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# The relationship between audit quality and accounting conservatism in the Iraqi banks

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## Abstract

The main objective of this study is to study and measure both concepts and the impact of audit quality on the accounting conservatism. The study employed both the SPSS and STATA as tools of analysis techniques to achieve reliable results. From the number of conclusions of the study, the most important of them is that the sample selected is of high quality, but did not limit the practice of accounting conservatism, although the financial statements of the Iraqi banks listed in the Iraqi Stock Exchange (ISX).

**Keyword:** audit, quality, accounting, conservatism, banks.

# La relación entre la calidad de la auditoría y el conservadurismo contable en los bancos iraquíes

## Resumen

El objetivo principal de este estudio es estudiar y medir ambos conceptos y el impacto de la calidad de la auditoría en el conservadurismo contable. El estudio empleó tanto SPSS como STATA como herramientas de técnicas de análisis para lograr resultados confiables. De las conclusiones del estudio, la más importante de ellas es que la muestra seleccionada es de alta calidad, pero no limitó la práctica del conservadurismo contable a pesar de los estados financieros de los bancos iraquíes que cotizan en la Bolsa de Valores de Iraq (ISX).

**Palabra clave:** auditoría, calidad, contabilidad, conservadurismo, bancos.

## 1. INTRODUCTION

The formation and expansion of human societies prompted the idea of accounting and growth. The personal orientation of individuals for the purpose of profit, the emergence of private businesses, and the discovery of money after the disposal of the system of barter in business trading have all contributed to the development of accounting. Accounting has also helped in the discovery of writing and numbers which are the basis of accounting measurement and evaluation of the financial items. Then, it was the project owner who monitors all activities of transactions. External auditing appeared as a means of controlling the agent's business (management) after the start of the

separation of ownership from management and industrial revolution. This is as a result of a company to be part of what is known as the theory of the agency, which was highly concerned with the emergence of the financial markets. A set of laws that regulate and direct the work of auditors began due to the collapses suffered by companies as a result of fraudulent accounting practices. The result of the issuance of the law of foreign fraud practices of 1977 is meant to monitor the work of the auditors and ensure the extent at which the implementation of the audit work is done carefully and professionally in the early eighties of the last century. Similarly, the law increased attention to the need to implement the audit process into high quality after the scandals that lasted long globally in 2002. This has led those who are interested in the legislative aspects to put more stringent controls on corporate governance. The Sarbanes-Oxley Act of 2002 imposed the preparation of financial statements in order for the focus on the implementation of the audit of high quality of one of the requirements of entities with an interest in auditing accounts.

In the process of economic reform in all countries, the banking sector is the main pillar as this sector is important in directing the economy of a nation. There is a focus on the need to carry out an audit of high quality due to the collapses suffered by some banks in the local environment. The audit process of high quality contributes to the guidance of accounting work and in preparation of reliable financial statements in financing investments and decisions. Thus, an accounting conservatism is the practices of accounting that affect the credibility of

the financial statements and the quality of financial reporting of listed companies in the Iraqi Stock Exchange.

The following questions are asked to tackle the problem of the study:

1. Is the work of auditors in Iraqi listed banks in ISX a sample of high quality?
2. Do the Iraqi listed banks in ISX study accounting conservatism?
3. Does the quality of the audit affect the accounting conservatism in the Iraqi listed banks in ISX?

The importance of this study is realized by measuring the quality of auditing and accounting conservatism and formulating a model to measure the impact of the quality of audit in the accounting conservatism in accordance with the research problem.

The main objective of this study is to examine the quality of auditing and accounting conservatism using the most important recent studies for the measurement and the effect of the quality of auditing on accounting conservatism using the historical data included in the statements of the Iraqi banks listed in ISX to measure the effect. This study is based on this following set of assumptions:

1. The financial statements of the listed banks in ISX shall contain the sample of the research at an acceptable level of audit quality.
2. There is an acceptable level of accounting conservatism in the financial statements of the listed banks in ISX.

3. There is a significant relationship between the audit quality and the accounting conservatism in the financial statements of the banks listed in ISX.

