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The Impact of Audit Committees on the Realization of an Integration Relationship between Internal and External Audit when Conducting Audits. A Study on Public Shareholding Corporations

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Abstract:

This study aims to investigate methods of achieving an integrating relationship between internal and external audit when conducting audit procedures in Jordanian public shareholding corporations, as well as investigate the impact of audit committees achieving such a relationship since an effective internal audit effective the external auditor's estimations regarding control risks. The study concludes that all aspects of the realization of an integration relation between internal and external audit have achieved a fair ratio exceeding 60%. Spearman test was used to show the nature of the relationship between the internal and external audit. The test results showed that the relationship between these methods is vulnerable in Jordanian public shareholding corporations, and that audit committees have no statistically significant impact on achieving an integrating relationship between internal and external audits in conducting audit in Jordanian public shareholding corporations, since the ratio of audit committees interpretation (R²) which amounted to (.145) of the dependent variable difference (achieving an integrating relationship between internal and external audit in conducting audit) is relatively low, and that the P- value derived for this relation amounted to (.615) which is more than (5%) .

Keywords: audit committee; external audit; internal audit; internal control system.

JEL Classification: M41; M42; M48.

Introduction

Many professional organizations and international bodies have stressed the formation of audit committees by the corporation's boards of directors as per governance best practices, since these committees are considered the main ones stemming from the board of directors for the experience skills, and competencies required from members of such committees. These committees stress a culture of commitment and accountability within the company regardless of the nature of its work and size. They also carry out control and surveillance operations on all the corporations operational processes, present reasonable guarantee on the efficiency and effectiveness of the company's internal control system and risk management, and ensure the independence of the external auditor's work. In sum, these committees are the link that connects the board of directors to the internal and external auditors. Wolinzer (1995) has identified the three responsibilities placed upon audit committees as follows:

- (1) responsibilities relating to corporate accounting and financial reports;
- (2) responsibilities related to auditors and their activities;
- (3) governance responsibilities.

In consideration of the role played by these committees as a control and surveillance authority to internal and external auditors, identifying the effectiveness of internal and external audits as well as revising the coordination of the internal auditor's work arrangements since this work affects the procedures taken by the external auditor as defined by auditing standards. The auditing standard No.5 issued by PCAOB defined the procedures that help the external auditor identify his dependence on the internal auditor and the audit committee. The International Auditing Standard No. 610 and the American Standard No. 65 has defined that the external auditor shall evaluate the work and effectiveness of internal auditors, since the work of internal auditors affect the procedures taken by external auditors, and having an efficient and effective internal audit affects the risk assessments of external auditors. Therefore, the external auditor shall observe and evaluate the appropriateness of the internal audit as defined by the International Auditing Standard through the following:

- (1) the position of internal audit in the organizational structure. Internal auditors are not permitted to perform any operational responsibilities; the administration shall not impose any constraints on internal auditors; internal auditors shall have complete freedom of communication with external auditors;
- (2) the scope and nature of the internal auditor's work, and whether the administration relies on their recommendations;
- (3) competence and professional experience of the internal auditor that qualifies him to work as such;
- (4) assessing internal auditors' work to ensure that they have planned internal audit, examined audit programs and revised documents to be used in the audit process.
[https://www.ifac.org/system/files/publications/files/ISA-610-\(Revised-2013\).pdf](https://www.ifac.org/system/files/publications/files/ISA-610-(Revised-2013).pdf)
https://pcaobus.org/Standards/Archived/PreReorgStandards/Pages/Auditing_Standard_5.aspx.

When observing the internal auditor's work, the external auditor shall analyze the temporary internal audit plan and discuss it with the internal auditor. To achieve integration in their relationship, the internal and external auditors shall agree in advance on the work to be done, audit procedures and coverage, samples testing and level, setting periodical meetings during the period audit operations are carried out, both sides access to audit programs and documents, exchanging reports and administration tools, as well as exchanging experience, techniques and knowledge to achieved the administration's desired objectives as well as their own from this integration process.

Hence, this study is of significance to address the impact of audit committees on achieving an integrating relationship between internal and external audit when conducting audit operations within Jordanian public shareholding corporations to achieve the desired objectives of such integration for the company and auditors.

1. Literature Review

Many previous studies have addressed the partnership between the internal and external audit and their impact on auditing fees. Al-Hajri (2017) aimed to investigate the impact of internal auditing on the fees of the external auditor. The study concluded that there is a negative impact between the internal auditing partnership on the external auditing and the external auditing fees. Axén (2018) concluded that there is a positive relationship between external auditing fees and external auditing compensations based upon the company's achievement.

