The impact of Key Audit Matters (KAMs) on financial information quality: Evidence from Lebanon

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Abstract

The purpose of this study is to discover the impact of Key Audit Matters (KAMs) on financial information quality and their value for Lebanese auditors. The value creation of KAMs is determined by its financial information quality, its ability to help during investment decisions, and its effect on the audit expectation gap. The empirical part is conducted through a survey that was filled by 38 Lebanese external auditors who audit Lebanese banks exclusively and are involved in the new audit report. Collected data consists of statements related to KAM's such as financial information quality, investment decision, and audit expectation gap measured with a Likert scale (from 1 to 5) then, a quantitative analysis is conducted. The main results show that reporting by using Key Audit Matters adds value to the audit report from the perspective of Lebanese external auditors, and can reduce information asymmetry, increase trust in accounting and reduce the expectation gap. Moreover, the results marked that KAM improves the auditee's understanding of the audited entity, builds confidence in the audited financial statements, and helps to reduce the audit expectations gap.

Keywords: KAM, information quality, investment decision, audit expectation gap.

JEL Classification: M42
INTRODUCTION

In recent years, financial information has evolved and has increased judgments, estimates, and uncertainties (Deloitte, 2016). Users of financial statements have called upon the auditors to provide more detailed information about the audited entity (IAASB, 2015c). In the same perspective, they claimed: "additional information about significant elements in the audit, which often relate to headings in financial statements that are subject to significant judgments by the management and the auditor" (IAASB, 2015c, p.1). Some authors listed the significant audit risks, the audit procedures that respond to these risks, and the results of these procedures as some of the data that readers would like to know (Mock, 2013). In general, audit reports users are frustrated because auditors know better about their company than themselves (Cordoş & Fülöp, 2015).

The changes that occurred to the audit reports emanate from a long development process that followed the global financial crisis that unfolded in 2008. The audit industry suffered much criticism in the aftermath of the crisis, especially since the audit reports' users questioned their thoroughness. The discrepancy between the pure audit reports and the bank's identified economic problems raised a discussion about how the statutory audit's current regulatory framework should change to prevent a new crisis from occurring. Critics opined that the auditors should have communicated the problems at an earlier stage and that many auditors did not utilize their full potential during the audit (FAR, 2013).

The International Auditing and Assurance Standards Board, IAASB, was continually working on auditing standards to improve audit quality (Catasús, Hellman & Humphrey, 2013). This quality was achieved by the introduction of a new paragraph describing the "Key Audit Matters." The objective of communicating Key Audit Matters (KAMs) as "those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements for the period under review" (International Auditing and Insurance Standards Board [IAASB], 2015, ISA 701, paragraph 8, page 5) is revealed in the new standard ISA 701: Communicating Key Audit Matters in the Independent Auditor's Report (IAASB, 2015). According to several experts, this innovation should enable readers to see the auditors' attention points and understand how they responded to the important questions they asked themselves. In general, the new ISA 701, which deals exclusively with KAMs, requires that auditors
be much more transparent in their work. Therefore, a major change is expected: to move from a standardized report into a more complete and clearer report. The IAASB declared that the audit report would pass from the standardized format to an entity-specific report (IAASB, 2015).

Furthermore, the IAASB requests that the disclosure of KAM contains a description of how the auditors treated the key matter. This description shall include the reason behind determining KAM and a straightforward approach to the performed procedures (IFAC, 2016). The disclosure of KAMs could have a significant impact on auditor liability (Gimbar et al., 2016).

The purpose of this paper is to identify the impact of disclosed Key Audit Matters on the informational value of the audit report and the audit expectation gap. It contributes to the literature by exploring the informational impact of disclosed KAMs through two dimensions: the investment decision and investor’s confidence in the audit report and the indirect effect on the perceived audit expectation gap.

This paper examines KAMs value to Lebanese auditors through the following research questions:

Does the reporting of KAMs provide an informational value to the audit report?

Does KAMs give a better insight into the investment decision and confidence in the audit report?

Can the reporting by KAMs increase the auditor’s role and thus reduce the expectation gap?

LITERATURE REVIEW

The need for KAMs by professionals and the changes introduced by ISA 701 to the audit report has moved the reporting to a new level with new requirements and settlements. This section underlines the origin of KAMs, their effect, and their uses.
The need for KAM by professionals and Changes in audit report according to ISA 701

The most comprehensive change in the audit report introduces a whole new section: Reporting of Key Audit Matters, KAMs. It exposes the most important items in the audit performance, according to the auditor's assessment. Lee, Ali, and Bien (2009) believe that stakeholders tend to consider a pure audit report to guarantor the revised company’s morale and continued vitality. Arnold Schilder, IAASB Chairman, pronounces that “... while the auditor's opinion is valued, many perceive that the auditor’s report could be more informative. Change, therefore, is essential.” (IAASB, 2012).

