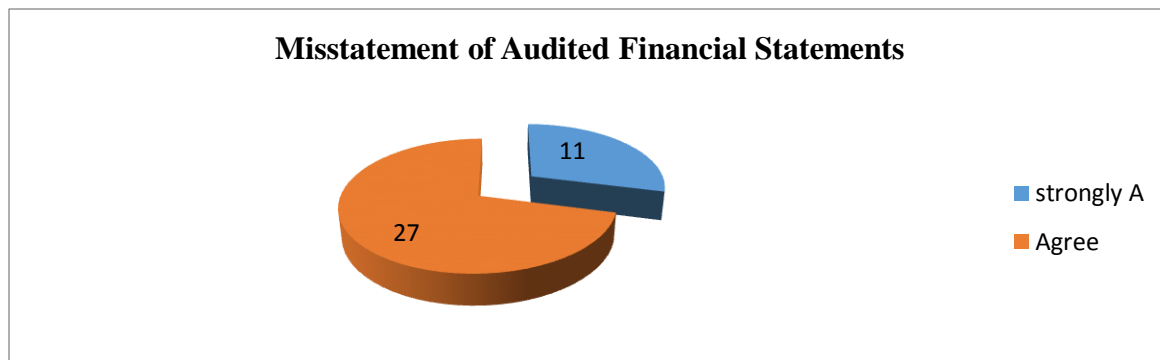


Source: researcher own computation

As it is depicted in the above Graph 4.7, all the respondents (100%) agreed that preparation of financial statements is the responsibility of the management of the client organization. Accordingly, the interview result revealed that all the interviewee responded like that, preparation of financial statements is the responsibility of the management, whereas it is the responsibility of the auditor's to express an opinion whether the financial statements produced presents the "true and fair view" of the entity. From the above analysis, it is wise to conclude that preparation of financial statements is that of the client whereas the auditor's responsibility is examining financial statements produced by their client (see appendix number 15).

4.4.2 Misstatement of Audited Financial Statements

Figure 4.7: Respondents response to auditor's statutory responsibility



Source: researcher own computation

As depicted by the above figure 4.7, the entire respondent (100%) agreed that private auditors are legally liable for subsequent discovery of misstatement audited financial statements. Similarly, all the interview respondents showed agreement to the same conclusion. However, the interviewee argued that this holds true only if the auditor expressed an inappropriate opinion.

From the above data collection, the researcher concludes that the auditors not liable for subsequently discovered misstated audited financial statements if their opinion was qualified for these effects (see appendix number 16).

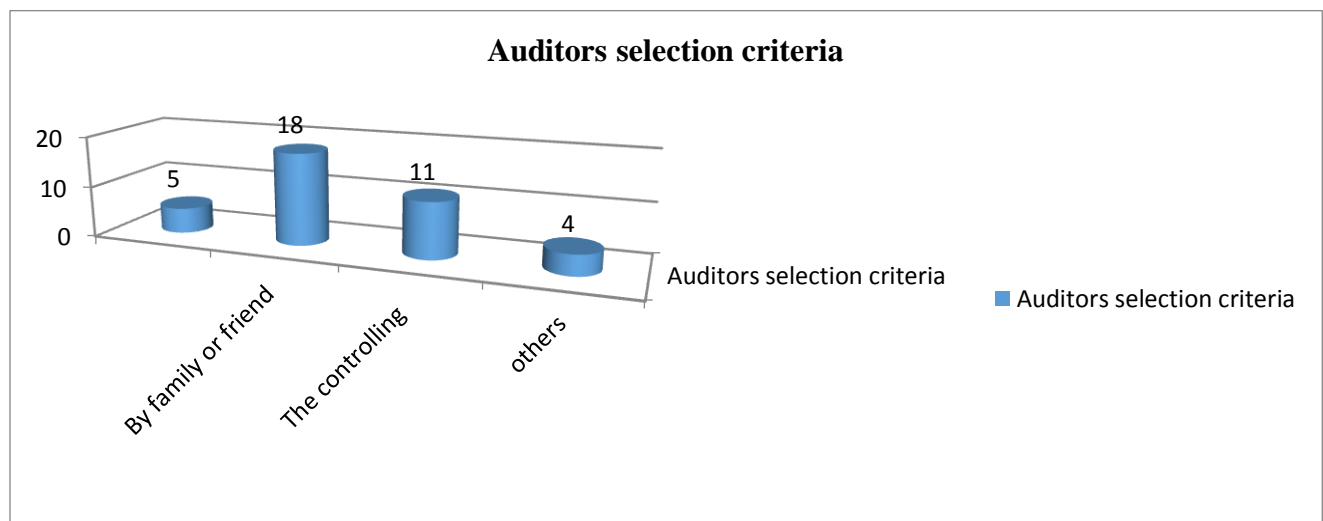
4.5: Responses with Regard to Auditor’s rules of Professional Responsibility

Advertising and solicitation should be aimed at informing the public in an objective manner and should be decent, honest, truthful, and in good taste. Solicitation by the use of coercion or harassment should be prohibited.

Supporting the above Jack C. Robertson (1990) argued that professional responsibility for auditors is not simply a matter covered by a few rules in a formal code of professional conduct. Concepts of proper professional conduct permeate all areas of practice. Ethics and its accompanying disciplinary potential are the foundation for public accountant’s self-regulatory efforts (Jack C. Robertson: 1990). The survey result in this regard showed the following:

4.5.1 Selection of Auditors

Graph 4.8: Respondent’s response on criteria for auditor’s selection



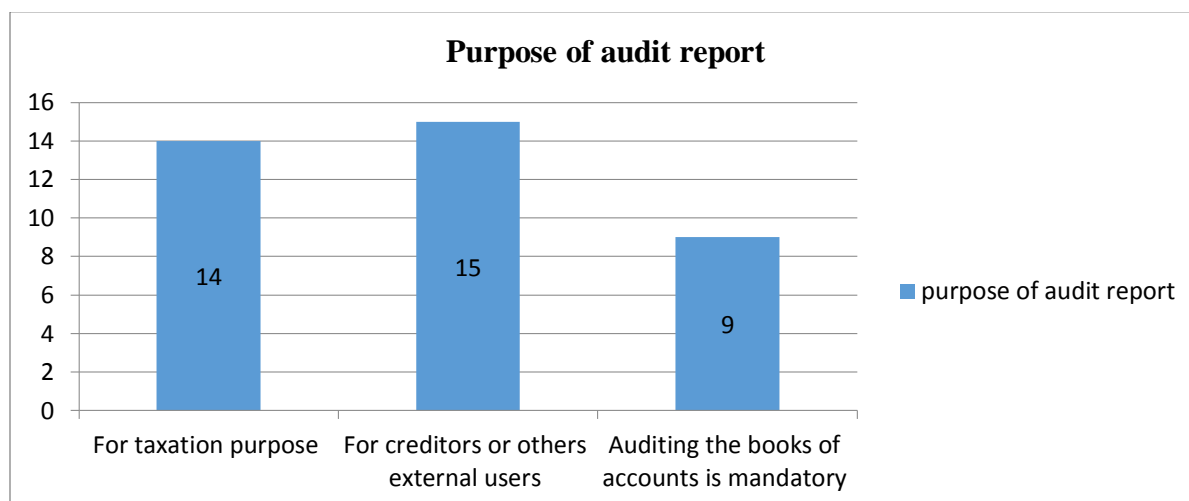
Source: researcher own computation

As we can observe from the above graph 4.8, 17.85% of respondent responded by saying that, they select auditors through advertisement on the media, while 47.40% of respondents responded as saying; they select auditors by their family or friend relationship and 28.90% of respondents responded as; controlling part can assign the auditors to audit financial statements of the companies. Finally, (10.5%) of respondents responded as saying the assign auditors based on recommendations. So the results of the data collection show that; it is obvious that the organization selects audit firms based on individual organization decision (see appendix number 17).

4.5.1 Purpose of Audit Report

In order to make rational investment, credit rating, business expansion, and other decisions, decision makers rely on the financial information of business entities. The decision makers are more confident when such financial information is examined by independent professional auditors. From the above perspective, the survey tried to look at the following questions.

Graph 4.8: Respondent’s response to the purpose of the audit report.



Source: researcher own computation

As shown by the above response result on graph 4.8, 39.48% of the respondents agreed that the purpose of auditing books of accounts is in order to satisfy the creditors in making decisions regarding loan and trade on accounts. On the other hand, 36.84% of the respondents argued that

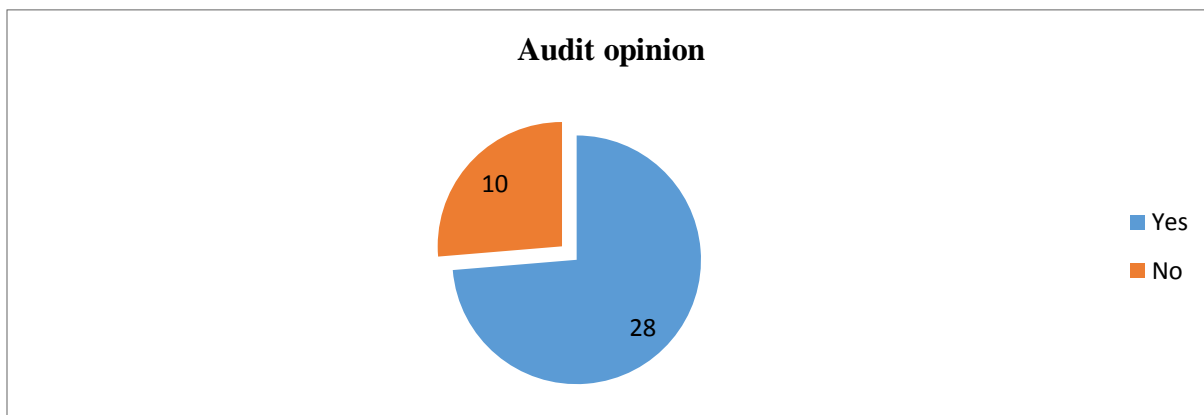
the purpose of the audit report is for taxation purpose and 23.68% of respondents replied that it is mandatory to audit books of accounts.

