QUALITY OF BANK AUDIT IN BANGLADESH AND RELATIONSHIP BETWEEN AUDIT QUALITY AND SHARE PRICE

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ABSTRACT

Fifty-six scheduled banks are operating in Bangladesh and among them only thirty banks are listed in Dhaka Stock Exchange (DSE). This study examines the audit quality of thirty listed banks and determines whether there is any relationship between audit quality and share price. Here the term audit quality refers to the auditor’s ability to discover breach in client’s financial statements and report that breach, and share price represents the value of company’s future earnings. Since investors have vital interest in companies’ financial statements and audit provides a reasonable assurance about the quality of the financial statements, audit quality can intensely influence share price. The audited financial statements of thirty listed banks and their share prices have considered for this study. Results have shown that three listed banks have poor audit quality in the year 2013. The share prices of these banks are relatively low compared to the other banks. Results of this study are dependent on the loan, advances and investment, and share price data. This study will give the idea about the audit quality of thirty listed banks within Bangladesh. Additionally, it will also provide the knowledge about the relationship between audit quality and share price.

Keywords: Listed banks in Dhaka Stock Exchange, Loan classification, Loan provision, Auditor independence, Auditor ethics, Audit quality, Share price

1. Introduction

Banks play significant role in the economy. They hold public savings and finance businesses. In order to gain efficiency, banks need to get larger, and becoming a public company is one way to achieve that. Among the fifty-six scheduled banks, thirty banks are public company. To become a public company, banks need to issue IPO and then trading goes to the secondary market. Once trading starts, share prices are largely depend on supply and demand. Demand of a particular share is generally depend on the investors’ confidence. Investor’s confidence mostly depends on the financial performance of the banks. Moreover, financial statements must have to be certified by an auditor. According to Levitt, (1998) audit quality is recognized to influence financial reporting and have an impact on investors’ confidence.

Banking sector is largely dependent on the loans, advances and investments. The loan recovery rate is relatively poor in Bangladesh.
For this reason, Bangladesh Bank introduced loan classification and loan provisioning. Every bank is required to classify their loans according to the loan performance and maintain loan provisioning according to the loan classification, but some banks do not do proper loan provisioning. Therefore, these wrongdoings cast doubt upon the credibility of the financial statements of this sector. In this case, proper audit can restore the credibility in this sector and that may elevated investors’ confidence. The objective of this study is to evaluate the audit quality, determine the relationship between the audit quality and share price.

2. Statement of the problem
Audit quality is one of the most important parameter that can strongly influence share price by impelling investors. The value of company’s share depends on the company’s earnings, however sometimes company’s managers manipulate the earnings report to match a predetermined target. In an ideal scenario, an appropriate audit can effectively constrain the earnings misrepresentation and financial statement manipulations.

In idyllic situation, auditors are independent in appearance and they are independence of mind. Moreover, they uphold ethics while they are doing audit. Moreover, investors take investment decision upon the audited financial statements.

In Bangladesh, auditor’s independence and ethics are not properly maintained. This is because; the size of the market for audit services in Bangladesh constrains the bargaining power of the audit firms and thus affects the quality of audits. The total number of companies listed on the DSE is 307. These listed companies are shared among around 180 audit firms suggesting that the competition for clients is intense. Thus, auditors in Bangladesh are to be expected to face greater financial inducements to comply with client reporting practices. Since the market size for audit service is small, the cost of breaching independence and not upholding their ethics may be lower than the economic benefits extracted from client fee revenue. For this reason, sometimes auditors do involve in transgressions and that may affect the investor’s decisions.

The purpose of this study is “To evaluate audit quality (auditor independence, auditor ethics) and identify whether there is any concerning relationship between audit quality and share price.”

3. Literature Review
3.1 Auditor Independence
According to the IESBA (International Ethics Standards Board for Accountants) code, independence contains:

(a) Independence of mind
Mind considered as independent when auditor express a conclusion without being affected by any influences so that auditor can exercise objectivity and professional skepticism.

(b) Independence in appearance: Independence in appearance refers that third party consider auditors as independent.