Previous surveys show that users value the auditor's statement but that the audit report should be more informative by communicating additional information about the revised business (IAASB, 2015a).

The current audit report is incomplete and is based on a brief, binary, black and white opinion (PwC, 2015b, p.2). This incompleteness mainly refers to an information gap that could have been the main reason behind the expectation gap. Others stated that the audit mission ends annually with a standardized report almost identical by word to the previous one. Because of this standardization, investors find it hard to perceive what the auditor has finished. (Wooten, 2003, cited by Cordoș & Fülöp, 2015). Also, the responsibility and the role of auditors in detecting fraud and error have been controversial (Cordoș & Fülöp, 2015).

A previous study has shown that investors who receive a KAM section in the audit report will base their investment decision upon it, along with the related information in a management’s footnote (Christensen et al., 2014). The presentation framework of communication in today’s audits has been criticized for failing to convey the information that investors seek and need in their decision making (IAASB, 2011). Investors' low interest in the audit report is reasonably due to the discrepancy between the requested and the available information. Carcello (2012) further finds in his study that investors seek more information from the auditor.

A process was launched in 2006 to update the design of the audit report and to meet users' expectations and requirements for audit reports. Initially, a comprehensive survey was conducted on the expectations and information needed from different stakeholder groups about audit reports (IAASB, 2015b). All organizations were invited to comment on the
information they believed the audit report should provide and on the
issues identified by the IAASB. Through feedback, practical work was
undertaken to adapt the existing standards to the changes that the IAASB
intended to implement. In June 2012, a draft of the planned changes was
made clear. Organizations were invited for a second round to give
comments on the proposed changes and the ability to influence the process
(IAASB, 2012). Many comments were received from a wide range of
organizations that had views on developing the audit report. The
comments were predominantly positive regarding the changes, although
views on the implementation were raised by several organizations (IAASB,
2015c). After further processing of the reforms, the IAASB published the
completed changes in the New and Revised Auditor Reporting in January
2015. The changes involve a series of adjustments in the existing ISAs that
deal with the audit report. The main purpose of these changes is to update
the formal audit report and adapt the current standards to the new ones
implemented, the ISA 701. The standard, which dictates how key audit
matters are identified and reported in the audit report, is the most
comprehensive change that IAASB has produced in the current work
development (IAASB, 2015a).

Key audit matters specificities
The introduction of the standard stipulates that the KAM's purpose is to
improve the audit report's communication value by underlining the audit
process's transparency. Furthermore, it is emphasized that KAM shall
provide the auditor's report with an insight into the most important areas
in the auditor's performance of the audit. This provision aims to give the
reader an insight into complex accounting issues, which may facilitate the
interpretation of the financial statements and contribute to an increased
understanding of the revised business. Finally, IAASB's goal is that the
reporting of KAM will serve as a basis for further discussion on these issues
with the company's management (IAASB, 2015d). According to the
auditor's professional judgment, the matters reported as KAM are chosen
from the issues discussed with the company's management and defined as
areas that were of the most significant importance implementation of the
auditor's professional judgment the audit.

The communication of KAMs necessitates a professional judgment from
the auditor in charge of the mission, based on the communication with
those charged with governance (TCWG). Following ISA 315, the auditor
should first identify the matters representing risk and mark them with sufficient and appropriate audit evidence. These matters may require difficult evaluations, especially if the internal control system has some disadvantages linked to the analyzed matter (IAASB 2013, ISA 701). The areas determined as KAM by auditors will then be communicated in the audit report. KAM’s explanation should include an overview of relevant completed control activities and important observations to allow the audit report's users to understand why a particular area is considered KAM (IAASB, 2015d). Deloitte and Touche (2015) explained the process for KAM’s identification according to figure 1.

**Figure 1: The process for identifying KAMs**

![Diagram showing the process for identifying KAMs](Image)

*Source: Deloitte and Touch (2015)*

One of the major objectives of introducing the new requirement is strengthening the communication between the auditor and those charged with corporate governance. In the context of the new ISA 701 standard, the auditor must reveal, or report to them, any possible KAM. According to the IAASB, this conversation should help the auditor to understand the management’s point of view on the importance of the adverse consequences that necessitate the communication of some issues (IAASB, 2015, ISA 701). In addition to the entries included in ISA 701, notes have been inserted in various standards. For example, ISA 260 states that the auditor must communicate to the person’s corporate governance the obligations incumbent upon it about the audit (IAASB, 2009, ISA 260). Now, the auditor will have to evoke his/her responsibility in the determination and the communication of KAM. ISA 260 adds that the auditor should
communicate to those charged with governance the broad outline of the planned scope and timing of the audit work, specifying the identified significant risks” (IAASB, 2015, ISA 260, 15, p.5).

