

## **Audit Conservatism or Opinion Shopping? Audit Reporting Challenges in a Developing Country**

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### **Abstract:**

The purpose of a financial statement audit is to enable the auditor to express an opinion on whether the statements are prepared in accordance with the financial reporting framework. This actually helps the business to remain viable in a competitive global environment and ensure its financial statements remain solid. Despite the importance of auditing, so far, no analysis has yet been done on the types of opinions issued in a developing country, Bangladesh. Specifically, there is no review published in recent times, when a number of significant incidents happened that might have an impact on listed companies' reporting practices. Examples include the adoption of the *International Financial Reporting Standard* (IFRS) in 2013, introducing the new *Financial Reporting Act* in 2015, adaptation of a new format of auditor's report effective from the beginning on or after January 2018, etc. This research aims to assess the auditor opinions issued for the companies listed on the Dhaka Stock Exchange over a five-year period, and provides some in-depth understanding of the challenges it faces when providing an audit opinion.

This research takes a sample from Dhaka Stock Exchange-listed companies during the period 2014–2018, explores the trend of issued audit opinions, and provides some analysis behind issued opinions. This research also compares the trend between audit report issued by Big 4 and non-Big 4 affiliated audit firms and any variation in opinion issues based on industry classification. This research entailed conducting interviews to gain some insights about the challenges faced by auditors when providing options.

**Keywords:** Audit Report, Unqualified Opinion, Qualified Opinion, Emphasis of Matter, Qualified, Disclaimer and Adverse Opinion

### **1. Introduction**

An audit report is an effective means of communication with companies' stakeholders. Listed companies must issue an audit report and state whether the financial statements are prepared according to legislation such as the Company Act, specifically, whether the statements represent a true picture of the business and whether all the relevant accounting standards and other regulatory requirements are followed. Company management or those in charge of governance matters are responsible for preparing

and presenting the financial statements. The auditors' main responsibility lies with reviewing whether financial reports comply with the Accounting Standards and the Company Act.

At the end of the audit, the auditor provides an opinion based on the review of sample data taken from the report. This research will take a sample from Dhaka Stock Exchange-listed companies during 2014 – 2018, explore the trend of issued audit opinions, and explain what they mean. This research also aims to compare the number of audit opinions issued by Big 4 and non-Big 4 audit firms and auditor opinion issues based on industry classification. The research data is taken from Bangladesh, which is located in a delta in Southeast Asia but does not have enough natural resources to feed a growing population. Nonetheless, the country is among the fastest-growing economies globally, and it took the most significant infrastructure initiative in the last decade for this to happen. In the 1990s, the government of Bangladesh built Jamuna Bridge to connect to the north of the country, and now it has confirmed Padma Bridge to connect to the south. The country is classified as one of the Next Eleven emerging market middle income economies and a frontier market. Bangladesh wants to be a developed country by 2041 (Paul, 2017). The port is an important consideration, and currently, only ships' feeders arrive at Bangladesh's Chittagong port. Big ships cannot get there so Bangladesh is building a port for big ships. Bangladesh has exponentially increased its electricity production and now solar panels are providing rural areas with electricity. Corruption and poor governance are challenging but the country is moving ahead regardless of the obstacles that have arisen in the last decade. The Dhaka Stock Exchange will play a critical role in Bangladesh in this development.

The audit industry in newly independent Bangladesh in 1972. Established audit firms that were located in Bangladesh continued their business in the post-Pakistan period. The audit industry follows the standard set by the *International Auditing and Assurance Standards Board*. At its inception in Bangladesh, the audit industry was small but demand for chartered accountants grew. Bangladesh currently has 2000 chartered accountants and the accounting and finance industry is dominated by CA-course complete (CA-CC) graduates, who did not pass the chartered accountants exam but received course completion certificates. Different companies in various industries give these CA-CCs job preference, and there are approximately 25,000 CA-CC in the market. This oversized influence of chartered accounting in Bangladesh's accounting and finance job market ensures that financial reporting in the different sectors is on par with international standards. Backed by the right infrastructure development, Dhaka Stock Exchange will play a pivotal role to achieve developed country status by 2041. The auditing industry plays an important role because accountability is one of the pillars of any developed country. This is why it is critical to look at the quality of both the audit industry and audit reports in Bangladesh.

Auditors are not responsible for monitoring management, but at the end of the audit, they provide a management letter directing how the administration can improve the internal control system of the business. The extent to which financial statements can reduce agency cost depends on the quality of the audit and this functions as a control mechanism. Although the Company Act requires the preparation and auditing of financial statements, there is significant variation in the quality of audits performed and

their resulting ability to reduce agency costs. If the reduction in agency costs exceeds the audit cost, the audit can be seen as an added value to reducing such costs. As part of the corporate governance mechanism, auditors are expected to increase the quality of reporting throughout their audit report.

