INTRODUCTION

External audits are done based on specific auditing standards to ascertain the validity and reliability of the financial statements prepared by companies. Yet despite general guidelines, actual auditing practices vary considerably from country to country. For example, U.S. and British accountants must pass extensive and rigorous certification exams. However, many other countries may require only a college degree in accounting or business as qualification for conducting external audits. This variation in actual auditing practices poses problems for international investors and creditors and, of course, for multinational firms.

Several factors in the world’s economy exist today that provide incentives for more uniformity or harmonization among auditing standards. For example, the nature of industry and capital markets has become increasingly international over the last decade. Paralleling the increased activity in international financial markets, Multinational Corporations (MNCs) also reflect the globalization of business during the 1980s and 1990s. A parent company in one country may have operations all around the world. The company may control hundreds of subsidiaries and have investments in hundreds of other associated companies in many different countries. Other important international capital markets, like in Europe, used to be regulated, but are now deregulated to improve efficiency. Some markets, which have traditionally prohibited or restricted ownership of securities, are opening up to foreign investment. The surges in international trading have increased the use of, and demand for, reliable financial statements. When the information is used internationally, there is a need to ensure that auditing standards and procedures applied to it are of an equally high quality wherever in
the world the information originated or wherever the audit took place. When auditing standards are determined and set on a country-by-country basis, financial statement users are more likely to be unsure of reliability of the information in the financial statements.

The objective of harmonizing auditing standards is to reduce the differences in auditing practices among countries. The efforts to harmonize auditing standards have met with limited success in their implementation (Choi and Mueller 1992; Muller, et al., 1991; Rivera 1989). Reasons for this limited success are lack of enforcement by the international auditing standard’s bodies, such as the International Federation of Accountants (IFAC) and lack of adequate representation of developing nations’ interests on councils developing those standards (Abu-Ghazaleh 1989). A more fundamental reason, which may be responsible for this lack of progress toward harmonization, is differences in each nation’s cultural, social and political environments. These differences may prevent or severely limit the extent of audit harmonization across nations (Choi and Mueller 1992; Beresford 1990; Puxty 1987).

**Independence**

In a 1985 address by Don Kirk, then Chairman of the FASB, in a forum on harmonization, he states that in order to establish acceptable international auditing standards, first there must be an agreement on fundamental international concepts (Beresford, 1990). One fundamental concept in auditing is independence. The credibility that financial statement users can place in the audit process will differ between countries if the concept of independence differs between countries. If different countries have a different understanding of the concept of independence, then there is little chance for having universal standards.

Agacer and Doupnik’s (1991) study examined whether CPAs in three countries (USA, West Germany, and Philippines) have a wide agreement about the concept of independence in appearance. Agacer and Doupnik (1991) found that CPAs in three countries (USA, West Germany, and Philippines) have different perceptions of auditor independence. They concluded that the difference in the perception of auditor independence is associated with a cultural difference among these three countries. Agacer and Doupnik further concluded that the process of developing auditing standards in
which audit opinions have similar meaning and value across all countries would be more difficult to achieve. Thus, establishing generally accepted international auditing standards based on a country by country agreement is difficult to achieve because of the lack of agreement on the most important concept in auditing, that of independence.

The Research Question

The goal of this study was to examine an alternative to establishing worldwide international standards. This alternative suggested by many researchers is a “regional approach” to establishing standards (Wood, 1993 and Rivera, 1989). Rivera (1989, p.329) suggests that achieving harmonization could be more successfully done on a regional level, involving homogenous countries, than on a global level. The regional approach looks at clustering countries by regions according to similar cultural and environmental factors and narrowing differences in auditing standards among member nations. Worldwide economic growth and increasing competition in the capital and money markets have made it difficult for a country to survive economically on its own. Therefore, throughout the world, there is a movement for many countries in a single region with similar culture and common political and economic goals to cluster themselves and establish a unified economic system. This clustering is called Regional Economic Integration, which reduces the economic significance of national political boundaries within a geographical area. One example is the Arabic Gulf countries - Saudi Arabia, Kuwait, Qatar, Oman, Bahrain, and United Arab Emirates. Because of economic integration, countries belonging to a region will compromise and remove barriers that hinder harmonization among member countries. Other regional groupings are the European community (EC), the Association of Southeast Asian Nations (ASEAN), and the North America Free Trade Agreement (NAFTA). Therefore, a study of perception of auditor independence by regions is needed to answer the research question, “Is the concept of independence similar among countries within one region that share similar cultural and environmental factors?”

The results of this study would help regional and international organizations involved in harmonization in one of two ways:
(1) If the results of this study show that independence is perceived differently across regional countries, then the process of developing audit standards in which audit opinions have similar meaning and value across these countries and worldwide will be more difficult; or

(2) If on the other hand, this study finds similar meaning and value across countries in the same region, then harmonization of auditing standards can be achieved on a regional basis first, with globalization to follow.

The results of this study could also help multinational CPA firms in setting one set of rules and regulations for their operations in this region to reduce or eliminate any threat to auditor independence.

