Received 4 November 2021
Revised 19 April 2022
20 June 2022
Accepted 27 July 2022

Disclosure of key audit matters (KAMs) in financial reporting: evidence from an emerging economy

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Abstract

Purpose – The new audit regulation for disclosure of key audit matters (KAMs) in financial reporting has been introduced in both developed and developing countries. This study investigates the influence of three distinctive sets of variables, namely industry features, firm characteristics and auditor attributes, on the extent, pattern and level of disclosure of KAMs by companies listed in Bangladesh, an emerging economy.

Design/methodology/approach – The study uses qualitative and quantitative research approaches to investigate the pattern of disclosure of KAMs and their determinants. With a sample of 447 firm-year observations from companies listed on the Dhaka Stock Exchange over 2018–2020, the study reveals industry-level, firm-level and auditor-specific characteristics that affect KAMs' communication in the new audit reporting model.

Findings – The findings suggest that significant differences exist between firms in the number and types of KAMs reported and the extent of their disclosure. The study findings also observed variations both within and across different industry sectors. Highly regulated firms disclose a greater number of KAMs, while environmentally sensitive firms are found to provide a greater detail of the issues presented as KAMs. Further, both firm size and age positively impact the number of KAMs disclosed and the extent of the disclosure provided. Big-4-affiliated auditors do not issue a significantly higher number of KAMs but deliver extensive details to their KAMs description, compared to non-Big-4 auditors. In addition, while auditors, in general, tend to issue boilerplate KAMs, Big-4 associates are found to disclose more new KAMs. However, audit fees and auditor rotation do not influence KAMs disclosure.

Research limitations/implications – This study is based on two years of publicly available data. However, future studies could consider in-depth interviews to explore the motivation behind KAMs' disclosure in Bangladesh and other developing countries with similar cultural and contextual values.

Practical implications – These findings have substantial policy considerations for improving firms' audit quality and, thus, their financial reporting quality, with implications for national and international standard-setters, regulators and other stakeholders.

Originality/value – This study is one of the earliest endeavours to investigate KAMs in a context of an emerging country, such as Bangladesh, which adopted KAMs' disclosure in 2018.

Keywords Financial reporting regulation, International standard on auditing (ISA) 701, Key audit matters, Emerging economy, Bangladesh

Paper type Research paper

Journal of Accounting in Emerging Economies
Vol. 13 No. 3, 2023
pp. 666-702

2042-1168
DOI 10.1108/JAEE-11-2021-0355

The authors thank Associate Editor Venancio Tauringana and two anonymous referees for helpful comments and constructive suggestions.

1. Introduction

Recent reforms to the external auditing report worldwide require firms to disclose more information to increase transparency and establish confidence in their financial reporting among stakeholders before making the investment decisions (Rautiainen *et al.*, 2021). The audit report's content, structure and formulation have generated an intensive discussion amongst auditing practitioners, academics, investors and other stakeholders (Brasel *et al.*, 2016). Concerns have arisen about the adequacy of the standard audit report and, specifically, whether it is still fit for demonstrating the transparency of the state of clients' affairs. Standard audit reports have also received extensive condemnation as they lack a message about the audit scope (Carnegie, 2014). Moreover, critics have argued that the standard audit report was not sufficiently informative and that it overlooked information about how the audit was conducted (Asare and Wright, 2012). Thus, both standard-setters and researchers have argued that more information must be disclosed about the audit process to regain public confidence in the report (Gray *et al.*, 2011). Consequently, the global standard-setting body, the International Auditing and Assurance Standards Board (IAASB), has calibrated some extant standards and issued a new International Standard on Auditing (ISA) 701 to countermand boilerplate reporting and launch the issuance of firm-specific fit-for-purpose reporting. Among other requirements, the new standard requires auditors to disclose key audit matters (KAMs) that auditors determine when applying their professional judgment in a new section of the audit report. The prime objective of including KAMs in the independent audit report is to improve reporting transparency by providing more audit insights into the information required by users and eliminating the expectation gap (Gold *et al.*, 2012). With the enhanced responsibilities, auditors are now required to sign the audit report in the engagement partner's name unless such disclosure is reasonably expected to lead to a significant personal security threat (IAASB, 2013). The IAASB announced the adoption and application of new reporting standards for listed entities, effective for audits of financial statements from the period ending on or after December 15, 2016.

While most concurrent studies in developed economies have explored the appropriateness and pertinent concerns of the new reporting model by investigating KAMs and their impacts on investors and the market (e.g. Gimbar *et al.*, 2016; Sirois *et al.*, 2018; KPMG, 2017; Wei *et al.*, 2019), little is known about KAMs' disclosure in developing countries. For example, many developed economies such as the United Kingdom (UK), the Netherlands, Poland, Spain, Romania, Australia and New Zealand adopted and mandated ISA 701 soon after its formulation and declaration (Suttipun, 2020; Abdullatif and Al-Rahahleh, 2020). More recently, following developed countries, several developing countries, namely Malaysia, Jordan, India, Pakistan, China and Bangladesh, have also adopted KAMs in their external auditor reporting. However, only a few studies have explored KAMs from firms in developing countries, especially in the South Asian context. Therefore, it is crucial to focus our attention on markets such as those in Bangladesh as 50% of the world's gross domestic product (GDP) is predicted to be originating from emerging markets by 2050 (PricewaterhouseCoopers [PwC], 2017a). The new KAMs-inclusive audit reports' communicative and informative value varies from country to country (Abdullatif and Al-Rahahleh, 2020); hence, a gap exists in the literature. To minimize this gap, our study focuses on Bangladesh, a fast-growing emerging economy in South Asia with a booming corporate sector.

Currently, Bangladesh is of interest to the international community. Remarkable progress in key economic indicators has allowed Bangladesh to graduate from the United Nations' (UN) least developed countries (LDCs) (CPD, 2021). Being a leading economy with immense prospects in South Asia, Bangladesh represents that region's business activities and capital market structure. The continuing foreign direct investment (FDI) in the country has drawn the attention of many developed countries around the world. The GDP rank of Bangladesh is predicted to shift from 31 to 23 by 2050 (PWC, 2017a). However, a heightened concern is that a stock market implosion is a common scenario that prevails at regular intervals in the country. The capital market in Bangladesh has witnessed significant regulatory reform. However, it is characterized by a poor legal system with an inadequate shield of minority shareholders' rights, concentrated ownership, limited presence of investor actions and institutional investors and a lack of demand for quality audit services (Khan *et al.*, 2016). Most business entities in Bangladesh are privately held companies owned by families. The accumulation of business capital in the country mainly depends on political connections and family networks (Belal *et al.*, 2017). The concentration of ownership and control causes conflicts of interest between controlling and minority shareholders (Young *et al.*, 2008). Firms, therefore, do not demand high-quality audit services, even though minority shareholders want a safer and more reliable financial market. In this typical situation, independent external auditors can fill the existing emptiness in corporate governance mechanisms and function as conceivable and trustworthy monitors of the controlling shareholders (Khan *et al.*, 2016).

However, most audit firms in Bangladesh are small, with only a few relatively large with international affiliations. Only one Big-4 firm operates in Bangladesh, although some have alliances with Big-4 auditors and other foreign audit firms. In most cases, the Big-4 firms launch correspondent firms (instead of full member firms) in Bangladesh and offer restricted service lines (Belal *et al.*, 2017). Nevertheless, all audit firms in Bangladesh are regulated and supervised by the Institute of Chartered Accountants of Bangladesh (ICAB) and, to some extent, by the Bangladesh Securities and Exchange Commission (BSEC), while affiliated firms are also guided and supervised by their international alliances. Nevertheless, a substantial lack of expertise and ineffective monitoring systems are apparent in the audit market in Bangladesh (Siddiqui, 2020). Moreover, audit engagement partner tenure is usually seven years in Western countries, whereas, in Bangladesh, the tenure is three years. Prior studies show that auditor judgment and risk disclosure are affected by audit tenure (Mali and Lim, 2018). Despite this backdrop and the idiosyncratic features of the Bangladeshi audit market, as with many other developing countries, Bangladesh is keen to adopt international auditing standards to align with the global convergence of audit reform. In line with this, the ICAB recently adopted the new ISA 701 reporting framework for audits of financial statements for the period ending on or after December 31, 2018 (ICAB, 2019). Given the distinctive features of the capital market and the audit market in Bangladesh, it would be worthwhile to investigate how corporate auditors are reacting to KAMs' disclosure in its efforts to protect the public interest. To the best of our knowledge, no empirical studies have investigated KAMs' disclosure in Bangladesh. Moreover, while contemporary studies have tried to identify the drivers of KAMs disclosure, the role of industry features and industrial regulations in KAMs communication has yet to be underresearched.

The current study aims to investigate the influence of three distinctive sets of variables, namely industry features (i.e. industry category, industry regulations, environmental sensitivity, etc.), firm characteristics (i.e. firm size, firm age) and auditor attributes (i.e. Big-4 affiliation, audit fees, auditor rotation) on the extent and level of disclosure of KAMs by companies listed in Bangladesh. Furthermore, the study examines consistencies or inconsistencies in KAMs' reporting within and across industry sectors. There is existence of industry-wide externalities from firms' disclosure (Leuz and Wysocki, 2016). We argue that industry features impact KAMs disclosure. This study utilised a sample of 447 firm-year observations from firms listed on the Dhaka Stock Exchange (DSE), Bangladesh, that had disclosed KAMs in their reports with fiscal year-ends during the period 2018–2020. In line with our hypotheses, the study findings reveal an increasing pattern of KAMs' disclosure adoption by auditors as they apply the new reporting model. Auditors are reporting diverse issues in the KAMs' report section, with these significantly different among firms. The number of KAMs and the length of their disclosure vary both within and across industry sectors. Highly regulated firms disclose a greater number of KAMs, while environmentally sensitive firms are found to provide greater detail of the issues presented as KAMs. Further, the firm size and firm age both positively impact KAMs disclosure. Big-4-affiliated auditors do not issue a significantly higher number of KAMs but provide extensive details in their KAMs description than non-Big-4 auditors. In addition, while auditors, in general, tend to issue boilerplate KAMs, Big-4 associates are found to disclose more new KAMs. However, audit fees and auditor rotation do not influence KAMs disclosure. The disclosure of KAMs shows an increasing trend compared to the previous year, with the size of the issued report showing a similar trend. Furthermore, auditors appear to prefer one issue over another in the sequence of KAM topics disclosed.