In the last half-century, demand has risen for greater accountability and closer scrutiny of accounts. This is especially evident in recent years following bank scandals such as Basic Bank, Farmers Bank and the 2011 Bangladesh stock market crash due to fraud, earnings mismanagement, and many governance issues. More recently, greater emphasis has been given to auditors' assessments of businesses during and following the Global Financial Crisis (GFC) in 2007–2008 and 2011 stock market crash of Bangladesh. It is a general expectation of clients that the auditor will: (i) review and confirm that the financial information is correct (true and fair); (ii) information was checked for, and no fraud exists; and (iii) the business is a sound investment based ongoing concern assumption. However, the expectation gap is a reality. Major issues associated with the expectation gap are: firstly, the nature and meaning of audit report messages; thirdly, detection and reporting of fraud; and thirdly, early warning of corporate failures (going concern issue).

The rest of this paper is organised as follows. Section 2 provides a brief overview of different types of audit opinions available to auditors. Section 3 discusses the literature on audit opinions. Section 4 outlines the data and research design. The results are presented in Section 5, and the final section highlights the implications of the results obtained.

## **2. Nature and Meaning of Audit Opinion**

Four broad categories of audit opinions are: *Unqualified*, *Qualified*, *Disclaimer* and *Adverse opinion*. They are discussed in more detail below.

### **2.1 Unqualified opinion**

*Unmodified opinion* (also referred to as *Unqualified opinion*) is the best opinion an entity may receive. This type of opinion is expressed when the auditor is satisfied that the financial report in all material respects has been prepared in accordance with the Corporations Act 2001, and that the financial data is honest, true and fair. An *Unqualified* opinion is expressed when the auditor has concluded that he/she has obtained a reasonable assurance that the financial report is free from material misstatement, whether due to fraud or error.

### **2.2 Qualified opinion**

The auditor expresses a *Qualified opinion* when: firstly, the auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in aggregate, are material but not pervasive to the financial report; or secondly, the auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion. However, the auditor concludes that the possible effects on the financial report of undetected misstatements, if any, could be material but not pervasive. The *Qualified opinion* is generally issued in the following circumstances:

- where a scope limitation exists;
- where a disagreement is evident between the auditor and those charged with governance;

- where a non-compliance with applicable accounting standards exists, that is material but not extreme in nature.

### 2.3 Disclaimer Opinion

A *Disclaimer* of opinion is expressed when the possible effect of a limitation on the scope is so material and pervasive that the auditor is unable to express an opinion on the financial report. The opinion paragraph is generally headed "Disclaimer of Auditor's Opinion" (Gay and Simnett, 2019). The following circumstances give rise to a *Disclaimer Opinion*:

- when the auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, and the auditor concludes that the possible effects on the financial report of undetected misstatements, if any, could be both material and pervasive.
- When, in extremely rare circumstances involving multiple uncertainties, the auditor concludes that, notwithstanding having obtained sufficient appropriate audit evidence regarding each of the individual uncertainties, it is not possible to form an opinion on the financial report. This is due to the potential interaction of the uncertainties and their possible cumulative effect on the financial report.

### 2.4 Adverse Opinion

An Adverse opinion is generally issued when the auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in aggregate, are both material and pervasive to the financial report. Subsequently, the auditor concludes that Qualification of the auditor's report is not adequate enough to disclose the misleading or incomplete nature of the financial report. The opinion paragraph is headed "Adverse Auditor's Opinion". Other than these four, based on the circumstances, the auditor can also extend his/her opinion with 'Emphasis of matter' and 'Other Matter'. These are additional paragraphs which the auditor might add if he/she thinks it is essential to draw the user's attention to them.

### 2.5 Emphasis of Matter (EOM)

In some circumstances, the auditor may issue an *Unqualified opinion* with EOM or a *Qualified opinion* with EOM. The Emphasis of matter paragraph was introduced to draw attention to certain issues in the financial report. This type of opinion may be issued in circumstances where the auditor wishes to highlight a matter affecting the financial report. This matter is generally included in the notes to the financial statements. It is important to note that the emphasis of the matter is not a qualification, so steps need to be taken to ensure that this is communicated to the audit report user.

### 2.6 Other Matter

Other matter paragraph included in the auditor's report refers to a matter other than those presented or disclosed in the financial statements that is relevant to users' understanding of the audit. Other matter paragraph is added to the auditor's report after the opinion paragraph.

### 3. Literature Review

#### Agency Theory

The theory underlying this research is agency theory. According to Jensen and Meckling (1976), agency relationships are those where managers work as an agent and the owner of the business is the principal. In these contractual relationships, managers are responsible for preparing financial statements and handing them over to the owners, but keeping the rights of shareholders in mind. In practice, this relationship creates conflict since managers aim to improve their own interests, whereas shareholders want to receive higher dividends from the business. To reduce the phenomenon of agency conflict, auditors work as agents for shareholders and report to them after reviewing the financial statements. The shareholders (owners) authorise the management (agent) to operate on behalf of the company. Hence the agent has more information than the owner. This is commonly referred to as information asymmetry. Given that an agent has more information, the agent may be tempted to manipulate financial statements, and typically, it could mean not disclosing the true information, which may not match the expectations of the principal. Therefore, the role of auditors is critical in terms of thoroughly reviewing the financial statements and make sure they are prepared according to the Company Act.