Standardized formulations risk undermining the informative value of the declaration and make the explanation understandable to users who do not have an in-depth understanding of the auditor's work practices (IAASB, 2015a). Otherwise, KAM does not affect the management’s responsibility to establish the company financial statements, including the notes that should be presented to increase the understanding of the financial information. KAM is more likely to highlight the areas that the auditor, through his/her professional assessment, has considered to be the most important in the audit (IAASB, 2015a).

Given that the objective of reporting on KAMs is to provide a problem-oriented report on the final audit, ISA 701 explicitly discloses specific issues to the company according to the audit opinion. Regarding the form of representation, it should be noted that in addition to the verbal representations in the text stream, tabular representations are also used for further clarity. The following points should be presented:

- Reference to representations of KAM in the financial statements (for example, referring to an accurate appendix)
- Explanation of why a KAM was assessed as a particularly important aspect of the audit
- Presentation of the facts that were taken into consideration during the audit

It should be emphasized that ISA 701 does not expect a "fragmented opinion" separate from the respective KAM. Taking the KAM into consideration shows that the opinion is not independent and rely on these KAMs.
Table 1: Review of some KAM research.

| Authors                                      | Conclusions                                                                                                                                                                                                 |
|----------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Louis-Philippe Sirois, Jean Bédard, & Palash Bera (2018) | The study shows that KAM attracts users directly especially if there are communicated in the auditor's report. However, users devote less attention to other sections of the audit report when exposed to an auditor's report with KAM. |
| Annette G. Kohler, Nicole V. S. Ratzinger Sakel, Jochen C. Theis, (2016) | The economic situation of the company will be much better when KAM suggests minimal changes that will lead to a goodwill impairment (KAM negative) than when KAM suggests significant changes (KAM positive) |
| Louis-Philippe Sirois, Jean Bédard, Palash Bera, (2014) | Users' financial information acquisition is significantly affected by additional matters in the audit report. KAM attracts the users and reduces the level of attention for the audit report. |
| Brant E. Christensen, Steven M. Glover Christopher J. Wolfe (2014) | They find that nonprofessional investors react to the inclusion of a CAM paragraph in terms of both its information content and its source credibility, and are less likely to react to a CAM paragraph if it is followed by a resolution paragraph containing auditor assurance for the critical audit matter. *CAM: Critical Audit Matters is used in the same meaning as Key Audit Matters |

Source: Prepared by the authors

Table 1 summarizes some recent studies that outline the role and importance of Key Audit Matters. The selected studies highlight some common points with our research center: they address the importance of KAM in the audit report, the quality of the financial information it generates, and the confidence in the investment decisions.

Lebanese Institutional environment

In the Lebanese field, many regulations have been put in place to provide applications that conform to KAM requirements. The Intermediate Circular No 447 issued by the Central Bank of Lebanon decides that the external auditors operating in Lebanon must comply with the International Standards on Auditing (ISA), including ISA 700-701-705-706-720, and to prepare the financial statements accordingly. The Lebanese companies
listed on the Beirut stock exchange should also report by using KAM. Thus, the external auditors of Lebanese banks and these companies should add the Key Audit Matters section to their reports. This new obligation leads the auditors to orient their work towards new, more detailed, and explanatory opinions that will affect the audit report’s financial information quality and auditors’ perception in their investment decision and audit expectation. Auditors address the KAM in the whole audit context and do not separate opinions on these matters.

After consulting all the audit reports of Lebanese Banks, we noticed that all these reports have some common points in the KAM section:
- Impairment of loans and advances
- Impairment of investment in a subsidiary
- Impairment of investment in a direct associate

Development of hypotheses
To highlight the research’s hypothesis, a conceptual framework is utilized to emphasize themes around financial information quality, investment decisions, and the expectation gap.

Conceptual Framework
As explained at the outset, the new audit report represents the biggest revolution not only for auditors but for audit reporting since the Great Depression. The auditor’s detailed opinion provides valuable information about the company’s financial statements using KAMs chosen within diligence areas. KAMs can be useful for both financial and non-financial information. Hence, it provides highlighted information and a valuable decision basis as a platform to the reader. The disclosure of KAM in the audit’s report above is meant to bridge the gap between the audit company's expectations and its stakeholders, especially investors. With additional information and a broader scope, it sets out the company’s main financial risks and how they were treated during the audit. The new audit report thus enhances audit report credibility and helps in building confidence in the audit.