This paper contributes to the existing accounting and auditing literature in several ways. Firstly, the study findings extend our knowledge of risk disclosure by auditors of listed companies in Bangladesh, identifying through KAMs, the nature and types of issues disclosed. Secondly, the study analyzes reporting similarities and variations across industry sectors as well as by years. This is in line with the relevant literature, which has predicted some divergence in risk disclosure across industry sectors (Elzahar and Hussainey, 2012). Thirdly, the study further contributes to the literature by disentangling how regulation posed in specific industries may affect the KAMs disclosed by firms. Fourthly, the study results unearth how environmentally sensitive industries influence KAMs disclosure. Fifthly, the study provides additional analysis on the types of new KAMs disclosed and their association with Big-4 auditors and auditor rotation. The users of KAMs find these details of interest in relation to their decision-making. Moreover, earlier KAMs' studies have predominantly concentrated on developed countries, whereas this study provides evidence from an emerging economy context, in this case, Bangladesh with its weak regulatory accounting, reporting and auditing structures. Prior studies have shown the need to unravel risk disclosure, for example, of KAMs, in emerging economies (e.g. Dobler *et al.*, 2011). Finally, the study offers valuable insights into the newly promulgated auditing standards for regulators and policymakers, corporate managers, investors and other stakeholders, as previous studies have shown that observations from developed countries substantially differ from those in the developing country setting (e.g. Dobler *et al.*, 2011).

The remainder of the paper is organized as follows: Section 2 reviews the contemporary literature on KAMs and discusses the theoretical lenses used in the study. In Section 3, we discuss hypotheses development. In Section 4, we outline the research method, including the sample selection and data collection, while Section 5 presents the results and additional analyses. Section 6 concludes the paper with a discussion, acknowledging its limitations and describing avenues for future research directions.

2. Literature review

2.1 Recent literature on key audit matters (KAMs)

Over time, several notable changes have been made worldwide to both the form and content of the auditor's report. Fueled by a series of accounting scandals, continuous debate on the expectation gap has led to this much-needed transformation. The IAASB executed the most recent reform in 2015 with the incorporation of *ISA 701: Communicating Key Audit Matters in the Independent Auditor's Report,* as well as modifications to extant standards to provide more entity-specific and audit-specific information in the audit report. Realizing the benefits of KAMs' disclosure, a growing number of countries, such as Australia, New Zealand, China, Singapore, Hong Kong, the UK, Malaysia, Thailand and Spain have adopted ISA 701 and firms in these countries now disclose KAMs to stakeholders (Suttipun, 2020). However, accounting and auditing professionals, standard-setting bodies and academic researchers have raised questions about the local and global consistencies of KAMs' disclosure (IAASB, 2013) as inconsistent KAMs' presentations could eventually impair users' decisions in capital markets. With the new reporting model implemented by accounting practitioners worldwide, the standard-setters and regulators, along with groups of researchers, are assessing the effectiveness and adequacy of the paradigm shift.

The relevant contemporary literature has investigated the probable impacts of KAMs' disclosure on users' decisions (e.g. Christensen *et al.*, 2014; Cade and Hodge, 2014; Sirois *et al.*, 2018; Wei *et al.*, 2019; Moroney *et al.*, 2021); on capital markets (Lennox *et al.*, 2018); and on how analysts, legal experts and jurors regard the disclosure of KAMs about litigation against the auditor (e.g. Brown *et al.*, 2015; Gimbar *et al.*, 2016). For example, Cade and Hodge (2014) documented the reluctance of management to impart information to auditors as they know that KAMs will be disclosed in the audit report. In contrast, Christensen *et al.* (2014) found that investors are more likely to change their decisions if they know about the KAMs. Sirois *et al.* (2018) reported that users consider the disclosure of KAMs in their decision-making. In their experimental study, Moroney *et al.* (2021) found that the inclusion of KAMs improves the perceived value of the audit and the auditor's credibility only when a Non-Big-4 firm conducts the audit. The perceived value and credibility are high regardless of the inclusion of KAMs when Big-4 auditors conducted the audit. However, other studies have noted that different investor groups react differently (Kohler *et al.*, 2016). For example, Kipp *et al.* (2017) noticed that non-professional young investors perceive the communication of KAMs as a sign of greater audit quality and, consequently, have increased confidence in the reporting.

Gimbar *et al.* (2016) proclaimed that KAMs' information could increase the auditor's liability when any litigation issue is reported as a KAM: when auditors disclose KAMs in detail, the procedures followed must deal with perceived risk. Conversely, Brown *et al.* (2015) predicted that risk disclosure could decrease auditors' legal exposure. However, Lennox *et al.* (2018) posited that auditors might use standard language that is not informative to protect themselves from the risk of litigation. Independent audit reports may not be as beneficial as expected in such cases. Wei *et al.* (2019) found no significant improvement in audit quality but observed a rise in audit fees. Nevertheless, most research efforts were in the pre-implementation stage to foresee the consequences of increased disclosure. Some contemporaneous analyses, although very few, have been undertaken to identify the nature and types of KAMs disclosed by independent auditors in different countries, although this was primarily in developed countries (e.g. Deloitte, 2017; Wei *et al.*, 2019).

In developing countries, very few studies on KAMs have been conducted (e.g. Suttipun, 2022). Suttipun (2022) investigated the KAMs disclosure in Thailand and found a positive relationship between audit fees, auditor type and KAMs reporting. However, audit markets in emerging economies, such as Bangladesh, have notably different features from developed countries. The concern that KAMs' disclosure may have a lower added value than that predicted by the IAASB is stronger in developing countries than in developed countries (Abdullatif and Al-Rahahleh, 2020). This concern is fueled by inefficient capital markets, the lack of sophisticated investors and ineffective legal systems (Hopper *et al.*, 2017). Countries with strong legal enforcement of reporting requirements gain the capital market benefits of standard adoption (Daske and Gebhardt, 2006). However, evidence has shown that risk disclosure varies across countries (Elshandidy *et al.*, 2015). Prior literature has shown that, in emerging economies, weak governance and poor practices prevail in the application of international standards. In developing countries, standards adoption and implementation face many obstacles and difficulties, such as lack of expertise, resources allocated for standards enforcement and implementation, other regulatory complexities, etc (Larson and Street, 2004). In a recent note, Boolaky *et al.* (2020) explore the International Standards on Auditing (ISAs) from the contexts of developing countries, and they found that a majority of developing countries have a lack of education and training, appearing to significantly hamper the development of auditing standards and the adoption of ISAs. Earlier, Boolaky and Soobaroyen (2017) reported that the protection of minority interests, regulatory enforcement, lenders/borrowers' rights, foreign aid, the prevalence of foreign ownership, educational attainment and particular forms of the political system (level of democracy) prevailing in a country, are considered as significant factors of the extent of commitment to the adoption and harmonisation of ISAs.

International bodies are keen to observe and examine emerging markets (United Nations [UN], 2011). Indeed, "capital" is now a global commodity. Emerging economies need to adopt international standards for financial reporting and auditing (Baker and Wallage, 2000). Therefore, emerging economies, including Bangladesh, try to develop and project an image of quality financial reporting to their clientele by applying globally accepted reporting standards (Peng and Bewley, 2010). However, less regulated markets, greater information asymmetry and lack of adequate regulatory bodies have raised questions about the success of standards implementation, particularly in emerging economies (Ismail *et al.*, 2013). With the new standard, additional disclosure has further added to the auditor's stressful tasks (Bhattacharjee *et al.*, 2017).

2.2 Institutional setting

In the current study, we choose Bangladesh to examine our research questions. Bangladesh is the second-fastest-growing economy globally, with an expected average growth of 6.9% from 2021 to 2025 (Focus Economics, 2022). Unlike many other emerging economies, firms in Bangladesh are characterised by family ownership, high power distance and weak governance with a very poor regulatory environment where external auditing is the key external firm monitoring mechanism (Fan and Wong, 2005; Khan *et al.*, 2016). Wealthy business families often tend to develop political leaders and top bureaucrats to create power triangles to create reciprocal dependence for mutual benefits (Alam and Teicher, 2010). A majority of the industrialists with political ties have been accused of engaging in several financial fraud and irregularities (Khan *et al.*, 2016). Managers in emerging markets with a weak regulatory environment are likely to use political connections to materialise self-interest at the expense of minority shareholders (Faccio, 2006). The poor enforcement of regulations is the key cause of failure to protect minority shareholders' interests. However, corporate governance, accountability and transparency in financial reports are vital for attaining and sustaining economic progress in any country (Abhayawasnsa and Azim, 2014). Bangladesh is among the developing countries that marked the inception of an era of improved financial reporting by "adopting" international standards (e.g. IASs) after the global financial crisis (GFC) (Nahar *et al.*, 2016). Due to pressure from donor agencies (e.g. the World Bank), lending institutions and professional accounting bodies (e.g. ICAB) for greater transparency and a free market economy, Bangladesh has been adopting international standards over the past 2 decades (Mir and Rahaman, 2005).

Yet, the audit market in Bangladesh is featured by the absence of Big-4 auditors. Here, the Big-4 and their local affiliates command only around 18% of listed audit clients (Karim, 2010). Moreover, a lack of demand for audited financial statements is evident in Bangladesh, as stakeholders are not sufficiently educated to read financial statements properly (Ahmed and Goyal, 2005). In addition, a weak legal and regulatory framework, a lack of shareholder activism and a high family ownership concentration negatively contribute to poor audit quality in Bangladesh (Khan *et al.*, 2016). Moreover, poor accounting education and training, inadequate adherence to professional ethics, ineffective enforcement mechanism and widespread noncompliance with accounting and auditing standards have contributed to poor quality financial reporting (The World Bank, 2003). To improve professional education and training, upgrade statutory framework, strengthen enforcement mechanisms and enhance the capacity of regulatory and professional bodies, the World Bank has been urging for the establishment of an independent oversight body-Financial Reporting Council (FRC) (The World Bank, 2021).