RELEVANT LITERATURE

Cross-cultural Studies

Several studies have examined the impact of culture on accounting and financial reporting. Agacer and Doupnik (1991) found the difference in the perception of auditor independence was caused by the difference in culture among countries and concluded that harmonization of auditing standards would be difficult to achieve. Agacer and Doupnik’s (1991) conclusion was supported by Bloom and Naciri’s 1989 study, which concluded that significant differences in the standard-setting process of nine countries are due to cultural differences. Riahi-Belkaoui and Picur (1991) found that the meaning of accounting concepts varies in the manner with which they can be recognized, grasped or understood by users from different cultural groups working for the same global organization.

A number of studies focused on country groupings based on accounting and economic variables. Doupnik and Salter 1993, Doupnik 1987, Nobes 1983, Nair and Frank 1980, and Frank 1979, all based their classifications on accounting aspects such as measurement and disclosure practices, accounting practices or judgmental aspects. On the other hand, Hussein, et al., 1986 and Wood 1993 utilized auditing characteristics.

A number of studies have investigated the professional and work characteristics of accountants across cultures. In a study of American CPAs and British Chartered
Accountants, Shoenthal (1987) attributed the differences between the two groups to auditing procedures, professional ethics, educational preparation, training and culture.

In addition to the above studies, other authors such as Alhashim 1973, Nair and Frank 1980, Beazley 1968, Choi and Mueller 1992, and Ueno and Wu 1993 have examined the effects of national culture on accounting and harmonization.

Studies of Auditor Independence

Various aspects of independence have been studied on a within-country basis, in the United States, the UK, Canada, West Germany, and Malaysia. Most of the empirical studies, however, were conducted in the US.

Schulte (1965) and Hartley and Ross (1972) found that respondents did not believe that performing management consulting, in addition to external audit, seriously endangers the CPA’s audit independence. In examining the same issue, Titard’s (1971) respondents thought it might result in some loss of auditor independence.

A review of the existing literature on auditor independence shows that there are currently no studies that examine the regional perception of auditor independence. Since differences in perception of auditor independence was found between countries, examinations of smaller units are needed. Examining perception of countries in the same region is a logical next step in the search for consensus of perception. Many studies have suggested that harmonization of accounting or auditing may be enhanced with less opposition if standards are constructed for an individual grouping of countries that share homogeneous factors (Wood 1993; Doupinik 1987; and Rivera 1989). It is assumed that the inhabitants of these countries share similar factors that affect their perception and understanding of concepts. However, there is no empirical research examining whether countries with homogeneous factors have a similar understanding of concepts. A review of the literature, further suggests that regional harmonization should be first undertaken prior to global harmonization. Regional harmonization of auditing standards should face less opposition than that of global harmonization.
METHODOLOGY

The objective of this study was to examine empirically whether a consensus on the perception of auditor’s independence exists between countries belonging to the same region. Specifically, the study examined the effects of four variables on the perception of two subject groups (CPAs and financial analysts) with respect to the auditor independence in three countries – Saudi Arabia, the State of Kuwait, and the United Arab Emirates. The four variables are (1) the percentage of total office revenues generated from the client, (2) whether management advisory services (MAS) are provided in addition to the external audit, (3) the number of months client fees remain unpaid, and (4) whether a relative of a member of the audit staff is employed by the client.

The study extends Agacer and Doupnik’s (1991) study in two ways. First, the study increases the tested groups to two instead of one. Second, the present study tests the difference in the perception of auditor independence between the three countries for each subject group.

HYPOTHESES

Two primary null hypotheses and eight null sub-hypotheses were constructed to test the independent variables. The main justification of these hypotheses is that culture has been shown to be a major obstacle to harmonization. The inhabitants of a country might have a different perception of the concept of independence, notably that of “independence in appearance” vis-à-vis that of another country. Therefore, countries with similar cultures, which possess of homogeneous factors, should have similar perceptions of auditor independence.

The two primary null hypotheses are:

H1: There is no difference in the perception of the risk of losing independence between professional accountants in Saudi Arabia, the State of Kuwait, and the United Arab Emirates.¹

H2: There is no difference in the perception of the risk of losing independence between financial analysts in Saudi Arabia, the State of Kuwait, and the United Arab Emirates.

¹ Professional accountants here are meant to be the CPAs.
The sub-null hypotheses associated with each independent variable for each of the above primary null hypotheses appear below:

H1.1: There is no difference in the perception between professional accountants in Saudi Arabia, the State of Kuwait, and the United Arab Emirates of the risk of losing independence between an audit firm with a relatively large percentage of its revenue derived from a particular client and an audit firm whose billing to a particular client is a relatively small percentage of total revenue.

H1.2: There is no difference in the perception between professional accountants in Saudi Arabia, the State of Kuwait, and the United Arab Emirates of the risk of losing independence between an audit firm that provides MAS to a client and an audit firm that does not provide MAS to a particular client.

H1.3: There is no difference in the perception between professional accountants in Saudi Arabia, the State of Kuwait, and the United Arab Emirates of the risk of losing independence between an audit firm with fees remaining unpaid by a particular client for a relatively long period of time and an audit firm with fees remaining unpaid by a particular client for a relatively short period of time.

H1.4: There is no difference in the perception between professional accountants in Saudi Arabia, the State of Kuwait, and the United Arab Emirates of the risk of losing independence between an audit firm where any family member of the audit staff is employed by the client and an audit firm where the family member of the audit staff is not employed by the client.