Although the economy of Bangladesh is growing fast and there is a rapid growth of industries and companies listed on the stock exchange, no analysis has been done on the types of auditing opinions issued in Bangladesh. Specifically, there is no review for the period 2014–2018, when some significant incidents happened that might have had an impact on listed companies' reporting practices. There are not many studies available in some developed countries on the issue of the audit report. For example, Craswell's (1986) review shows that in Australia, before 1970, fewer than 5% of audit reports for public companies were *Qualified*. Legislative changes and the introduction of new accounting standards led to an increase in the number of qualifications during the early 1970s. Carson, Ferguson and Simnett (2006) in an Australian study, found that since the amendment of the audit reporting standard in 1996, the rate of qualifications for publicly listed companies has fallen to around 4%. It is much less than the pre-amendment qualification rate of around 15-20%. This means that the changes to the audit reporting standards have had a significant and desired effect of improving disclosure in financial statements. Xu, Jiang, Fargher and Carson (2011) found the main reason for audit report modification is going concern and that modification rates increased from 12% in 2005–2007 to 18% in 2008 and 22% in 2009. Serious audit report qualification rates remain around 3%. Azim (2013) examines the trend of audit opinions issued to Australian listed companies during a fifteen-year period. In total 20,473 audit opinion was cited over a fifteen-year period, i.e., from 1996 to 2010. This research found that, over this 15-year period, *Unqualified* was the most common type of audit report issued in Australia, with an average of 96.4%. The average rate at which the Big 4 audit firms issue *Unqualified* reports is 88% compared to 76% issued by the non-Big 4 firms.

Again, some research has been done on opinion shopping (i.e., shopping for an improved audit opinion from a new auditor) in developed countries. For example, US analyses claim opinion shopping is pointless since incoming auditors' first opinions are not generally more favourable than outgoing auditors' final opinions (Krishnan, 1994). In

the UK, Lennox (2000) argues that a comparison of opinions issued by outgoing and incoming auditors is a flawed test for opinion shopping. He predicts how likely companies would receive unfavourable audit opinions if audit firm changes are different to those actually observed, and he shows opinion shopping is a highly significant predictor of audit firm changes in the UK. Interestingly no previous research in a developing country was conducted on the 'opinion shopping' practice. Given this, it is interesting to explore the phenomenon in an emerging market economy like Bangladesh.

#### 4. Methodology and Data Collection

Given the dearth of research, the following three research questions are posited here:

- **Research question 1:**  
What is the most common type of audit report issued in Bangladesh over a five-year period?
- **Research question 2:**  
What is the trend of audit opinion between Big 4 and non-Big 4 audit firms?
- **Research question 3:**  
Are the auditor opinions issued based on industry classification?

#### 5. Empirical Findings of the Study

##### 5.1 Most popular Audit reports in Bangladesh

Previous literature found that *Unqualified* audit report is the most common type of audit report issued in any developed countries. Bangladesh is no exception to this. As shown in Table 1, *Unqualified* opinion was the most common type of opinion given by auditors in Bangladesh, ranging from 90.86% (in 2014) to 95.43% (in 2016). Of this number, *Unqualified with EOM* range from 2.69% (in 2014) to 9.72% (in 2018) and *Unqualified with OM* range from 0.91% (in 2016) to 4.15% (in 2015). *Qualified* reports taking 4.57% (in 2017) to 9.14% (in 2014). There is no *Qualified with EOM* and *OM* reports issued in 2014 and 2015. Only 4 (1.83%), 5 (2.55%) and 3 (1.21%) companies received *Qualified with EOM* in 2016, 2017 and 2018, respectively, and only one (0.81%) company received *Qualified with OM* in 2018.

Surprisingly, there is no *Adverse* or *Disclaimer* report issued during this period (2014–2018). We did verify this information and can confirm the data. These findings conclude that, on average, in 93% of cases the auditors have been able to secure sufficient and appropriate evidence to support the financial reports being prepared. They have been done so in accordance with the appropriate accounting framework, relevant corporation legislation and international accounting standards. Expert opinion shed some light on these findings when we interviewed five experts from the top audit firms. All the experts who we interviewed are fellow members of the Institute of Chartered Accountants of Bangladesh, are in practice and have over 30 years' experience doing audits.

Table 1 shows that from 2014 to 2018, *Unqualified* reports with EOM are gradually increasing. This is the period when some major changes happened: introducing the new *Financial Reporting Act* in 2015; adaptation of the new format of auditor's report effective

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from 2018; and probably auditors become more conservative when they issued *Unqualified* reports. Again, the percentage of *Unqualified* opinion was between 80.57% (in 2015) to 88.58% (in 2016).

**Table 1: Types of Audit Opinion Issued in Bangladesh (2014-2018)**

	2014	2015	2016	2017	2018
Unqualified	160	159	194	168	199
	86.02%	82.38%	88.58%	85.71%	80.57%
Unqualified with EOM	5	9	13	12	24
	2.69%	4.66%	5.94%	6.12%	9.72%
Unqualified with OM	4	8	2	7	9
	2.15%	4.15%	0.91%	3.57%	3.64%
Total Unqualified	169	176	209	187	232
	90.86%	91.19%	95.43%	95.41%	93.93%
Qualified	17	17	6	4	10
	9.14%	8.81%	2.74%	2.04%	4.05%
Qualified with EOM	0	0	4	5	3
	0	0	1.83%	2.55%	1.21%
Qualified with OM	0	0	0	0	2
	0	0	0q	0	0.81%
Total Qualified	17	17	10	9	15
	9.14%	8.81%	4.57%	4.59%	6.07%
Adverse	0	0	0	0	0
	0	0	0	0	0
Disclaimer	0	0	0	0	0
	0	0	0	0	0
Total number of audit reports	186	193	219	196	247