## **2. LITERATURE REVIEW**

### **2.1. The Concept of Audit Quality and Accounting**

#### **2.1.1. Audit Quality**

In the audit profession, the quality audit is one of the most important aspects where the auditor is able to report and detect a material error while the audit process is of high quality (Mohamed & Habib, 2013; Talab et al., 2018; Talab et al., 2017). According to De Angelo (1981), audit quality is the potential of an auditor to detect and report misinterpretation and error in the financial statements of the customer's accounting system. According to Generally Accepted Auditing Standards (GAAS), the audit quality is the reasonable assurance that the audited financial statements and related disclosures are: in compliance with the Generally Accepted Accounting Principles; and free of misinterpretation due to either fraud or error (Bedard et al., 2010).

Series of accounting scandals have heightened the importance of high quality auditing at the beginning of the second millennium. These scandals concerning the legislative arms have led to strict controls of the preparation of financial statements and corporate governance. Also, bodies like the Oversight Board On the accounting of public

companies in the United States and the United Kingdom Public Control Board were established (Kleinman et al., 2014).

Audit quality is still an on-going research with a connection to so many variables and factors affecting the level of quality. Also, the extent of which audit quality impacts accounting practices to mislead the financial statements is on-going. The study of Mohamed and Habib (2013) examined how the independence of the auditor and the mandatory rotation in Egypt affect the quality of an audit. The study investigated the reasons for the mandatory rotation of the auditor; this is to know whether this change improves the audit quality or not. The study found that audit quality is improved through a mandatory change of auditors.

Tepalagul and Lin (2015) provided a comprehensive review on the most important academic research on auditor independence and audit quality. Through the study of nine leading journals, this study was conducted using published articles from 1976 to 2013. The four main dimensions such as client importance, non-audit services, auditor tenure, and client affiliation with audit that pose as threat were examined in the study. Tepalagul and Lin (2015) concluded that these four dimensions affect the quality of the audit and the independence of the auditor.

In another vein, Huang et al. (2016) examined the relationship between the specialization in the activity of the auditor and audit fees and audit quality in China. The study found that out of the fierce competition and relatively weak legal environment in China compared

to most developed countries during the year 2001 to 2011, there is a statistical significant relationship between the specialization in the activity of auditors and audit fees. The study proved that the specialization in the activity of the auditor improves the quality of the profits of customers and reduces the need for auditors to issue conservative opinions on auditing by an increment in the fees. Additionally, the study indicates that greater focus on the auditors' labor market led to increase in the audit fees and the quality of customers' profits. The result is associated with a lower probability that executives and auditors will be penalized for audit failures and found that wage increases audit quality.

The account auditors are considered by the traditional agency theory as having a monitoring mechanism to reduce the costs and lack of harmonization of incentives between shareholders and managers. The agency theory assumes that audit effectiveness depends on the independence of those who provide audit services. Hossain et al. (2016) opined that wage reliance having a negative impact on auditors and their independence and the quality of audit are concern expressed by the audit regulator.

The Public Company Accounting Oversight Board (PCAOB) rendered the impact of services for the period of 2005-2006 on tax of auditors. The services were imposed to improve audit quality and enhance the independence of the auditor by another auditor of high quality (Lennox, 2016).



Gaynor et al. (2016) found out the determinant of quality by examining the quality of the financial statements and the quality of an audit. The study found out the variables in the field of a wide range that either weaken or reinforce quality. A high quality financial statement is known to be freer of error, neutral and complete. Quality financial statement provides predictive or certain information (economic position and performance) of the economic growth. The study concluded that the implementation of high quality auditing provides a higher level of assurance and that the financial statements faithfully represent the economic performance of economic growth as auditors obtain sufficient evidence.

Furthermore, Li et al. (2017) evaluated the relationship between auditors' failure and audit quality in China. The identity of the auditors is revealed in the audit report, while the study found that the observer of the accounts that perform low quality audit also perform failed audits.

Gul et al. (2017) used a sample from public companies listed in the Chinese market for the years 2000-2009 to study an emerging market on the quality of audit. The study found that the quality of the audit is related to the size of the customers of the audit company, i.e. the lower the audit quality, the more their number. As the audit of multiple clients dispel the efforts of audit partners, the audit quality is reduced which indicates that these results contributes to better understanding of the behavior of audit firms in emerging markets.