In September 2015, the Bangladesh Parliament passed the Financial Reporting Act of 2015, which calls for the establishment of an independent regulatory oversight body, the Financial Reporting Council (FRC), to oversee the profession, the performance of auditors and audit firms that conduct audits of financial statements of listed entities and financial institutions. Under the Financial Reporting Act of 2015, the Financial Reporting Council, once established, are authorized to set auditing standards in Bangladesh. Meanwhile, as of June 2022, the Institute of Chartered Accountants of Bangladesh (ICAB) remains the de facto standard-setter under the Bangladesh Chartered Accountants Order of 1973. *Ab initio*, ICAB's Technical and Research Committee adopted the 2013 version of International Standards of Auditing (ISAs) as Bangladesh Standards on Auditing (BSAs) for application in the country with limited modifications due to local laws. The International Standards on Review Engagements, International Standards on Assurance Engagements and International Standards on Related Services have also been adopted by ICAB. ICAB has established an ongoing process to incorporate new and revised International Auditing and Assurance Standards Board (IAASB) pronouncements and updated its standards to the most recent version of the ISA. The institute has been adopting IASs continually to enhance the quality of the financial reports while attaining reporting harmonization to ensure comparability of the financial reports.

However, while the economic progress of Bangladesh is well evident, qualitative development has not seen any notable progress like any other emerging economy (Saha, 2019). Rapid industrialisation and fastest-growing foreign investment have led to increasing demands for enhanced accountability and transparency in business practices and financial reporting (Muttakin and Khan, 2014). To fulfil the expectations and needs of stakeholders for more information, Bangladesh adopted KAMs' reporting for fiscal periods ending on or after 31 December 2018. While three reporting periods have already been completed in the post-KAMs' regime, we are unsure about the nature and types of KAMs disclosed in Bangladesh or their consistency or divergence from one period to the next. Neither have any KAM characteristics within and across industry sectors been revealed. In Bangladesh, the unstable capital market with its extreme growth potential, lack of proper implementation of standards and inadequacy of robust monitoring and controlling bodies, along with a different audit market scenario, necessitate an empirical investigation of the adoption of the new KAMs' reporting.

2.3 Theoretical lenses

Previous auditing research has used a range of theories, such as legitimacy theory, institutional theory, stakeholder theory, agency theory and communication theory, to explain the reasons for risk disclosure to stakeholders (Suttipun, 2022). For example, agency theory (Watts and Zimmerman, 1986) suggests that the auditor is hired in the interests of both stakeholders and management. The current study has used the dual theoretical lenses of legitimacy theory and institutional theory to explore the newly adopted KAMs in an emerging economy, in this case, Bangladesh. Many earlier studies have used legitimacy theory to explain organizations' motivation for KAMs' disclosure (Suttipun, 2020). Scholars have argued that organizations act legitimately to secure their existence and survival in society and that they, therefore, disclose KAMs' information in their audit reports. Legitimacy theory is constructed based on the idea that a social contract exists between business and society.

Organizational legitimacy is a dynamic concept (Lindblom, 1994), with a legitimacy gap possibly arising when an organization's activities do not meet stakeholders' expectations (Brown and Deegan, 1998). Suttipun (2020) argued that voluntary KAMs' disclosure might be used by an organization to communicate with stakeholders to reduce the legitimacy gap.

One recent study has suggested that legitimacy theory is the best theory for explaining the relationship between external auditor factors and KAMs' reporting in the audit reports of listed companies (Smith, 2017). Auditors are believed to be part of society and need to respond to community expectations (the community where they live and operate) by providing information on KAMs. It is also a matter of their reputation to verify their existence as professional auditors and members of an elite profession (Smith, 2017). Therefore, auditors decide where and how they provide KAMs' information to stakeholders in response to the demands or expectations of the community.

Legitimacy theory explains how society's expectations stimulate corporate actions (Gray *et al.*, 1995). Organizations consider themselves part of their society and, thus, are motivated and influenced by social needs (Suttipun, 2020). Many past studies have used legitimacy theory to explain organizations' motivation for their actions (De Villiers and Van Staden, 2006; Suttipun, 2020). Management employs disclosure media, such as annual reports, to alleviate community concerns when a discrepancy arises between corporate actions and societal expectations (Gray *et al.*, 1995). In line with this view, legitimacy theory can posit why firms allow their auditors to disclose KAMs in the independent auditor's report (De Villiers and Van Staden, 2006). In fact, through the auditor's report, firms legitimize their actions while informing various stakeholders that they are complying with applicable standards. It is argued that firms act legitimately to secure their existence in society and therefore disclose the necessary information in various published reports (Deegan and Islam, 2012). Legitimacy theory, thus, can be applied to explain whether firms are meeting stakeholders' information needs with KAMs' disclosure or whether the information thus disclosed remains inadequate.

On the other hand, the institutional theory describes the institutional pressures faced by firms and provides a purview that helps understand how firms respond to institutional pressures and expectations. Institutional theory has two dimensions: isomorphism and decoupling (Cahaya *et al.*, 2012). Organizational practices are interconnected and influenced by societal values where firms tend to achieve homogeneity in maintaining organizational legitimacy (Deegan and Unerman, 2011). This homogenization process of organizational practices and behaviour can be referred to as "isomorphism". DiMaggio and Powell (1983) defined isomorphism as "a constraining process that forces one unit in a population to resemble other units that share the same set of environmental conditions". In line with institutional theory, DiMaggio and Powell (1983) argued that a firm under pressure but intending to survive would follow its mainstream counterparts to present the similarities of its enterprise and business model. Therefore, in the current global marketplace, all organizations are trying to better comply with standards and surpass their competitors in every aspect. This also helps avoid legal and social warrants that may arise due to non-compliance.

Companies' information disclosure could be influenced by normative, mimetic, or coercive forces (Scott, 2008). Coercive isomorphism results from formal or informal pressures exerted by institutions that affect the organization's survival (e.g. imposition of laws and regulations by the Securities and Exchange Commission) (Kholeif, 2010). Coercive pressures could also be from capital markets, institutional leaders and foreign bodies (Boolaky and Soobaroyen, 2017). Mimetic pressures on an organization could arise to imitate the practices of other successful organizations. For example, Big-4 audit firms provide the best quality audit and information users; therefore, they want their investee firms to be audited by Big four auditors (Albu *et al.*, 2014). Normative isomorphism is caused by pressures related to the application of best practices in the industry (Al-Omari, 2010) or pressure arising from the norms of groups (DiMaggio and Powell, 1983). For example, managers of certain firms might be pressured to adopt and implement a certain institutional practice, CSR disclosure. By contrast, decoupling occurs when there is a gap between what organizations actually practice and what they show as practice. Dillard *et al.* (2004) defined "decoupling" as "the situation in which the formal organizational practice is distinct and separate from actual organizational practice." Under institutional pressure, organizations sometimes adopt and apply certain standards and practices, although they behave in a different manner (Deegan and Unerman, 2011).

Prior studies have found variability in disclosure, depending on whether institutional pressure is coercive or normative (Samaha *et al.*, 2012). Empirical studies have asserted the significant impact of pressure from governments on business firms' behaviour toward protecting the environment (Dasgupta *et al.*, 2000). This indicates that pressure groups influence how firms operate and interact with stakeholders. Prior studies utilised institutional theory to investigate the adoption and application of International Financial Reporting Standards (IFRS) in emerging economies (Tahat *et al.*, 2018; Aburous, 2019). Recently, Nguyen and Kend (2021) reported that KAMs disclosure increases audit quality. The standard-setting body ICAB adopted ISA 701 and mandated the disclosure of KAMs by listed firms in Bangladesh. With KAMs' disclosure mandatory in Bangladesh, firms are expected to comply with KAMs' disclosure requirements. We argue that the degree to which institutional pressures will impact KAMs' disclosure composition will be mediated by the industry sector where firms are nested. Auditors are pressured to comply with the new standard's requirement as the regulatory bodies adopt ISA, i.e. ICAB (coercive isomorphism). Big-4 affiliated auditors may have pressure from the mother Big-4 firm to ensure better quality audit and extensive KAMs disclosure (coercive isomorphism). On the other hand, auditors may have counterpressure from the clients to report less in KAMs (decoupling). Again, pressure for disclosing KAMs may vary across industries. Stakeholders of financial institutions may exert more pressure and expect more in KAMs than those of other sectors. Auditors of the environmentally sensitive industry might feel more pressure to disclose information about environmental assets or environmental degradation than their usual financial disclosures. Firms survive based on their legitimacy, and in their pursuit of legitimacy, they surrender to industry-specific demands (Brown and Deegan, 1998).

3. Hypotheses development

3.1 Industry features and KAMs disclosure

Standard setters expect at least one KAM in the audit report. The number, type and extent of disclosures are vested in the auditor's professional judgment. Therefore, an incredibly diverse range could be observed in KAMs' disclosures, specifically in the number and type of KAMs disclosed and the number of words used. Numerous factors, including client-firm and industry characteristics, could be determinants. Firm characteristics have significant explanatory power on disclosure choice (Elshandidy *et al.*, 2015), and industry-level variables also influence reporting behaviour (Elzahar and Hussainey, 2012). Many prior studies (e.g. Wanderley *et al.*, 2008; Madrigal *et al.*, 2015; Jain *et al.*, 2016; Dumay and Hossain, 2018) have concentrated on industry sectors in their analyses of corporate disclosures. Wanderley *et al.* (2008) investigated whether corporate social responsibility (CSR) disclosure on the web is affected by the industry sector, finding that it significantly influenced information disclosure.

Another study by Madrigal *et al.* (2015), investigating the determinants of corporate risk disclosure, documented a significant association between risk disclosure and industry sectors. However, the effects of the firm- and industry-specific factors on business affairs differ drastically in emerging markets (Khanna and Rivkin, 2001). Jain *et al.* (2016) investigated corporate orientation across industry sectors in emerging markets and found a significant difference between sectors. Empirical research has shown a meaningful relationship between the industry sector and risk information disclosure (Khlif and Hussainey, 2016). Given the distinctive nature of products and services, manufacturing processes, associated risks and the nature and extent of interaction with the state and society, every industry sector possesses a set of exclusive threats and opportunities that differ from those in other industries (Jain *et al.*, 2016). Due to the uniqueness of each industry sector, risk disclosure is expected to vary across industry sectors. For example, environmentally sensitive industries disclose more environmental information in response to the greater pressure from environmentalists (De Villiers and Van Staden, 2011).