H2.1: There is no difference in the perception between financial analysts in Saudi Arabia, the State of Kuwait, and the United Arab Emirates of the risk of losing independence between an audit firm with a relatively large percentage of its revenue derived from a particular client and an audit firm whose billing to a particular client is a relatively small percentage of total revenue.

H2.2: There is no difference in the perception between financial analysts in Saudi Arabia, the State of Kuwait, and the United Arab Emirates of the risk of losing independence between an audit firm that provides MAS to a client and an audit firm that does not provide MAS to a particular client.

H2.3: There is no difference in the perception between financial analysts in Saudi Arabia, the State of Kuwait, and the United Arab Emirates of the risk of losing independence between an audit firm with fees remaining unpaid by a particular client for a relatively long period of time and an audit firm with fees remaining unpaid by a particular client for a relatively short period of time.

H2.4: There is no difference in the perception between financial analysts in Saudi Arabia, the State of Kuwait, and the United Arab Emirates of the risk of losing independence between an audit firm where any family member of a member of
the audit staff is employed by the client and an audit firm where the family member of a member of the audit staff is not employed by the client.

The rationale for testing these above hypotheses and specifically choosing these independent variables is discussed below.

Treatment Variables

**Past Due Fee**

Section 101.01 (a) of the Professional Standards (1982) states that “Independence will be considered impaired if, during professional engagement, or at the time of expressing an opinion, the firm had or was committed to acquire any direct or material indirect financial interest in the enterprise…” The past due fees are considered loans which imply a financial interest in the company (Bailey 1992). Unless audit fees are paid in advance, auditors risk losing fees if their audit decisions conflict with the wishes of their client. Unpaid fees, therefore, may provide audit clients an opportunity to exert pressure on auditors to revise their opinion. On the same question of whether an audit firm’s independence would be considered impaired with respect to a client whose fees for the preceding year are unpaid and past due, the AICPA Ethics Committee ruled (ET 191.104):

Independence of the member’s firm may be impaired if more than one year’s fees due from a client for professional services remain unpaid for an extended period of time. At the same time a member issues a report on a client’s financial statements, the client should not be indebted to the member for more than one year’s fee… (AICPA Professional Standards, 1982, p.4445).

Thus, the variable “past due fee” is selected to operationalize “financial interest in the enterprise.”

**Client Size**

When one client provides a large portion of an accounting firm’s revenue, an independence problem could exist or be perceived to exist. This issue is frequently raised and discussed in the accounting literature (Mautz and Sharaf, 1961, p.213). Some researchers found that to have a client that is the source of a large portion of a firm’s
revenue can affect the perception of independence vis-à-vis that client. However other researchers found the perception of independence was not affected by such a relationship.

Lindsay et al., (1987) examined the effect of fifteen auditor-client relationships. There are a number of relationships, which significant numbers of users (financial analysts and bankers) saw as impairing independence, which include the issue of client size.

Pany and Reckers (1980) asked a sample of shareholders to examine the ability of the auditor to resist pressures under various conditions. These conditions included the issue of client size in combination with gift size and discount size. They chose 1 percent and 10 percent of office revenue respectively to approximate a small-to-average-size client and a large client. They found that client size did not appear to have a significant effect, but it was noted that in all cells the mean score of the larger client level of the size of a client factor exceeded the mean score of the smaller client level. This meant that less confidence was expressed for audits of large clients.

Although the ethical standards of the AICPA do not consider this issue, the Accounting International Study Group (1976) recommended that auditors be restrained from accepting engagements for which the fee constitutes 10 percent or more of the auditor’s total fee income. From the above discussion, additional empirical investigation is warranted to see whether the CPAs, bank loan officers, and financial analysts of three developing countries in one region will perceive client size as an important factor that may impair the independence of the external auditor.

Management Advisory Services (MAS)

Providing MAS raises unresolved questions of auditor objectivity and independence. The question of whether providing MAS harms independence has been extensively debated and is the most prevalent topic for independence-related research. The effect of MAS on independence has been examined extensively in the U.S. Researchers from other parts of the world that have examined the effect of MAS on independence include Lindsay, et al. (1987) in Canada; Gul (1987) in Australia; and Gul and Yap (1984) in Malaysia. A number of studies support the argument that MAS increases an audit firm’s independence or that providing MAS does not significantly
affect perceptions of financial statement reliability (Schulte, 1965; Hartley and Ross, 1972; and McKinley et al., 1985). On the other hand, several studies found that auditor independence was perceived to be impaired when MAS services are provided (Titard, 1971; Hartley and Ross, 1972; Lavin, 1976; Shockley, 1981; and Pany and Reckers, 1980).

Because of the conflicting results of previous research and because of requirements of the rules of conduct in Saudi Arabia and Kuwait, which prohibit CPA from rendering MAS to external audit clients, the MAS-independence issue is in need of more research, and therefore represents an important variable in this study.

**Family Member of the Audit Staff Employed by Client**

Personal relationships such as those arising from family bloodlines and marriage give rise to circumstances that may impair a CPA’s independence (AICPA Professional Standards, 1991). This becomes more relevant in countries known to value close family ties. Rule of Conduct 101 prohibits relationships that impair a CPA’s independence through direct financial interests, material indirect financial interests, or other involvement. The employment of a relative of a member of the audit staff by the client is selected to represent and operationalize “personal relationship and protection of someone else’s interest.”