### 2.1.2. Interested Parties in Auditing Quality

The audit profession was greatly affected by the corporate scandals and the resulting bankruptcy of 565 companies from 2000-2008. This bankruptcy has led to a high level of uncertainty about the quality of audit statements (Feldmann & Read, 2010). How to improve measure and monitor audit quality indicators on a routine basis were examined by organizers of audit firms and academic researchers. Development of quality audit indicators and their usefulness to stakeholders are discussed by a panel of groups of participants at a seminar hosted by the Audit Quality Centre in 2012. The seminar also comprises how academic research can contribute to the development and use of quality audit indicators by stakeholders. According to Martin (2013), the seminar concluded that there is a set of indicators for audit quality as listed below:

1. Audit Firms: From an audit point of view, the quality of audit is managed as a continuous process and as an identification of important issues that affect audit performance. Also, it is referred to as analysing conditions, monitoring and enhancing performance through the collection of data and identifying the causes of issues that indicate quality audit.
2. Audit Committees: Due to the audit committee's oversight of internal and external controls and the resistance of the pressures and interventions of management on the control process, it plays a vital role in ensuring the quality of financial reports and achieving confidence in accounting information. From the information published in the financial statements, the role of the

audit committees in increasing confidence in information shows that companies with audit committees have decreased the rate of occurrence of illegal financial transactions and confidence in financial statements' information is increased regarding companies listed on the stock market (AL-Timemi & Flayyih, 2015).

3. Investors and Creditors: The users of the financial statements (both investors and creditors) are interested in the indicators related to the evaluation of that quality and in the quality of the audit.

4. Regulators: How to assess the audit quality and the explicit role of auditing standards in developing quality expectations should be considered by the regulators also responding to the deficiencies in the audit process, and how to apply auditing standards.

5. Management: Obviously, the management of the economic unit ensures the preparation of high quality financial statements, and conduct audits efficiently as possible because there is essential interest in the quality of audit.

### 2.1.3. Miller Ratio to Measure Audit Quality

There are many indicators that may be useful in the assessment of auditing in spite the difficulties inherent in determining audit quality (Bedard et al., 2010). Due to the difference and the multiplicity of the beneficiaries of the services of the auditors and the lack of indicators to measure the quality of the audit directly, the process of determining the

level of quality of auditing is difficult. Nevertheless, several indicators can be used to measure the quality of the audit.

The quality of the audit is measured by the Miller Ratio model as it was previously used to measure profit management practices. The model predicts the ratio of the change in working capital as an exposed element to the manipulation and cash flow of operational activities as a non-manipulative element (Al-Daour, 2013). The percentage realized in the calculation is used to detect the manipulation of profits. There is no manipulation regardless of whether the result is negative or positive, if a percentage of the value is smaller than zero. The manipulation of the amount of profits indicates that the value is more than zero. Since the quality of the audit is linked to have a negative relationship with the profit management, it can be used as a measure of the quality of the audit. If the value is zero, it indicates a high implementation of audit quality, but if the value is different from zero or the value is 1 or larger, it means audit process is of high quality and the financial statements are not free of profit management. This indicates that there is a manipulation of profits prepared according to the accrual basis.

Due to the large and extensive data needed by the previous models in the measurement process, the Miller 2007 model differs from the previous models on profit management. The Miller model can be used if the data is annual or interim and does not require large data (Miller, 2009). The Miller Quality Audit Model is presented below:

$$\text{Miller Ratio} = (\text{WC}_n - \text{WC}_{n-1}) / \text{CFO}$$

Where:

WCn = Change in net working capital

CFO = Cash flow from operating activities

#### 2.1.4. The Concept of Accounting Conservatism

Traditionally, the concept of conservatism is: "not to expect profits, but to anticipate all losses" (Basu, 1997, 12). This rule according to Basu (1997) is interpreted as the tendency of accountants to demand a higher degree of verification until good news is recognized as a gain against recognition of bad news. This is mentioned in the second statement of the Financial Accounting Standards Board in 1980 when addressing the concepts of financial accounting in paragraph 95. The concept reveals that: if there are estimates of received or paid amounts that are likely to be settled in the future, the conservatism tends to use the higher estimate (Basu, 1997).

Moreover, conservatism is an accounting practice that is inculcated in order to include uncertainty and risk inherent in business conditions. In accounting information, custody is an attribute often cited. There are several values that represent alternatives in the evaluation, in many situations related to asset evaluation and income determination. Therefore, the value of the elements of the assets does not increase in the statement of financial position (Al-Ani & Flayyih, 2018). Accounting conservatism is the most influential principle in the assessment process in accounting (Schroeder et al., 2009).