The basic notion of institutional theory assumes that firms respond to the pressures from their operating environments and adopt policies and practices that other organizations accept in the same field (Powell and DiMaggio, 1991). Firms within an industry sector experience a sophisticated but similar concoction of global and local institutional pressures that accrue from the co-location of multiple mimetic, coercive and normative drivers to that particular industry sector (DiMaggio and Powell, 1983). Some industry sectors are more difficult to audit than others (Hay *et al.*, 2006). Auditing financial firms, for example, may be more challenging due to their complex accounting standards and interrelated on-balance sheet and off-balance sheet exposures. Furthermore, auditors belonging to a certain industry sector may follow others to see what they are reporting. Eventually, a high similarity is expected in KAMs' disclosure within each industry sector. Based on the above, we develop the study's hypotheses as follows:

H1a. The number of KAMs reported by auditors of listed companies in Bangladesh is similar within an industry sector but varies across industry sectors.

H1b. The lengths of KAMs' descriptions reported by auditors of listed companies in Bangladesh are similar within an industry sector but differ across industry sectors.

Banks and financial firms are essential services and are considered the most regulated industry. They are subject to closer regulatory oversight due to their complex business nature, high political involvement and monitoring difficulty (Boo and Sharma, 2008). The so-called regulated industries (banks and financial institutions) are highly affected by a set of constraints posed by the government (Chuang *et al.*, 2013). Although the government is a key stakeholder in all industries, the magnitude to which any decisions of government bodies influence firms varies between regulated and unregulated industries (Delgado-Márquez *et al.*, 2015). Firms in regulated industries must cope with the quality standards or norms regarding industry access restrictions, consumer protection and corporate reporting (Lezu and Wysocki, 2016). The upshots of non-compliance and fraudulent reporting are greater for regulated industries as a failure of regulated firms, such as banks, results in significant losses to stakeholders and the economy (Tadesse, 2006). Regulatory oversight of the government thus increases the risk of lawsuits against the company directors. In this line, the regulatory environment for specific industries could impact the demand for additional assurance from the independent auditor (Boo and Sharma, 2008). The closer monitoring by industry-specific regulators, the varying nature of regulations and the underlying complications could incentivize and impact KAMs' disclosure; highly regulated industries are expected to disclose more KAMs (Pinto and Morais, 2019). Past studies found a positive link between industry regulation and corporate disclosures (e.g. Bose *et al.*, 2016).

H1c. There is a positive association between industry regulation and KAMs disclosure.

Unlike banks and financial firms, environmentally sensitive industries such as oil, gas and coal exploration and distribution have larger environmental footprints, and now they report environmental, social and governance (ESG) issues. During the past decade, many have urged an introduction of external audit to enhance such reports' credibility (Chersan *et al.*, 2018). Audit committees and auditors now have added responsibilities regarding the disclosure of ESG aspects (Arif *et al.*, 2021). Firms need to enhance the credibility of environmental reports to protect their image and reputation (Gillet-Monjarret, 2015). External assurance is a key tool to improve the company's perceived reliability (Casey and Grenier, 2015), and it has recently become widespread for environmental disclosure (Radhouane *et al.*, 2020). However, the auditor's role regarding such assurance remains unclear.

Firms operating in the food and allied sector have to conduct third-party audits and inspections to ensure food safety, sanitation and hygiene as per industry standards. However, concern remains about the efficacy of the extant third-party audits and inspections due to outbreaks of foodborne illness caused by foods that passed the inspections. Unhealthy food processing has environmental and social hazards. Therefore, polemicists urged the introduction of external audits to ensure food safety (Powell *et al.*, 2013). The industries' environmental sensitivity and increased pressures for disclosure from auditors may affect the number of KAMs disclosed and their extent presented.

H1d. Auditors of environmentally sensitive industries disclose more KAMs with greater details.

3.2 Firm characteristics and KAMs disclosure

Legitimacy theory posits that larger firms meet social expectations more proactively than smaller firms (Taylor and Liu, 2008). Larger firms have an increased social burden and disclose more information than smaller firms (Brammer and Millington, 2006; Velte, 2018). KAMs reporting has enhanced the communicative value of the audit report (Sirois *et al.*, 2018) and is now considered the best tool of communication between the auditors and information users (Rahaman and Chand, 2021). The audit process of more prominent companies involves more audit activities than smaller ones (Suttipun, 2020). Auditors of the large firms are likely to have more noticeable observations brought to the boardroom and eventually on the KAMs report. Prior studies revealed that firm size significantly affects the quality of financial reporting (Kibiya *et al.*, 2016). Studies suggest that large firms are less likely to fail and larger firms have strong negotiation power with auditors (Wu *et al.*, 2016). Auditors may be reluctant to issue a modified opinion to a large firm due to losing the client's significant business (Carcello and Neal, 2000; Mutchler *et al.*, 1997). Recent studies documented inconclusive findings on the association between firm size and KAMs disclosure. Velte (2018), investigating UK firms, found a positive connection between company size and the level of KAMs reporting. Boonyanet and Promsen (2018), on the other hand, found no significant relationship between firm size and KAMs disclosure by companies operating in Thailand.

H2a. There is a positive relationship between firm size and KAMs disclosure.

Older companies have a broader stakeholder base and are involved with numerous social and community groups (Suttipun and Nuttaphon, 2014). Mature firms are likely to expand their operations and engage multiple stakeholder groups with divergent products and services. Societies have more expectations from long-aged firms than newer ones (Suttipun, 2020). Aged firms may feel more pressure to disclose more information due to the varied information needs of different stakeholder groups. Past studies find a positive influence of firm age on corporate disclosure (Suttipun and Nuttaphon, 2014) and reporting quality (Echobu *et al.*, 2017). However, Whiting and Woodcock (2011) found no statistically significant relationship between firm age and intellectual capital disclosure. Arguably, older firms may have stronger internal controls (Ettredge *et al.*, 2014), resulting in fewer issues of concern that auditors could consider a KAM to report in the independent audit report. As the firm age increases, the probability of restatements decreases (Beasley, 1996). Moreover, mature companies may assume reputational risk and have no or low tendency to manipulate earnings (Chen *et al.*, 2008; Alzoubi, 2017). On the other hand, younger firms may have a relatively weaker internal control system and tend to fabricate earnings and experience financial restatements. Newer firms are more susceptible to failure and more likely to receive a going concern opinion

(Knechel and Vanstraelen, 2007). The observations on firm age associated with corporate disclosure are inconclusive and mixed. We, therefore, hold a non-directional hypothesis.

H2b. There is an association between firm age and KAM disclosure.

3.3 Auditor characteristics and KAMs disclosure

Audit functions and quality in Southeast Asian countries, including Bangladesh, are deficient because of lax regulation and family ownership (La Porta *et al.*, 2000; Claessens *et al.*, 2000). Local auditors are approaching global Big-4 firms by becoming partnership firms or affiliated firms to enhance the audit quality (Fan and Wong, 2005). Firms with higher agency costs incline to engage Big-4 auditors that provide higher-quality audits (Jensen and Meckling, 1976). Big-4 auditors in Bangladesh are expected to mitigate the agency problem by providing a greater external monitoring function than smaller local audit firms (Khan *et al.*, 2016). Empirical research finds differences in audit quality between Big-4 and non-Big-4 firms, and investors consider big firms to provide better audit quality (Lawrence *et al.*, 2011). The differences emerge not only because of the technical expertise, highly experienced and trained auditors that large audit firms have but also because of their perspective of brand equity, firm reputation and the efforts and approaches to protect the reputation (Barako *et al.*, 2006; Bepari *et al.*, 2014). Big-4 auditors are concerned about maintaining auditor image and have incentives to shield any reputational damage (Chalmers and Godfrey, 2004; Reichelt and Wang, 2010). Big-4 auditors have incentives to maintain independence and prestige, and therefore, they impose more stringent and extensive disclosure standards as they assume to lose more from any damage to their reputations (Wang *et al.*, 2008).

Moreover, large auditors are perceived to have the resources and ability to identify internal control problems and are more likely to pressure the client companies to report any deficiencies (Ahmad *et al.*, 2015). Highly visible auditors are sensitive to reputational concerns and are expected to be less tolerant of the client's reporting deficiency (Mutchler *et al.*, 1997; Kovermann and Velte, 2019). Giant audit firms are more likely to issue a going-concern modification as they have more resources and expertise that they exploit to exhibit better audit quality (Geiger and Rama, 2006). Wuttichindanon and Issarawornrawanich (2020) found a positive association between Big-4 auditors and the number of KAMs disclosed by firms in Thailand. Contrastingly, Velte (2020) found no significant association between Big-4 and KAMs furnished by firms in the UK However, in the context of Bangladesh, auditors affiliated with Big-4 firms would encourage their client companies to provide more information to avoid reputational damage and maintain the audit firms' high image. We anticipate the following:

H3a. There is a positive association between the engagement of Big-4 auditors and KAMs disclosure.

A glut of past research shows that audit fees impact audit effort and audit quality (e.g. Alareeni, 2017; Li *et al.*, 2019). Vanstraelen *et al.* (2011) claimed that adopting the new extended auditor reporting will require additional resources. The enhanced responsibilities of the auditor will require the auditors to charge extra and hence an increased audit fee (Suttipun, 2022). Causholli and Knechel (2012) suggest that auditors may charge added fees even if the KAMs disclosure may not require significant extra audit effort. Mock *et al.* (2013) posit that KAMs could be from the observations that auditors usually have and, therefore, no additional effort and costs are needed for the requirement of KAMs. Contemporary studies examined the impact of KAMs adoption on audit fees (Bédard *et al.*, 2019; Li *et al.*, 2019). Li *et al.* (2019) found an increased audit fee in the post-KAM adoption regime in New Zealand.

In contrast, Bédard *et al.* (2019) documented no significant association between KAMs and audit fees reported by firms in France. A more recent study in Thailand, Suttipun (2022), found a positive impact of audit fees on KAMs reporting. In the context of the present study, we argue that KAMs disclosure would require additional audit efforts and, therefore, added audit costs. Moreover, there is an increased risk of litigation associated with KAMs disclosure. Auditors may charge a premium to counter the increased risk. As a result, firms paying higher audit fees may have better audit quality resulting in the revelation of more significant issues and eventually more KAMs in the audit report. The relevant hypothesis is as follows:

H3b. There is a positive association between audit fees and KAMs disclosure.