Hence, from the above analysis, it is possible to conclude that; the responses made by respondents are mainly based on their understanding about the purpose of auditing in a different perspective because most clients confirmed that the purpose of auditing the books of account is for creditors or other external users (see appendix number 18)

4.6. Constraints to Private Auditors in Attempting to Exercise their Responsibility

As stated in the review of literature part of the study, in order to make rational business decisions, investors, creditors, managers, shareholders of a business need financial information of their own as well as competitors. Accordingly, in order to be confident in making a decision, they base their decision on audited financial statements. Therefore, it is the responsibility of auditors to disclose information shown on the financial statements to the users of audited financial statements. However, there are constraints on auditors in attempting to exercise their responsibilities. Thus, as determined from the survey questionnaire and interview result, auditors are subject but not limited to the constraints:

Figure 4.8: Respondents response to the Audit opinion



Source: researcher own computation

As it can be seen in the above figure 4.8, most respondents (73.7%) responded that; they have an expectation on another audit opinion than unqualified audit opinion. While 26.30% of respondents responded that; they have no expectation on other audit opinions than unqualified

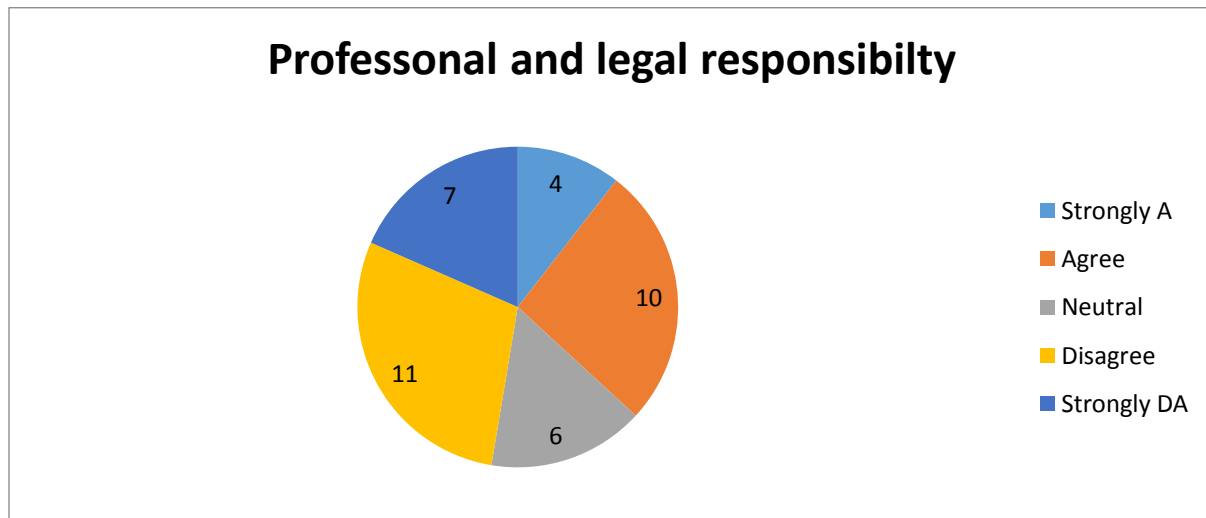
audit opinion. Similarly, the data conducted through interview showed that all the time organizations demand unqualified opinion; when the opinion goes too qualified or disclaimer or adverse, they tried to change that audit firm (see appendix number 19).

In this regard, Tesfaye Mengasha articulated on Capital weekly newsletter dated 13 July 2003 cited in muluneh (2007) shows how to audit opinion can be affected. The issue is discussed in the following paragraph.

Some of us might find it difficult to imagine as to how the same Bank with two different auditors could arrive at two different results using numbers, which we normally understand them to be precise. Unfortunately, accounting is full of estimates. An audit is simply an exercise of professional judgment. Both the international and local auditors are entitled to their own opinion. However, to me, as an outsider now, the divergence of this magnitude cannot be easily accommodated within the spectrum of "opinion" difference, of course, assuming the two exercises to be similar in scope". (Capital: 2003). This shows that, though the auditing standards applicable by both international and local auditors are the same; there could be an occasion that auditors compromise professional responsibility.

From the above analysis and discussions, the researcher concludes that there is a circumstance where the auditors are negotiating with their client to change the opinion.

Figure 4.9: Respondents Response on exercising professional and legal responsibility of Auditors.



Source: compiled by a researcher

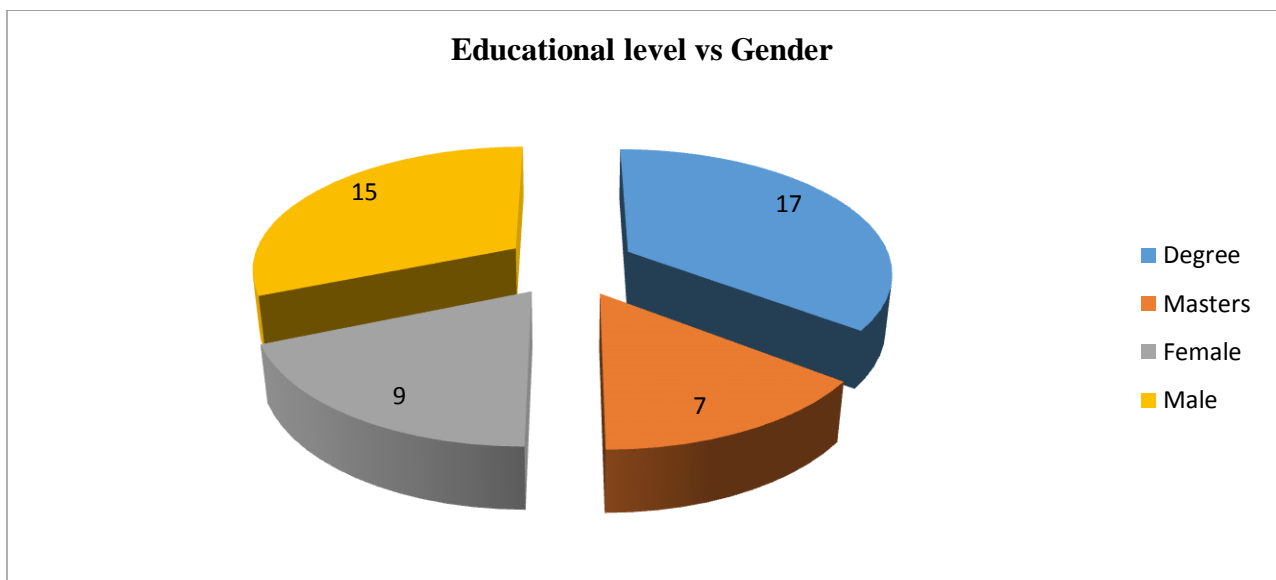
As it can be seen in figure 4.9, the results of data collected show that; a large number of respondents 18(47.37%) were not agreed with the question provided to them in order to know whether private auditors in Ethiopia exercise professional and legal responsibility or not. The result of the data collected shows that; most of the respondents do not agree with this fact. On the other hand, a considerable number of respondents (36.8%) were agreed on that; the Ethiopian private auditors exercise both professional and legal responsibility. Furthermore, the result of the interview also showed the mixed result with regard to exercising professional as well as the legal responsibility of private auditors. In which, most of the respondents were agreed on that; there is a violence of professional as well as legal responsibility by auditors; since most of them are engaged in audit activity of one company through family or friendship relationship. From the data collected, the researcher concludes that; the issue of exercising professional and legal responsibility is considered at risk in Ethiopia.

4.7. Responses from Auditor’s concerning as to what Extent Ethiopian Private Auditors are Exercising Professional and Legal Responsibilities.

4.7.1. Demographic characters of respondents

In the first part of this chapter; the discussion for demographic characteristics of clients was analyzed and interpreted; in this part, the demographic characteristics of the auditors is discussed and presented hereunder.

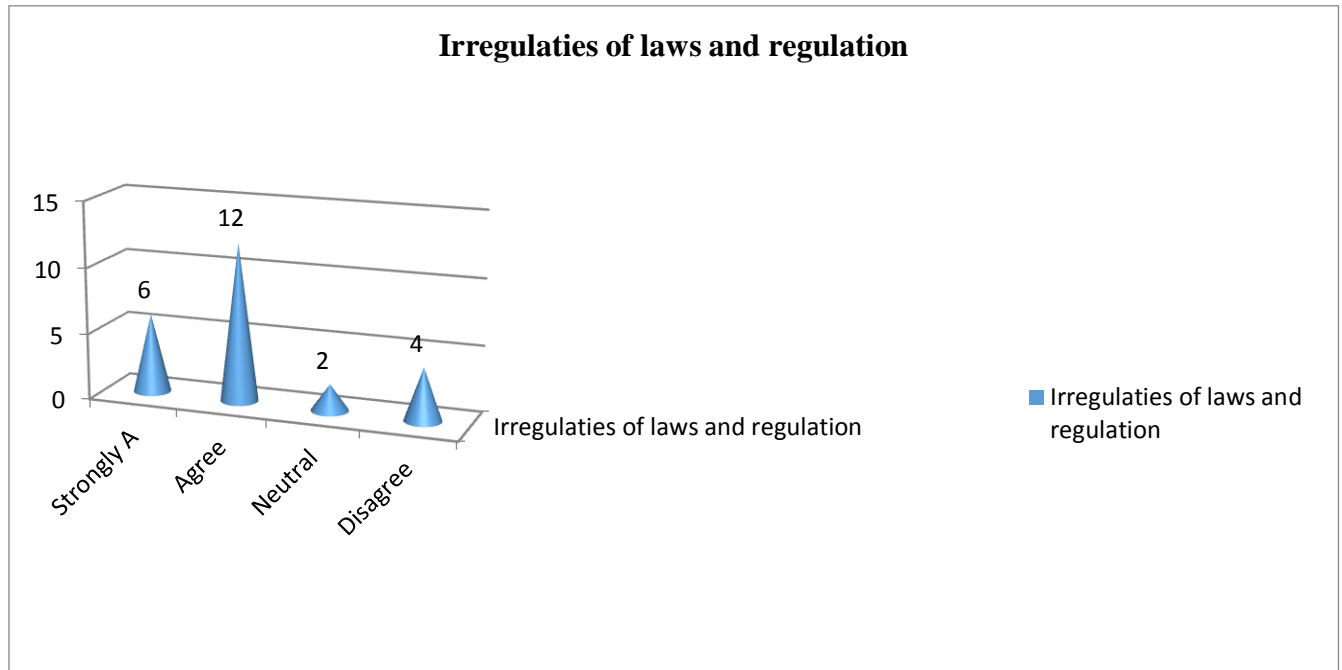
Figure 4.10: Respondents (Auditors) response with regard to their Gender and Educational level