### 5.2 Types of reports issued according to the industry in 2014

Table 2 shows that *Unqualified* opinions were issued across the board. We asked veteran auditors about the process of reaching this conclusion. Auditors indicated that this ensures survival for them in the Bangladesh audit industry. The worst opinion they could issue is a *Qualified* opinion. In 2014, banking and financial institution irregularities dominated the media, which explains qualifications in the table. However, both jute and textiles experienced a downward spiral. Jute has been struggling ever since Bangladesh's independence. Textiles faced a new reality in 2014 following the traumatic Rana Plaza collapse in 2013, which explains this industry's Qualification.

**Table 2: Types of reports issued according to industry in 2014**

Industry	Total	Unqualified	Unqualified with EoM	Unqualified with OM	Qualified
Bank	30	27 (90%)	0	1 (3.33%)	2 (6.67%)
Cement	6	6 (100%)	0	0	0
Ceramics	4	3 (75%)	0	0	1 (25%)
Engineering	18	16 (88.9%)	0	0	2 (11.11%)
Financial institutions	19	17 (89.47%)	0	0	2 (10.52%)
Food	10	5 (50%)	1 (10%)	2 (20%)	2 (20%)
Fuel	13	9 (69.23%)	2 (15.38%)	0	2 (15.38%)
Insurance	32	30 (93.75%)	2 (6.25%)	0	0
IT	4	4 (100%)	0	0	0
Jute	2	1 (50%)	0	0	1 (50%)
Miscellaneous	4	4 (100%)	0	0	0
Pharmaceuticals	18	17 (94.44%)	0	1 (5.56%)	0
Textiles	25	20 (80%)	0	0	5 (20%)

Another example of a *Qualified* report is Dulamia Cotton. In 2014, the company was issued with a *Qualified* opinion for charging finance costs to suspended accounts instead of spending over 20,000,000 taka to cover the interest payment owed. Dulamia's executives explained that they were expecting a waiver on interest expenses from its bank, but the bank sued Dulamia according to the company's annual reports, which prompted the auditor to issue a *Qualified* opinion. In 2014, Dacca Dyeing Ltd. received a *Qualified* opinion because it did not reveal depreciation expenses and there were other irregularities. *Qualified* opinion ought to be treated as a severe warning if one looks at the *Qualified* opinion given to ICB Islamic Bank by its auditor. ICB Islamic bank grew out of a troubled bank named Oriental Bank, but it carried the burden of paying the latter's debts and was never able to function properly as a bank.

If we look at the history, in 2006, Bangladesh Bank appointed an administrator to run Oriental Bank. Bangladesh Bank later sold this bank to a Swiss holding group named ICB in a tripartite agreement. This Swiss group took over the troubled bank and repackaged its name as ICB Islamic Bank, and then sold it in 2010. ICB Islamic Bank was delisted from Dhaka Stock Exchange in 2010, but the worst opinion it ever received from auditors was *Qualified* throughout its existence and finally an *Unqualified* with EOM in 2018. This is in effect a bankruptcy warning. The ICB Islamic Bank still exists but it was delisted from the DSE. In 2014, Premier Bank received a *Qualified* opinion because of a 33 crores taka tax case pending in the High Court. The bank did not report its VAT expenses. Monno Ceramic Industries Ltd. received a *Qualified* opinion because it did not account for approximately 4.5 crore taka worth of depreciation expenses, resulting in an overstatement of profit and earnings per share. In the engineering industry, Anwar Galvanizing Ltd. did not report its deferred tax and did not have sufficient funds to pay dividends to shareholders, resulting in a *Qualified* opinion.

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In the food industry, Beach Hatchery Ltd. received advances without any provision, did not pay or reschedule taka 3 crore worth of loans to Krishi Bank, and did not pay taka 2 crore worth of taxes, resulting in a *Qualified* opinion. Fu-Wang Foods Limited was issued a *Qualified* opinion because it did not prepare a consolidated statement for one of its subsidiaries, specifically Fu-Wang Beverage even when it had 99% ownership of that subsidiary. Khulna Power Ltd. adjusted Foreign currency earnings, which resulted in a *Qualified* opinion because this practice was a departure from the Bangladesh *Financial Reporting Standards (BFRS)*. Missing registration papers for property, plant and equipment, movement of inventories, the addition of exchange rate loss to property, plant and equipment, and unfunded gratuity are among the serious issues that led to the Qualification given to Power Grid Company Bangladesh Ltd. Violation of the revenue recognition principle, exclusion of substantial amounts of deferred tax, non-confirmation of accounts receivable and misallocation of customer security deposits led to the Qualification audit finding for Titas Gas in 2014.

Referring to Jute Spinner Limited Company, several issues led to the *Qualified* audit report given to this business. The company violated the Company Act 1994 by giving substantial advances to directors. Also, the company transferred approximately 4 crore taka as a gratuity from its workers' profit participation (WPP) fund, which understated the amount in the WPP. The company did not document any of its foreign currency gains or losses. The company had a going concern issue due to approximately taka 8 crore net loss, and the gratuity was unfunded by a substantial amount.