According to Magill and Previts (1991), auditor’s independence is an attribute that increases the trustworthiness. Knapp (1985) define auditor independence as the ability to resist client pressure.

Generally Accepted Auditing Standards (GAAS) states that independence in mental attitude must be maintained in all matters relating to the assignment by an auditor. SEC considers that if reasonable investors, who have knowledge of all appropriate circumstances and facts, would conclude that auditor is not exercising objective and
impartial judgment then an auditor is not independent (SEC 2000, p.3). Auditor independence provides assurance that an impartial and skilled professional examines financial statements (SEC 2000, p. 2). Elliot and Jacobson (1998) added that this assurance enhances credibility to financial statements, adding significant value to the entire capital markets system. According to Kinney (1999), legislation and regulation can ensure auditor independence. Overall, the independence of auditors increases the creditability of audit report.

The ownership of direct or indirect material investment in a client firm can affect the auditor’s independence in appearance (Elder, R.J., Arens, A.A. and Beasley, M.S. 2008). Therefore, SEC imposed some regulation to maintain auditor independence. In 2003, SEC enforced Sarbanes Oxley Act (SOX) that bans the auditors to have direct or indirect relationship with the client. Moreover, it also bans some services such as consulting services (Elder et al., 2008). There are some unconscious biases which hinders the auditor independence such as excessive familiarity, long-term attachment with the client (Barret, 2001; Umar and Anandarajan, 2004; Ainsworth, 2006). Some discounting factor like damage relationship between the auditors and client’s management might affect the auditor’s current judgment that affects auditor’s independence of mind.

According to agency theory, the management of organizations may not present full and fair financial information to the external users. For this reason, independence is required. An audit report provided by the external independent auditors increase the creditability of audit report so that users can rely on the information presented.

3.2 Relationship between Auditor Independence and Audit Quality

Auditor independence is one of the pillars of audit quality (Beattie V, Fearnley S, Brandt R, 2001). Richards (2006) states that audit quality will get lower when auditor independence is lower. Baotham (2009) suggested that audit quality is significantly influenced by auditor’s independence. Srinivasan K, Zhou J, Zhou N (2002) tested the effects of auditor’s independence in audit quality by testing a sample of several Anderson’s clients. The result showed that auditor independence not only affects the audit quality but also affects the credibility of the audited financial reports. Pike (2003) also claimed that when the auditor is not independent, the determination to produce high quality audit becomes low since the auditor does not make a serious attempt to detect material misstatement in the financial statements and when it is identified, the auditor will not necessarily report it.

Kim, J., Song, B.Y. and Tsui, J. (2007) states that long-term attachments whether financial or psychological, may affect the auditor independence, and this may deteriorate the audit quality because it might hinder the auditor from carrying out his/her duty to detect material misstatements in client financial report and report them.

3.3 Auditor Ethics

According to Hosmer (1994, p. 20), ethical principles vary with cultural, social, and economic conditions. Rather than subjective statements, they are objective statements that excel countries, religions, and times. David Satava, Cam Caldwell, Linda Richards (2006) suggested that auditors duties are based on ethical principles, which do not to change irrespective of the company involved or any financial benefits to forgo their duties. Moreover, they are committed to honor duties to the societies to the society that involve the prosperity of all stakeholders. According to Bartels, L., Harrick, E., Marel
E., & Strickland, D. (1998), ethical issues come under into consideration once two criteria are met: volition and consequences. First, an auditor must have a choice when he/she dealing with the ethical issues. Secondly, there must have consequences for his/her choice.

Windsor (1996) suggested three types of auditor. Three types are self-governing, pragmatic and accommodating. Windsor use Kohlberg’s theory as the ground to make these divisions. Kohlberg’s proposes three broad levels of superiority in ethical reasoning. The first one is pre-conventional level. Here, self-interest influences the decision. The second is called conventional level. In this level, individuals rely upon rules and regulations to determine the right from wrong. Post-conventional is the third level. On this level individual decides right from wrong using universal ethical principles such as justice and fairness. Willingham and Carmichael (1968) described ethics as the written code of relational norms, which guides the range of appropriate behavior in various situations. The codes guides the proper ways of relating to clients, the public, superiors or subordinates.