Other studies have addressed the relationship between internal and external auditing. Sukker *et al.* (2018) aimed at identifying the key factors affecting the extent to which the external auditor benefit from the internal auditor's work in the Jordanian corporations. The study results indicated that the objectivity factor was the most influencing in decision-making, while efficiency came second and work performance came last since it relies on internal audit. Thnaibat, Shunnaq (2006) found diversity in the views of internal and external auditors regarding the application of ISA 610, where internal auditors indicated that there is an application of this standard but to a lesser degree, while external auditors indicated that this application is higher than the average.

Khan *et al.* (2019) concluded the effectiveness of audit committees and the quality of external auditing, and that these have an impact on the accounting reservation. The accrual basis has intermediated in the relationship between the audit committee effectiveness and corporation performance in the market, and that these results contribute to many theories such as the signs and agency theory, reputation, and caution in nascent economy.

Some studies have addressed the dependence of the external auditor on the internal auditor in using advanced techniques and electronic processing. Sutton and Malaescu (2015) aimed at assessing the extent to which the external auditor benefits from the internal auditor's work when the latter make use of advanced techniques, and the impact of benefiting from the audit hours listed in the budget. This study showed, through its results, that auditors increase the number of hours regarding the budget participation to a higher rate when the client uses traditional auditing procedures. Farkas, Hirsch (2016) have concluded that external auditors perceptions are fully treated when deposited electronic processing strategies are used. This indicates the vulnerability of the

IAF and the low degree of dependence, while the manual processing strategies partially treat. The most frequent processing is also the most effective in improving the vulnerability of the IAF and the lower degree of dependence.

Alnaami (2014) aimed to identify the role of audit committees, and the internal and external auditors in addressing financial corruption in the banks of Gaza. The study concluded that the internal audit function is to ensure the commitment of corporations to the policies, and financial and administrative orders, as well as the country's rules. These committees also assess the accounting system in the company until it carries out the financial procedures in an effective and efficient way, to reduce corruption. It also concluded that audit committees recommend appointing the external auditor and allocating their fees.

Mukhina (2017) aimed to clarify the problems related to internal auditing. The researcher has developed an effective model for internal auditing to achieve the goals of companies

2. Study Methodology

This study is based on one main hypothesis and three sub-hypotheses:

H0: there is no statistically significant impact of audit committees on achieving an integrating relation between internal and external audit when conducting audit operations within Jordanian public shareholding corporations.

The following three sub-hypotheses branch from the main one:

HO1: there is no statistically significant impact of audit committees on the external auditor's use of the internal auditor's work when conducting audits within Jordanian public shareholding corporations.

HO2: there is no statistically significant impact of audit committees on the internal auditor's use of the external auditor's work when conducting audits within Jordanian public shareholding corporations.

HO3: there is no statistically significant impact of audit committees on achieving an integrating relation between internal and external audit when conducting audit operations within Jordanian public shareholding corporations.

In order to conduct an applied study, a questionnaire comprising four axes has been developed. The first axis contains 15 questions directed to audit committees, while the second one contains 34 questions directed to external auditors, covering the extent to which the external auditor has benefited from the internal auditor's work when conducting audits within the Jordanian public shareholding corporations. The third axis includes 21 questions directed to internal auditors on the extent to which internal auditors have benefited from external auditors' work when conducting audits within Jordanian public shareholding corporations. The fourth axis includes 20 questions on methods of achieving integration between the internal and external auditor when conducting audits within Jordanian public shareholding corporations. To test the validity and reliability of the questionnaire questions, Cronbach's Alpha was used, and it reached (.720), which is considered high, indicating the validity and reliability of all the questionnaire 90 questions.

Table 1. Reliability Statistics

Cronbach's Alpha	No. of Items
.720	90

The questionnaire axes have been discussed and analyzed in the light of the study hypotheses through relying on the arithmetic mean and standard deviation to identify external and internal auditors and audit committees answers to the questionnaire statements. Results are shown in Table (2) indicating the arithmetic mean and standard deviation on the extent to which the external auditor benefits from the internal auditor's work in conducting audit operations within Jordanian public shareholding corporations.