Source: Researcher own computation

With regard to auditors educational level and gender, as it can be observed from the above figure 4.10; from the total respondents of 24, 15(62.5%) of respondents were as a male auditor; while on the other hand, 9(37.5%) of respondents were female. With regard to their educational level of auditors working in an audit firm; most of them are holders of BA degree. As can be seen from the above figure 4.8; from the total respondents, 17(70.8%) have educational qualification of bachelor’s degree. Furthermore, the remaining 7(29.20%) was master’s degree holders. From this, easily one can understand that; most of the auditors those working in different private audit firm have the educational qualification of BA degree. (See appendix number 20)

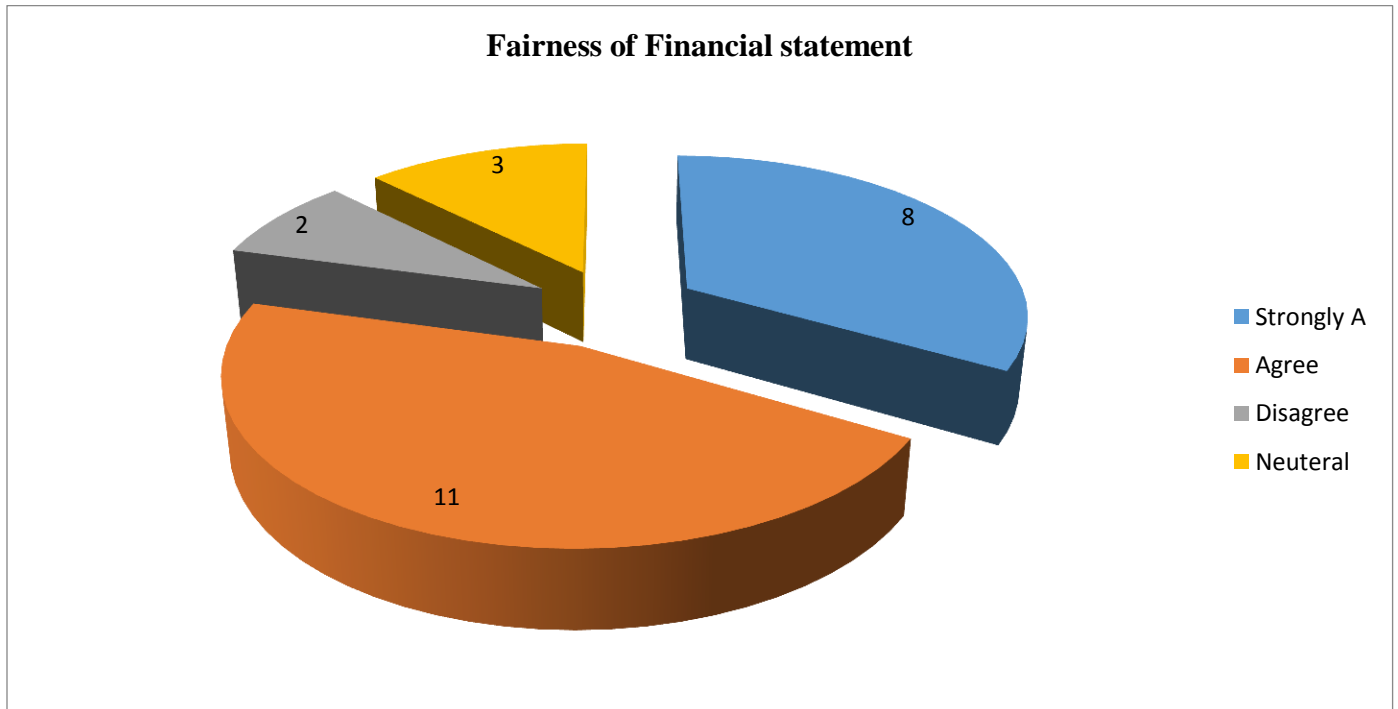
Graph 4.9: Respondent's response Related to Irregularity of laws affecting professional responsibility.



Source: Researcher own computation

The above graph 4.9 shows responses of the respondents related to the question; if there are any irregularities, on the part of law enforcement bodies in the application of laws and regulations pertaining to the professional responsibility of the auditors. With regard to this, Auditors consider the absence of a regulatory body to be the most serious challenge within the legislative environment followed by lack of professional responsibility, which is the cause for lack of development opportunity and absence of accounting standard. The data collected indicate that 18 (75%) of respondents agreed with irregularities on laws and regulations directly affects the professional responsibility of private auditors. While on the other, 4(16.67%) of respondents do not agree with the stated questions. From this, the researcher concluded that; since the absence of regulatory body dealing mainly with the profession where the prevalence of irregularities is attested by 75% of respondents. The findings are consistent with the overall setting of the profession in Ethiopia (see appendix number 21)

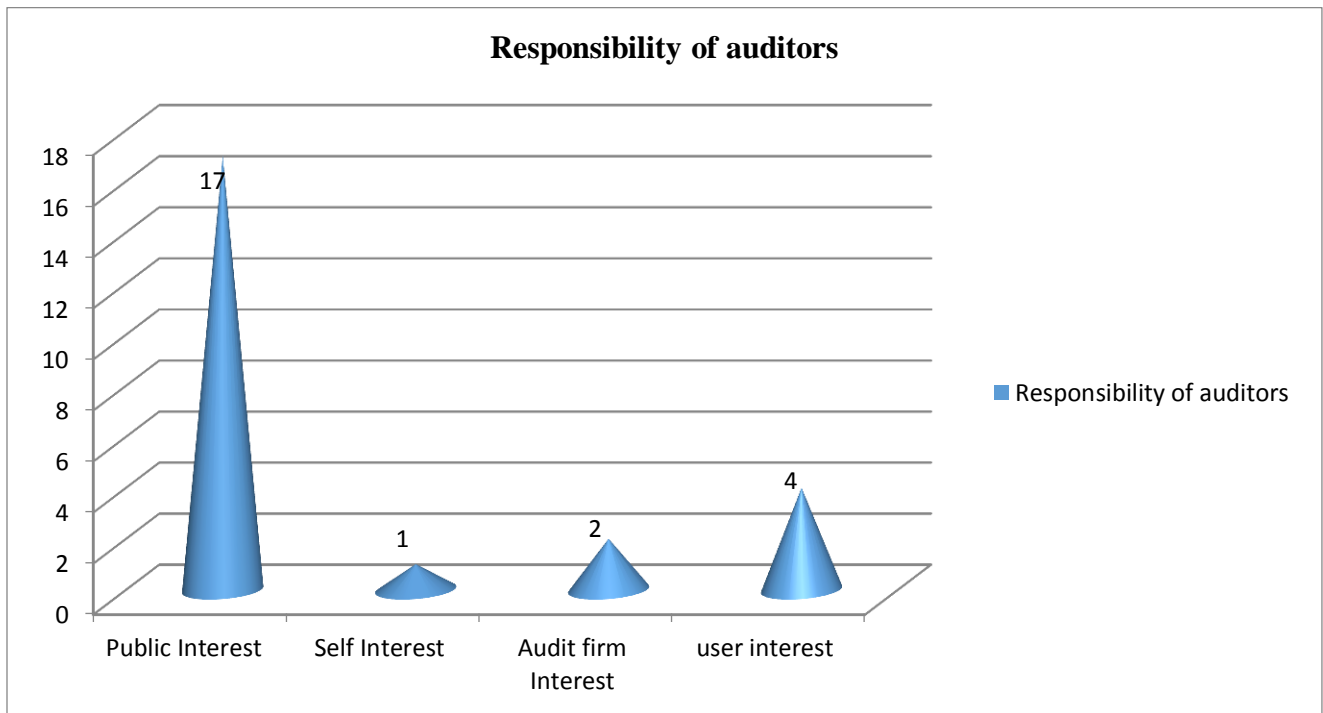
Figure 4.11: Respondents response with regard to Fairness of Financial statement



Source: Researcher own computation

Figure 4.11 shows the respondents' response related to if the financial statements submitted to stakeholders are a fair presentation of facts of reporting entities. In this case, the survey question was meant to address the extent to which private Auditors are confident that the reports which are given assurance service by them represent the fair presentation of the facts surrounding the reporting entities. The response collected from the respondents revealed that; the majority of financial statements submitted to stakeholders are a fair presentation of facts of reporting entity, which is supported by 19(79.16%) of respondents. While an alarming number of respondents 2(8.33%) consider that the financial statement submitted to stakeholders does not represent fair representations of the facts of the reporting entity. From this, the researcher concluded that the financial statements submitted to stakeholders are a fair presentation of facts of reporting entity (see appendix number 22)