A conceptual framework has helped define our perspective and hypothesis to analyze the defined approach given to Key audit Matters in this study(figure 2).
To summarize, the conformity to ISA 701, while auditing Lebanese banks and listed companies, has brought changes to the original audit report. The addition of the KAM section will affect some values for audit perception such as expectation gap and for reporting quality such as financial information quality and investment decision. The following parts are devoted to the development of a hypothesis related to this matter.

**Financial information Quality**

Some studies propose that KAM can have an attention-orienting effect, an information effect, or be a source of credibility (Pelzer, 2016, Sirois et al., 2014). Menon and Williams (2010) stipulate that investors show their interest in audit reports when they provide new information. The disclosures of KAMs related to the fair value in the financial statements attract nonprofessional investors, as proved by Christensen et al. (2014). Thereby, the investment decision made by investors is more likely to be changed when the audit report discloses KAMs. Conversely, Backof et al. (2015) and Kohler et al. (2016) find that for non-professional investors...
KAMs have no communicative value, while professional investors think that a negative KAM can lead to a better evaluation of a company’s economic situation than a positive KAM. On the other hand, Sirois et al. (2014) found that the disclosure of audit matters attracts financial statement users (attention directing effect), but the negative impact of KAMs is represented by the reduction of user’s attention to other areas of the financial statements. Indeed, KAMs are an instrument to underscore areas that auditors found critical instead of being an instrument to report areas of risk, even in the presence of unqualified opinion (Pelzer, 2016).

On the other side and according to Limperg’s theory of inspired confidence: “the demand for audit is the direct result of stakeholders (third parties) participation in the economy” (Hayes, 2005). The audit is highly needed to certify the information’s credibility to stakeholders. Accordingly, managers and investors tend to engage reputable auditors so they can rely on the information provided (Hayes et al., 2005). The information will be more credible when it is provided by auditors because users can have more confidence in the information, which helps them in their decisions (Soltani, 2007).

The new standard ISA 701 was introduced due to the user’s request for a more informative audit report. An audit report would not be informative if it does not affect the investor’s reaction. Based on the above discussion, KAMs effectively link the auditor’s report to specific pointed disclosures that are oriented to susceptible strategic areas. So KAM is expected to enhance the quality of the information provided through the audit report. The communicative dimension of KAM provides a view of the company’s economic situation and enriches the report, which is usually standard, with matters deemed important by the auditors. And thus, we formally state the first hypothesis:

**H1:** The Key audit matters communicated and implemented in the audit report affect the quality of financial information.

The quality of financial information communicated through the KAM section will affect the transparency of the audit report and thus the investment decision.
Investment decision

The investment decision of an individual investor is subject to change when a KAM section is added to the audit’s report or management’s footnote (Christensen et al. 2014). Yet, an added resolution paragraph can reduce the impact of a KAM section. Also, Pringle et al. (1990), Bamber and Stratton (1997), Vico and Pucheta Martínez (2001), have confirmed that auditor gives useful and relevant information when companies need to take loan and investment decisions.

When there is a lack of information for investment decisions, and the company’s financial statements do not offer any useful information, then there is an information gap (IAASB, 2015; Barker, 2002). ISA 701 was developed by IAASB to counteract the information gap as auditors will highlight the most important areas in the financial report to facilitate investment decisions for investors (IAASB, 2015). Furthermore, Soltani (2000) or Loudder et al. (1992), verified that auditors’ opinions are important to investors when making investment decisions. This point of view has also been adopted by KPMG (2013) and Litjens et al. (2015), who adds that areas presenting essential risks or high complexity shall be disclosed to restrain the information gap. According to conceptions of trust, communication between the auditor and the user based on the auditor’s report constitutes a situation of trust. Users base their investment decisions on auditor reports. More reliable reports and richer in information about the matters confronted during the audit mission, reassure the investors and subsequently constitute a source of confidence for decision-making. Therefore decisions will be guided by the perceived assurance provided by the auditor and their credibility. Accordingly, we hypothesize the following:

H2: The Key audit matters affect the investment decisions and reactions of investors.

