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A STUDY ON THE LEVEL OF PERCEPTION AND USEFULNESS OF AUDITED FINANCIAL STATEMENT AND ANNUAL REPORTS AMONG INVESTORS IN INDIA

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ABSTRACT

Analytical procedures have become an increasingly important part of financial statement auditing and have received significant attention in the Auditing literature. The use of Analytical procedures is prescribed by auditing standards at both the planning and conclusion stages of the audit. This study describes how auditors perform analytical procedures at perception audit in financial reporting. I conducted an experiment in which subjects performed analytical procedures and answered the questions. This study analyzes the decision effectiveness of audit reports in, Mysore city. The sample respondents were selected from this city to enquire into the perceptions of respondents towards the effectiveness auditing information in their investment decisions in view of the city having heterogeneous, economic, social and cultural environment, which represents the country adequately. The empirical results have been presented under Universal findings. The major findings were evidenced with regard to the effectiveness of audit report.

KEYWORDS: *Financial Statements, Standards, Effectiveness, Audit Reports.*

INTRODUCTION

The cost and benefit of a system of audited accounting information is potentially affected by officially established accounting and audit reporting rules and rules governing sufficiency of audit. Various theories have been proposed to explain accounting standards, It has suggested that accounting principles boards members chase accounting rules based on the preference of the member's firm's major clients [Wheat (1972), Rockness and Nikolai (1977). Also, it has been

argued that corporate management lobby in support of accounting rules that benefit management [Watts and Zimmerman (1978) andHorngren (1973). Similarly, there have been charges that big and auditing firms dominate auditing standards setting [U.S. Congress (met call report) (1976)].

In this paper we explore the perception on audit report in auditing firm preferences and voting patterns for recent auditing and reporting issues considered by auditing standards board (ASB). The perceptions regarding are auditing of firms commonly selected together (or express the same preference) on seemingly divers issues We propose high theory and low theory to explain the observed selected perception pattern. In particular, we hypothesize that firms perceptions audit are the functions of their use of structured technology.

For the period studied, a relative perception measure is associated with preference for proposed statements and size of the firm. This result is consistent with the proposed technology-based annual report theory for user financial reporting.

LITERATURE REVIEW

In United States of America (USA), prior research in this area has been conducted mainly by Brenner (1971), Epstein (1975), Chang and Most (1985), Epstein and Pava (1993). Brenner (1971) found that 96.9% of his respondents (American investors) read financial reports, but that only 93.8% had read them in the year prior to his survey. With regard to the various statements within the annual report, the income statement was the item that was most carefully read by his respondents, followed by the statement of the enterprise's financial position. When they were asked to respond with regard to the usefulness of financial statements, 80.37% of the respondents agreed with the statement. Epstein's (1975) sample of 1 766 shareholders indicated that only 15% of his respondents relied on the annual report as the primary basis for their investment decisions, whereas 48.8% relied on the advice of stockbrokers. The income statement was the item the respondents read most thoroughly, as well as the item they found most useful for investment purposes. Only 14.1% of the sample found annual reports very useful for investment decisions, 46.7% thought that the annual report was moderately useful, and 18.8% and 26.4% respectively found such reports to be of little or no use. Epstein thus concluded that corporate annual reports were not useful to shareholders in investment decision-making. Chang and Most (1985) and Hawkins and Hawkins (1985) found that even though individual investors did not consider the annual report particularly useful in decision-making, and felt that it did not meet their information needs, they did read the annual report more thoroughly than any other source of information. Epstein and Pava (1993) expanded on the work of Epstein (1975) and found that the annual report as a source of information had increased in importance. Furthermore, they found that the importance of the balance sheet had increased, and that over the same period the perceived usefulness of the income statement had declined.