Furthermore, accounting conservatism reduces the amount of equity over market value from time to time. This is a criterion for choosing between accounting principles that leads to the reduction of reported cumulative profits and the immediate recognition of expenses, through late recognition of revenue. The reporting of the higher values of liabilities and expenses is termed accounting hedge. This is also referred to as accelerating recognition of expenses and postponing recognition of revenues. It is therefore preferable to evaluate assets at lower values and to calculate the income that leads to less value in the available group (Al-Najjar, 2014).

In another vein, an accounting conservatism is an exceptional principle that acts as a limitation on the presentation of appropriate accounting information. Preference is given to what will have the least positive effect on the rights of the shareholders when a choice is made between two or more accounting methods. Belkaoui (2004) stated that the accounting conservatism means reporting assets on the value of liabilities and higher expenses. Al-taie et al. (2017) added that accounting conservatism shows the highest value among the liability and expense values and the least of a set of potential values of assets and revenues.

It remains one of the most important accounting principles that accountants are still insisting on applying despite the criticisms of the tools of accounting conservatism. Accounting conservatism has become increasingly important over time as stated by convincing evidences from the previous studies (Hamdan et al., 2012). Accounting conservatism and other parties involved in the financial reporting

process, after the collapse of the early twenty-first century to a large number of companies in the world resulted in heavy losses, which was due to opportunistic practices of the management of these companies (Al-Kaabi, 2015).

According to Hamdan et al. (2012), the accounting conservatism directs the economic unit to recognize "bad news" faster than "good news". Al-taie et al. (2017) classified conservatism into two types: the conditional conservatism where a bad news is recognized immediately in comparison with good news; and the unconditional accounting conservatism which represents a decline amount of equity over market value.

From all the large number of models used in measuring the accounting conservatism, the model provided by Basu 1997 is one of the most used models in accounting measurement. The following regression equation was used by Basu (1997):

$$X_{it}/P_{it1} = \alpha_0 + \alpha_1 DR_{it} + \beta_0 R_{it} + \beta_1 R_{it} DR_{it}$$

Where:

$X_{it}$ : Earnings per share for Company  $i$  for the period  $t$ .

$P_{it1}$ : The shares price of Company  $i$  at the beginning of the period  $t$ .

$DR_{it}$ : A dummy variable equal to 1 if  $R_{it}$  is less than zero and equal to zero if  $R_{it}$  is greater than zero.

$R_{it}$ : The market yield of the company  $i$  for the period  $t$ .

Basu (1997) employed the model to conclude that, the conservatism leads to the expectation of profits (the good news) and will be postponed until they are realized while the negative changes reported the profits. Similarly, the conservatism reflects the results of profits "bad news" faster than the "good news" which involves in methodological differences between the extended bad news and good news.

## **2.2. Effect of Audit Quality on Accounting Conservatism**

Goh and Li (2011) studied the impact of the internal control system and accounting conservatism practices. The study found that a high quality of internal control system led to a decline in accounting practice. This is in contrast to companies that have weaknesses in the internal control system.

Hamdan et al. (2012) studied industrial companies listed on the Amman Stock Exchange with the aim to verify the existence of an accounting conservatism in the financial statements of the companies. The main aim of the study is to examine the impact of audit quality characteristics (such as: size of the audit firm, the period of the customer retention, audit fees and specialization in the field of activity) in enhancing the level of accounting conservatism of 39 selected companies for the period of 2001-2006. The study found that the level of accounting conservatism in the financial statements issued by the Jordanian industrial companies is less than the selected sample and



audit quality improves the level of the accounting conservatism (Hamdan et al., 2012).

Using a sample of 494 Australian companies, Sultana and Mitchell (2015) examined the impact of the audit committees on the accounting conservatism. The study found that the financial expertise of the audit committees affects the accounting conservatism (Sultana & Mitchell, 2015). Survey form that was distributed to the auditors working in the Iraqi audit offices was used to measure the quality of the audit while the level of the accounting conservatism was equally measured. In other words, for the sample using the model of BTM and Basu, the study found that there is a significant relationship between some of the quality characteristics of the audit (such as specialization in the customer's industry, the experience of the auditor) and the accounting conservatism (Al-Kaabi, 2015). Thus, the main contribution of this study is to quantify the audit quality quantitatively through the Miller ratio index and then measure the impact of audit quality on accounting conservatism.