According to Miller and Bahnson (2004) auditors are responsible to protect the investors but many auditors fail to do their job, and then the objectivity of the auditor and the accuracy of the client’s financial statements are immediately suspected. Sometimes auditors involved in unethical activities because of their economic dependence, since they are hired and fired by their own clients (Moore, D. A., Tetlock, P. E., Tanlu, L. and Bazerman, M. H., 2006).

Ethics in auditing is very necessary for doing audit in banking sector. People do consider banks as a system of wealth creation. Auditor should maintain ethical principles while they are auditing. There are number of issues which auditor should judge ethically such as loan collection rate from the debtors, loan provision etc.

3.4 Relationship between Auditor Ethics and Audit Quality

According to Dedoulis (2006) audit ethics includes a set of rules and principles intended to exclude undesirable activities in the audit work. It refers to the public interest, integrity and audit quality. Auditor, who has greater audit ethics, inclines to better protect public interest and increase the audit quality. It is difficult to reclaim a reputation of creditability in the public eye. Thus audit ethics reassures auditors to concern with audit morality in the audit process and gain audit quality. According to Schwartz (2002), audit ethics includes trustworthiness, respect, responsibility, fairness, caring, and citizenship. Therefore, it is positively related to and audit quality.

3.5 Audit Quality

Audit quality has been defined as outcome on the existence of certain qualities of auditors. DeAngelo (1981) defines audit quality as the auditor’s ability to discover the breach in client’s financial statements and report that breach. This definition refers the two components of audit quality: the probability that an auditor discovers existing misstatements and appropriately acts on the discovery. The first component refers to the auditor’s competence to detect the misstatements in the financial statements and the second component refers to the auditor’s independence, skepticism and ethics. These two components actually suggest that audit quality can be influenced by different aspects of the audit. The discovery of misstatements requires proper resources and those resources be effectively used in the audit process. Additionally, auditor needs to take proper action at the end of audit report.
Government Accountability Office (GAO 2003, 13) defines audit quality as auditor perform auditing compliant with Generally Accepted Auditing Standards (GAAS) to provide reasonable assurance that audited financial statements are not materially misstated and financial statements are prepared in accordance with Generally Accepted Accounting Principles (GAAP). Carcello (2002) indicate that audit quality is directly linked to the amount of audit work.

Casterella, J. R., K. L. Jensen, and W. R. Knechel. (2009) stated poor audit quality as they believe poor audit quality is observable with reflection if there is any litigation or claim for malpractice against the audit firm.

U.K.’s Financial Reporting Council (FRC) (2008) identified five drivers for audit quality. They are: (1) the culture within an audit firm; (2) personal attributes and skills of audit staff and audit partners; (3) the usefulness and reliability of audit reporting; (4) the effectiveness of the audit process; and (5) factors affecting audit quality outside the control of auditors

Francis (2011) proposed another framework based on a structural view of the audit environment. Francis (2011) argues that six levels of analysis influence audit quality. They are: (1) audit inputs, (2) audit processes, (3) audit industry and audit markets, (4) accounting firms, (5) institutions, and (6) economic significances of audit outcomes.

The various frameworks for audit quality highlight that both theoretical and practical perspective the evaluation of audit quality is a multidimensional challenge. According to Palmrose (1988) actual audit quality can be measured by litigation activities. Krishnan & Schauer’s (2000) measured audit quality based on how audited financial statements comply with the Generally Accepted Accounting Principles. According to Krishnan and Schauer (2001), material deviation from the standards reflects poor audit quality. This study measures audit quality by examining that whether thirty listed banks have deviated from the standards that are set by Bangladesh Bank.