The investment decision is built when users have a reduced audit expectation gap. Stakeholders ask for more information in the audit report with an estimation of significant risk, on which they can rely to make their decisions (Brouwer A., Eimers P. & Langendijk H, 2016). Several studies further indicate a correlation between the economic experience of users and the expectations of the audit (Manson & Zaman, 2001; Gold, Gronewold & Pott 2012), which further relates to the relevance of our survey which centers on investment decision, and then on the audit expectation gap.
The expectation gap could be described as "the difference between the public expectations of auditors and the opinions of the audit industry on what auditors should do" (McEnroe & Martens 2001). The expectation gap refers to the fact that audit report users often expect from auditors more information than what is mentioned in the audit report (Carrington, 2014). These high expectations lie at the basis of the limited knowledge of the auditor's role by users (Lee, Ali and Bien, 2009); so auditors couldn’t guarantee the viability of all the entries in the financial statements as users tend to expect.

Such expectations from the audit and the role of the auditor (which are not in line with the information available to the auditor) have been identified in a variety of studies and are mentioned in the literature as the audit expectation gap (Epstein & Geiger, 1994; Manson & Zaman 2001; McEnroe & Martens 2001; Porter, Óhartarta & Baskerville, 2012). Several authors declared that the audit report said nothing “informative” (Church, Davis, & McCracken, 2008; Mock et al., 2013).

The lack of information about the subject of the auditor's role subjects the standardized audit report to be significantly criticized (Carcello, 2012; Coram et al., 2011). Thus, an extended audit report with additional information and clarifications about the auditor's responsibility and role have the power to reduce the expectation gap (Koh and Woo (1998) and Boyd et al. (2001). Deloitte (2016b) and the IAASB (2015) highly support this idea. Although, Vanstraelen et al. (2011) state that KAM alone cannot reduce the expectation gap since, to start with, the users of the audit report do not have sufficient knowledge about the auditor's responsibilities. Accordingly, auditors should provide a clear view of any significant risks that were found while auditing, and how those risks were managed in the KAM section. By describing, via KAM, what measures have been taken to ensure a fair valuation of the reporting areas characterized by higher than ordinary uncertainty, users’ confidence in these values and financial reports as a whole may increase (CFA, 2013). Finally, users' understanding of the auditor's role and tasks can increase as a result of the explanation of actions taken by the auditor about the areas identified as KAM. The increased knowledge can, in turn, lead to a reduction in the audit gap (MIA, 2011). Further explanations of corresponding audit matters included in the auditor's report may lower the expectation gap. Usually,
users expect more specific information about risky areas in the company. KAM will fulfill this need for complementary information, related to the perception of audit quality. Hence,

H3: The Key audit matters communicated in the audit report affect the investor's perceptions of the audit expectation gap.

The upcoming section will develop the research methodology and test the discussed hypotheses.

METHODS

Our study focused exclusively on the external auditors of Lebanese banks and listed companies subject to ISA 701, which are required by the Central Bank of Lebanon and the stock exchange authorities to add a KAM section in their reports. Also, the target population composed of external auditors is limited to the big 4 Audit companies (KPMG, Deloitte and touch, PWC, Ernest, and Young), and 2 other national reputable audit offices, exclusively responsible for auditing banks and listed companies. These 6 audit offices cover the audit of all banks and listed companies that are obliged to include KAM in their audit report. In each, an audit team is responsible for the audits concerned by the KAMs.

The study aims to investigate KAM's impact and value for Lebanese auditors through their impact on financial information quality, investment decision, and expectation gap. To investigate this relationship, a quantitative approach in the form of a survey was appropriate. By using a quantitative survey method, more respondents were reached, which increased the generalization of the study (Bryman & Bell, 2011). This survey is divided into four parts and consists of a total of 18 questions. The first part of the survey regarding background factors aims at the benefits respondents in different subgroups based on aspects that may be relevant to how they value new information in the audit report and thus the impact on the investment’s decision. The second part of the survey is the main component of the study’s quantitative survey and consists of issues relating to KAMs such as financial information quality, investment decision, and audit expectation gap. The response options consist of using the Likert scale (from 1 to 5) that indicates the degree to which respondents agree with the given statement.

The survey was filled by 38 Lebanese external auditors. This number is quite reasonable since it represents more than 10% of our
population, which contains a restricted number of auditors who are charged with auditing banks and listed companies, to guarantee the representativeness of this study. These surveys were collected by hand and by email. Data were entered on SPSS software (Statistical Package for the social sciences) to help to analyze and obtaining results through statistical tests. Appendix 1 evokes all the variables that are used in this research.

Based on previous literature, we expect that the value of KAMs will be positively associated with the financial information quality it provides, and with an investment decision. Finally, we also investigate if there is any relation between and reduction of the expectation gap.