**Table 3: Types of reports issued according to industry in 2015**

Industry	Total	Unqualified	Unqualified with EoM	Unqualified with OM	Qualified
Bank	30	28 (93.33%)	0	0	2 (6.67%)
Cement	5	5 (100%)	0	0	0
Ceramics	5	5 (100%)	0	0	0
Engineering	19	18 (94.74%)	0	0	1 (5.26%)
Financial institutions	21	18 (85.71%)	1 (4.76%)	0	2 (9.52%)
Food	10	3 (30%)	2 (20%)	3 (30%)	2 (20%)
Fuel	18	13 (72.22%)	2 (11.11%)	1 (5.56%)	2 (11.11%)
Insurance	38	32 (84.21%)	4 (10.53%)	0	2 (5.26%)
IT	4	4 (100%)	0	0	0
Jute	2	1 (50%)	0	0	1 (50%)
Miscellaneous	1	1 (100%)	0	0	0
Pharmaceuticals	18	12 (66.67%)	0	4 (22.22%)	2 (11.11%)
Textiles	23	20 (86.96%)	0	0	3 (13.04%)

Table 3 shows there are only a few modified opinions issued across companies listed on the Dhaka Stock Exchange. In 2015, more DSE-listed companies received *modified audit reports* in various industries. We contend that irregularities were so extreme that auditors had to modify their opinions in rare cases across the sectors. Interestingly, our interview (Interview 1) with a 40-year industry veteran can only modify opinion in extreme cases and never consider giving a DSE-listed company an adverse or *Disclaimer opinion*. In 2015, Fu-Wang Foods received a *Qualified* opinion despite

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auditors discovering several irregularities. Fu-Wang Foods owns 99% of the subsidiary Fu-Wang Beverage, but its consolidated financial statement was not prepared according to the Company Act 1994 and BAS 27, which prompted the auditor to issue a *Qualified* opinion in 2015. ICB Islamic Bank was issued a *Qualified* opinion due to the detection of a 50% gratuity funding. Anwar Galvanizing Ltd. was issued a *Qualified opinion* by auditors for the same reasons in 2014, in that it had insufficient funds to pay dividends. Beach Hatchery received a *Qualified report* again for the same reasons in 2014. Khulna Power Ltd. and Titas Gas were both issued a *Qualified opinion* by auditors in 2015 for the same reason in 2014 as described above. Auditors emphasised in the matter paragraph that Central Insurance Co. Ltd. did not comply with proper management of the WPP fund. Eastern Insurance was issued a *Qualified opinion* for unfunded gratuity and overstated profit. Jute Spinners Ltd. was issued a *Qualified opinion* for not complying with the WPP fund rule.

**Table 4: Types of reports issued according to the industry in 2016**

Industry	Total	Unqualified	Unqualified with EoM	Unqualified with OM	Qualified	Qualified with EoM
Bank	29	28 (96.55%)	0	0	1 (3.45%)	0
Cement	6	6 (100%)	0	0	0	0
Ceramics	5	5 (100%)	0	0	0	0
Engineering	20	20 (100%)	0	0	0	0
Financial institutions	22	18 (81.82%)	2 (9.09%)	0	0	2 (9.09%)
Food	10	6 (60%)	2 (20%)	0	1 (10%)	1 (10%)
Fuel	18	14 (77.78%)	2 (11.11%)	1 (5.56%)	1 (5.56%)	0
Insurance	44	41 (93.18%)	2 (4.55%)	0	1 (2.27%)	0
IT	6	5 (83.33%)	1 (16.67%)	0	0	0
Jute	1	1 (100%)	0	0	0	0
Miscellaneous	4	4 (100%)	0	0	0	0
Pharmaceuticals	19	17 (89.47%)	0	1 (5.26%)	0	1 (5.26%)
Textiles	35	29 (82.86%)	4 (11.43%)	0	2 (5.71%)	0

In 2016 there were fewer banks than in 2015, and only one bank received an opinion with modification. Premier Bank was issued a *Qualified opinion* for not deducting VAT on office rent. One out of two banks receiving the Qualification in 2015 disappeared in 2016, which shows us that modification of opinion as a Qualification is a severe warning in Bangladesh. However, modifications of opinion fell from 2015 to 2016, but some companies received a *Qualification with an emphasis of matter* paragraph. This is significant because this means that companies might disappear in the future because this is the worst kind of audit. In 2016, Bangladesh Industrial Finance Limited and First Finance Limited were both issued *Qualified with EOM* as opinion. These opinions were significant because the embattled PK Halder was director of these financial institutions. Halder was charged with money laundering offences to the tune of 2,500,000,000 taka from different financial institutions in Bangladesh. Here again it should be emphasised

that a *Qualified* opinion means a severe warning on the Dhaka Stock Exchange because auditors issue this opinion only in rare instances, and they do not issue an