3.6 Relationship between Audit Quality and Share Price

Lev (1989) stated that the value of company’s share represent the value of its future earnings. Therefore, it explains that why investors have vital interest in companies earnings report. Subsequently, to match predetermined target company managers use certain kinds of strategies to manipulate their earnings that help to attain smooth income, triumph high earnings level and power the company’s stock price (Schipper, 1989; Healy & Wahlen, 1999). Audit provides shareholders and potential shareholders reasonable assurance that management’s financial statements are free from material misstatements (Watts & Zimmerman, 1986). Audit quality can influence the quality of reported earnings by effectively constraining earnings misrepresentation and financial statement manipulation (Badawi, 2008; Enofe, 2010). Since, investing decision on stocks heavily relied on audited financial statements; investors depend on auditors to confirm the accuracy and completeness of financial information (kane, 2004). According to Levitt, (1998) audit quality is recognized to influence financial reporting and strongly impact on investors’ confidence. Eventually that affects the share price. Some prior studies (Teoh & Wong, 1993; Heninger, 2001, Balsam, Krishnan & Yang, 2003) have attempted to establish a distinct relationship between audit quality and share prices of a company.

3.7 Share Price
Share price is the price of a single saleable share of a company. Generally, when a company wants to raise capital, going public is one way to raise capital. Here, company needs to issue IPO (initial public offering). After issuing IPO, trading goes to the secondary market. Once trading starts, share prices are largely depend on the supply and demand. Some issues like long-term earning potential, good audit quality, favorable news may attract more buyers, and sooner or later it will increase the share price. On the contrary, a company with poor financial performance, poor audit quality may lessen the shareholder’s confidence, which will induce more shareholders to sell shares. As a result, supply of the share will rise and demand will fall. Ultimately, share price will fall.

Figure 1: Conceptual framework

4. Research Questions
Q1: Is there any relationship between auditor independence and audit quality?
Q2: Is there any relationship between auditor ethics and audit quality?
Q3: Is there any relationship between audit quality and share price?

5. Research Hypotheses
H_{01}: There is no relationship between auditor independence and audit quality
H_{a1}: There is a relationship between auditor independence and audit quality
H_{02}: There is no relationship between auditor ethics and audit quality
H_{a2}: There is a relationship between auditor ethics and audit quality
H_{03}: There is no relationship between audit quality and share price
H_{a3}: There is a relationship between audit quality and share price

6. Methodology
The main purpose of my data collection is to assess the impact of auditor ethics and auditor independence on share price. I used secondary source to collect my data. I collected data from annual reports, journals and websites. I collected audit report, loan outstanding and loan provision data from annual reports of the year 2013, and share price of listed banks from DSE website. I used audit report, loan outstanding and loan provision data to measure the audit quality. Afterwards, I used share price data to determine whether there is a relationship between audit quality and share price.

7. Research Design
Research can be designed in seven categories. These are given below:
i. The Method of Data Collection: I used monitoring method to collect data. This is because I inspected bank’s annual report and DSE website without attempting to elicit response from anyone.

ii. Researcher Control of variables: In this research, I have no control over the variables. I actually report what is happening. So this research is considered as ex post facto design.

iii. Degree of Research Question Crystallization: Between Exploratory Studies and Formal Study, my research design could be categorized as Formal Study. This is because the purpose of my research is not to develop any hypothesis or question for the further future research. The goal of my research is to test the hypothesis.

iv. The Purpose of Study: The purpose of the study is categorized as Descriptive. In this research, I am trying to measure the effect of audit quality on share price.

v. The Time Dimension: Time dimension is categorized as Cross-Sectional Study. Cross-Sectional Study is carried out once and represented a snapshot of one point in time, which is very much similar to my research. I have used 2013 year’s data to do this research.

vi. The Topical Scope: The topical scope for my research is statistical study because I use statistical data to test my hypotheses.

vii. The Research Environment: Among Field Setting, Laboratory Research and Stimulation; my research environment is specified as Field Settings. This is because; I conduct the survey within an original environment.

8. Sampling

Sampling is the act, process, or technique of selecting a representative part of a population for determining parameters or characteristics of the whole population. For doing this research, I have selected thirty listed banks among the 307 listed companies of DSE.

I used non-probability sampling procedure because I did not randomly select my sample. In non-probability sampling, I followed purposive sampling procedure. This is because; I selected thirty listed banks for their unique characteristics.