To avoid ambiguity for subjects, a specific type of employment for the relative of a member of the audit staff had to be selected. The employment must include job activities that are somewhere between bookkeeping and management level. The position of computer programmer was selected because this is a type of employment whose activities are not obviously management level or obviously bookkeeping. The type of countries included in the study motivates the use of a relative of a member of the audit staff instead of the spouse. These countries are family oriented and described as possessing collectivism cultural value, which means that an individual is not isolated from relatives and will work for their interests.
Grouping Variable

**Homogeneous Cultural and Environmental Factors**

Since differences in cultural factors have shown to be the cause of the differences in the perception of auditor independence (Agacer and Douplik, 1991), then countries with similar cultural and environmental factors should have similar perceptions of independence. Data was gathered in three countries with similar culture and possessing homogenous environmental factors. Therefore, in addition to the four treatment variables described above, similar cultural and homogenous environmental factors represent a non-repeated grouping variable. The construct “similar cultures and homogenous environmental factors” was operationalized by a grouping variable with three levels (the three countries involved in the study).

**Countries Selected**

The purpose of this study was to examine the regional perception of auditor independence. Because of the expenses and limited availability of data, the data was gathered in only three countries in one region. The three countries are Saudi Arabia, the State of Kuwait, and the United Arab Emirates. The selection of these countries was based on the following criteria: (1) they share similar cultural and environmental factors; (2) all three countries follow auditing standards and/or accounting laws that directly or indirectly stress both the appearance and the fact of independence; and (3) they belong to the same regional organization.

The primary criterion in the selection of countries was that these countries share similar cultural and environmental factors. The international accounting literature has suggested that accounting practices are shaped and formed by their environments (Muller 1967; Nobes 1983, 1984; Arpan and Radebaugh 1985; Hofstede 1987; Schreuder 1987; Riahi-Belkaoui and Picur 1991; Perera 1989; and more). Hofstede (1983b) grouped the three countries in one cluster because they have similar indexes of cultural values – high Power Distance, high Uncertainty Avoidance, lower Individualism, and high Masculinity. Ronen and Shenkar (1985) classified Saudi Arabia, the State of Kuwait, and the United Arab Emirates in one cluster based on four attitudinal variables – work goals, values, needs, and job attitudes.
Muller, et al. (1991) and Hussein, et al. (1986) identified type of economy as one of the major environmental factors that affects the development of accounting and auditing. According to Choi and Muller, inventory methods, accounting for accretion or discovery of natural resources, audit function, and other accounting and auditing procedures all have some relevance to the type of economy involved. The economies of the three countries in the study depend on exploitation of a natural resource – oil. As to the type of economic system, the three countries fall into a category known as “capitalist-statist” (Belkaoui 1985, p.46).2

Wood (1993) and Alkafaji (1983) suggested that stage of economic development is an important factor that can affect the accounting profession. The literature suggests using the per capita income and the average annual growth of Gross Domestic Product (GDP) to measure the level of economic development. The three countries are considered to have high per capita income. In 1992, per capita income was $10,338 for Saudi Arabia, $14,000 for the United Arab Emirates and $15,984 for the State of Kuwait. The average growth of GDP for the 1985-1992 periods was 5.4% for Saudi Arabia, 4.6% for the United Arab Emirates, and 7.9% for the State of Kuwait. The high Kuwaiti’s average growth GDP was caused by the Gulf war that caused the GDP to almost double after the liberation in 1991. From these numbers it could be said that these countries are experiencing similar average growth of GDP. Since these countries are relatively similar in terms of per capita income and average GDP growth rates, they can be grouped together.

In reviewing the status of the political system of the three countries, it was found that families rule these countries.3 The political events in these countries are dominated by a member of a family, while other members of the family head important ministries and agencies. The political system in each of these countries is highly centralized and every activity and organization is controlled by the government, including those of the accounting profession. Thus, the accounting profession is government-regulated, unlike

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2 Capitalist-statist states have very large government productive enterprises, either because of an elitist development philosophy or a major dependence on a key resource such as oil.
those of other developed countries, which are self-regulated. The political system of these countries falls under the classification of a traditional monarchy.

Because language mediates our worldview, it plays a central role in the development of cognition and perception. Individuals, as they learn a language, acquire not only a store of lexical and grammatical characteristics but also a linguistic mode of cognition and perception. The importance of language in the international accounting and country classification literature is very noticeable. Frank (1979) and Alkafaji (1987) had used the official language to operationalize the term culture. Their results found some statistical significance. Since language has been found to be important in clustering countries, this environmental factor is included to show that these three countries have a similar language—Arabic. Besides the Arabic language, the English language is used in these three countries very often as the language of business.

Religion may also affect the conduct of business and accounting in a given country. The effect can be through the legal system or through restricting or forbidding certain kinds of transactions. The most evident case in today’s world is the impact of the Moslem religion on the way people behaves, think, or deal with others. The religion factor also has an impact on business, for example the impact of Islam on the way Islamic banks can conduct their affairs. Regarding the religion factor these three countries are very similar; they are 100% Moslem countries. Therefore, these countries should be grouped together.

Alkafaji (1987) cited the legal system as a non-accounting variable that may influence accounting. Countries have different national legal systems. The national law of each country defines most directly and frequently the conduct of business and so the practice of accounting. Nobes (1988) have identified the origin of the legal system to proxy for the complex legal system found in each nation. Since the religion of these countries is Islam, their legal systems are mainly based on the Islamic law.