RESULTS AND DISCUSSION

The surveys were sent by mail or by hand to external auditors working in Big 4, and 2 reputed national audit offices charged in auditing banks and listed companies. Data were collected and inserted in SPSS for exploration. The primary findings are presented from the study of the questionnaire. Initially, the respondents' profiles are illustrated in the background factors section and are then used to highlight differences within the group. The answers to the different sections of the questionnaires are also analyzed based on relevant basic data.

Background factors

The survey's first questions are called background factors and concern the external auditor experiences and education in relevant areas. This sets the selection group's profile based on different parameters.

The first question illustrates the respondents' experience level and shows that 39.5% of the external auditors involved in KAM have a minimum experience of 10 years in the field. The responses received are illustrated in Table 2. The concerned auditors have an average professional experience between 10-20 years.

|                | Frequency | Percent | Valid Percent | Cumulative Percent |
|----------------|-----------|---------|---------------|--------------------|
| Valid <5y      | 9         | 23.7    | 23.7          | 23.7               |
| 5-10           | 12        | 31.6    | 31.6          | 55.3               |
| 10-20          | 15        | 39.5    | 39.5          | 94.7               |
| >20y           | 2         | 5.3     | 5.3           | 100.0              |
| Total          | 38        | 100.0   | 100.0         |                     |
The second question concerns the respondents' age. The results show that 54.1% of participants have an average age between 30-40 years. The third question shows the position held by the external auditors who are charged with auditing the firms that require a KAM section in their reports. The result reveals that the majority are senior audit managers or assistant audit managers.

Table 3: Distribution of respondents according to their position

| Position                          | Frequency | Percent | Valid Percent | Cumulative Percent |
|----------------------------------|-----------|---------|---------------|--------------------|
| Auditor                          | 6         | 15.8    | 15.8          | 15.8               |
| Assistant Auditor Manager        | 12        | 31.6    | 31.6          | 47.4               |
| Supervisor                       | 4         | 10.5    | 10.5          | 57.9               |
| Audit Manager                    | 6         | 15.8    | 15.8          | 73.7               |
| Senior Audit Manager             | 10        | 26.3    | 26.3          | 100.0              |
| Total                            | 38        | 100.0   | 100.0         |                    |

Overall, background factors show a varied sample, which was the expected outcome. This reinforces the idea that the selected group correctly reflects the total population that is assumed to be varied. Furthermore, the experience indicates a self-awareness of auditors towards the new regulation and procedure. The high proportion of respondents who have a title of supervisor or assistant manager suggests greater knowledge in this area, which increases confidence that the respondents can understand and answer the questions regarding KAM.

Financial information quality statements will be studied and explored before reaching our research question.

Financial information quality

To ensure the trustworthiness of the study, the questionnaire items were subjected to a Cronbach alpha which resulted in an internal consistency score of 0.832. The results indicate an overall positive response regarding the usefulness and value of KAM. Almost half (58.1%) of participants believe that KAM is not less important than audit opinion.
The percentage of respondents who believe that reporting by KAM adds value to an audit report is 73.4% which is a very high percentage and underlines the importance of the KAM section for financial information quality. Only 6.3% believe that KAM does not add any value.

Based on the experience and position of the respondents no significant differences are registered between the groups. In all groups, approximately 50% agree with the statement that KAM will reduce standardized audit reports. This explains why respondents perceive that KAM creates an overall value.

### Table 5: Correlation between the audit opinion and the KAM's contribution

| Kendall's tau_b | v1     | v5     |
|-----------------|--------|--------|
| Correlation Coefficient | 1.000  | .548   |
| Sig. (2-tailed)   | .      | .038   |
| N                | 38     | 38     |

| v5               | v1     | v5     |
|------------------|--------|--------|
| Correlation Coefficient | .548   | 1.000  |
| Sig. (2-tailed)   | .038   | .      |
| N                | 38     | 38     |
Table 5 shows that KAM is not less important than audit opinion, because it contributes towards better governance through the conversation between the auditor and those charged with governance. The auditor will have to communicate all the founded matters during their mission with TCWG. Ipso facto, the new section KAM will clarify the accomplished mission for users and reduce standardized audit reports due to its specificity in each field and company, which will increase the quality of the information provided by the auditor (figure 3). Thus H1 is confirmed.

Figure 3: Information quality in function of KAM effect on the standardized audit report

The negativity towards KAM is almost inexistent and auditors show a high percentage of “agree” and “strongly agree” which reflect the importance of KAM during their mission and reporting.