Table 2. Arithmetic mean and Standard deviation

Statement	Arithmetic Mean	standard deviation	Order
The external auditor uses the internal auditor's work to reduce the audit risks to a reasonable level.	4.70	0.461	1
Tables, charts and analyzes are prepared and submitted by the external auditor and the internal auditor.	1.30	0.461	34
All statements	3.4588	1.45267	

Results of Table (2) show that the highest arithmetic mean has reached (4.70), referring to the statement 'the external auditor uses the internal auditor's work to reduce audit risks to a reasonable level' with a standard

deviation of 0.461 lowest arithmetic means reached (1.30), referring to the statement 'analyzes, tables and statements are prepared and submitted by the external auditor with the internal auditor', with a standard deviation reaching 0.461. Results also show high overall arithmetic mean for all the questionnaires' statements, amounting to 3.4588, with a standard deviation of (1.45267). Results show that the external auditor benefits from the work of the internal auditor in conducting audits within Jordanian public shareholding corporations.

While results of Table (3) show that, the internal auditor benefits from the work of the external auditor in conducting audits within Jordanian public shareholding corporations

Table 3. Arithmetic mean and Standard deviation

Statement	Arithmetic mean	Standard deviation	Order
The external auditor carries out the audits, taking into account assessing the functionality of the internal audit to determine its effectiveness and efficiency.	4.60	0.493	1
The internal auditor follows a defined method of communication with the external auditor to perceive and understand any challenges faced by the external auditor while doing his work before conferring with the board of directors.	4.60	0.493	1
The internal auditor follows a defined method of communication with the external auditor to perceive and understand weaknesses in the internal control before conferring with the board of directors.	1.49	0.503	21
All statements	3.0667	1.51269	

Results in Table (3) show that the highest arithmetic mean has reached (4.60), referring to the statement 'the external auditor carries out audits taking into account assessing the functionality of the internal auditor to determine their effectiveness and efficiency', with a standard deviation of (0.493). Another high arithmetic mean has reached (4.60), referring to 'The internal auditor follows a defined method of communication with the external auditor to perceive and understand any challenges faced by the external auditor while doing his work before conferring with the board of directors', with a standard deviation of 0.493. While the lowest arithmetic mean has reached (1.49), referring to 'The internal auditor follows a defined method of communication with the external auditor to perceive and understand weaknesses in the internal control before conferring with the board of directors', with a standard deviation of 0.503. Results also show an increase in the overall arithmetic mean of all the questionnaires' statements amounting to 3.0667, with a standard deviation of (1.51269). Results show that the internal auditor benefits from the external auditor's work by a low ratio compared to that of the external auditor's benefit from the work of the internal auditor in conducting audits within Jordanian public shareholding corporations.

Results in Table (4) relate to methods of achieving the integration between the internal auditor and the external auditor in conducting audits in Jordanian public shareholding corporations

Table 4. Arithmetic mean and Standard deviation

Statement	Arithmetic mean	Standard deviation	order
Each report to the other any information regarding the efficiency of the activity, or any new information that might be discovered during the audit process	4.60	0.493	1
Reports and management letters are exchanged between them.	4.60	0.493	1
After examining the management letters and starting any action required by the administration and the board of directors regarding any corrections, the external auditor must ensure that the correction is made.	4.60	0.493	1
Experience, techniques and knowledge are exchanged to enable both to coordinate and communicate successfully with each other.	4.60	0.493	1
Each is informed with the work related to audit documentation and programs of the other to define their level of experience and skill	1.40	0.493	20
Each is informed with the work related to audit documentation and programs of the other to achieve a conviction and obtain approval of the audit program.	1.40	0.493	20

Statement	Arithmetic mean	Standard deviation	order
Experience, techniques and knowledge are exchanged so that the internal audit director can ensure that the methods and terms used by the external auditor are understood by internal auditors.	1.40	0.493	20
All statements	3.5619	1.42176	

Results in Table (4) show that the highest arithmetic mean reached 4.60 with a standard deviation of 0.493, referring to the following statements: 'each is informed by the other of any information related to the activity efficiency or any other issues that might arise during the audit process', 'after verifying the administration's letters and starting any work required by the administration and the board of directors about any corrections, the external auditor shall make sure that such correction has been made', 'the administration's reports and letters are exchanged between them', 'experience, techniques and knowledge are exchanged between them enabling each to coordinate and communicate successfully'. On the other hand, the lowest arithmetic mean amounted to 1.40, referring to the following: 'each is informed with the work related to audit documentation and programs of the other to define their level of experience and skill', 'each is informed with the work related to audit documentation and programs of the other to achieve a conviction and obtain approval of the audit program', 'experience, techniques and knowledge are exchanged so that the internal audit director can ensure that the methods and terms used by the external auditor are understood by internal auditors' with a standard deviation of 0.493. Results also show that there is an increase in the overall arithmetic mean of all the questionnaire's statements, reaching 3.5619 and a standard deviation of (1.42176). Results show that there are methods to achieve integration between the internal auditor and the external auditor in conducting audits within Jordanian public shareholding corporations. As for the independent variable relating to the audit committees:

Table 5. Below show the results of the analysis

Statement	Arithmetic mean	Standard deviation	Order
Audit committees observe company policies and practices based on ethical considerations.	4.59	0.495	1
Audit committees review the reports of internal control systems inspection and verify the compatibility between actual practices and systems.	1.48	0.503	15
All statements	3.9108	1.13589	

Results in Table (5) show that the highest arithmetic mean reached 4.59, referring to 'audit committees observe company policies and practices based on ethical considerations', with a standard deviation of 0.495. The lowest arithmetic mean reached 1.48, referring to 'audit committees review the reports of internal control systems inspection and verify the compatibility between actual practices and systems' with a standard deviation of 0.503. Results show that there was an increase in the overall arithmetic mean for all the questionnaire's statements reaching 3.9108 and a standard deviation of (1.13589). This indicates that audit committees have a role in achieving integration between internal and external auditing.

The following is a detailed description of the statements related to the integrating relationship between internal auditing and external auditing in Jordanian public shareholding corporations in order to determine the relative significance of the study sample respondents' assessment on the integrating relationship. Table (6) shows the arithmetic mean and standard deviation as well as the relative significance of the integration mechanisms. To answer the question of the study: is there integration in the relationship between internal and external auditing in conducting audits within Jordanian public shareholding corporations?

Table 6. Arithmetic mean and Standard deviation

Statement	Arithmetic mean	Standard deviation	Order
The external auditor has benefited from the work of the internal auditor in conducting audits within Jordanian public corporations.	3.4588	1.45267	2
The internal auditor has benefited from the work of the external auditor in conducting audits within Jordanian public corporations.	3.0667	1.51269	3

Statement	Arithmetic mean	Standard deviation	Order
Methods of integration between the internal auditor and the external auditor in conducting audits of Jordanian public corporations	3.5619	1.42176	1
Statements average	3.3625		

To answer the study question of whether there is an integrating relationship between internal and external auditing in conducting audits within Jordanian public shareholding corporations, the table above shows the views of the study sample respondents. The Table indicates that the highest arithmetic mean refers to 'methods of achieving integration between the external and internal auditor in conducting audits within Jordanians public shareholding corporations' amounting to (3.5619), considered to be the best method to achieve integration efficiency between them. While the statement 'the internal auditor benefits from the external auditor's work in conducting audits within Jordanian public shareholding corporations' reached the lowest arithmetic mean of (3.0667), considered to be the weakest method to achieve integration between the internal and external auditors with a reasonable ration exceeding 60%.

With regard to the correlation between the integration relationship aspects regarding internal and external auditing in conducting audits within Jordanian public shareholding corporations, Spearman testing was used to determine the extent of this correlation. Table (7) shows the results of Spearman testing.

Table 7. Correlations

			A2	A3	A4
Spearman's rho	A2	Correlation Coefficient	1.000	.001	.149
		Sig. (tailed-2)	.	.997	.532
		N	34	21	20
	A3	Correlation Coefficient	.001	1.000	.630
		Sig. (tailed-2)	.997	.	.003
		N	21	21	20
	A4	Correlation Coefficient	.149	.630	1.000
		Sig. (tailed-2)	.532	.003	.
		N	20	20	20

Table (7) shows that that there is no correlation between the utilization of the internal auditor's work by the external auditor in conducting audits within Jordanian public corporations, and between the utilization of the external auditor's work by the internal auditor in conducting audits within Jordanian public shareholding corporations, where the test value exceeded 5% and the correlation is weak reaching (001.). The correlation ratio between the utilization of the internal auditor's work by the external auditor in conducting audits, and between methods of achieving integration between the internal and external auditor in conducting audits is also considered low, where the strength of the relationship between them amounted to (149.) and the test value (532.). On the other hand, there is a positive relationship and strong correlation between utilization of the external auditor's work by the internal auditor in conducting audits, and between methods of achieving integration between the internal and external auditor in conducting audits, where the test value has not exceeded 5%, amounting to (003.), and that the force of the relationship between them reached (630.). This is proved by the arithmetic means in Table (6), where the utilization of the external auditor's work by the internal auditor in conducting audits within Jordanian public shareholding corporations, reaching the lowest arithmetic mean of (3.0667). This is considered the most vulnerable method to achieve integration between the external and internal audit.