### **3. METHODOLOGY**

#### **3.1. Sample of the population**

The population of the study consists of ten banks listed on the Iraqi stock exchange.

### **3.2. Scope of the study**

The time frame for the study of the financial statements was for the period of 2008 to 2014 while the selected sample is ten Iraqi banks listed in ISX. The study was based on the inductive method by selecting a sample of 10 banks from the existing 94 companies listed in ISX.

## **4. RESULT ANALYSIS**

### **4.1. The quality of audit in the selected banks**

A total number of ten Iraqi banks listed on the Iraqi stock market were selected for the period of 2008 to 2014, and Table 1 below shows the level of audit quality according to the Miller index.

Table 1: Measurement of the level of audit quality

Sample	Percent	Frequency	Std. Deviation	Mean
Statements that are quality	81.4%	57	0.39	1.81
Statements which are not quality	18.6%	13		
N	100%	70		

It is clear from table 1 that the quality statement of 57 banks were 81.4%, while the banks' non-quality bank statements (13) were (18.6%) with mean (1.81) (1.5) and a standard deviation of (0.39). The

percentage of banks whose statements are of audit quality and banks with no audit quality is shown in diagram 1.

Diagram 1: the Statements that are quality and which are not quality

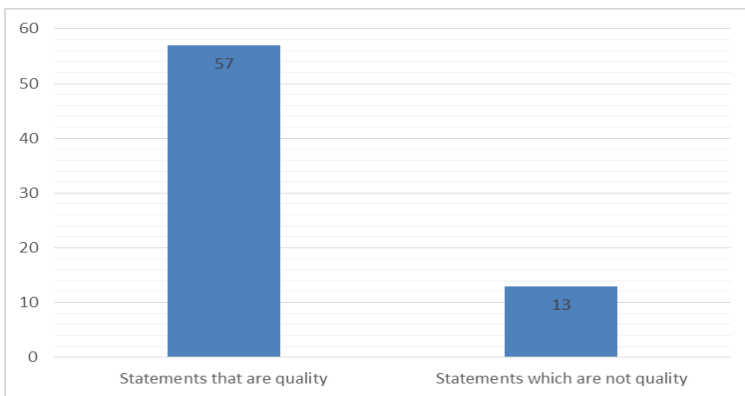
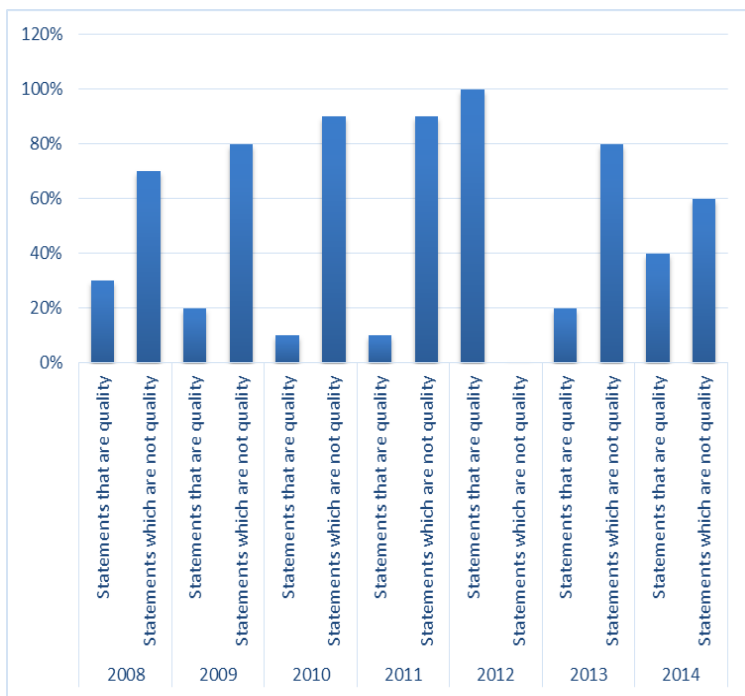