Table 6: Correlation between information quality of reporting and KAM’s contribution to a better understanding of the company

| Kendall's tau_b | v2 Correlation Coefficient | v4 Correlation Coefficient | Sig. (2-tailed) | N |
|----------------|-----------------------------|-----------------------------|-----------------|---|
|                | v2                          | 1.000                       | .603*           | 38 |
|                | v4                          | .603*                       | 1.000           | 38 |

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In the same perspective Gold et al., (2020), suggested that KAMs serve as a beneficial mechanism for enhancing financial reporting quality by attenuating aggressive financial reporting behavior, regardless of the precision employed by auditors. So, KAMs are an important concept and their introduction and applicability will have a positive effect on the audit reporting process and quality of disclosed information (Cordoş and Fülöp, 2015).

Investment decision
Auditors tend to assess the investor’s decision to be dependent on KAM and tend to be relatively confident in their assessment. Almost 45% of respondents think investment decisions rely on KAM which creates more responsibility towards the new exigency. Hence, 46% of external auditors believe that the indications of risks and how they were controlled in the KAM section entice investors. Transparency is the main driver to invest in a business. Also, 73% of the respondents say that the present format of the audit report, especially with the added KAM section, is adequate to meet user’s requirements in the Lebanese bank’s context. The following table discusses the importance of KAM’s to assist investors in their investment decision from the Lebanese auditors’ perceptions

| Table 7: Distribution of auditors’ perceptions for investment decision statements |
|--------------------------------------|----------------|-------|------|-------|---------------|
| Users rely on KAM revealed in the audit report while taking an investment decision | Strongly Disagree | Disagree | Neither | Agree | Strongly Agree |
| The indication of risks and how they were controlled in KAM attract the investors | 2 | 5 | 4 | 20 | 7 |
| The present format of a performance audit report is adequate to meet the user’s requirement | 0 | 1 | 8 | 26 | 3 |

When interpreting the survey results, it is assumed that approximately 66% of respondents perceive KAM reports to provide a better understanding of the reviewed company, which helps in attracting investors who rely on them. It is easier to evaluate the information
provided by the audit report when the reporting of KAM includes an explanation of the measures that were taken to ensure a correct valuation of the areas identified as KAM. Furthermore, the majority of the respondents stated that they fully or partially agreed with the claim that the reporting by KAM can lead to further investigations in the areas to which KAM relates. Thus, KAM reporting implies a commitment that extends beyond the audit report, which further underlines the perception of Lebanese auditors’ value creation with KAM.

The new reporting format creates a more informative audit report for investment decisions, which explains the overwhelming majority of respondents who, in a general context, were positive to KAM and believed that its reporting increased the communicative value of the audit report.

Hypothesis H2 predicts that Key audit matters affect the investment decisions and reactions of investors. So investors who receive a KAM section in the audit report can make a more confident investment decision. Accordingly, H2 is confirmed. In parallel, Kipp (2017) affirms that audit report disclosures are most valuable to investors in informing their confidence in the underlying accounts and the audit. As for other authors, their results show that the KAM section could eventually lead to a better assessment of the economic situation of a particular company and thus to investment decisions (Köhler et al., 2016).

In the past, users of the financial statements were not aware of the key elements of audit. Auditors find that investors and users of financial statements will be capable to better notice the important work that the auditors do. So the next analysis will treat the Audit Expectation GAP.

**Audit Expectation GAP**

One of the primary benefits of reporting KAM is that the communicated information can help users gain a better insight into the audited company’s business. Thus, an attempted effect is to reduce its information asymmetry. The questionnaire investigates 4 variables concerning whether the respondents perceive the audit expectation gap through KAM. The answers are surprisingly positive to the aspect of KAM, as shown in the table below.
Table 8: Statistics of variable related to Audit expectation gap

| Statistic | N | Range | Mean | Std. Error | Mode |
|-----------|---|-------|------|------------|------|
| v9        | 38 | 3.0   | 4.027| .1255      | 4    |
| v10       | 38 | 2.00  | 4.0541| .11590     | 4    |
| v11       | 38 | 3.00  | 3.8919| .12725     | 4    |
| v12       | 38 | 4.00  | 3.6757| .15035     | 4    |
| Valid N (listwise) | 38 |

The respondents tend to agree that KAM reduces the audit expectation gap through their evaluation of 4 statements related to KAM.

The answers to statement 9, illustrate that the respondents believe that reporting by KAM creates a better understanding of what the auditor is doing which provides more confidence in the applied audit and, thus, the audited company's accounts. 84% agree fully or partially with the claim, which indicates that KAM significantly improves the transparency of the audit process, the audit vision, and the readability of the report. The majority of respondents believe that confidence in the audit and the accounts increase when the auditor's actions about complex accounting records are reproduced.