Wood (1993), Mueller (1967), and Nobes (1983) all have cited that education is an important factor that affect the business and accounting professions in every country. The accounting function in an illiterate country becomes difficult if not possible. External usage of accounting reports becomes useless and beyond the understanding of the general public. This leads to less demand for auditing services, and few rules and
requirements for the auditing profession. Therefore any plan to establish one set of international standards should consider differences in educational levels. Furthermore, setting standards for everyone to follow will be meaningless because countries with low levels of education are not going to appreciate these standards. This study uses the literacy rate as a proxy for educational environment (Wood 1993; and Alkfaji 1983). The literacy rates of the three countries are considered to be above average with 79.6% for the State of Kuwait, 62.8% for Saudi Arabia, and 79.2% for the United Arab Emirates. Thus, a literacy rate gives support to grouping the three countries based on levels of education.

In summary, these countries can be grouped together according to the above environmental and cultural factors. Therefore, the first criterion that the three countries share similar cultural and environmental factors was met.

The second criterion required that countries have similar auditing standards and/or accounting laws that stress both the appearance and the fact of independence for the external auditor. Needles (1985, p.26) defined concepts of independence as independence in fact and in appearance. All three countries follow auditing standards and/or accounting laws that directly or indirectly stress both the appearance and the fact of independence. The reason for including this criterion is to show that the results of this study would be free from the confounding effect of different laws concerning the concepts of independence.

The third criterion required that countries be members of a regional organization. Currently, countries in all parts of the world are grouping themselves primarily for economic and political reasons. As a consequence, different areas of endeavors, of which the accounting profession is an example, are being integrated into a harmonized system. The willingness to belong and then to compromise is an important criterion because enforcement power is one of the success tools for any harmonization process. One example is the European Community (EC). In 1981, similar economic, social, and political goals drove Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates to establish the Gulf Cooperation Council (GCC). One of the results of the efforts of GCC is the proposal for regional auditing regulations to regulate the auditing profession across these countries. When finalized, member states are required to adopt and follow the regulations. Therefore, the criterion of belonging to a regional
organization is met because the three countries are members of the same regional organization.

Subjects

This study examined the perception of two respondent groups. This study compared the perceptions of CPAs and one group of financial statement users. Financial analysts are chosen as a surrogate group for investors or creditors. The selection of these three groups of subjects was motivated by the need to obtain a general perception of two groups whose opinions are valued when establishing or setting new standards. Financial analysts are sophisticated users of financial statements. Most (1994, p.5) mentioned, “Financial analysts have become important influencers on accounting standard-setting and harmonization, both directly and through their professional associations.” CPAs’ opinions are important in this study because of their familiarity with the concept of independence and for their role in implementing the auditing standards.

In this study, the financial analysts of national commercial bank institutions in Saudi Arabia, the State of Kuwait, and the United Arab Emirates were chosen to represent financial statements’ users. Financial analysts of loan departments and investment departments were selected to be included in this study. Financial analysts from the commercial national banks were selected because of the lack of national organizations representing this group in these countries. Another reason for selecting this group of financial analysts was because they represent a well-informed and important segment of financial statement users in these countries. The reason for choosing national banks in Saudi Arabia and the State of Kuwait is because only banks with more than 50% of the capital owned by local shareholders are permitted to do business within their borders. To be consistent with respect to the remaining country, United Arab Emirates, this study limited the subjects of user groups to include only those who are working with national commercial banks.

Data Collection

Due to the physical distance of the countries included in this study, data necessary for this study was obtained using the medium of a mail survey. The questionnaire was
initially reviewed and tested in a pilot study involving Saudi Arabian academicians and auditors. A number of steps were taken to increase responses. The questionnaire included a cover letter requesting cooperation in responding to the survey and guaranteeing the anonymity of the individual and the firm. An official letter from King Saud University requesting that the respondent cooperate and answer the questionnaire was included. A space was provided for the respondent to write his or her address for a copy of the study’s results. For the CPA subject group in the three countries, a follow-up letter with a copy of the questionnaire was sent four weeks after the first attempt. The purpose of this letter was to thank them if they had already sent the questionnaire back and to ask them to ignore the attached questionnaire, or to remind the respondent to answer and send the attached questionnaire. Each questionnaire included a postage-paid return envelope.

Three trips were made to the three countries to collect the data for the two subject groups. Since the number of CPAs allowed to practice in the audit profession in each country is relatively small, this study obtained the opinion of all CPAs actively involved in external audits. For Saudi Arabia, the list of CPA practitioners came from the Saudi Organization for Certified Public Accountants (SOCPA). The list showed that there were 216 CPAs who were permitted to and were actually practicing in the area of external audits in 1995. For the State of Kuwait, the list was obtained from the Kuwaiti Accountants and Auditors Association (KAAA). The list showed 52 CPAs who were permitted to practice and are actually practicing in external audits in 1995. For United Arab Emirates the list was obtained from the Commercial Directory of United Arab Emirates for the year 1995. The list shows 102 CPAs allowed to conduct the external audit throughout the seven Emirates.