9. Data Analysis and Findings

In banking sector there is lack of transparency in loan sanction and repayment process. Bangladesh is trying to maintain their banking regulation and accounting standards to the international standard. In 1989, Bangladesh Bank introduced loan classification and loan provision with a view to attain international standard. From 1 January 1999, revised policy for loan classification and provision was introduced. Bangladesh Bank classified loan as unclassified, substandard, doubtful and bad.

<table>
<thead>
<tr>
<th>Classification</th>
<th>Rate of provision %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unclassified</td>
<td>1</td>
</tr>
<tr>
<td>Sub-standard</td>
<td>20</td>
</tr>
<tr>
<td>Doubtful</td>
<td>50</td>
</tr>
<tr>
<td>Bad/Loss</td>
<td>100</td>
</tr>
</tbody>
</table>

Table 1: Rates of provision

If a continuous credit or demand loan remains non-performing for six months, it is considered as substandard loan. It is acknowledged as doubtful, if it remains non-performing for nine months. It is recognized as bad/loss when loan remains non-performing for twelve months or more. In case of term loan that is repayable within a
maximum period of five years, if any installment is not paid within the time equivalent of six months then it falls under the substandard classification. If the time of unpaid installment is equivalent to twelve months and eighteen months, then it is taken into account as the doubtful and bad/loss respectively. Rates of provision for classified loans are given in table 1.

Total amount of loans and advancement of thirty listed banks is BDT 3.3trillion. Among them BDT 166billion is classified loan that is 5.05% of total amount (table – 2). These thirty-listed banks require keeping provision for their classified loan. However, among the thirty listed banks, three banks did not keep adequate provision in the year 2013.