FINANCIAL REPORTING AND REGULATION

Very few economic and social activities escape regulation of one kind or the other and the scope of regulatory activity provides no easy definition. The case for reporting regulation scheme form the failure of market economy and it is considered a public good, which needs regulation. Regulation of financial reporting is also intended to provide investor protection. Added to this, Ross [1965] observes that development in regulations have come about in response to scandals failures perpetuated through wrong financial reporting. The regulation of financial reporting may be

undertaken mainly in three different ways. Firstly, a government may adopt a prescriptive approach by which detailed principles, rules and procedures laid down and enforced by law. Secondly, government may establish less defined rules and private sector bodies may develop detailed rules, which are to be observed by the profession as additional regulations. Lastly, legal regulations may provide only general requirements and private regulatory bodies are expected to assist in their interpretation. In fact, the financial reporting regulation falls into this third category in majority of the countries in the sense that the broad framework of financial reporting is provided under regulation in terms of format and contents of financial statements and detailed rules of measurement and valuation are left to be established by the accounting profession itself through its independent judgment. In this regard, Flint [1982] observed. In such circumstances, much reliance is placed, either explicitly or by default, upon the independent judgment of those qualified by training and experience to conform that, within the legal and social framework, financial reports follow the general requirement prescribed by law. As a result, financial reporting has traditionally relied on a general framework prescribed by law and the judgment by the professionals. To meet the needs of increasingly large-scale industrial enterprises subjected to rapid technological changes, external finance became more important. With the development of Joint Stock Company a new group of people having an interest in the affairs of the enterprises emerged, namely shareholders. Management and ownership were divorced and financial statements became the important vehicle of information to actual and potential shareholders. More recently, the position of, for example, members of an enterprise's work force has been recognized as more skin to that of stake-holders than employees. As a result of the emergence of new classes of users of financial information, new categories of transactions have also emerged and with them new accounting problems.

USER NEEDS OF ANNUAL REPORT

Joshi and Abdulla (1994) emphasized that information requirements of users of annual reports should be recognized by companies. The authors analyzed 157 responses received from 'sophisticated investors' and 55 responses from 'non-sophisticated' investors, residing in Bombay, India. Sophisticated investors refers to professional chartered accountants-cum-investors and accounting teachers-cum-investors and 'non-sophisticated investors' refers to other investors. It was found that the responses of both the groups ranked value added statement and cash profit per share as very significant. Indian companies did not use to disclose these two information items in that time. However, significant differences have been observed with regard to information requirements of 'sophisticated investors' and 'non-sophisticated investors' relating to 37 items in financial statements.

The issue of users' needs in annual reports has been addressed by Stanga (1976) as well. The author analyzed 275 completed questionnaires received from Chartered Financial Analysts (CFAs) in order to rank 79 information items by taking the significance level assigned by these respondents as the basis. Then, the author examined the annual reports for the fiscal periods ending from October 31, 1972 through September 30, 1973 of 80 companies from "Fortune 1,000" to investigate as to whether these annual reports contain those information considered significant by the respondents. The author suggests that there were deficiencies in the published annual reports of large industrial firms. Secondly, differences in size of companies did not appear to be related in explaining the differences in annual report disclosure among large industrial firms. Finally, the industry variable played a relatively significant role in helping to explain the differences in the extent of annual report disclosure among large industrial firms Cook and Sutton (1995) stresses on the fact that companies

should focus on the information requirements of shareholders so that the annual report satisfies their needs. Preparing summary annual reports rather than engaging into information overload by providing a detailed annual report can satisfy their needs. Hence, companies should disclose main pieces of information in a clear and understandable format in a summary annual report that will increase the relevance and value of shareholder communication.

OBJECTIVE

1. To analyze audit perception of financial reporting.
2. To survey auditing report in annual report.

HYPOTHESES

The high perception on audit report is more important than low perception on audit report to enhance decision usefulness of annual reports.

METHODOLOGY OF THE STUDY

In this study the primary data were gathered from 200 respondents who represented the top, middle and lower levels of corporate investors of Mysore city India through structured questionnaires. Secondary data is data has also been collected from books, articles and research reports.

The population of this research study consists of all investors in India but we choose investors of Mysore city as a sample respondents south of India. In this study the researcher uses random sampling and Cochran formula select suitable sample size. According to this formula, the research design is based on Likert view point scale and research statistic is based on Morgan table.