For the user groups (financial analysts) the survey instrument was carried to the targeted bank and distributed to the bank’s financial analysts including the directors of the loan departments and investment departments. The respondents had the choice of filling the questionnaire and submitting it in person or mailing it back using the self-stamped envelop provided. The goal of the visits was to see how many respondents could understand and were willing to answer the questionnaire. Because of the difficulty in accessing each individual financial analyst in each bank in the three countries, the
heads of the investment and credit department in each contacted bank were given a number of questionnaires to distribute among the financial analysts in their departments. In Saudi Arabia 110 questionnaires were distributed; in the State of Kuwait, 75 questionnaires were distributed; and in United Arab Emirates, 84 questionnaires were distributed.

**Research Instrument**

The research instrument in this study was the one used in Agacer and Doupnik’s 1991 study. The instrument involved a scaling task. Each subject was presented with seventeen scenarios, one of which was a repeated scenario. Figure 1 shows an example of a scenario. Each scenario represented one of the 16 possible combinations of two levels of the four treatment variables: client size; provision of MAS; number of months client’s fees remaining unpaid; and employment by the client of a family member of a member of the audit staff. Each subject was asked to indicate the level of risk that the auditor independence may become impaired along a numerical scale from one (very low) to nine (very high risk). Thus, the dependent variable in this study was the risk that an audit firm’s independence may become impaired. The sixteen scenarios were randomly ordered to minimize any possible bias due to order and learning effects. Figure 2 shows the two levels for each treatment.

<table>
<thead>
<tr>
<th>Scenario 1</th>
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<tbody>
<tr>
<td>Client size (as a percentage of office revenues)</td>
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<tr>
<td>MAS rendered</td>
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<tr>
<td>Number of months client’s fees remain unpaid</td>
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<tr>
<td>Relative of a member of the audit staff of the CPA firm is employed as a computer programmer by client</td>
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<tr>
<td>Risk that external auditor’s independence may become impaired:</td>
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<td>very low risk</td>
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*Figure 1. Example Scenario*

The choice of the high and low level of the treatment is based on Agacer and Doupnik’s (1991) study that states:

The choice of the 10% to indicate high level for the variable client size was based on the Accountants International Study Group’s 1976 recommendation that the auditor should refrain from accepting engagement for which the fee constitutes 10% or more of the total fee income. Choosing the low treatment level for the
same variable presented a problem in that the difference should not be too obvious as to direct the subjects into a no choice position, e.g., the choice of 1% vs. 10%. The selection of 3% appeared to offer more of a choice vis-à-vis 10% than 1%. The selection of 12 months to represent the high treatment level for the variable “number of months fees remaining unpaid” was based on the AICPA Ethics Ruling that independence may be impaired if more than one year’s fees due from a client remain unpaid (ET 191.04). Again, the choice for the low level of three months was arbitrary to provide a less clear choice than one month is against 12 months. For the variables “MAS provided” and “member of family employed by client” the use of “yes” to represent the high treatment level and “no” for the low level are obvious.

<table>
<thead>
<tr>
<th>Independent Variables</th>
<th>Treatment Levels</th>
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<tr>
<td>Client size (as a percentage of office revenues)</td>
<td>1 (low)</td>
</tr>
<tr>
<td>MAS rendered</td>
<td>3%</td>
</tr>
<tr>
<td>Number of months client’s fees remain unpaid</td>
<td>3 months</td>
</tr>
<tr>
<td>Relative of a member of the audit staff of the CPA firm is employed as a computer programmer by client</td>
<td>No</td>
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<th>2 (high)</th>
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<tr>
<td>10%</td>
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<tr>
<td>Yes</td>
<td></td>
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<tr>
<td>12 months</td>
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<td>Yes</td>
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The instrument contained full instructions. Additional information includes a hypothetical audit firm described as a national firm and a hypothetical audit firm described a having shares of stock that are publicly traded. Based on this information, each subject was asked to indicate the risk of impairment of independence in each scenario. Additional questions were included at the end of the instrument to collect demographic data about the respondents.

Before using this instrument, a pilot study was conducted involving Saudi academicians and CPAs to make sure that Agacer and Doupnik’s instrument is valid in obtaining perceptions of independence from inhabitants of that part of the world. The result showed that this instrument could be used for its purpose. Scenarios were translated into Arabic by a competent person and then translated back to English by a different person to insure that the translated measurement carried the same meaning as the English original. The questionnaire was available in two languages, Arabic and English, and the respondent had the choice of using either the English or the Arabic version of the questionnaire.
DATA ANALYSIS

The experimental design called for repeated judgment by individual subjects across the sixteen scenarios (scenario seventeen is a duplicate). The experimental design is a repeated-measure block design with one grouping factor and four trial factors (Winer, 1971, p.514-603). The grouping factor, which is defined as similar cultural and environmental factors in this study, has three levels corresponding to the three countries. The four trial factors correspond to the four treatment variables – each has two treatment levels corresponding to the levels defined implicitly in H1.1 through H2.4 and shown in Figure 1.

The research hypotheses were tested by employing Statistical Analysis System (SAS) Repeated Measures Analysis of Variance (ANOVA) under the GLM procedure. The GLM procedure uses the method of least squares to fit general linear models. The repeated measure Analysis of Variance (ANOVA) under the GLM procedure provides both the univariate and multivariate tests of significance for each of the treatment variables, the grouping variables, and each of their interactions.