Table 2: Classified loans, loan provision and share price

<table>
<thead>
<tr>
<th>Bank</th>
<th>Total loan (BDT mn)</th>
<th>total classified (BDT mn)</th>
<th>Provision required (BDT mn)</th>
<th>Actual provision (BDT mn)</th>
<th>Provision shortfall/ surplus (BDTmn)</th>
<th>*Share price</th>
</tr>
</thead>
<tbody>
<tr>
<td>AB Bank</td>
<td>140,121.30</td>
<td>4,636.87</td>
<td>3,620.97</td>
<td>3,980.33</td>
<td>359.36</td>
<td>25.20</td>
</tr>
<tr>
<td>Dutch Bangla Bank</td>
<td>105,936.99</td>
<td>4,175.63</td>
<td>3,356.549</td>
<td>3,356.55</td>
<td>0.001</td>
<td>87.00</td>
</tr>
<tr>
<td>Bank Asia</td>
<td>104,911.26</td>
<td>5,878.79</td>
<td>4,112.63</td>
<td>4,112.63</td>
<td>-</td>
<td>17.90</td>
</tr>
<tr>
<td>Brac Bank</td>
<td>119,514.55</td>
<td>7,600.70</td>
<td>5,728.62</td>
<td>6,988.44</td>
<td>1,259.82</td>
<td>25.80</td>
</tr>
<tr>
<td>The City Bank</td>
<td>89,878.63</td>
<td>7,251.01</td>
<td>2,944.00</td>
<td>3,645.23</td>
<td>701.24</td>
<td>16.10</td>
</tr>
<tr>
<td>Dhaka Bank</td>
<td>99,595.88</td>
<td>4,136.69</td>
<td>2,287.42</td>
<td>3,141.99</td>
<td>854.58</td>
<td>19.50</td>
</tr>
<tr>
<td>Southeast Bank</td>
<td>135,690.09</td>
<td>5,350.24</td>
<td>3,860.90</td>
<td>3,877.00</td>
<td>16.09</td>
<td>19.70</td>
</tr>
<tr>
<td>Eastern Bank</td>
<td>102,910.22</td>
<td>3,998.58</td>
<td>1,929.24</td>
<td>1,946.81</td>
<td>17.57</td>
<td>28.10</td>
</tr>
<tr>
<td>United Commercial Bank Ltd</td>
<td>148,664.86</td>
<td>4,427.65</td>
<td>1,662.68</td>
<td>2,122.87</td>
<td>460.19</td>
<td>27.40</td>
</tr>
<tr>
<td>First Security Islami Bank</td>
<td>114,601.80</td>
<td>2,483.82</td>
<td>976.48</td>
<td>1,005.1</td>
<td>28.62</td>
<td>11.10</td>
</tr>
<tr>
<td>ICB Islamic Bank Limited</td>
<td>9,788.56</td>
<td>7,175.92</td>
<td>4,148.31</td>
<td>4,148.31</td>
<td>-</td>
<td>5.10</td>
</tr>
<tr>
<td>IFIC Bank</td>
<td>84,110.39</td>
<td>3,168.08</td>
<td>2,069.99</td>
<td>2,432.36</td>
<td>362.37</td>
<td>24.80</td>
</tr>
<tr>
<td>Bank</td>
<td>Total loan (BDT mn)</td>
<td>total classified (BDT mn)</td>
<td>Provision required (BDT mn)</td>
<td>Actual provision (BDT mn)</td>
<td>Provision shortfall/surplus (BDT mn)</td>
<td>*Share price</td>
</tr>
<tr>
<td>---------------------------------</td>
<td>---------------------</td>
<td>--------------------------</td>
<td>-----------------------------</td>
<td>----------------------------</td>
<td>---------------------------------------</td>
<td>-------------</td>
</tr>
<tr>
<td>Rupali Bank</td>
<td>106,907.82</td>
<td>17,998.51</td>
<td>6,899.22</td>
<td>6,899.22</td>
<td>-</td>
<td>60.7</td>
</tr>
<tr>
<td>Social Islami Bank Limited</td>
<td>84,776.29</td>
<td>4,593.33</td>
<td>2,773.38</td>
<td>2,773.38</td>
<td>-</td>
<td>11.2</td>
</tr>
<tr>
<td>Mercantile Bank Ltd.</td>
<td>97,688.50</td>
<td>4,659.75</td>
<td>3,360.97</td>
<td>3,420.05</td>
<td>59.08</td>
<td>15.3</td>
</tr>
<tr>
<td>Mutual Trust Bank</td>
<td>58,010.82</td>
<td>2,155.77</td>
<td>1,666.01</td>
<td>1,933.97</td>
<td>267.96</td>
<td>18.1</td>
</tr>
<tr>
<td>Uttara Bank</td>
<td>64,829.77</td>
<td>5,209.55</td>
<td>1,357.66</td>
<td>1,419.49</td>
<td>61.83</td>
<td>24.4</td>
</tr>
<tr>
<td>Standard Bank</td>
<td>74,049.89</td>
<td>2,599.27</td>
<td>2,339.89</td>
<td>2,339.89</td>
<td>-</td>
<td>11.4</td>
</tr>
<tr>
<td>One Bank Ltd</td>
<td>76,573.35</td>
<td>3,740.75</td>
<td>2,617.10</td>
<td>2,617.10</td>
<td>-</td>
<td>12.9</td>
</tr>
<tr>
<td>Premier Bank</td>
<td>52,800.46</td>
<td>3,021.34</td>
<td>1,155.87</td>
<td>1,155.88</td>
<td>0.01</td>
<td>10.4</td>
</tr>
<tr>
<td>Prime Bank</td>
<td>153,588.76</td>
<td>7,814.50</td>
<td>5,423.02</td>
<td>5,433.24</td>
<td>10.22</td>
<td>24</td>
</tr>
<tr>
<td>Trust Bank</td>
<td>79,279.58</td>
<td>2,470.36</td>
<td>907.65</td>
<td>907.66</td>
<td>0.01</td>
<td>14.9</td>
</tr>
<tr>
<td>Pubali Bank</td>
<td>136,940.46</td>
<td>8,136.10</td>
<td>6,281.46</td>
<td>6,282.91</td>
<td>1.45</td>
<td>26.6</td>
</tr>
<tr>
<td>Shahjalal Bank</td>
<td>85,706.61</td>
<td>5,542.69</td>
<td>3,103.23</td>
<td>2,246.32</td>
<td>(856.91)</td>
<td>11.3</td>
</tr>
<tr>
<td>NCC Bank</td>
<td>88,146.51</td>
<td>4,862.41</td>
<td>2,663.39</td>
<td>2,663.39</td>
<td>-</td>
<td>11</td>
</tr>
<tr>
<td>Exim Bank</td>
<td>143,847.38</td>
<td>5,279.94</td>
<td>2,755.39</td>
<td>2,755.39</td>
<td>-</td>
<td>10.3</td>
</tr>
<tr>
<td>Al-Arafah Islami Bank</td>
<td>121,298.99</td>
<td>3,598.83</td>
<td>1,128.03</td>
<td>1,128.03</td>
<td>-</td>
<td>14.2</td>
</tr>
<tr>
<td>National Bank Limited</td>
<td>151,098.99</td>
<td>4,898.83</td>
<td>1,612.58</td>
<td>1,461.48</td>
<td>(151.1)</td>
<td>11.5</td>
</tr>
<tr>
<td>Islami Bank</td>
<td>406,804.56</td>
<td>14,941.90</td>
<td>9,037.05</td>
<td>9,037.80</td>
<td>0.75</td>
<td>24.9</td>
</tr>
<tr>
<td>Jamuna Bank</td>
<td>67,699.38</td>
<td>5,133.75</td>
<td>3,202.00</td>
<td>2,902.00</td>
<td>(300)</td>
<td>12.3</td>
</tr>
<tr>
<td>Total</td>
<td>3,305,772.65</td>
<td>166,941.56</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