Table 2: Audit Quality Level for the period of 2008 to 2014

Years	Quality	Frequency	Percent	Std. Deviation	Mean
2008	Statements that are quality	3	%30	0.48	1.7
	Statements which are not quality	7	%70		
2009	Statements that are quality	2	%20	0.42	1.8
	Statements which are not quality	8	%80		
2010	Statements that are quality	1	%10	0.31	1.9
	Statements which are not quality	9	%90		
2011	Statements that are quality	1	%10	0.31	1.9
	Statements which are not quality	9	%90		
2012	Statements that are quality	10	%100	0	2
	Statements which are not quality	0	%0		
2013	Statements that are quality	2	%20	0.42	1.8
	Statements which are not quality	8	%80		
2014	Statements that are quality	4	%40	0.51	1.6
	Statements which are not quality	6	%60		

The table 2 above shows that highest percentages of companies implement the audit quality and the arithmetic mean is higher than the satisfactory mean of 1.5 is reached for most of the result. Also, it shows that 2012 achieved the highest percentage in the implementation of audit quality while the year 2014 achieved the lowest level of quality of 40% during the period of the study in the statements that are not quality and 60% in the statements of quality. 1.6 is the arithmetic mean which is higher than the satisfactory medium of 1.5 while the standard deviation is 0.51. The diagram 2 below shows the level of audit quality of the selected banks.

Diagram 2: the level of audit quality of the selected banks



#### 4.2. The Level of the Accounting Conservatism in the Banks

The level of custody in the financial statements of the banks listed in ISX was measured by the Basu model for the fiscal year 2008 to 2014. This model is based on the amounts present in information related to shares, market values, profitability and prices and the statement of income statement at the beginning. Observations up to 70 were made and analysed through SPSS to investigate whether there is conservatism or not in the selected banks. Table 3 below presents the statistical results of the model variables.

Table 3: Statistical Results of  $\beta$  coefficients of independent variables in the Basu model

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	0.121	0.027		4.438	0.000
$\beta_1$ Rit	-0.039	0.054	-0.186	-0.713	0.478
DRit	-0.057	0.037	-0.218	-1.541	0.128
RitXDRit	0.063	0.066	0.238	0.963	0.339

(Prepared by researchers based on SPSS statistical results)

From the table 3, the coefficient of  $\beta_1$  with the value -0.039 represents the response of the profits to the positive returns while the coefficient  $\beta_2$  shows -0.057. As this result is negative, it shows that regardless of good news or bad in the practice of accounting conservatism, the banks listed in ISX exercise accounting conservatism in the preparation of their financial statements. The coefficient ( $\beta_3$ )

with the value (0.063) indicates a positive response of profits to negative returns in the accounting of the financial statements of the selected banks. The value of the coefficient of ( $\beta_1$ ) also indicates a high level of accounting conservatism in the financial statements of the selected banks.

### **4.3. A Model for measuring the impact of the audit quality in the accounting conservatism**

A mathematical model was constructed for the purpose of measuring the effect of audit quality in accounting conservatism. The model represents the assumed relationship between the quality of the audit as an independent variable and the accounting conservatism as a dependent variable. A set of variables was therefore used to determine the relationship between the variables.

**Design Model of the Study:** The objective of this model is to measure the effect of audit quality on the accounting conservatism in a sample of Iraqi banks listed in ISX for the year 2008 to 2015.

**Method of Measuring the Variables:** The variables of the study will be measured as follows: The independent variable (explanatory) which is the quality of the audit is represented by a percentage while the accounting conservatism which is the dependent variable is measured using dimensions of the model as illustrated in table 4.

**Table (4) Methods of measuring study variables**

Variables		Model	Measurement
Dependent variable	Accounting conservatism	Basu	$X_{it}/P_{it} = \alpha_0 + \alpha_1 DR_{it} + \beta_0 Rit + \beta_1 RitDR_{it}$
Independent variable	Audit quality	Miller Ratio	Miller Ratio = $(WC_n - WC_{n-1}) / CFO$ A dummy variable give 1 if the company have audit quality, 0 for otherwise

#### 4.4. The model of the study

To evaluate the effect of audit quality in applying the accounting limitation, the model (Basu) was used to denote accounting conservatism practices. The model used is as follows:

$$y = \alpha_0 + \alpha_1 x_1 + \beta_0 x_2 + \beta_1 x_3 + \beta_2 MR + e$$

Where:

$X_{it}/P_{it}$  is the dependent variable representing the accounting conservatism measured under the Basu model in year, t.

The constant value is represented by  $e$  while  $\beta$  is the coefficient of the independent variable and control variables,  $i$  per year,  $t$ . ( $I$ ) in year ( $t$ ), which is a Dummy Variable whose value is (1) if the quality of the check is (0) the opposite.