4. Method

Prior studies in the field of auditing have employed different approaches, such as a questionnaire survey (Chong and Pflugrath, 2008); experiments (Gold *et al.*, 2012; Brasel *et al.*, 2016; Sirois *et al.*, 2018); statistical models (Wei *et al.*, 2019); and content analysis (Prasad and Chand, 2017). However, content analysis is often used and most highly accepted in the risk disclosure literature (Amran *et al.*, 2008; Abraham and Cox, 2007).

The current study employs content analysis, which uses qualitative and quantitative approaches to analyse our research questions. Content analysis is a technique for making replicable inferences and has many advantages. First, it provides convenient opportunities to measure the quantity and quality of information disclosed in content or report. Second, a transparent and inobtrusive research method permits longitudinal analysis (Bryman and Bell, 2015). Third, the technique allows large amounts of data to be grouped or broken down into categories or codes. Finally, content analysis is an ideal tool for data analysis as it enables a meaningful set of data (Milne and Adler, 1999). We use appropriate univariate and multivariate tests and regression models with associated validity and reliability tests to examine our study's hypotheses.

4.1 Sample selection and data collection

The study sample was composed of companies listed on the Dhaka Stock Exchange (DSE) from 2018 to 2020. The standard, ISA 701, was made applicable for the period ending on or after December 31, 2018; however, some companies end their fiscal year on December 31, 2018, while others had their year-end date on June 30, 2019. Therefore, we consider both groups as being in the first year of implementation. We account in the same way for the second year post-KAMs' disclosure adoption. Thus, the population underlying the analysis comprises 1,178 company-year observations.

The industry sector taxonomy revealed 22 industry groups on the DSE website. Several exclusions were made from this initial population, consistent with the prior literature (e.g. Wei *et al.*, 2019), namely, corporate bonds, treasury bonds, debenture, mutual funds and various industries, due to the very distinctive nature of their operations. The final sample of selected firms and the selection criteria are presented in Table 1 (Panel A). Some industry sectors comprised only a few companies, and the data for some of these sectors were not available. Therefore, we categorised these sectors for our study's purpose: jute, paper and printing, services and real estate, telecommunications and the tannery industry under a single "others" sector group. In all, 12 industry sector groups, as presented in Table 1 (Panel B), are contemplated in our study. The sample of 246 firms covered 78.59% of all firms that fall within our study's industry sectors.

We used the annual reports of companies in our sample to collect the data, with these reports collected from the respective company's websites. We then carefully studied the independent auditor's report included in each annual report to code the required data.

Panel A: Composition of sample	Companies	Observations
Listed during the study period 2018–2020 (two fiscal years)	589	1,178
Intentionally excluded due to their different nature (294 companies)	−294	−588
Companies that did not apply BSAs (five companies)	−5	−10
Non-availability of reports (Year 1: 44 companies; Year 2: 89 companies)	−44	−133
Total sample	246	447

Panel B: Industry sector concentration in sample	Total companies	Sample selected	% of sample
Banks	30	25	83.33
Cement	7	7	100.00
Ceramics	5	5	100.00
Engineering	39	33	84.62
Financial institutions	23	21	91.30
Food and allied	17	13	76.47
Fuel and power	19	20	105.26
Insurance	47	37	78.72
IT sector	10	7	70.00
Pharmaceuticals and chemicals	32	23	71.88
Textiles	56	42	75.00
Others	28	13	46.43
Total	313	246	78.59

Table 1.
Sample selection

Regarding the coding: for certain items, namely, the number of KAMs disclosed and the number of paragraphs and words used, we used the total count, and for categorical data, that is, industry category, KAM types, we used predetermined codes. More specifically, for KAM types, we matched each of the KAMs disclosed against the 27 types of KAMs identified by Mazars (2018), the French audit firm. We take Mazars (2018) as a benchmark for KAM types because of the broader sample size of their study covering 11 sectors and 51 subsectors from twelve countries across the world.

4.2 Regression model

We use the following regression specification as baseline models to test our hypotheses:

$$\begin{aligned} NumKAM_{it} = {} & \alpha_0 + \beta_{1-12}\sum INDUSTRY_{it} + \beta_{13}FIRM\_SIZE_{it} + \beta_{14}FIRM\_AGE_{it} \\ & + \beta_{15}BIG-4_{it} + \beta_{16}AUDIT\_FEES_{it} + \beta_{17}AUDIT\_SWITCH_{it} \\ & + \sum CONTROLS_{it} + \varepsilon_{it} \end{aligned} \tag{1}$$

$$\begin{aligned} WordKAM_{it} = {} & \alpha_0 + \beta_{1-12}\sum INDUSTRY_{it} + \beta_{13}FIRM\_SIZE_{it} + \beta_{14}FIRM\_AGE_{it} \\ & + \beta_{15}BIG-4_{it} + \beta_{16}AUDIT\_FEES_{it} + \beta_{17}AUDIT\_SWITCH_{it} \\ & + \sum CONTROLS_{it} + \varepsilon_{it} \end{aligned} \tag{2}$$

For our hypotheses (H1c) and (H1d), we use the following regression models:

$$\begin{aligned} NumKAM_{it} = {} & \alpha_0 + \beta_1 REGULATED_{it} + \beta_2 ENVIRONMENT_{it} + \beta_3 FIRM\_SIZE_{it} \\ & + \beta_4 FIRM\_AGE_{it} + \beta_5 BIG-4_{it} + \beta_6 AUDIT\_FEES_{it} \\ & + \beta_7 AUDIT\_SWITCH_{it} + \sum CONTROLS_{it} + \varepsilon_{it} \end{aligned} \tag{3}$$

$$WordKAM_{it} = \alpha_0 + \beta_1 REGULATED_{it} + \beta_2 ENVIRONMENT_{it} + \beta_3 FIRM\_SIZE_{it} + \beta_4 FIRM\_AGE_{it} + \beta_5 BIG - 4_{it} + \beta_6 AUDIT\_FEES_{it} + \beta_7 AUDIT\_SWITCH_{it} + \sum CONTROLS_{it} + \varepsilon_{it} \quad (4)$$

For KAMs' variability across Big-4 and non-Big-4 auditors, we use the following model:

$$NumKAM_{it} = \alpha_0 + \beta_{1-12} \sum INDUSTRY_{it} + \beta_{13} FIRM\_SIZE_{it} + \beta_{14} FIRM\_AGE_{it} + \beta_{15-19} \sum BIG - 4_{it} + \beta_{20} AUDIT\_FEES_{it} + \beta_{21} AUDIT\_SWITCH_{it} + \sum CONTROLS_{it} + \varepsilon_{it} \quad (5)$$

For sensitivity analysis, we change our dependent variable and use the following regression model:

$$Report\_Size_{it} = \alpha_0 + \beta_1 FIRM\_SIZE_{it} + \beta_2 FIRM\_AGE_{it} + \beta_3 BIG - 4_{it} + \beta_4 AUDIT\_FEES_{it} + \beta_5 AUDIT\_SWITCH_{it} + \sum INDUSTRY_{it} + \sum CONTROLS_{it} + \varepsilon_{it} \quad (6)$$

The dependent variable is the natural logarithm of the number of KAMs disclosed for model 1, model 3 and model 5 and the natural logarithm of number of words to describe KAMs for model 2 and model 4 and the size of the audit report measured by the number of pages for model 6 (sensitivity analysis). Our independent variable *INDUSTRY* is an identifier dummy for each of the industries. Significant variation among the coefficients for the industry dummy is expected as the number of KAMs and their extent of disclosure is hypothesized to vary within and across industries. *REGULATED* is a dummy variable coded 1 for banks and financial firms; 0 otherwise. Auditors of the regulated industries are expected to disclose more KAMs. *ENVIRONMENT* is a dummy for environmentally sensitive industries. In line with prior studies, we consider industries such as food and allied, textile, engineering, pharmaceuticals and chemicals and tannery are sensitive to the environment (Harrison, 1993). A positive coefficient is expected for *ENVIRONMENT* as environmentally sensitive firms are likely to furnish more in KAMs disclosure.

Firm size (*FIRM_SIZE*) is measured by the natural logarithm of total assets. A positive relationship between firm size and KAMs disclosure is expected because auditors of larger companies may have more issues to disclose in the boardroom and eventually to the users of financial information. Firm age (*FIRM_AGE*) is measured by the natural logarithm of the number of years since the company was formed. Older firms are predicted to disclose more in their reports.

In developing countries, the operations of international Big 4 auditors are not still widespread. However, some local firms have international affiliations. Big-4 affiliated auditors (*BIG-4*) are expected to disclose more KAMs for several reasons, including a better experience and expertise to uncover more risk issues, protect their image and reputation that could be damaged through litigation and maintain audit quality as they have international affiliations. The list of matters disclosed is expected to be longer for firms paying a greater audit fee *(AUDIT_FEES)*. The firms paying a greater amount of audit fees may receive more KAMs in their reports as we perceive that a higher fee indicates the need for more extensive audit works, a greater audit riskand more critical issues to deal with, thereby raising and reporting more issues in the audit report. In line with prior studies (e.g. Wuttichindanon and Issarawornrawanich, 2020; Suttipun, 2022), we control for auditor rotation *(AUDIT_SWITCH)*, leverage *(LEV)*, year *(YEAR)*, consolidation (*CONSOL*) and yearend *(YEAR _END)*.

5. Empirical results

5.1 Nature and extent of KAMs' disclosure

Table 2 presents descriptive statistics of the number and types of KAMs disclosed by listed firms in Bangladesh in the first two years of adopting the new ISA 701.

The auditors reported the number of KAMs, ranging from 0 to a maximum of eight, producing a mean value of 3.24 per audit report in the year of adoption. This observation is inconsistent with both developed markets (Australian firms reported 2.01 KAMs, on average) and developing markets (Thai firms reported 1.63 KAMs, on average) (Wei *et al.*, 2019; Suttipun, 2020). Most of the sampled companies revealed three (30%) or two (24.70%) KAMs. Twelve (12) firms did not disclose any KAM, compared to the maximum of eight KAMs disclosed by two firms. To describe KAMs, auditors, on average, utilized 31 paragraphs and 825 words. No prior study has concentrated on the paragraph as a unit. However, one study by Suttipun (2022) in Thailand documented an average count of around 600 words for KAM presentation, which is inconsistent with our findings. Our study found that the audit report's length ranged from one page to 10 pages, with an average of 4.54 pages after this additional disclosure. However, in the following year, an increasing trend was found, reporting 3.77 KAMs per report while utilizing, on average, 1,013 words in 34 paragraphs. The size of the audit report increased to 5.04 pages (on average).