Graph 4.10: Respondent's response Related to the responsibility of auditors

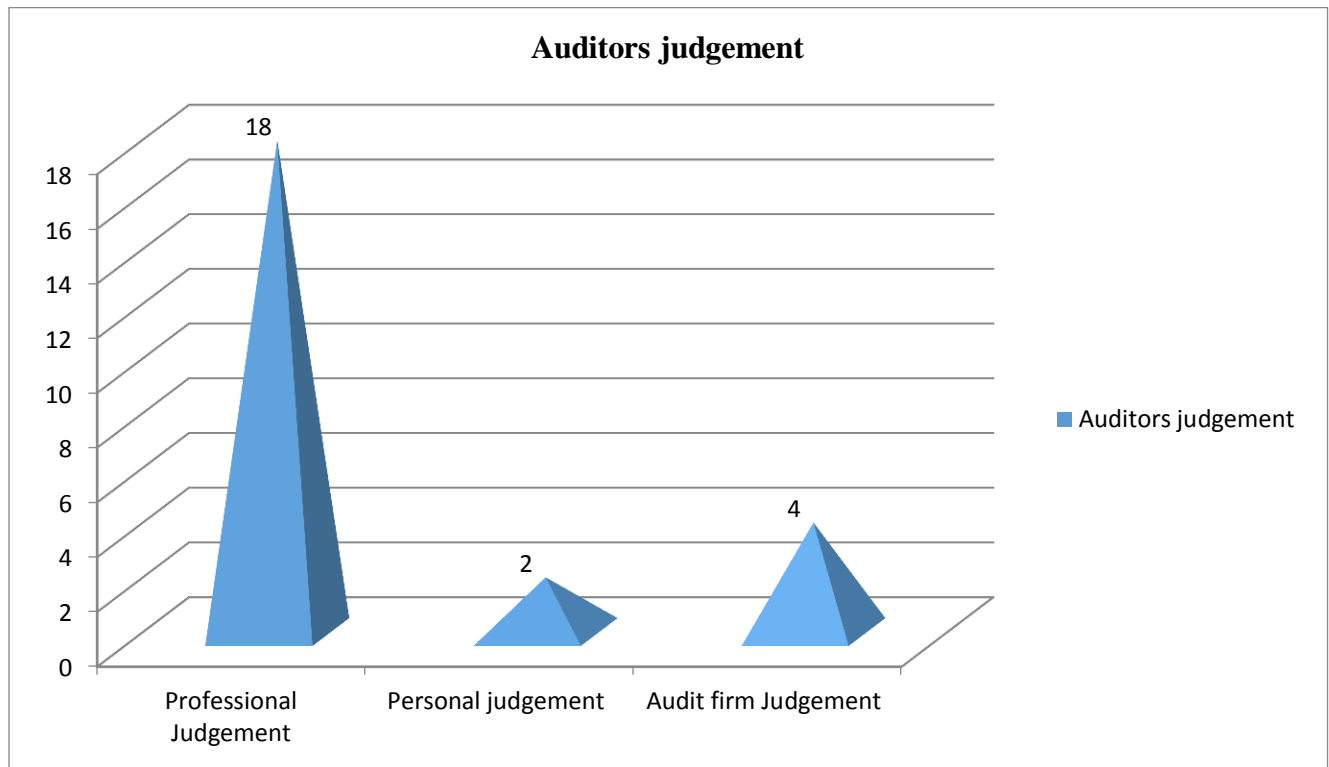


Source: Researcher own computation

The result of the above graph 4.10 represents the respondent's responses related to the question that; the primary responsibility of private auditors in conducting audit work should have to be?; The data collected from respondents with respect to the primary responsibility of Auditors; shows they acknowledge their public responsibility by ranking public interest as their prime concern. In which, 17(70.83%) of respondents agreed with the primary responsibility of the private auditors should have to be the public interest. While 4(16.67%) of respondent responded as saying user interest, 2(8.3%) of responded as saying audit firm interest and finally, 1(4.16%) of respondent responded as saying the primary responsibility of the private auditors should have to be self-interest.

From this finding, the researcher concludes that; private auditors in Ethiopia are mainly given attention to the public interest than self or user interest. But there is an alarm which shows, on some occasion a number of private auditors involved in audit activities consider their own interest than public interest (see appendix number 23).

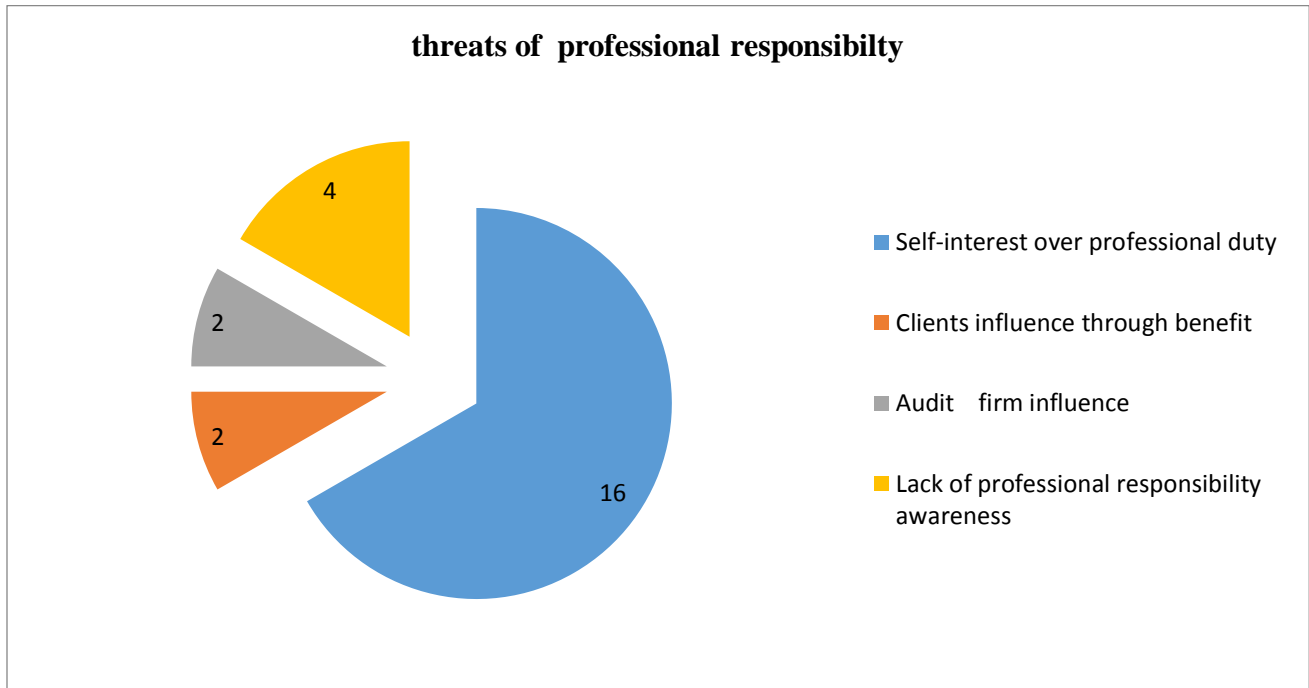
Graph 4.11: Respondent's response Related to auditors judgment



Source: Researcher own computation

As it can be seen, the above graph 4.11 shows the respondents' response related to the question provided for auditors; what kind of judgment they should consider, if a choice of decision is given for auditors. The result of data collected from respondents shows that most private auditors make a decision based on professional judgment. While there are a number of respondents which give a decision based on personal judgment and audit firm judgment. The result revealed, 18(75%) of respondents responded by saying professional judgment, while, 4(16.6%) responded as saying audit firm judgment is their decision and finally, 2(8.33%) of respondents make their own personal judgment on conducting audit work. So, since a large number of respondents responded as saying consideration for professional judgment. The researcher comes up with the conclusion of that, private auditors in Ethiopia give their decision based on professional judgment (see appendix 24).

Figure 4.12: Respondents response with regard to threats of professional responsibility

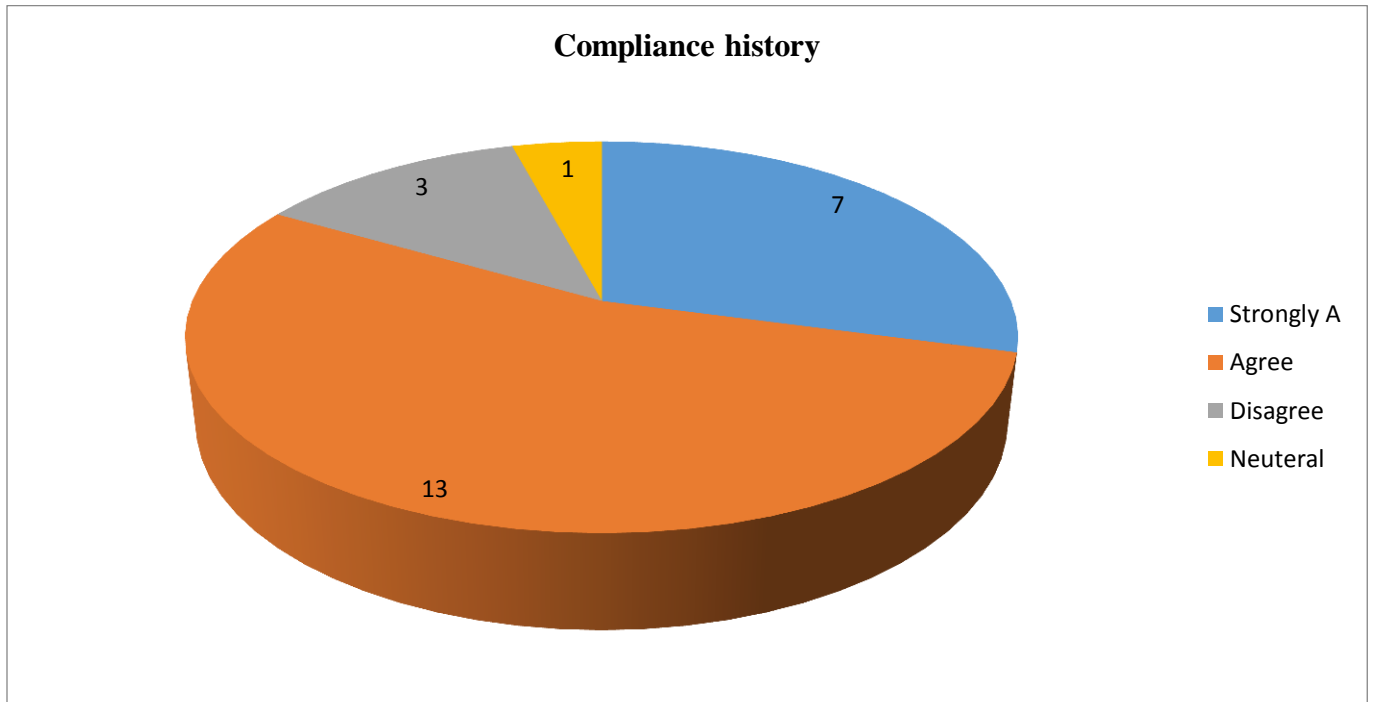


Source: researcher own computation

The above figure 4.12 shows the respondents response with regard to a question; threats of professional responsibility of auditors with regard to the individual level of auditors; The response to the major threats to professional responsibility at individual auditor level was identified as the promotion of self-interest over professional duty, which is supported by 66.67% of respondents. Additionally, lack of awareness and the influence of clients ranked as second and third respectively; in which they affect professional responsibility of auditors. The other threat ranked in last was audit firm influence; actually, the frequency of respondents with regard to lack of professional responsibility and influence of audit firm was the same.