*as of 2nd July, 2014

This under provisioning for classified loan ultimately leads to overstated profit. This is because provisioning is considered as an expense. According to the Banking Companies Act, Auditors are required to state unambiguously whether financial statements of the bank have been prepared complying with the regulation issued by Bangladesh Bank. The firms those were auditing these three banks were certifying that these three banks’ financial statements presented true and fair view of these banks’ financial position. In this case, audit firms who audited these three banks have compromised their...
integrity, objectivity and professional skepticism. Therefore, these audit firms are not independent in appearance. These data also imply that these audit firms were not upholding their ethical principles while they were doing audit to these three banks. Therefore, these audit firms were not independent and ethical. For this reason, they did not report the misstatement that upset the audit quality of these three listed banks. Rest of the twenty-seventeen listed banks did properly maintain the provision requirement. Audit firms, who audited these banks, reported that financial statements of these banks represented true and fair view of these banks’ financial position. Considering the loan provision data, these audit firms were independent and maintained ethical values. Moreover, there were no discrepancies between the audit report and financial statements of those twenty-three banks in view of the loan provision data. Therefore, the audit quality of these twenty-seven listed banks was decent in respect of loan provision data.

Therefore, true hypotheses are:

\( H_{a2} \): There is a relationship between auditor ethics and audit quality

\( H_{a1} \): There is a relationship between auditor independence and audit quality

Among the thirty listed banks, three banks’ audit quality was poor. These banks’ average share price was BDT 11.7 on July 2 2014. On the contrary, rest of the twenty-seven listed banks’, whose audit quality was considered satisfactorily fair in terms of the loan provision data, average share price was BDT 22.15 on July 2 2014 that is more than double of the poorly audited banks (Figure-2).

![Figure 2: Average share price](image)

Therefore, true hypothesis is:

\( H_{a3} \): There is a relationship between audit quality and share price

10. Limitations

The results of this study are solely dependent on the numerical values. So, human perception is very low in this study. Moreover, this research portrays the relationship between audit quality and share price only for the banking sector among the twenty-two sectors of Bangladesh.

11. Suggestions for Further Research

This study only gives insight about the audit quality and relationship between audit quality and share price of banking sector. Therefore, further research can be done by evaluating the audit quality of other sectors like Food and allied sector, cement sector etcetera. This research is based on the cross sectional data. So, this research can be extended by using longitudinal data.

12. Conclusion

Auditors are required to disclose any matter regarding the violation of rules and regulations. In this case, three banks overstated their profit by violating loan provision requirements that are set by the supreme banking authority of Bangladesh. Auditors of these three banks compromise
their independence and ethics by reporting that those banks’ financial statements present true and fair view of their financial position rather than reporting the violation, and this violation lowers investors’ confidence resulting low share price. In order to sustain investor’s confidence, auditors must respect the standards that are imposed by the authorities.

References


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