We use both ANOVA and regression analysis to test our hypothesis (H1). However, for hypotheses (H2) and (H3), we rely on regression models. Before regression analysis, we examined correlations between the variables and computed the VIF values to check for multicollinearity. No such strong correlation was observed, and the VIF values were found to be less than 5 against the general rule of thumb of a maximum of 10.

Concerning our first hypothesis (H1a), the analysis of variance (ANOVA) results ($F = 5.917, p = 0.000$) in Table 3 shows statistically significant differences in the number of KAMs presented within and across industry sectors. Thus, the findings partially contradict our prediction that the number of KAMs do not vary within the industry sector. However, the outcome supports our anticipation that the number of KAMs varies across industry sectors. Some firms disclosed no KAMs, while others disclosed a maximum of eight. These observations confirm the uniqueness of the new reports issued by auditors. Some auditors were perhaps more agile in reducing their liabilities by disclosing more KAMs, while others could compromise due to clients' demands for less disclosure. Banks were found to be disclosing more KAMs compared to other industries. This is consistent with the argument

	Year 1 (n = 246)					Year 2 (n = 201)[1]				
Particulars	Mean	S.D.	Min	Max	Med	Mean	S.D.	Min	Max	Med
Number of KAMs disclosed	3.18	1.60	0	8	3.18	3.77	1.75	0	10	4
Number of paragraphs used[2]	30.47	16.18	1	79	30.47	34.37	17.64	1	114	31.50
Number of words used	824.88	445.82	62	2,361	790	1013.50	540.54	72	3,615	948
Number of pages[3]	4.54	1.37	1	10	4.54	5.04	1.30	2	10	5

Note(s): S.D. = standard deviation
[1]Owing to non-availability of annual reports, our observations comprise 201 firms in the second year of KAMs' adoption
[2]In the auditor's report, the auditor uses a combination of paragraphs and bulleted paragraphs to describe key audit matters (KAMs). However, both types are considered as paragraphs for the purpose of our analysis
[3]To count the number of pages, we consider full pages plus a fraction of a page for more accuracy. For example, if a report runs to two and a half pages, this would be coded as 2.5

Table 2. Descriptive statistics of listed Bangladeshi companies: number of KAMs disclosed, presentation length and audit report length

Table 3.
Univariate and ANOVA[1] results for various industry sectors in Bangladesh: number of KAMs disclosed in audit reports of listed companies

	Industry sector	Number of KAMs				
		N	Mean	S.D.	*F*	*p*-value
	ANOVA (across 12 industry sectors)				5.917	0.000**
1	Banks	50	5.08	2.00	4.46	0.000**
2	Cement	14	2.93	1.64	80.33	0.000**
3	Ceramics	10	3.70	1.16	29.00	0.001**
4	Engineering	38	3.53	1.37	3.258	0.007**
5	Financial institutions	38	3.58	2.24	7.447	0.000**
6	Food and allied	22	3.36	1.84	7.589	0.001**
7	Fuel and power	30	3.13	1.43	4.238	0.004**
8	Insurance	70	2.97	1.12	2.992	0.001**
9	IT sector	14	3.00	1.47	27.00	0.002**
10	Pharmaceuticals and chemicals	36	3.44	1.78	2.855	0.017*
11	Textiles	62	3.29	1.12	2.573	0.005**
12	Others	18	3.61	1.38	2.697	0.080

Note(s): ANOVA = analysis of variance; S.D. = standard deviation; superscript asterisks **significant at 1% level; *significant at 5% level
[1]We used ANOVA taking data from both the first year and second year of KAMs' adoption. To analyze within industry variations, we used company dummies while, for across-industry analysis, we used industry dummies as predictor variables

that banks may require more disclosure due to their diverse and complex rules and regulations (Hay *et al.*, 2006) and agrees with Dumay and Hossain (2018) that financial firms disclose more risk information. In contrast, companies in the cement and insurance industry sectors were furnishing a relatively smaller number of KAMs in their reports. Institutional theorists proclaim that organizations working in the same socio-political environment tend to adopt the same reporting policies since they face the same legal and professional pressures (Carpenter and Feroz, 2001; Hassan, 2008).

Regarding the length of disclosure, the results ($F = 2.991$, $p = 0.001$) support our third hypothesis (H1b) that the number of words used to present KAMs differs across industry sectors, as presented in Table 4. Moreover, the number of words firms use within a particular industry sector significantly diverges, thus being contrary to our hypothesis of similar

Table 4.
Univariate and ANOVA results for number of words used to describe KAMs in audit reports of listed companies within and across various industry sectors in Bangladesh

	Industry sector	Number of words				
		N	Mean	S.D.	*F*	*p*-value
	ANOVA (across 12 industry sectors)				2.991	0.001**
1	Banks	50	1,194	454	5.274	0.000**
2	Cement	14	762	501	23.138	0.013*
3	Ceramics	10	787	341	6.906	0.029*
4	Engineering	38	943	325	1.377	0.248
5	Financial institutions	38	970	649	6.252	0.000**
6	Food and allied	22	935	494	5.399	0.005**
7	Fuel and power	30	854	491	3.219	0.016*
8	Insurance	70	730	252	4.636	0.000**
9	IT sector	14	842	579	57.578	0.009**
10	Pharmaceuticals and chemicals	36	968	701	5.580	0.000**
11	Textiles	62	970	502	2.735	0.000**
12	Others	18	1,065	483	4.004	0.027*

Note(s): ANOVA = analysis of variance; S.D. = standard deviation; superscript asterisks **significant at 1% level; *significant at 5% level

KAMs' descriptions within the same industry sector. A similar observation ($F = 2.272$, $p = 0.011$; untabulated) is made concerning the number of paragraphs describing KAMs utilized by auditors. These findings conform to prior studies investigating corporate risk disclosure (e.g. Amran *et al.*, 2008; Madrigal *et al.*, 2015). The observation about the greater extent of disclosures by banks and the financial sector is harmonious with the findings of Dumay and Hossain (2018), who finds a similar observation on sustainability risk disclosure by Australian firms. These observations, however, do not match the findings of Abraham and Cox (2007), in which the authors reported no significant association between the extent of risk disclosure and the specific industry sector. Nevertheless, the variations in KAMs' presentation, even within the industry sector, support the notion that auditors have departed from making boilerplate statements and are disclosing different issues in divergent ways. However, this observation is inconsistent with the concern shown by the AUASB (2013).

Besides ANOVA, we use regression analysis to test our hypotheses. The descriptive statistics for the study variables used in the regression models are presented in Table 5.

Variables	*N*		Mean	S.D.*	Minimum		Maximum	
Dependent variable(s)								
NumKAM	412		3.54	1.67	0.00		10.00	
Ln_NumKAM	412		1.17	0.47	0.00		2.30	
WordKAM	412		926.18	490.46	62.00		3615.00	
Ln_WordKAM	412		6.68	0.61	4.13		8.19	
Report_Size	412		4.77	1.29	1.00		10.00	
Ln_Report_Size	412		1.52	0.28	0.00		2.30	
Independent variables (continuous)								
Ln_FIRM_SIZE	412		15.92	1.93	11.37		20.86	
FIRM_AGE (years)	412		26.42	11.40	5.00		66.00	
Ln_FIRM_AGE	412		3.18	0.44	1.61		4.19	
AUDIT_FEES (million BDT)	412		0.76	1.47	0.046		18.02	
Ln_AUDIT_FEES	412		6.03	0.970	3.83		9.80	
LEV	412		0.57	0.35	0.01		3.70	
Independent variables (dichotomous)			Frequency (0)	%	Frequency (1)		%	
REGULATED	412		326	79.13	86		20.87	
ENVIRONMENT	412		221	53.64	191		46.36	
Big-4	412		324	78.64	88		21.36	
AUDIT_SWITCH	412		220	53.40	192		46.60	
YEAR_END	412		261	63.35	151		36.65	
CONSOL	412		281	68.69	129		31.31	
Independent variables (dummy)	Freq.(1)	%	Freq.(2)	%	Freq.(3)	%	Freq.(4)	%
Big-4_Individual	30	7.28	28	6.80	23	5.58	7	1.69

Note(s): *S.D. = standard deviation
Number of KAM, Words in KAM, Audit Report Size, Firm SIZE, Firm Age and Audit Fees, are measured as the natural logarithm of the respective items. LEV is the total debts divided by total assets. Big 4 = 1 if the company was audited by Big-4 or an audit firm affiliated with Big-4 international auditors, 0 otherwise. REGULATED is a dummy variable = 1 if the company belongs to the industry is a bank, and financials, 0 otherwise. ENVIRONMENT is a dummy variable = 1 if the company belongs to the industry is food and allied, textiles, engineering, pharmaceuticals and chemicals, and others (tennary, papers and printing). Big4 Auditor is a categorical variable to identify affiliation with the audit firms: Deloitte = 1, PwC = 2, Ernst & Young = 3, KPMG = 4, and non-Big4 or no affiliation = 5. Switch = 1 if the company switched an audit firm in the current year, 0 otherwise. YEAR_END is a dummy variable = 1 if the reporting period ended on December, 0 otherwise. CONSOL is a dummy variable = 1 if the firm reported a set of consolidated financial statements, 0 otherwise

Table 5.
Descriptive statistics

The mean number of KAMs reported by firms in Bangladesh is 3.54, while some report no KAMs and some a maximum of 10 KAMs. Firms use 926.18 words, on average, to describe KAMs that eventually produces a longer audit report (around 4.77 pages, on average) now than ever before, particularly due to the requirement of KAMs disclosure. About 21% of the firm-year observations belong to the regulated industries, while a relatively higher proportion of around 46% falls into the category of environmentally sensitive industries. The mean of Ln(firm size) is 15.92, which is comparable to the mean of 12.31 reported by Muttakin and Khan (2014). The average age of the sampled firms is around 26 years, with newly incorporated firms having an age of 5 years against the oldest firms ageing more than 60 years; Muttakin and Khan (2014) reported a mean firm age of 23.66 years. As appears in Table 5, a relatively lower proportion (21.36%) of the sampled firm-years have financial statements audited by Big-4 and their local affiliates. Firms listed in DSE pay BDT 0.76 million, on average, for the audit services received in a year. Audit fees varied from BDT 0.046 million to a maximum of BDT 18.02 million, indicating a wide disparity in audit fees paid. Around 47% of the sampled observations have auditor switch (engagement of a new auditor) for the reporting period. The mean of leverage is 0.57, which is consistent with Khan *et al.* (2016) reporting 0.65.