Since all Auditors are members of ACCA, lack of awareness of professional responsibility does not seem justified as they are required to go through a serious of lessons and sessions of professional ethics. From the above data collection, the researcher concludes that; the main factor or threat influence private auditors in Ethiopia are looking for self-interest than professional duty (see appendix number 25).

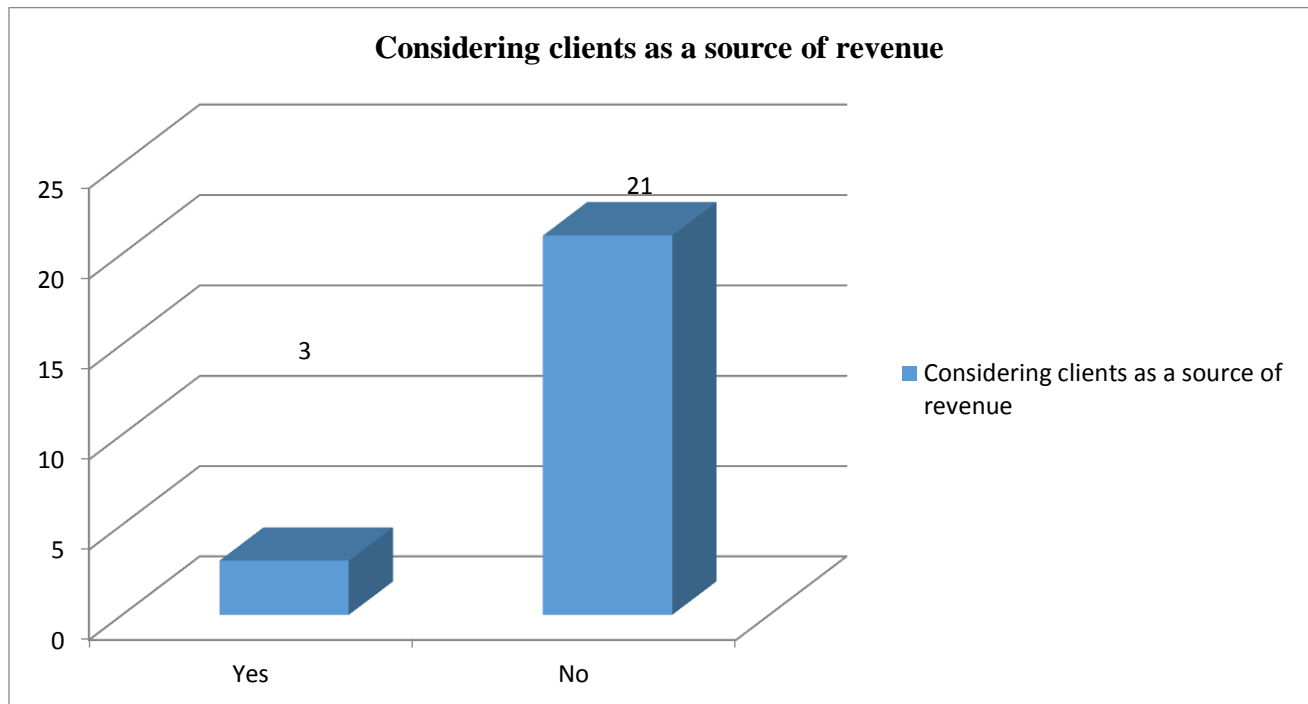
Figure 4.13: Respondents response with regard to the compliance history of clients



Source: Researcher own computation

Figure 4.13 shows the respondents' response related to clients compliance history. One of the safeguards to protect against undue exposure to professional liability is verification of potential clients' compliance history and the nature of business they are engaged in, before taking a professional appointment. The issue of contingent fee which depends on the outcome of results, unless fixed by a third party, creates the conducive ground for self-interest threat or advocacy threat on the side of the auditor while it may also be used as an intimidation threat by the client. With this regard, the above figure 4.13 shows the result of respondents regarding verifying compliance history of the clients; according to the data collected 83.33% of respondents agreed that they check compliance history of clients before starting any professional activities. While the remaining 12.5% of respondents do not give any consideration about compliance history of the clients; from this, the researcher concludes that private auditors in Ethiopia check clients' compliance background before starting any professional activities (see appendix number 26)

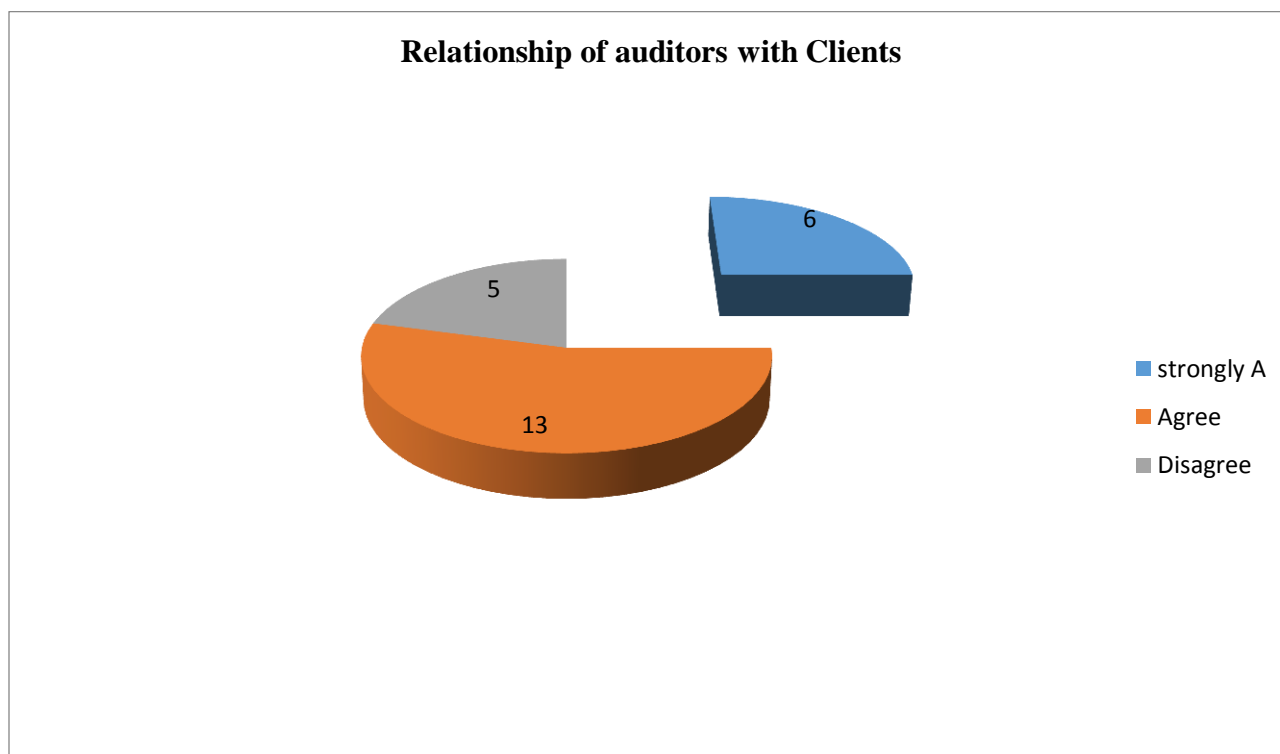
Graph 4.12: Respondent's response Related to considering clients as a source of revenue



Source: researcher own computation

As it is indicated in the above graph 4.12; the question was provided to private auditors in order to identify, whether private auditors consider their clients as a source of revenue or not. As it is revealed in the graph, most of the respondents, 21(87.5%) agreed that; they do not give any consideration about their clients to be a source of revenue. While a number of respondents, 3(12.5%) agreed on that; they consider their clients as of a source of revenue. The existence of a client which is considered too important as a source of revenue makes the professional vulnerable to pressures and intimidation. This can be taken from a lesson of Arthur Anderson which is related to a case of Enron, in this case, the clients were considered as the major source of revenue, which is managed to force bending of values to its own interest. Revenue dependence signifies major implication. In this connection, such heavy dependence on a client is likely to create threats to objectivity and or self-interest threats; which directly affect professional responsibility of the profession (see appendix 27).