*Adverse or Disclaimer of opinion.*

However, looking at the aggregate claims that arose against Bangladesh Industrial Finance Corporations, 71% loans and leases were written off, hundreds of crore taka worth of deferred taxes were not calculated, did not satisfy liquidity requirements, there were no audit committee meetings, violation of Institutional Act – 1993. Beach Hatchery Ltd. and Eastern Insurance were again issued a *Qualified opinion* for the same reason in 2014 and 2015. Power Grid Company of Bangladesh was issued a *Qualified opinion*, based on the auditor's six qualifying points. These qualifying points were as follows:

- The carrying amount of Plant Property and Equipment (hereafter, PPE) amounting to 85,368,136,099 register was not maintained properly. The company never performed impairment tests for PPE, and no policy regarding impairment was found.
- The inventory register was not maintained properly. Approximately 200M taka worth of inventories were nonexistent, according to the auditors.
- 857,867,261 taka worth of disputed amount with Dhaka Power Distribution Company Ltd (hereafter, DPEC) and 274,407,626 worth of disputed amounts with Dhaka Electric Supply Company Limited (hereafter, DESCO) were not documented, which resulted in overstatement of earnings per share and net asset value.
- Net income was overstated by 1,100,215,757 since the effects of foreign exchange rates were not recognised as a loss.
- Auditors could not verify the loan amount of 4,339,480,698 Bangladesh Power Development Board (hereafter, BPDB) to BPDB.
- The company had an unfunded gratuity.

The aggregated total amount of qualification points is material enough for an adverse opinion, but the company was issued a *Qualified* opinion by its auditors. We interviewed veteran chartered accountants who confirmed that accounting firms in Bangladesh do not give Adverse Opinion or *Disclaimer of opinions* to DSE-listed companies.

**Table 5: Types of reports issued according to the industry in 2017**

Industry	Total	Unqualified	Unqualified with EoM	Unqualified with OM	Qualified	Qualified with EoM
Bank	30	27 (90%)	1 (3.33%)	1 (3.33%)	1 (3.33%)	0
Cement	7	7 (100%)	0	0	0	0
Ceramics	5	5 (100%)	0	0	0	0
Engineering	27	27 (100%)				
Financial Institutions	22	16 (72.73%)	3 (13.67%)	1 (4.55%)	0	2 (9.09%)
Food	11	9 (81.82%)	2 (18.18%)	0	0	0
Fuel	18	13 (72.22%)	1 (5.56%)	2 (11.11%)	1 (5.56%)	1 (5.56%)
Insurance	43	37 (86.05%)	3 (6.98%)	2 (4.65%)	1 (2.33%)	0
IT	5	4 (80%)	1 (20%)	0	0	0
Jute	1	1 (100%)	0	0	0	0
Miscellaneous	6	5 (83.33%)	0	0	1 (16.67%)	0
Pharmaceuticals	21	17 (80.95%)	1 (4.76%)	1 (4.76%)	0	2 (9.52%)
Textiles						

In 2017, ICB Islamic Bank was issued a *Qualified opinion* for the same reason it was given a Qualification from 2014 through 2016. Power Grid Company of Bangladesh L was issued a *Qualified opinion* by auditors, and auditors gave six qualification points which are as follows:

- The carrying amount of PPE is Tk 113,398,236,005, and the inventory register was not maintained properly. 71% of the company's assets were unverified. The company never performed impairment tests for PPE, and no policy regarding impairment was found.
- BDT 93,162,942 went unreported in the financial statements. The inventory register was not maintained properly. Physical verification of inventories could not be done by auditors.
- The company was unlikely to recover BDT 2,708,645,728 from transmission/wheeling and optical fibre charges, which resulted in an overstatement of earnings per share and net asset value.
- Net income was overstated since the effects of foreign exchange rates worth BDT 739,548,745 were not recognised as a loss.
- Auditors were unable to verify the loan amount of BDT 1,705,943,235 to BPDB from BPDB.
- The company had an unfunded gratuity.

Here, the aggregated total amount of qualification points is material enough for an adverse opinion, but the company was issued a *Qualified opinion* by its auditors. We interviewed veteran chartered accountants (Interviews 2 and 3) who confirmed that

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accounting firms in Bangladesh do not give Adverse or *Disclaimer of opinions* to DSE-listed companies.

Dhaka Insurance was issued a *Qualified opinion* due to non-compliance with worker profit participation fund and improper land evaluation. GQ Ballpen was issued a *Qualified opinion* because there was a carry forward deposit of 99-million-taka worth of investments for three consecutive years.

**Table 6: Types of reports issued according to the industry in 2018**

Industry	Total	Unqualified	Unqualified with EoM	Unqualified with OM	Qualified	Qualified with EoM
Bank	28	27 (96.43%)	1 (3.57%)	0	0	0
Cement	5	5 (100%)	0	0	0	0
Ceramic	5	4 (80%)	0	0	1 (20%)	0
Engineering	30	30 (100%)	0	0	0	0
Financial Institutions	18	17 (94.44%)	0	0	0	1 (5.56%)
Food	9	7 (77.78%)	2 (22.22%)	0	0	0
Fuel	15	9 (60%)	1 (6.67%)	3 (20%)	1 (6.67%)	0
Insurance	35	30 (85.71%)	2 (5.71%)	0	3 (8.57%)	0
IT	8	7 (87.5%)	1 (12.5%)	0	0	0
Jute	1	1 (100%)	0	0	0	0
Miscellaneous	6	5 (83.33%)	0	0	0	1 (16.67%)
Pharmaceuticals	26	21 (80.77%)	2 (7.69%)	0	2 (7.69%)	1 (3.84%)
Textile	45	33 (73.33%)	10 (22.22%)	1 (2.22%)	1 (2.22%)	0