Our regression results are presented in Table 6. Model 1 presents the relationship between the number of KAMs and the predictor variables, while Model 2 presents the regression results for the number of words used in KAMs. In Model 1, eight out of eleven industries have significant positive coefficients, which indicates a significantly different number of KAM disclosures against the base industry- Cement. Model 2 provides more robust results showing ten industries disclosing KAMs with a varied description compared to the base industry. Like our ANOVA results, these observations from regression also support our hypothesis (H1a) and (H1b) that KAMs disclosure varies across industries. According to the proposition of institutional theory, organizations seek to mimic their counterparts, which leads them to adopt similar strategies and policies to sustain in the institutional context (Cohen *et al.*, 2008).

The findings for presentation length share similarities with the number of KAMs presented. The number of KAMs (paragraph and words) varies within and across industry sectors. Nevertheless, some inconsistencies are observed. Industry sectors that present more KAMs do not necessarily use a greater number of words than others. A general explanation of such incongruity could be that auditors presenting more KAMs are using less detail per KAMs. Furthermore, the business environment and pertinent complexities of a certain sector may demand more KAMs to be disclosed; for example, more KAMs are disclosed by banks. Prior literature on risk disclosure (e.g. Khlif and Hussainey, 2016) found a divergence between industry groups. Conversely, auditors of some industry sectors may face difficulty in choosing KAMs and, therefore. Although they present fewer KAMs, they provide sizable descriptions of whatever issues they are reporting as KAMs.

We find a significant coefficient for firm size as a predictor of the number of KAMs disclosed (+2.32, $p = 0.021$) and the number of words used (+3.39, $p = 0.001$). This supports our prediction (H2a) that firm size has a positive association with KAMs disclosure. The finding is consistent with Velte (2018) and Suttipun (2022), that documented similar observations but inconsistent with Boonyanet and Promsen (2018), who found no significant relationship between firm size and KAMs disclosure. In line with Legitimacy theory, larger firms tend to meet social expectations more proactively than smaller firms (Taylor and Liu, 2008). Bigger firms are perceived to be involved with various social communities and a wide range of stakeholders. Moreover, larger firms usually engage Big auditors and spend more on audit services (Aldamen *et al.*, 2018), which may result in more issues disclosed in KAMs.

Our hypothesis (H1c) of a positive association between industry regulations and KAMs disclosure is justified and supported by our regression results (+1.75, $p = 0.049$). The findings suggest that the auditors of regulated firms disclose more in KAMs than the

Table 6. Regression results for KAMs disclosure and size of the new audit report

	Model-1 (No. of KAMs)	Model-2 (words in KAMs)	Model-3 (No. of KAMs)	Model-4 (words in KAMs)	Model-5 (KAMs: Big 4)	Model-6 (report Size)
INDUSTRY (Ref: Cement)						
Bank	4.39*** (0.000)	2.12** (0.035)	–	–	4.48*** (0.000)	4.46*** (0.000)
Ceramics	1.96** (0.0511)	1.15* (0.253)	–	–	2.11** (0.035)	0.81 (0.418)
Engineering	2.14** (0.033)	3.37*** (0.001)	–	–	2.63*** (0.009)	1.21 (0.150)
Financial Ins	3.54*** (0.000)	2.26** (0.034)	–	–	3.47*** (0.001)	5.38*** (0.000)
Food and *Allied*	2.79*** (0.006)	2.97*** (0.003)	–	–	2.93*** (0.004)	2.27** (0.024)
Fuel and *Power*	1.09 (0.278)	1.40 (0.163)	–	–	1.48 (0.141)	1.26 (0.207)
Insurance	3.37*** (0.001)	3.47*** (0.001)	–	–	3.10*** (0.002)	5.56*** (0.000)
IT Sector	0.90 (0.370)	2.01** (0.045)	–	–	1.08 (0.280)	1.92* (0.056)
Pharm. and *Che*	2.57** (0.011)	3.37*** (0.001)	–	–	2.59** (0.010)	1.79* (0.074)
Textiles	2.32** (0.021)	3.99*** (0.000)	–	–	2.61*** (0.009)	2.10** (0.037)
Others	2.95*** (0.003)	3.54*** (0.000)	–	–	2.92*** (0.004)	2.36** (0.019)
REGULATED	–	–	2.31** (0.022)	−0.68(0.498)	–	–
ENVIRONMENT	–	–	1.33(0.184)	3.73*** (0.000)	–	–
FIRM_SIZE	2.28** (0.023)	3.56*** (0.000)	2.17** (0.031)	3.11*** (0.002)	2.09** (0.038)	2.11** (0.035)
FIRM_AGE	2.57*** (0.010)	2.14** (0.033)	2.96*** (0.003)	2.29** (0.022)	2.78*** (* (0.006)	0.70 (0.482)
Big 4	−0.01 (0.995)	2.64*** (0.009)	−0.28 (0.779)	2.45** (0.015)	–	0.19 (0.847)
Big 4 Auditor (Ref: Deloitte)	–	–	–	–	–	–
PwC	–	–	–	–	−4.77*** (0.000)	–
Ernst & Young	–	–	–	–	0.30 (0.764)	–
KMPG	–	–	–	–	1.18 (0.238)	–
Non-Big 4	–	–	–	–	−1.66* (0.097)	–
AUDIT_FEES	0.30 (0.765)	−0.98 (0.330)	0.71 (0.478)	−0.88 (0.380)	0.30 (0.763)	−0.53 (0.597)
AUDIT_ SWITH	0.65 (0.516)	0.36 (0.720)	0.46 (0.643)	0.29 (0.771)	0.54 (0.588)	0.43 (0.664)
LEV	0.47 (0.640)	0.85 (0.395)	0.53 (0.594)	0.61 (0.541)	0.35 (0.726)	1.96** (0.050)
YEAR _END	−3.17*** (0.002)	−1.47 (0.142)	−1.80* (0.072)	−0.60 (0.546)	−2.46** (0.014)	−3.40** (0.001)
CONSOL	0.49 (0.626)	1.88* (0.067)	0.34 (0.733)	1.69* (0.093)	0.49 (0.621)	0.52 (0.606)
Year (Ref: Year 1)						
Year 2	2.80*** (0.005)	3.71*** (0.000)	2.73** (0.007)	3.63*** (0.000)	3.05** (0.002)	3.20*** (0.001)
constant	−2.61*** (0.009)	6.30*** (0.000)	−1.31 (0.192)	11.64*** (0.000)	−1.83** (0.067)	3.05*** (0.002)
Observations	412	412	412	412	412	412
R^2	0.1961	0.1951	0.1409	0.1577	0.2637	0.1886
Prob.> *F*-test	0.000***	0.000***	0.000***	0.000***	0.000***	0.000***

Note(s): *Significant at 10%. **Significant at 5%. ***Significant at 1%. *p*-value in parentheses
For the regression model, we use data of first two years of KAMs adoption T1 (211 observations), and T2 (201 observations) that were collected from three calendar years; this inconsistency is because all of the companies did not adopt KAM in the same year. INDUSTRY is a categorical variable

unregulated firms. Institutional theory can be used to explain the observations. Auditors of the regulated industry might feel pressure to disclose information on whether firms are complying with the industry regulations. This is also inconsistent with the argument of Boo and Sharma (2008) that the extensiveness of the external audit is lower in regulated firms. The finding does not conform to the conclusions from Pinto and Morais (2019), which showed a negative association between the level of industry regulations and the number of KAMs disclosed by firms in the UK The findings are also not in conformity with Delgado-Márquez *et al.* (2015), who evidenced a lower degree of environmental disclosure by regulated firms than unregulated ones.

Regarding the environmentally sensitive industries (H1d), the study findings do partly support the hypothesis with a significant positive coefficient (+3.73, $p = 0.000$) for the number of words in KAMs, while the coefficient is found to be insignificant for the number of KAMs. Auditors of environmentally sensitive firms, thus, provide an elaborative description for the issues selected and reported as KAMs. While sustainable development is now a concern for all stakeholders, an increased demand for more information from auditors is perhaps a driving factor behind such extensive disclosure from environmentally sensitive industries.

Our hypothesis (H2b) anticipates a positive impact of firm age on KAMs disclosure. Also, we find a positive coefficient for both the number of KAMs (+2.61, $p = 0.009$) and the number of words (+2.40, $p = 0.017$), suggesting that older firms disclose more in the KAMs section of the independent auditor's report. The observation is consistent with Suttipun and Nuttaphon (2014), documenting a positive link between firm age and corporate disclosure. Aged firms with more extended periods of operations in the marketplace have a higher social burden and are considered as socially responsible entities (Khaireddine *et al.*, 2020). In addition, older firms tend to ensure better financial reporting quality (Carey and Simnett, 2006).

As far as Big-4 is concerned (H3a), the study finds no significant impact of Big-4 affiliation and the number of issues disclosed as KAMs. However, a significant positive coefficient for the number of words (+3.04, $p = 0.003$) indicates a detailed disclosure by Big-4 affiliated auditors. The findings are not in agreement with that of previous studies. Wuttichindanon and Issarawornrawanich (2020) documented a positive association between Big-4 auditors and the number of KAMs disclosed by firms in Thailand. However, Velte (2020) found a significant association between Big-4 and KAM's readability in the audit reports of UK firms. In terms of extent of disclosure, our finding is consistent with the argument of Prasad and Chand (2017), declaiming a greater disclosure by Big-4 firms. Both institutional and legitimacy theories can explain why Big-4 affiliated auditors provide greater detail in KAMs disclosure than non-Big 4 auditors. The Big-4 affiliated firms need to serve more social expectations than their counterparts while maintaining their reputation of better audit quality and informative disclosure, as required by the parent Big-4 internationals.