Hypotheses testing:

Table 8. Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.381a	.145	-.088	1.18477

a. Predictors: (Constant), A4, A2, A3

Table 9. Anova

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	2.623	3	.874	.623	.615b
	Residual	15.440	11	1.404		
	Total	18.063	14			

a. Dependent Variable: A1
b. Predictors: (Constant), A4, A2, A3

Tables (8 – 9) above show the results of the simple linear regression analysis of the impact of audit committees on achieving an integrating relationship between internal audit and external audit in conducting audits within Jordanian public shareholding corporations. It is found that the ratio of audit committees interpretation (R2) amounted to (.145) of the dependent variable difference (achieving an integrating relationship between the internal auditor and external auditor in conducting audits), is a relatively low interpretation, and that the P value generated for this relationship amounted to (.615b) being that more than (5%). Following the previous results analysis, the null main hypothesis is accepted, stating, 'There is no statistically significant impact for audit committees in achieving integration in the relationship between internal and external auditing in conducting audits within Jordanian public shareholding corporations.

Conclusions Recommendations

There is no statistically significant impact of the audit committee impact at the level (5%) for all methods of achieving integration between the internal and external auditing in conducting audits within Jordanian public shareholding corporations. Statistical tests interpreted a ratio of (.145) of the dependent variable difference (achieving an integrating relationship between internal and external auditing in conducting audits), being a relatively low interpretation ratio. This result is consistent with the study results of (Farkas, Hirsch 2016) and (Al-Hajri 2017) confirming that there is no impact of audit committees on achieving an integrating relationship between internal and external auditing in conducting audits within Jordanian public shareholding corporations. All members of the committee shall have good knowledge of governance and its requirements, as well as understand the corporation's business activity very well. One of these members shall have sufficient knowledge of the accounting requirements that relate to the corporation's business activity and its impact on financial statements. And there is no statistically significant impact of audit committees impact on achieving an integrating relationship between internal and external auditing in conducting audits within Jordanian public shareholding corporations, since the P- value generated amounted to (.615b) being greater than (5%). So, the main hypotheses are accepted indicating that there is no statistically significant impact of audit committees on the utilization of the internal auditor's work by the external auditor and the utilization of the external auditor's work by the internal auditor in conducting audits and in methods of achieving integration between the internal and external auditors in conducting audits. This study is consistent with (Farkas, Hirsch 2016) and (Al-Hajri 2017) that there is no integration between internal and external auditing, and that this may be due to the unawareness of the audit committees members of their responsibilities towards the effectiveness and efficiency of the internal audit activity, as well as not being aware of their strategic plan and its observance in internal audit procedures. Moreover, not discussing the external auditor's work plan and making sure of his independence and objectivity, not discussing with the external auditor about their view and work technique from the part of the audit committee, which may be due to the fact that the audit committee lacks a member who has knowledge and experience in accounting and audit, both internal and external. There is no statistically significant impact of audit committees in achieving an integrating relationship between internal and external auditing in conducting audits within Jordanian public shareholding corporations. This may be due to the non-existence of a correlation between the utilization of the internal auditor's work by the external auditor in

conducting audits within Jordanian public shareholding corporations, and between the utilization of the external auditor's work by the internal auditor in conducting audits within Jordanian public shareholding corporations, where the test value has exceeded 5% and the correlation proved to be weak reaching (001.). Moreover, the correlation ratio between the utilization of the internal auditor's work by the external auditor in conducting audits within Jordanian public shareholding corporations, and between methods of achieving integration between the internal and external auditors in conducting audits is considered low, where the strength of the relationship between them reached (149.) and the test value amounted to (532.).

Recommendations:

Audit committees shall have the necessary powers and appropriate mechanisms to practice their role in achieving an integrating relationship between internal auditing and external auditing, thus generating positive results to both corporations and society, and the committee members shall be aware of governance and its benefits as well as understand the nature of the corporation's business. Moreover, a member of the committee shall have professional experience and knowledge about internal and external auditing, and accounting.

Audit committees shall be responsible for revising internal and external auditing, as well as conduct check procedures of the internal control system and its achievements. They shall also conduct continuous monitoring of the internal auditing management, support the independence of the external auditor and increase the efficiency of the internal auditing activity and the internal control system.

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