In 2018, Standard Ceramic Industries Ltd. was issued a *Qualified opinion* because it gave a 2% cash dividend but had negative retained earnings. Bangladesh Industrial Finance Corporation was issued a *Qualified with EOM* opinion because it had a going concern issue. Most of this corporation's problems were tied to the actions of Prashanto Kumar Howlader, who stole 10,200 crore taka from this corporation and he fled Bangladesh. The auditor issued MJL BD Ltd. a *Qualified opinion* due to non-compliance with the WPP rule. Power Grid Company of Bangladesh Ltd. was issued a *Qualified opinion* by auditors who gave five qualification points as described here:

- The carrying amount of PPE amounted to BDT 115,120,606,842, and the inventory register was not maintained properly. 57.52% of the company's assets were unverified. The company never performed impairment tests for PPE, and no policy regarding impairment was found.

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- Inventory worth BDT 579,682,808 was unrecorded in financial statements, and the inventory register was not maintained properly. Physical verification of inventories could not be done by the auditors.
- The company is unlikely to recover BDT 3,235,740,095 from transmission/wheeling and optical fibre charges, which resulted in an overstatement of earnings per share and net asset value.
- Net income was overstated since the effects of foreign exchange rates worth BDT 2,027,402,595 were not recognised as a loss.
- The company had an unfunded gratuity.

In 2018, Titas Gas was issued a *Qualified* opinion and auditors delivered five qualification points which are as follows:

- Long-term liability included a security deposit of 1520 crores taka, which could not be verified by auditors.
- Actuaries valued pensions at Taka 160 crores, but only 50 crores were documented.
- Auditors undertook a cut-off test and found 2012 worth of gain worth 45 crores taka was recorded in 2018.
- Approximately taka 80 crore worth of penalty interest and meter rent charges were in doubt.
- Take 2 crore worth of transmission expenses revealed countless illegal connections compromised the revenues earned by Titas Gas.

We will report again that the aggregated total amount of qualification points is material enough for an adverse opinion, but the company was issued a *Qualified opinion* by its auditors. We interviewed veteran chartered accountants who confirmed to us that accounting firms in Bangladesh do not give adverse or Disclaimer of opinions to DSE-listed companies.

Dhaka Insurance was issued a *Qualified opinion* because its gratuity was underfunded and 8 million taka was spent on unjustified managerial expenses. Prime Life Insurance Co. Ltd. was issued a *Qualified opinion* because up to taka 5 crore worth of receivables could not be verified by auditors.

### **5.3 Types of reports issued by audit firms**

The world's three of the Big 4 audit firms have presence in Bangladeshi. They are KPMG, Deloitte and Ernst & Young. KPMG's member firm in Bangladesh is Rahman Rahman Huq & Co., while Deloitte's member firm is NUFHAS and Ernst and Young's member firm is A Qashem & Co. PWC does not do auditing in Bangladesh but does run a consultancy practice.

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**Table 7: Types of reports issued by Big 4 Associated Local Audit Firms**

Big Four Audit Firms	Local Affiliated Audit Firms	Total Audit Reports	Unqualified	Unqualified with EOM	Unqualified with OM	Qualified	Adverse	Disclaimer
<b>Year 2014</b>								
PWC	PWC Private Ltd.	0	0	0	0	0	0	0
KPMG	Rahman Rahman Huq & Co.	6	6 (100%)	0	0	0	0	0
EY	A. Qasem & Co.	7	7 (100%)	0	0	0	0	0
Deloitte	NUFHAS	0	0	0	0	0	0	0
<b>Year 2015</b>								
PWC	PWC Private Ltd.	0	0	0	0	0	0	0
KPMG	Rahman Rahman Huq & Co.	7	4 (57.14%)	0	3 (42.86%)	0	0	0
EY	A. Qasem & Co.	7	7 (100%)	0	0	0	0	0
Deloitte	NUFHAS	0	0	0	0	0	0	0
<b>Year 2016</b>								
PWC	PWC Private Ltd.	0	0	0	0	0	0	0
KPMG	Rahman Rahman Huq & Co.	8	6 (75%)	2 (25%)	0	0	0	0
EY	A. Qasem & Co.	12	11 (91.67%)	0	0	1 (8.33%)	0	0
Deloitte	NUFHAS	0	0	0	0	0	0	0
<b>Year 2017</b>								
PWC	PWC Private Ltd.	0	0	0	0	0	0	0
KPMG	Rahman Rahman Huq & Co.	7	4 (57.14%)	2 (28.57%)	1 (14.28%)	0	0	0
EY	A. Qasem & Co.	11	10 (90.91%)	0	0	1 (9.09%)	0	0
Deloitte	NUFHAS	0	0	0	0	0	0	0
<b>Year 2018</b>								
PWC	PWC Private Ltd.	0	0	0	0	0	0	0
KPMG	Rahman Rahman Huq & Co.	8	5 (62.5%)	1 (12.5%)	1 (12.5%)	1 (12.5%)	0	0
EY	A. Qasem & Co.	12	9 (75%)	1 (8.33%)	1 (8.33%)	1 (8.33%)	0	0
Deloitte	NUFHAS	0	0	0	0	0	0	0

Big 4 member firms cannot compete with second-tier and small audit firms on price. However, the Big 4 are free to audit DSE-listed companies that have diversified portfolios. They cannot accept a client on competitive bidding because of the independence issue. If they were to accept a client at a lower price, they will then be

violating the independence of their parent company. This is why the number of companies audited by Big 4 in Bangladesh are limited.