The test of the two primary null hypotheses of no difference in the perception of auditor independence between professional accountants and financial analysts in Saudi Arabia, the State of Kuwait, and the United Arab Emirates is equivalent to a test of the grouping variables, similar cultural and environmental factors. Rejection of any primary null hypotheses would indicate an overall difference in scale judgment across the three countries. Tests of sub-null hypotheses 1.1 through 2.4 are equivalent to the test of interactions between the grouping variables and treatment variables indicating differences between groups in the perceived significance of treatment variables. Rejection of the stated sub-null hypotheses (H1.1 through H2.4) would indicate that the scale judgments of the subject groups differ in an absolute sense.

The coefficient alpha was used for testing the reliability of the instrument across all groups and within groups, i.e., have the variables being used captured the construct of impairment of independence and do the subjects understand them? A large alpha indicates that the k-item test correlates well with true scores. A low coefficient alpha indicates the sample of items performs poorly in capturing the construct, which motivated

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4 The pilot study was conducted while attending the seminar in Accounting Research, Spring 1994.
the measure. This study used paired means comparison to measure how consistent each subject is in his responses. This test was performed across all groups and within each group.

Responses
The response rate for the first subject group (CPAs) is shown in Table 1. Out of 216 questionnaires sent to Saudi CPAs, 93 (43% response rate) questionnaires were returned and used in the analysis. Eleven of the questionnaires were received on the second attempt. Nine questionnaires of the 216 were undelivered or returned blank. In the State of Kuwait, out of 52 questionnaires mailed, three were either undelivered or returned blank. Twenty-one were completed and returned, giving a response rate of 40%. Two of Kuwait’s returned questionnaires were received on the second attempt. For the United Arab Emirates (U.A.E.), 102 questionnaires were mailed, but seven were either undelivered or returned blank. Thirty-four were completed and returned for a response rate of 33%. Seven of U.A.E.’s returned questionnaires were received on the second attempt. Thus, data used in this study for the CPA subject group came from 148 respondents.

For the financial analysts, the response rate is shown in Table 2. The questionnaires were distributed to the financial analysts who worked with national commercial banks through the heads of either the credit or investment departments. Each bank in each country was given a number of questionnaires to be answered by the financial analysts who work in either the credit or the investment departments. The financial analysts in those banks were indirectly contacted through their department heads. Because the department heads controlled the number of questionnaires answered and returned, only two or three questionnaires out of eight or even ten questionnaires given to them were completed and returned. One justification given by some of the department heads was that those returned questionnaires represented the views of the more experienced financial analysts in the bank.

Out of 110 distributed questionnaires in Saudi Arabia, only 42 were used in the analysis, with a response rate of 38%. In the State of Kuwait, out of 75 distributed questionnaires, 20 were used in the analysis, with a response rate of 26%. In the United
Arab Emirates, 21 questionnaires, with a response rate of 25%, were used in the analysis, out of 84 distributed questionnaires.

A summary of the demographic data collected from the CPA respondents is shown in Table 3. In summary, except for the type of firm, the respondents from the three countries exhibited similarities among the demographic characteristics. A majority of the respondents across the three countries held a college degree, had more than 10 years of experience, and were between 36-45 years of age. With the exception of Saudi Arabia, the majority of the respondents from the State of Kuwait and U.A.E. held either U.S.A. or European certifications.

Table 4 summarizes the data concerning the demographic information for the Financial Analysts subject group. In summary, respondents from the three different countries possessed similar characteristics. A majority of respondents did not hold any certificate. They had undergraduate degrees or advanced degrees. Respondents from Saudi Arabia and the United Arab Emirates were between the ages of 36-45 years and had more than ten years experience. The respondents from the State of Kuwait were younger and less experienced.

Test of the Reliability of the Instrument

The reliability of the instrument used in this study was tested using Cronbach’s alpha. Results for testing the reliability were obtained using the SPSS for windows release 6.1.2. From Table 5, the test applied to all CPAs and financial analysts resulted in alpha coefficients of 0.9263 and 0.9190, respectively, indicating how well the treatment variables captured the construct of impairment of independence. The next step was to test for the reliability of the instrument in each country. The results Table 5 indicated that the alpha coefficients for Saudi Arabia, the State of Kuwait, and the United Arab Emirates were in the direction of the overall alpha.

Test of Consistency Within Subjects

To test the subjects’ response consistency, an additional scenario was included (scenario #17) in the research instrument, which was the exact replication of scenario #4. To test the null hypothesis that there is no significant difference between the means of the
two identical scenarios, a paired comparison t-test was performed with each country and across countries for the two subject groups using SPSS for windows. As shown in Table 6, the results of the t-test for all groups failed to reject the null hypotheses of no group differences between the means of the identical scenarios. Also, the results of the within country tests failed to reject the null hypotheses of no respondents’ differences for each country.

Results of Hypotheses Testing

The objective of this study was to test whether two subject groups of three countries, which were located on one region and shared similar environmental, economic, political, and cultural factors, had similar perceptions of auditor independence. The two primary hypotheses of no group differences were examined by testing for between subject effect of the grouping variable, similar cultures.

The results presented in Table 7 failed to reject the two primary null hypotheses (H1 and H2) of no group differences for the CPAs’ group, and the financial analysts’ group as it was expected that the inhabitants of similar cultures would have similar perceptions.