The accounting conservatism is the dependent variable that accompanies the independent variable as its outcome is not specified and depends on the values of the independent variable. The multiple regression of the measurement of the variables consists of segmented data of time series and a group of companies at the same time. On the

other hand, the STATA program was used to address the possibility of non-distribution of natural data. Table 5 below shows the results of multiple regression tests of the hypotheses.

Table 5: Results of the regression model test

variables	B	F	R Square	R	Sig.
X1	-0.041	1.05	0.046	0.21	0.37
X2	-0.041				
X3	0.066				

Prepared by the researchers based on the results of the statistical program (STATA).

From the table 5 above, the calculated F-value of the model is 1.05; this is smaller than the tabular value of 4.19 at the 0.05 level of significance. This shows that in accounting conservatism, there is no significant effect statistically at the significant level of 5% with confidence level of 95%. From the coefficient of determination, the value of R square, 0.046 indicates that independent variable (audit quality) accounted for 4.6% of the changes in the adopted variable of the accounting conservatism while the remaining 95.6% is due to the contribution of other variables that were included in the regression model not addressed by the study. The value of P value (0.37) indicates that the coefficient of the regression model does not confirm the result of the estimation of the regression coefficient; thus, it is not fully significant and statistically significant as it is greater than the standard level of 0.05 for accounting conservatism. The value of correlation (0.21) between the dimensions of the independent variable shows that there is a weak correlation between these dimensions.



The coefficients of the slope angles of  $\beta_1$ ,  $\beta_2$  and  $\beta_3$  with values -0.041, -0.041 and 0.066 respectively shows that any increase in the quality of the audit in one unit will increase the level of the calculated conservatism variable by 4.1 % for  $\beta_1$  and  $\beta_2$  and by 6.6% for  $\beta_3$ .

#### **4.5. Proof of research hypotheses**

The result revealed that financial statements are characterized by the quality of the companies. Thus, the first hypothesis is accepted as:

"The financial statements of banks listed on ISX shall be the sample of the study at an acceptable level of audit quality".

The Basu scale depends on the extent of the profitability of the negative returns (bad news) of  $3\beta$  as compared to the profits of the positive returns (the good news) of  $1\beta$ . The ratio of the appropriate coefficient of profits for the bad news  $3\beta$  was two times greater than  $1\beta$ . This indicates that the selected banks are affected by positive news at a rate less than the bad news. Conversely, this study finds that 39.3% of the banks listed in ISX are influenced by positive news rather than bad news. This indicates the acceptance of the second hypothesis which states that:

"There is high acceptable level of accounting conservatism in the financial statements of selected banks listed in ISX".

The results obtained from estimating the regression coefficient are rejected by the third hypothesis despite the acceptance of the first and second hypotheses are proven; the hypothesis states that:

"There is a significant relationship between the quality of audit and accounting conservatism in the financial statements of banks listed in ISX".

## **5. CONCLUSION AND RECOMMENDATION**

### **5.1. Conclusion**

This study draws the following set of conclusions in accordance with the information that has been found:

1. The financial statements of the Iraqi banks listed in ISX are characterized by a high quality of the sample selected as shown by the Miller Index Ratio that 81% of the statements of these banks are of high quality.
2. Although the financial statements of the Iraqi banks listed in ISX are of high quality, they did not limit the practice of accounting conservatism. The selected Iraqi banks listed in ISX as the sample of the study practice accounting conservatism when preparing financial statements.
3. The results of the accounting conservatism for the Iraqi banks listed in ISX were greater for the bad news compared to the good news, when preparing the financial statements. This

implies that the selected banks for the study are affected by the bad news than the good news.

## **5.2. Recommendation**

This study recommends the following in accordance with the conclusion reached:

1. There is a need for further research and in-depth studies on the quality of auditing to enhance the credibility of financial statements.
2. There is a need to integrate the supervisory body of companies in ISX and the board of accounting and control standards, the board of the profession of control and auditing accountants and auditors for the issuance of accounting rules and audit evidence in order to reduce the negative effects caused by poor accounting practices related to the conservatism. The provision of means to limit such practices is a necessity to reduce the negative impact on the quality of financial reporting in financial statements.
3. Companies listed on ISX should be encouraged to practise the accounting conservatism in such a way that the positive aspect of the practice is directed by reporting good news when preparing the financial statements.

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