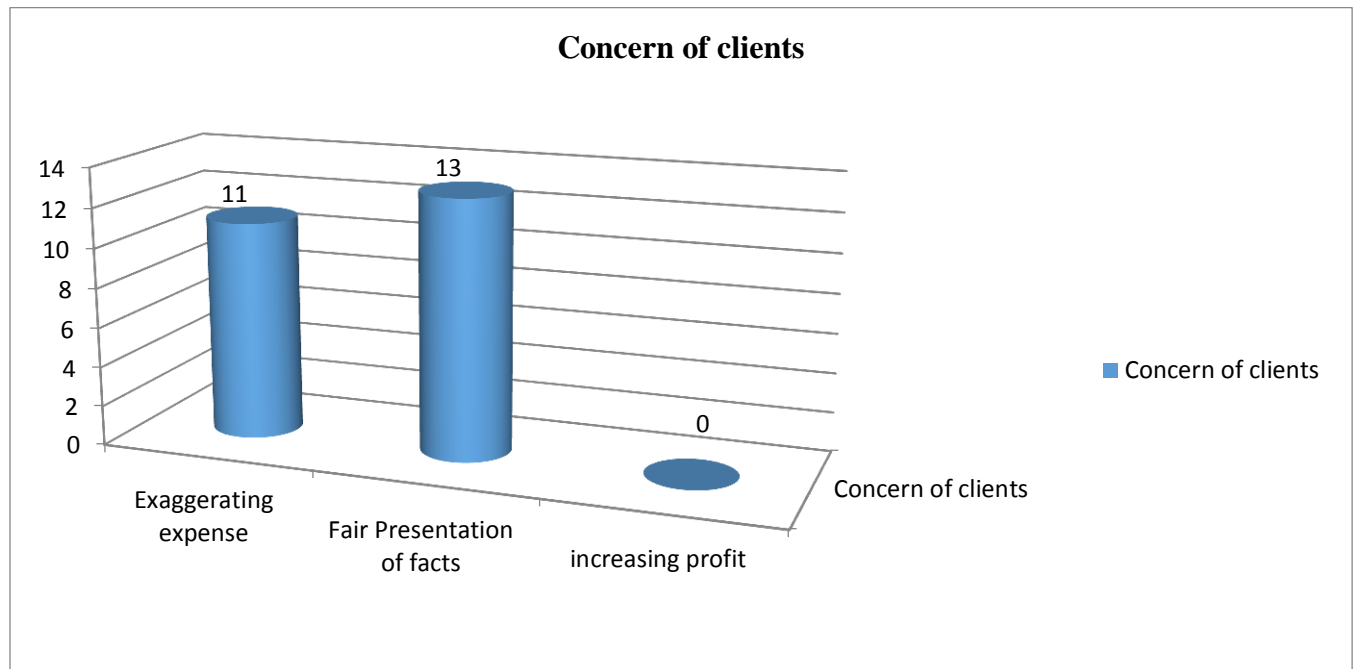
Figure 4.14: Respondent's response with regard to the effect of relationship



Researcher own computation

Having a relationship with clients affects the professional responsibility of auditors. And this can be evidence from the theoretical argument (IFRS code of ethics) cautions that long association or family relationship imposes a familiarity threat unless safeguards are put in place. As it can be shown in the above figure 4.14; the auditors were asked if the friendship or family relationship existed with clients affects their decision for a given financial statements opinion or not. The result of the respondents shows that; the majority of private auditors in Ethiopia affected by a kind of relationship they have with clients to give an opinion which is given on the audited financial statements; which is supported by 79% of respondents. And this will create a familiarity threat which influences their approach to take tasks with professional responsibility and legal liability. On the other hand, a number of respondents (21%) responded that the relationship with clients does not affect their decision with regard to the financial statement they have audited. From this, the researcher concludes that most private auditors in Ethiopia give their audit opinion without considering the relationship they have with the clients (see appendix 28).

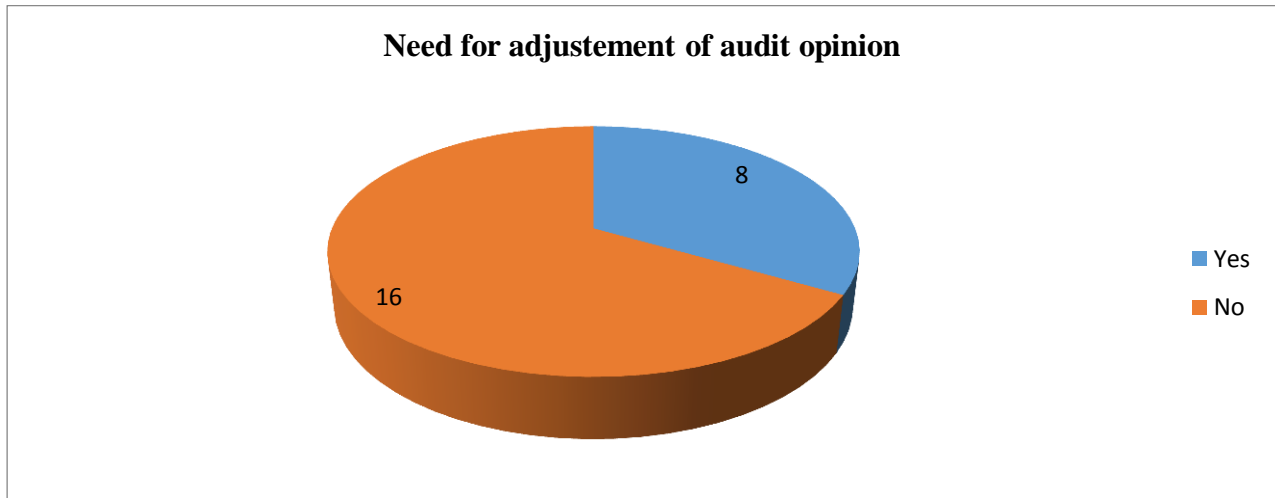
Graph 4.13: Respondent's response with regard to the concern of clients.



Source: researcher own computation

The above graph 4.13 is an indication for concern of clients in preparing financial statements. In doing so, the question was provided to private auditors sampled in this study to know the main concern of the clients in preparing financial statements. As it can be indicated in the above graph, most of the respondents (54.16%) agreed that; the main concern of clients in preparing financial statement is to present the fair representation of facts; while, (45.84%) of respondents agreed that the main concern of the clients are exaggerating expenses and finally, no number of respondent give their suggestion as saying the concern of clients in preparing financial statement is to increase profit. from this finding it is difficult to come up with the general idea that expresses the concern of clients in preparing financial statements is all about fair presentation of the fact; because the number of respondents those responded as saying the main concern of the clients are about exaggerating expense is almost near to those responded as fair presentation. So taking into account the external orientation of the financial reports, the findings of this study call for urgent attention to the matter. Because such like activity is mainly related to decreasing the tax amount that will be paid to the government (see appendix 29).

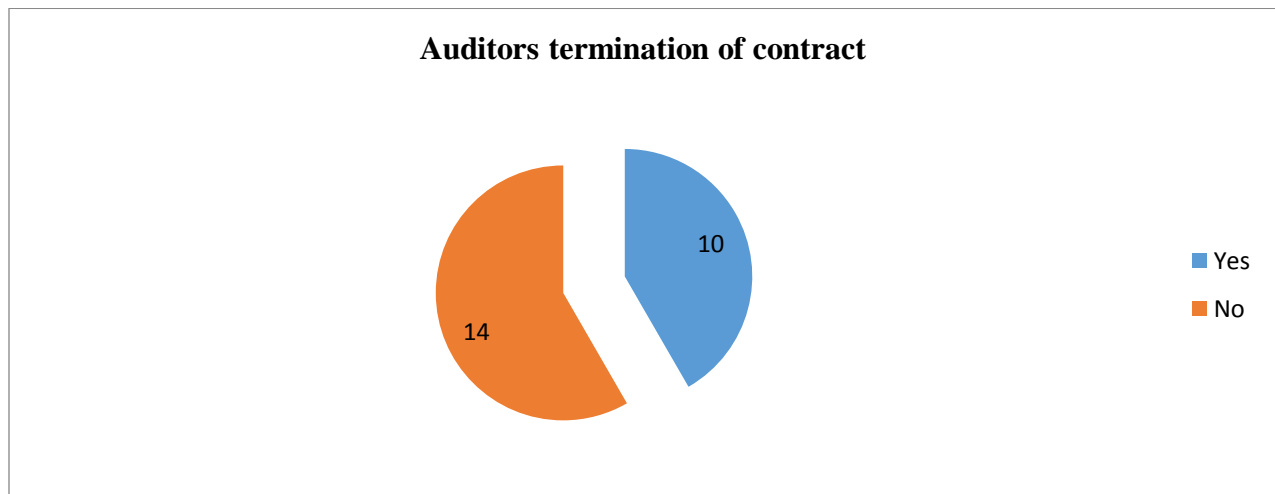
Figure 4.15: Respondent's response with regard to favor for audit opinion adjustment.



Source: researcher own computation

The response to question were there circumstances/cases where managers or owners approached the auditors to adjust audit opinion (in their favor) is further corroborates that; the management of reporting entities exerts pressure (of various kinds) to alter the audit opinions, thus, interfering in the auditor's independence and This is confirmed by a 33.33% response rate as having been approached to make modifications or changes to the audit opinions. While the other respondents responded that; they do not make any opinion modification because of the client's pressure (see appendix 30)

Figure 4.16: Respondent's response with regard to the termination of the contract



Source: Researcher own computation

In line with the above result of figure 4.15, figure 4.16 suggests or strengthened by the fact that 41.67% of the respondents had to withdraw from their engagement owing to a perceived threat to their profession and independence. This is a significant threat and concern for the profession. The intimidation threat encountered by Auditors finds its symmetry with that of Accountants. On the other hand, more than half of respondents has been responded that they fulfill the will of the clients rather than withdraw from audit engagement and this supported by 58.33% of respondents. So the researcher concluded from this, it is difficult to summarize that, the private auditors in Ethiopia are respecting their professional responsibility. Because since the majority of respondents responded that they will go through with interest of clients; it is difficult to summarize that they are protecting their professional responsibility and legal liability (see appendix number 31)

CHAPTER FIVE

SUMMARY OF MAJOR FINDING, CONCLUSION AND RECOMMENDATION

INTRODUCTION

This chapter is the last chapter of the study which sums up the whole thesis in a comprehensive manner. Accordingly, in the first part of this chapter, an overview of the thesis and its major conclusion are presented and finally, the chapter ends up with recommendations for remedial actions.