Thus, no significant differences between groups of countries for the two subject groups across all four treatment variables were found. This is confirmed by looking at the results for the eight sub-hypotheses (H1.1 through H2.4), which were tested by examining the interactions between the grouping variable and each of the four treatment variables. The results of the univariate tests are shown in Table 8. The probability of no interaction between grouping variables and each treatment variable is identical to the probabilities obtained under the multivariate tests as in Tables 9 and 10.

In summary, the results of the univariate and the multivariate tests conducted did not indicate any significant differences among groups for two subject groups or significant differences among the treatment variables.
SUMMARY AND CONCLUSIONS

The response rates for the total CPA subject group and the financial analysts were 40% and 30.8%, respectively. For CPA respondents, Saudi Arabia had the highest response rate of 43%, followed by the State of Kuwait at 40%, and by U.A.E. at 33%. For the financial analysts respondents, the response rates for Saudi Arabia, the State of Kuwait and U.A.E. were 38%, 26%, and 25%, respectively. The reliability of the instrument for the two groups was high, with alpha coefficients of 92.63% and 91.9% for the CPA and financial analysts groups, respectively.

The two primary null hypotheses tested in this study were that no difference in the perception of the risk of losing independence exists between CPAs (H1) and financial analysts (H2) in Saudi Arabia, the State of Kuwait, and the United Arab Emirates (U.A.E.). The results of the statistical tests conducted in this study have failed to reject the two primary null hypotheses as expected with respect to the four variables considered. The eight sub-null hypotheses related to the four treatment variables for the two subject groups all failed to be rejected at the 0.05 level, indicating that no significant differences regarding the impact each of these variables had on the perception of impairment of audit independence exist among CPAs and financial analysts in Saudi Arabia, the State of Kuwait, and U.A.E.

Thus, both the present study and Agacer and Doupnik’s study (1991) support the claim that the perception of auditor independence is sensitive to culture.

The finding of this study suggests that the process of harmonization should be and could be achieved first on a regional basis. This could lead later to harmonization involving more regions until worldwide internationalization is achieved.

In conclusion, the results of this study showed that wide agreement on concept could be achieved as a prerequisite for harmonizing auditing standards regionally. Moving the effort toward regional harmonization is needed to speed up the process of harmonization and to overcome some of the several obstacles standing in the face of harmonization. Among these are: different cultural values, different political systems, different legal systems, different languages, different accounting objectives, different religions, different levels of education, different levels of economic development, and different levels of capital markets. Other major obstacles are the lack of enforcement
power by the International Accounting Standards Committee (IASC), the lack of representation by smaller countries in both the drafting stage and the final decision stage, and the lack of recognition of different circumstances in different countries. To overcome these obstacles, this study recommends that the plan for harmonizing auditing standards should focus first on regions rather than on a country-by-country basis before worldwide harmonization can be attained. This argument is supported by the movement of establishing regional economic integration among countries in one region having similar cultural, political, and economic goals. Thus, economic integration has given the governments of member countries the power to set standards in cooperation with professional accounting groups. Consequently, enforcing the standards is made more effective through the action of the governments of member countries. The European Community (EC) exemplifies this, when all member countries automatically adopt any directive passed by the organization as law. Thus, it had been shown that harmonization is easily achieved through a regional approach. The involvement of regional professional accounting organizations will make the acceptance of international standards easier in a number of ways. First, the regional professional accounting group represents a smaller number of countries. The task of promoting understanding among member countries and sensitizing them to differences in each other’s needs is made easier because of the smaller number of countries involved. Secondly, the regional professional accounting group is able to formulate regional auditing standards that are either modified according to the needs of the member countries or are exactly similar to existing international auditing standards. Because of the involvement of the member countries’ governments and the efforts of the regional professional accounting group, successful harmonization of auditing standards in the region becomes a certainty.

Since this study has shown that Saudi Arabia, the State of Kuwait, and U.A.E. have similar perceptions of auditor independence, then international and regional CPA firms can draw up one set of rules and procedures to be followed by their staffs throughout the region without fear of impairing an auditor’s independence. Potential cost savings could be realized by having one set of rules for more than one country.

The contributions of this study are as follows: (1) it provides a framework within which factors should be used in grouping or clustering homogeneous countries; and (2) it
adds some knowledge to the international area by providing evidence as to the similarity of perception of an auditor independence within one region. Because of the above contribution, this study is able to provide guidance for the international bodies actively involved in their difficult task of harmonization.

LIMITATIONS

There are five limitations of this study. One of these limitations is of a nature that is commonly attributed to survey research methods and attitude measurement. There is always the possibility that sample subjects misunderstood the purpose of the research or misunderstood the questionnaire. However, the purpose of the research was explained and detailed instructions were provided to each subject so as to avoid any ambiguity that could have altered the results. Secondly, the results cannot be generalized beyond the three countries under examination. Thirdly, data gathered from banks (financial analysts) limits the generalizability of the results of the data to financial analysts working for national commercial banks only. Fourthly, the use of mail questionnaires in the study resulted in a lack of communication between the researcher and the user subject group. The indirect contact between the researcher and financial analysts working for national banks limited the number of questionnaires filled out and returned. As a result, the conclusions drawn from this subject group is confined to the subjects that responded. Lastly, the results of this study are limited only to the four independent variables that were used to test the perceptions of auditor independence. The selection of other auditor-client relationships could have resulted in different conclusions.
REFERENCES