Big 4 audit firms in Bangladesh rely on actuaries from India to do valuation work for insurance companies. Bangladesh does not have skilled actuaries. Like local audit firms that do work for DSE-listed companies, member firms do not issue Disclaimer or adverse opinion. Instead of a Disclaimer, they prefer to withdraw from the engagement and ask clients to find a "suitable" auditor who may compromise on quality. An interview with one audit manager (interview 4) of one of the Big 4 firms confirmed that this did happen at one audited firm he did work for. The firm withdrew from the engagement. Interestingly, we found this Bangladeshi practice unusual because there is a general difficulty in issuing an *Adverse* or *Disclaimer opinion*.

## 6. Conclusion

This paper provides some insights into auditing practices in a developing country, Bangladesh. First, it provides an understanding of the most common kind of audit report issues. Interestingly, we failed to find any audit firm that issued any disclaimer or adverse audit report in our sample period, 2014–2018. We explored this industry by industry and found some clear cases where the auditor could issue a *Disclaimer* or *Adverse* report, but only a *Qualified* report emerged. We interviewed expert practicing auditors and surprisingly found it is a common practice in Bangladesh to not issue any adverse or Disclaimer report. Instead, it is left to the company to find a suitable auditor who might be willing to compromise on quality. Also, we explore how many of these listed companies do business with the Big 4 audit firms and interestingly, only 5% of the listed companies are audited by the Big 4. Interview data reveals that because of the international connections of the Big 4 firms and price competitiveness, Big 4 audit firms are reluctant to check the financials of Bangladeshi companies.

If the auditor was to issue an adverse or Disclaimer, they lost clients. Also, the realities of Bangladesh do not allow them to issued an audit modified opinion in the form of an *Adverse* or *Disclaimer*. According to these expert opinions, it is difficult for them to issue a modified opinion as a Qualification to listed companies because of stakeholder pressure. According to experts, journalists could report these modifications, or others could leverage modified opinions that are connected to the BSE. Stakeholder pressure makes even the issuing of a *Qualified* opinion difficult.

Another reality that affects issuing an opinion in Bangladesh is a selection of auditors at the Securities Exchange Commission (SEC) and how it views the role of auditors. When we looked at the SEC lists of audit firms, it is apparent that veteran audit firms are competing with new auditing firms for clients, which we found relevant because it affects opinions issued to listed companies in Bangladesh. If a veteran auditing firm is unwilling to issue a preferred opinion for clients, then the latter can switch to more affable auditors because the SEC does not have any benchmark guidelines for auditors to adhere to.

We also believe the number of competent qualified and unqualified audit staff also affects the integrity and quality of audit opinion in Bangladesh. ICAB (Institute of Chartered Accountants of Bangladesh) is the highest authority determining qualified and unqualified skilled auditors. An *Unqualified* competent auditor is a high school graduate

or HSC passed student who received admission into the ICAB and can start working with an accounting firm. He or she will be qualified if he or she can pass three levels of education. For levels 1 and 2, he or she will have to pass knowledge level 1 subjects and application-level 2 subjects. Finally, that individual will have to pass four subjects and complete three years of training with an audit firm to become a *Qualified*, competent chartered accountant. According to the ICAB President, 25,000 students were able to complete training and obtain a CA-CC certification in the last 50 years. However, only 1800 were able to pass the requirements set by ICAB, adopted from ICAEW of the United Kingdom. As a result, Bangladesh has just over 1800 qualified chartered accountants. It is a minuscule number of auditors in Bangladesh given its population, even though it is fairly easy to get into the auditing industry.

The ICAB needs to reconsider its 3-year training requirement and stop giving CA-CC certification to students. Educational requirements need to be broadened but also tightened up, and only higher educated accounting and financial academicians and professionals should be allowed to work in the profession. This can be done by providing exemptions in education requirements. SEC needs to seriously review its selection criteria for auditors and select a rigorous benchmark. Finally, it needs to encourage auditors to exercise their independence if they are to their jobs honestly and produce high quality audits.

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**Appendix: Demographic Profile of Interviewees**

<b>Interview Demography</b>	<b>Sample</b>	<b>Percentage</b>
No. of interviewees	5	
Age group (years)	40-67	
Number of years of experience	a. One to Five years	0 (0%)
	b. Six to Ten years	0 (0%)
	c. Eleven to Fifteen years	1 (20%)
	d. Sixteen to Twenty years	1 (20%)
	e. Twenty-one to Twenty-five years	3 (60%)
	f. Twenty-six and more years	