5.1. SUMMARY OF MAJOR FINDING AND CONCLUSIONS

This study was conducted to assess auditor's professional responsibilities and legal liability with regard to private auditors in Ethiopia; the objective of the study was to assess if private auditors are respecting professional responsibilities and aware of legal liability in conducting their audit activity. The study used descriptive research design and mixed research approach. Furthermore, the data was collected from both primary and secondary source of data. More specifically, depth interview was conducted from key personnel's. As it has been examined in the study, the purpose of auditing standards is to establish standards and provide guidance on the objective and principles governing an audit of financial statements; and this will enable auditors to give an opinion on those financial statements taken as a whole and thereby to provide reasonable assurance that the financial statements give a true and fair view of that company. To investigate this matter, the data was collected through questionnaire and interview; the questionnaire was prepared with close-ended and open-ended questions and distributed to 72 personnel which are combined from different organizations and audit firms. While the interview was made with 6 personnel those are combined from the board of Ethiopian accounting and auditing and Ethiopian revenue and customs authority. The questionnaire distributed was targeted two groups; namely the client's group and the auditor's group. From the total 72 questionnaires distributed 86% (62) of them was returned while the remaining 10(14%) was not returned; which means, from 42 questionnaires distributed to clients 38 of them was returned and from 30 questionnaires distributed to auditors 24 of them was returned.

Based on the result of questionnaire and interview conducted; the study was arrived at following findings which are helpful to give awareness about the study area.

As determined from the interview responses and observed by the researcher; absence of well-organized professional bodies in Ethiopia causes auditors not to properly exercise their professional and legal responsibilities. Overall, the factors that were identified as the main reasons that hinder the professional responsibility of private auditors are; for instance, there was an occasion in different organizations, where selection of auditors are based on family or friends relationship, there is relatively auditor's dependence on their client's for financial and other interest, there is a number of situations when auditor's give an opinion based on the demand of their clients, and since clients demand is unqualified opinion, Doing both accounting and auditing services for one and the same client; which may result in violation of professional ethics and finally, irregularity of laws and regulations are some example revealed in the study. With regard to responsibility; the study showed that; preparation of financial statements is the responsibility of the management of the company, while the responsibility of auditors rests on examining the financial statements produced by the management and expressing an opinion based on findings. Besides, it has been identified through the study and in principle, auditors are legally liable for subsequently discovered misstatement audited financial statements.

The study also identified auditors shall be civilly liable to the company and third parties for any fault in the exercise of their responsibilities which occasioned loss. As per the law of the country, an auditor who knowingly gives or confirms an untrue report concerning the position of a company or fails to inform the public prosecutor of an offense which he was known to have been committed shall be punished under Art. 438 or Art. 664 of the penal code as the case may be. But as it has been revealed through the study, there has been an occasion that auditors have been violating legal responsibilities. For instance, there is a circumstance that auditors are not signing a contract agreement with their clients for the purpose of audit work, compromising of auditor independence, and assigning less competent auditors. It was found out in the study that, the following were identified as the major constraints to private auditors in attempting to exercise their responsibility.

There were occasions that clients demand unqualified opinion; there was low demand for audit service, and there was no strong professional association for auditors and also the educational level of auditors engaged in audit activities is another constraint that affects the audit profession in Ethiopia.

5.2. Recommendations

The following possible recommendations may be used in order to help auditors in exercising their professional and legal responsibilities, and in providing decision-makers with a relevant audit report.

- ✚ Concerned bodies (government) shall formulate strong association to follow up the activity of private auditors and shall make an adjustment on audit fees by referring the other countries experience.
- ✚ The audit firms, as well as government, should follow up the competence of auditors in conducting audit activities. In this case, As much as possible, the clients or audit organizations shall employ a professional accountant or train the existing staff to aware of the responsibility attached to the audit profession and legal liability before conducting audit activity.
- ✚ The government (Ethiopian government) shall prepare proper legislation that shows the maximum number of years one audit firm should audit the same companies.
- ✚ Concerned bodies (government) shall take serious action on those companies intentionally prepares a financial statement to overstate the expense of that organization. Because this will result in decreasing the total profit of the organization which is deliberately reducing the total amount of tax paid to the government.

5.3. Suggestion for further research

The aim of this study was to assess the professional responsibility and legal liability with regard to private auditors in Ethiopia. For this purpose, this study was only limited to private auditors found in Ethiopia; but further study is needed to assess the professional responsibility and legal liability with regard to public auditors in order to investigate if factors that causes auditors to not practice professional responsibility and legal liability are the same for not.

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Rift Valley University

Bole campus

Department Of Accounting and Finance

Instruction

This questionnaire is formulated to identify the overall professional responsibility and legal liability of private auditors in Ethiopia and only used for academic purpose only. **(For clients)**

General direction

Indicate your answer to the question by putting a check mark in the box and write your answers on the space provided for open-ended questions and writing your name is not required or mandatory.

Note: SD- strongly agreed. A – Agreed. N- Neutral. D- Disagreed. SD- Strongly disagreed

1. Sex: Male Female

2. Educational qualification

PhD MA/MSc BA/BSc College Diploma Certificate

3. Please indicate the type of Business organization you are working in.

PLC Share Company NGO Others specify _____

4. On average, what is the Year of the establishment of the company you are working in?

Less than 2 years 3 to 5 years 5 to 10 years Older than 10 years

5. In conducting the audit, do you think that auditors are independent of audited company or firms in all aspects?

SA A N D SD

6. Is there any moment you faced that auditors are not professionally trained and competent?

Yes No

7. If your answer for the above question number 6 is yes, please justify here under the decision you have made regarding to the auditor

8. Do you think that auditors are adequately planning and frequently preparing themselves for the work field?

SA A N D SD

9. Do you think that all auditing processes need due professional care?

Yes No

10. If your answer in question number 9 is no. please justify here under why you say no

11. Is the auditors examines the internal control structure of your organization?

SA A N D SD

12. is where you see a moment auditors are based on principles other than GAAS?

Yes No

13. If your answer for question number 12 is yes, please list out the principles they have followed

14. Do you think that the materiality principle is properly used by auditors as a base in disclosing an error obtained during an audit examination?

SA A N D SD

15. When your business is audited, are you signing a contract or an agreement with your auditor?

Yes No

16. Do you think that private auditors are liable for the violation of contractual responsibility?

SA A N D SD

17. Are private auditors liable for violation of statutory responsibility?

SA A N D SD

18. Is there an occasion where you invited your auditor for financial statements preparation?

Yes No

19. Do you think that private auditors legally liable, for subsequent discovery of misstated audited financial statements?

SA A N D SD

20. What are your criteria for selecting an auditor?

Through advertisement on media

By family or friend relationship

The controlling part can assign

Others, please specify-----

21. For what purpose is your business audited?

For taxation purpose

For creditors or other external users

Auditing the books of accounts is mandatory

22. When your auditor is examining your books of accounts, do you expect an opinion other than unqualified one?

Yes

No

23. If your answer for the above question number 22 is yes please justify here under why you select yes.

Rift Valley University

Bole Campus

Department Of Accounting and Finance

Instruction

This questionnaire is formulated to identify the overall professional responsibility and legal liability of private auditors in Ethiopia and only used for academic purpose only. **(For auditors)**

General direction

Indicate your answer to the question by putting a check mark in the box and write your answers on the space provided for open-ended questions and writing your name is not required or mandatory.

Note: SD- strongly agreed. A – Agreed. N- Neutral. D- Disagreed. SD- Strongly disagreed

1. Gender: Male Female

2. Educational qualification

PhD MA/MSc BA/BSc College Diploma Certificate

3. Do you think there are irregularities, on the part of law enforcement bodies in the application of laws and regulations pertaining to professional responsibility?

SA A N D SD

4. Do you think the financial statements submitted to stakeholders are a fair presentation of facts of reporting entity?

SA A N D SD

5. As an Auditor, what do you think is your primary responsibility?

Public Interest Self Interest Audit firm Interest user interest

6. When you faced with choices of decisions, you base your decision on?

Professional Judgement Personal judgment Audit firm Judgement

7. In your view what are the major threats to professional Responsibility at individual auditor level

Self-interest over professional duty Clients influence through benefit Audit
firm influence Lack of professional responsibility awareness

8. Before taking engagement with a client do you check the client's background
(compliance history?)

SA A N D SD

9. Have you ever used information obtained, as a result of your engagement to negotiate
fee?

Yes No

10. Do you have clients which you consider are too important as a source of your revenue?

Yes No

11. Do you think a relationship with a client (friendship, family, long-standing service, etc.)
influences your approach to the task?