Almost 81% of the respondents state that KAM will reflect the quality of the audit performed. Distributed based on their experience, the answers give a more polarized picture of the auditor's view. The group with high experience (5-10 years and 10-20 years) generally has a good understanding of the role of KAM and believes KAM will reflect the quality of the audit performed.

Table 9: Correlation between KAM and information gap

| Kendall's tau_b | v9 Correlation Coefficient | v9 | v11 Correlation Coefficient | v11 | N | N |
|-----------------|---------------------------|----|-----------------------------|-----|----|----|
| v9              | Correlation Coefficient   | 1.000 | .788                        |     | 38 | 38 |
| Sig. (2-tailed) |                           | .   | .043                        |     |    |    |
| N               |                           | 38  | 38                          |     |    |    |
| v11             | Correlation Coefficient   | .788 | 1.000                       |     | 38 | 38 |
As proven by table 9, KAM provides a better understanding of what the auditor is doing and thus it reduces the information gap (correlation coefficient 0.788).

**Table 10: Distribution of participants' answers to Audit expectation gap statements.**

| Statement                                                                 | Strongly Disagree | Disagree | Neither | Agree | Strongly Agree |
|---------------------------------------------------------------------------|-------------------|----------|---------|-------|----------------|
| 9. The KAM provides a better understanding of what the auditor is doing.  | 0                 | 2        | 4       | 22    | 10             |
| 10. KAM significantly improves the transparency of the audit process, the audit vision, and the readability of the report. | 0                 | 0        | 8       | 20    | 10             |
| 11. KAM reduces the information gap, and reflect the quality of the audit performed. | 0                 | 2        | 7       | 21    | 8              |
| 12. KAM creates greater confidence in audit and thus revised company accounts. | 1                 | 2        | 11      | 17    | 7              |

Auditors emphasized that the understanding of the auditor's duties should increase as a result of KAM, which supports the view of KAM’s educational aspect. This further means that the results of the study, in combination with the results of previous surveys (Epstein & Geiger, 1994; Vanstraelen et al., 2012) show that the expectation gap can be reduced by reporting KAM. Therefore, H3 is confirmed: The Key audit matters communicated in the audit report affect positively investor's perceptions of the audit.

Previous researches concluded the majority of respondents perceived that the new regulation would have impacted the reduction of the expectation gap. The reason for that is the audit report has become clearer in regards to auditors’ responsibilities and what they have reviewed and upon which placed extra focus (Christensen et al., 2014, Backof et al. (2017). Similarly, Kipp(2017) expected that detailed descriptions of critical matters will increase investor's confidence in the audit report and perceptions of audit quality which will reduce the expectation gap.
CONCLUSION

The study shows that reporting by KAM adds a great value to the audit report external auditors' perspective as the survey results illustrate a positive response regarding KAM's overall value creation. The estimated value of KAM by auditors is further emphasized by an increased interest in the audit report as a result of the updated content. Many respondents also stated that the reporting of KAM may lead to further investigations related to reported areas. Overall, the results indicate that the reporting of KAM is increasing audit report usability for investors. Its value creation can be later divided into financial information quality, investment decision, and expectation GAP. The study results show that external auditors see an informative value in the information communicated via the reporting of KAM. The auditors think that KAM gives a better insight into the revised company and thus can reduce the information asymmetry that arises as a result of investor's limited opportunity to monitor business operations.

The survey shows broad support for the reporting of KAM and a positive setting to its overall value. This applies regardless of the respondent's experience or specialization, similar to previous surveys (IAASB, 2015a) that suggest that users request a more informative audit report. The auditors' perception of KAM, as well as its value creation, is emphasized even more by the high percentage of respondents who believed that interest in the audit report will increase as a result of the introduction of KAM.

Moreover, the result of the study shows that the reporting of KAM adds great value to audit reports from the perspective of Lebanese external auditors and can reduce information asymmetry, increase trust in accounting and reduce the expectation gap.

This study is subject to some limitations. First, the restricted knowledge of KAM between auditors not concerned with auditing banks and listed companies is observed during the research. Second, the key audit matters are supposed to clarify the financial information and to make the audit report more informative and trustworthy, meanwhile, sometimes it is hard for investors to understand the details proposed in the KAM section which will affect their financial reporting quality, judgments, and expectation gap.
Indeed, many opportunities could be explored in future research. We will seek to obtain opinions from investors. KAM effects on investment decision and information quality could also be a subject of study through investors' perceptions and industry requirements.

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