$$n = \frac{z^2 pq}{e^2} = \frac{(1.96)^2 (0.5)(0.5)}{(0.07)^2} = 196$$

ANALYSIS AND INTERPRETATION

TABLE 1.PERCEPTIONS ON AUDIT REPORT

Items	Frequency Distribution and Weightage					Total	MV	SD
	Strongly disagree 1	Disagree 2	Neither 3	Agree 4	Strongly agree 5			
Usefulness of auditors report on directors report	22	64	32	2	80	200	3.27	1.51
Auditors non independence due to client retention motive	10	54	50	84	2	200	3.07	0.96
Audit reports to cover directors responsibilities	2	116	72	8	2	200	2.46	0.64
Qualified opinions as adverse audit opinions	2	114	76	8	0	200	2.45	0.60
Scope for auditors to enforce true and fair view	2	125	64	9	0	200	2.40	0.59
Elusive nature of audit opinion	6	130	58	6	0	200	2.32	0.58
Auditor's non independence due to pressure by management	14	148	36	2	0	200	2.13	0.52
Auditors rotation improving audit quality and independence	26	164	10	0	0	200	1.92	0.46

Inadequate communicationof audit findings	75	120	5	0	0	200	1.65	0.35
Total	17.67	115	44.78	13.22	9.33	200	2.40	0.69

BASIS OF ASSIGNMENT OF WEIGHTAGE POINT.

Strongly disagree = 1

Disagree = 2

Neither = 3

Agree = 4

Strongly agree = 5

$\mu_{ij}=\frac{j}{N}\times p_{ij}(1\leq i \leq 9,\ 1\leq j\leq 5)$

$\mu'_i = \sum_{j=1}^{5} \mu_{ij}(1\leq i \leq 9,\ 1\leq j \leq 5)$

$\mu=\frac{\sum_{i=1}^{9}\mu'_i}{9} = 2.40 \qquad (1\leq i \leq 9)$

$SD_{ij} = (j- \mu'_i)^2\times p_{ij}(1\leq i \leq 9,\ 1\leq j \leq 5)$

$SD'_i=\sum_{j=1}^{5} SD_{ij} \qquad (1\leq i \leq 9,\ 1\leq j \leq 5)$

$SD_i = \sqrt{\frac{SD'_i}{N}}(1\leq i \leq 9)$

μ_{ij}=average per home of answer respondents.

μ'_i = average per item of perceptions.

j = Likert view point scale for per answer.

i = items (perceptions).

N =total respondent.

P_{ij} =answer respondent for per item of μ_{ij}.

μ=total mean ofnine items.

SD_i=standard deviation per item of perceptions.

The audit report is one of the components of financial reporting. In the background of the highest importance perceived by the respondents on notes and significant policies and auditors report as evidenced in -depth analysis of the perceptions by the respondents on the annual report have been presented in Table 1 covering nine statements.

It was interesting to note that the various perceptions on audit report were assigned a moderately high perceptions and low perceptions were evaluated based on the standard mean values as 2.40. The perception level an five items on audit report were higher than 2.40, that called high perceptions statements and perceptions on 4 items of audit report were lower than 2.40 that called low perception statements. The first high perception is Usefulness of auditors report on directors report by assigning highest mean value of 3.27, that was the first important item of the perception ranked by the respondents on the annual report. The second high perception item was Auditors non independence due to client retention motive by assigning mean value of 3.07. The third high perception value item was Audit reports to cover directors responsibilities by assigning mean value of 2.46. The fourth high perception was Qualified opinions as adverse audit opinions by assigning mean value of 2.45. The fifth high perception was Scope for auditors to enforce true and fair view by assigning mean value of 2.40. The moderately low mean value 2.40 are considered as low perception. The first low perception item was Elusive nature of audit opinion with a mean value of 2.32. The second low perception item was Auditor's non independence due to pressure on management by assigning a mean value of 2.13. The third low perception item was Auditors rotation to improve audit quality and independence by assigning mean value of 1.92. The fourth low perception was inadequate communication of audit findings by assigning a mean value of 1.65.

CONCLUSION

Annual reports are important in financial reporting and audit report has its effect in annual reports. It enhances the decision usefulness of annual reports.In this research the researcher tries to find level importance of investor perceptions in audit reports of annual statements.In this study we surveyed 9 items to study the level of investor perceptions and found that 5 items has high perceptions levels and 4 items has low perceptions level in decision usefulness of annual report among all level of investors.

SUGGESTIONS

1. The corporations have experienced certain advantages and limitations with respect to adoption ofhealthy and progressive perception on audit reports practices.

2. The annual reports has to rise to the occasion and perfect perception on audit reports would benefitthe users a lots to take the right decisions.

3. The perception on audit reports in annual reports needs actively articulate of for an improved andconsistent information users. It should be based on the experience of the auditors, and the auditorsmust deliver it to their staff and to this approach in this profession.

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