SA A N D SD

12. In your experience, clients are primarily concerned with

Exaggerating expense Fair Presentation of facts increasing profit

13. Were there circumstances/cases where managers or owners approached you to adjust
audit opinion (in their favor)

Yes No

14. Have you withdrawn from an engagement due to a perceived threat to your professional
judgment?

Yes No

Appendix-3

Table 4.1: Description of respondents respect to their educational level, sex, and Nationality

No	Item	Respondents	
		Frequency	Percentage (%)
1	The educational level of respondents		
	PhD	-	
	MA degree	12	31.58
	BA/BSc degree	26	68.42
	Diploma	-	
	Certificate	-	
	Total	38	100
2	Gender		
	Male	25	65.79
	Female	13	34.21
	Total	38	100

Appendix-4

Table 4.2: Description of respondents respect the category of business and year of establishment

No	Item	Respondents	
		Frequency	Percentage (%)
1	Category of business		
	Share company	20	52.63
	PLC	13	34.21
	NGO	5	13.15
	Others	-	
	Total	38	100
2	Year of establishment		
	Less than 2 years	6	15.79
	3 up to 5 years	4	10.5
	6 up to 10 years	9	23.70
	More than 10 years	19	50
	Total	38	100

Source: Researcher own computation

Appendix-5

Table 4.3: Respondents response on auditor's independence:

No	Items	Respondents	
		Frequency	Percentage (%)
1	Conducting the audit, do you think that auditors are independent of audited company or firms in all aspects?		
	Strongly agree	5	13.15
	Agree	22	57.90
	Neutral	6	15.80
	Disagree	3	7.90
	Strongly disagree	2	5.20
	Total	38	100%

Appendix-6

Table 4.4: Respondents response on auditor's competence

No	Items	Respondents	
		Frequency	Percentage (%)
1	Is there a moment you faced that auditors are not professionally trained and competent?		
	Yes	6	15.80
	No	32	84.20
	Total	38	100%

Source: researcher own computation

Appendix-7

Table 4.5: Respondents response on the audit work plan and fieldwork supervision:

No	Items	Respondents	
		Frequency	Percentage (%)
1	Do you think that your auditor is adequately planning and frequently supervising the work of field auditors?		
	Strongly agree	12	31.58
	Agree	18	47.37
	Neutral	2	5.20
	Disagree	6	15.79
	Strongly disagree	-	
	Total	38	100%

Appendix-8

Table 4.6: Respondents response on auditor's due professional care exercise:

No	Items	Respondents	
		Frequency	Percentage (%)
1	Do you think that all auditing processes need due professional care?		
	Yes	38	100%
	No	-	
	Total	38	100%

Appendix-9

Table 4.7: respondent's response on internal control structure

No	Items	Respondents	
		Frequency	Percentage (%)
1	Is your auditor examines the internal control structure of your organization?		
	Strongly agree	6	15.79
	Agree	19	50
	Neutral	5	13.16
	Disagree	6	15.79
	Strongly disagree	2	5.20
	Total	38	100%

Source: Researcher own computation

Appendix-10

Table 4.8: Respondents response on consistent application of GAAP

No	Items	Respondents	
		Frequency	Percentage (%)
1	Is there a moment you base on principles other than GAAS?		
	Yes	20	52.63%
	No	18	47.37%
	Total	38	100%

Source: researcher own computation

Appendix-11

Table 4.8: Respondents response on materiality principle

No	Items	Respondents	
		Frequency	Percentage (%)
1	Do you think the materiality principle used as a base in disclosing an error obtained during an audit examination?		
	Strongly agree	6	15.79
	Agree	18	47.37
	Neutral	7	18.42
	Disagree	5	13.16
	Strongly disagree	2	5.20
	Total	38	100%

Source: Researcher own computation

Appendix-12

Table 4.9: Signing contractual agreement before the starting the audit:

No	Items	Respondents	
		Frequency	Percentage (%)
1	When your business is audited, are you signing a contract or an agreement with your auditor?		
	Yes	30	79%
	No	8	21%
	Total	38	100%

Source: Researcher own computation

Appendix-13

Table 4.10: Respondents response on auditor's contractual responsibility:

No	Items	Respondents	
		Frequency	Percentage (%)
1	Do you think that private auditor is liable for the violation of contractual responsibility?		
	Strongly agree	7	18.42
	Agree	22	57.90
	Neutral	3	7.90
	Disagree	6	15.79
	Strongly disagree	-	-
	Total	38	100%

Source: Researcher own computation

Appendix-14

Table 4.11: Respondents response on auditor's statutory responsibility

No	Items	Respondents	
		Frequency	Percentage (%)
1	Are private auditors liable for violation of statutory responsibility?		
	Strongly agree	6	15.79
	Agree	24	63.15
	Neutral	3	7.90
	Disagree	5	13.16
	Strongly disagree	-	-
	Total	38	100%

Source: Researcher own computation

Appendix-15

Table 4.12: Respondent's response on preparation of financial statements:

No	Items	Respondents	
		Frequency	Percentage (%)
1	Is there an occasion where you invited your auditor for financial statements preparation?		
	Yes	-	-
	No	38	100%
	Total	38	100%

Source: Researcher own computation

Appendix-16

Table 4.13: Clients' response on subsequent discovery of misstatements to audit financial statements:

No	Items	Respondents	
		Frequency	Percentage (%)
1	Do you think that private auditors legally liable, for subsequent discovery of misstated audited financial statements?		
	Strongly agree	11	28.95
	Agree	27	71.05
	Neutral	-	-
	Disagree	-	-
	Strongly disagree	-	-
	Total	38	100%

Source: Researcher own computation

Appendix-17

Table 4.14: Auditors selection criteria:

What are your criteria when selecting an auditor?	Response	
	Number	%
Through advertisement on media	5	13.16
By family or friend relationship	18	47.40
The controlling part can assign	11	28.90
Others	4	10.52
Total	38	100

Source: Researcher own computation

Appendix-18

Table 4.15: The purpose of the audit report:

For what purpose is your business audited?	Response	
	Number	%
For taxation purpose	14	36.84
For creditors or others external users	15	39.48
Auditing the books of accounts is mandatory	9	23.68
Total	38	100

Source: Researcher own computation

Appendix-19

Table 4.16: Respondents response on Audit opinion

No	Items	Respondents	
		Frequency	Percentage (%)
1	When your auditor is examining your books of accounts, do you expect an opinion other than unqualified one?		
	Yes	28	73.70%
	No	10	26.30%
	Total	38	100%

Source: Researcher own computation

Appendix- 20

Table 4.17: Distribution of Respondents (auditors) response with regard to educational level and gender

No	Item	Respondents	
		Frequency	Percentage (%)
1	The educational level of respondents		
	PhD	-	
	MA degree	7	29.16
	BA/BSc degree	17	70.8
	Diploma	-	
	Certificate	-	
	Total	24	100
2	Gender		
	Male	15	62.5
	Female	9	37.5
	Total	24	100

Source: researcher own computation

Appendix-21

Table 4.18: respondent's response with regard to irregularities of laws

No	Items	Respondents	
		Frequency	Percentage (%)
1	Do you think there are irregularities, on the part of law enforcement bodies in the application of laws and regulations pertaining to professional responsibility?		
	Strongly agree	6	25
	Agree	12	50
	Neutral	2	8.33
	Disagree	4	16.67
	Strongly disagree	-	-
	Total	24	100%

Source: Researcher own computation

Appendix-22

Table 4.19: Respondents response with regard to Fairness of financial statement

No	Items	Respondents	
		Frequency	Percentage (%)
1	Do you think the financial statements submitted to stakeholders are a fair presentation of facts of reporting entity?		
	Strongly agree	8	33.33
	Agree	11	45.83
	Neutral	3	12.5
	Disagree	2	8.33
	Strongly disagree	-	-
	Total	24	100%

Source: researcher own computation

Appendix-23

Table 4.20: Respondents response with regard to auditors' responsibility

No	Items	Respondents	
		Frequency	Percentage (%)
1	As an Auditor, what do you think is your primary responsibility?		
	Public interest	17	70.83
	Self interest	1	4.16
	Audit firm interest	2	8.33
	User/ client interest	4	16.66
	Total	24	100%

Source: researcher own computation

Appendix-24

Table 4.21: Respondents response with regard to auditors' judgment

No	Items	Respondents	
		Frequency	Percentage (%)
1	When you faced with choices of decisions, you base your decision on?		
	Professional judgement	18	75
	Personal Judgement	2	8.33
	Audit firm Judgement	4	16.67
	Total	24	100%

Source: researcher own computation

Appendix-25

Table 4.22: Respondents response with regard to threats to professional responsibility

No	Items	Respondents	
		Frequency	Percentage (%)
1	In your view what are the major threats to professional Responsibility at individual auditor level		
	Self-interest over professional duty	16	66.67
	Clients influence through benefit	2	8.33
	Audit firm influence	2	8.33
	Lack of professional responsibility awareness	4	16.67
	Total	24	100%

Source: researcher own computation

Appendix-26

Table 4.23: Respondents response with regard to clients' compliance history

No	Items	Respondents	
		Frequency	Percentage (%)
1	Before taking engagement with a client do you check the client's background (compliance history?)		
	Strongly agree	7	29.16
	Agree	13	54.16
	Neutral	1	4.16
	Disagree	3	12.5
	Strongly disagree	-	-
	Total	24	100%

Source: researcher own computation

Appendix-27

Table 4.24: Respondents response with regard to if their clients are a source of revenue

No	Items	Respondents	
		Frequency	Percentage (%)
1	Do you have clients which you consider are too important as a source of your revenue?		
	Yes	3	12.5
	No	21	87.5
	Total	24	100%

Source: researcher own computation

Appendix-28

Table 4.25: Respondents response with regard to the relationship they have with clients

No	Items	Respondents	
		Frequency	Percentage (%)
1	Do you think a relationship with a client (friendship, family, long-standing service, etc.) influences your approach to the task?		
	Strongly agree	6	25
	Agree	13	54.16
	Neutral	-	
	Disagree	5	20.84
	Strongly disagree	-	-
	Total	24	100%

Source: researcher own computation

Appendix-29

Table 4.26: Respondents response with regard to the concern of clients

No	Items	Respondents	
		Frequency	Percentage (%)
1	In your experience, clients are primarily concerned with		
	Exaggerating expense	11	45.83
	Fair Presentation of facts	13	54.17
	increasing profit	-	-
	Total	24	100%

Source: researcher own computation

Appendix-30

Table 4.27: Respondents response with regard to adjustment of audit opinion

No	Items	Respondents	
		Frequency	Percentage (%)
1	Were there circumstances/cases where managers or owners approached you to adjust audit opinion (in their favor)		
	Yes	8	33.33
	No	16	66.67
	Total	24	100%

Source: researcher own computation

Appendix-31

Table 4.28: Respondents response with regard to termination of audit agreement

No	Items	Respondents	
		Frequency	Percentage (%)
1	Have you withdrew from an engagement due to a perceived threat to your professional judgment?		
	Yes	10	41.67
	No	14	58.33
	Total	24	100%

Source: researcher own computation