We also run regression model 5 to estimate the association between the individual Big 4 affiliated firms and the number of KAMs, taking Deloitte as a reference. A negative coefficient for PwC (−4.77, $p = 0.000$) and the positive coefficient for Ernst &Young (+0.30, $p = 0.764$) and KPMG (+1.18, $p = 0.238$) provide evidence of a divergent number of KAMs across Big4 firms. The scenario is similar for the number of words in KAMs. This can be explained in line with the institutional theory, specifically with the leg of mimetic isomorphism. Adit partners of the same Big-4 associate (i.e. KPMG) might hold the same ideology and tend to follow the other partners of the same firm and disclose a similar number of KAMs in their reports.

Our results do not substantiate our hypothesis (H3b) for audit fees. A non-significant coefficient indicates no notable connection between audit fees and KAMs disclosure, whether measured by the number of issues disclosed or by the number of words used in KAMs. The findings conform to Bédard *et al.* (2019), recording no association between the justification of assessments (JOAs) and audit fees reported by firms listed in France. Our findings, however, contradict Suttipun (2022) and Pinto and Morais (2019), who found a positive impact of audit fees on KAMs reporting.

Finally, among the control variables, the results for audit rotation is consistent with Suttipun (2022), documenting evidence of no significant impact of auditor rotation on KAMs disclosure. This is, however, inconsistent with Velte (2018), who observed a link between auditor rotation and KAMs readability in UK firms. This suggests that audit rotation's impact varies between the developed and emerging economies.

5.2 Sensitivity analysis and robustness of the results

For our results' sensitivity analysis and robustness, we first use the length of the independent auditor's report instead of the number of KAMs and number of words, as shown in Table 6 (Model 4). Because of the issuance of a varying number of KAMs with divergent disclosure, the length of reports is expected to differ significantly across other industry sectors. However, consistent with our hypotheses (H1a) and (H1b), the coefficients for report size vary substantially across industry sectors. Notably, the lengthiest reports are issued to banks (mean = 5.40), whereas companies belonging to the cement sector (mean = 4.05) and the ceramic sector (mean = 3.82) receive relatively shorter reports. Other sectors receive audit reports of nearly 4.70 pages. These variations are presumably owing to industry characteristics. These observations align with the IAASB's expectation of unconventional and non-boilerplate reporting to indicate the commencement of a new era of audit reporting.

The significant positive coefficient for firm size supports our hypothesis (H2a) and is consistent with our main results. However, firm age was found not to be significantly associated with audit report size, thereby rejecting our hypothesis (H2b). Our observations for (H3a), (H3b) and (H3c) are consistent with our findings from primary models.

We then use the number of KAMs and number of words instead of their natural logarithm as a measure of KAMs disclosure to estimate the relationship between our variables of interest. The regression results (untabulated) are similar to the findings from the main analyses.

5.3 Additional analyses

We now concentrate on the types of KAMs disclosed by firms in Bangladesh. Table 7 presents descriptive statistics and ANOVA results of the types of KAMs reported within and across industries, as reported by auditors of listed firms in the first year of adopting the new standards. A total of 780 KAMs were observed in the 246 reports scrutinized in the current study. By a sizeable margin, revenue recognition was the most commonly reported KAM, disclosed by 156 firms (63.41% of companies in our sample) and embodying 20.00% of all KAMs presented. This observation is consistent with Suttipun (2020) findings, who found revenue recognition the most reported KAM in Thailand. However, it is inconsistent with Abdullatif and Al-Rahahleh (2020), who found that only around 6% of Jordanian firms reported this issue (against the most reported KAM "accounts receivable" disclosed by 35%). Although not the most common, this item was among the top five KAMs reported in developed markets, such as the UK, Australia and New Zealand (KPMG, 2017; External Reporting Board [XRB] and Financial Markets Authority [FMA], 2017). The KAM second most frequently furnished by auditors was issues related to taxation (observed in 101 firms), portraying 12.95% of the total KAMs' counts. Although taxation was the third and fourth most commonly reported KAM in the UK and Australia (Deloitte, 2017; KPMG, 2017), this item was not among the top five KAMs reported in other jurisdictions. Inventory valuation (reported by 91 firms) was the third most frequently reported KAM. This issue was among the top five KAMs reported by Thai, Jordanian and Australian firms but was not among those reported by firms in New Zealand. The reported sequence was investments (75 firms);

Table 7.
Descriptive statistics and ANOVA results for types of KAMs reported within and across industries in the year of adoption

KAM types	Obs	%	% Com	Mean[1]	ANOVA S.D.	F	p-value
Multivariate test (across 12 industry sectors)						44.36	0.000**
Accounts receivable	13	1.67	5.28	0.05	0.228	1.974	0.032*
Accruals/liabilities	46	5.90	18.70	0.19	0.396	15.133	0.000**
Accounting for long-term/complex contracts	11	1.41	4.47	0.05	0.211	1.418	0.166
Acquisitions/disposals	2	0.26	0.81	0	0.065	3.987	0.000**
Actuarial assumptions	1	0.13	0.41	0	0.065	0.464	0.924
Assets held for sale	8	1.03	3.25	0.03	0.181	2.234	0.014*
Asset impairment/property, plant and equipment	69	8.85	28.05	0.27	0.447	6.553	0.000**
Business combination/restructuring/ finance process	1	0.13	0.41	0	0.065	0.41	0.951
Controls and IT system	39	5.00	15.85	0.16	0.368	15.209	0.000**
Costs/charges	42	5.38	17.07	0.18	0.383	54.59	0.000**
Disclosure/presentation/classification	2	0.26	0.81	0.01	0.092	1.993	0.03*
Exceptional/one-off transactions	1	0.13	0.41	0	0.065	5.006	0.000**
Financial instruments	8	1.03	3.25	0.03	0.17	1.184	0.299
Goodwill impairment	3	0.38	1.22	0.01	0.112	0.311	0.983
Inventory valuations	91	11.67	36.99	0.38	0.486	12.654	0.000**
Investments/investment in subsidiaries	75	9.62	30.49	0.25	0.433	12.618	0.000**
Others	44	5.64	17.89	0.16	0.372	4.123	0.000**
Pensions/retirement benefits	9	1.15	3.66	0.04	0.192	1.134	0.335
Provisions/legal provisions/contingent liabilities	54	6.92	21.95	0.21	0.406	6.456	0.000**
Revenue recognition (fraud)	1	0.13	0.41	0	0.065	0.84	0.601
Revenue recognition	156	20.00	63.41	0.66	0.475	12.837	0.000**
Share-based payments	3	0.38	1.22	0.01	0.112	0.311	0.983
Taxation	101	12.95	41.06	0.41	0.494	3.421	0.000**
Total	*780*	*100.00*	–	–	–	–	–

Note(s): S.D. = standard deviation; superscript asterisks **significant at 1% level; *significant at 5% level
[1]We coded 1 and 0 for presence and absence, respectively, across 27 types of KAMs for each of the 237 companies

impairment and valuation of property, plant and equipment (69); and provisions and contingent liabilities (54). These top six KAMs represented 70.00% of all KAMs reported in the first year of extended reporting. The observations indicate that auditors are disclosing industry-specific KAMs. In line with institutional theory, auditors in Bangladesh are decoupling by restricting the application of ISA701 to disclose industry-specific KAMs, not making them firm-specific.

We examine whether the types of KAMs differ across industries. The ANOVA results ($F = 44.36$, $p = 0.000$), as in Table 7, reveal statistically significant differences among the types of KAMs disclosed. This observation exemplifies industry-specific disclosure. It is also consistent with prior studies that find significant differences in corporate risk disclosure across industry sectors (Amran *et al.*, 2008; Madrigal *et al.*, 2015). The results also align with how firms embedded in different industry sectors communicate their CSR activities and how firms in different industry sectors orient their stakeholders (Jain *et al.*, 2016). Standard-setters and regulators would be satisfied, at least to some extent, with this observation of non-boilerplate reports.

Our analysis further shows that of the 201 firms observed in the second year, 50 firms (24.87%) reported the same issues that were reported in the year of adoption of KAMs' disclosure. This observation recalls the concern shown by the AUASB that KAMs' disclosure would soon become boilerplate reporting (AUASB, 2013). However, the remaining 151 firms changed at least one item in their KAMs' selection. In contrast, 176 firms reported at least one item that was reported in the previous year. Therefore, only 25 firms (12.44%) reported totally new issues as KAMs in their report in the second year post-KAMs' disclosure adoption. According to institutional theory (decoupling), auditors may disclose KAMs as merely a compliance exercise but not necessarily as an opportunity to enhance the communicative value of the audit report.

We argue that the ongoing auditors tend to boilerplate reporting, and a new auditor might report a new KAM. Further, Big 4 auditors are also expected to disclose new KAMs to maintain their firm image and reputation. We thus assume an association between change in KAM type, Big-4 auditor and auditor rotation. We ran the following logistic regression and OLS regression to examine whether the introduction of a new KAM is associated with Big4 auditor and auditor rotation [1, 2]

$$AllNewKAM_{it} = \alpha_0 + \beta_2 BIG - 4_{it} + \beta_1 AUDIT\_SWITCH_{it} + \sum CONTROLS_{it} + \varepsilon_{it} \quad (7)$$

$$NewKAMratio_{it} = \alpha_0 + \beta_2 BIG - 4_{it} + \beta_1 AUDIT\_SWITCH_{it} + \sum CONTROLS_{it} + \varepsilon_{it} \quad (8)$$

As expected, our results of logistic regression (untabulated for brevity) show a significant positive (+1.80, $p = 0.070$) relationship between auditor rotation (*AUDIT_SWITCH*) and all new KAMs in the independent audit reports in Bangladesh. This indicates that the ongoing auditors tend to disclose the same type of KAM as reported in the previous year. On the other hand, we find no connection between Big-4 auditors and all-new KAMs.

Then, the regression results (untabulated for brevity) for the ratio of new KAMs show a significant positive coefficient (+3.57, $p = 0.000$) for Big-4, which indicates that the Big-4 affiliated auditors tend to disclose more new KAMs, compared to the non-Big-4 firms. These observations support prior literature that evidenced a better quality audit and reporting by Big-4 firms (e.g. Wang *et al.*, 2008; Ahmad *et al.*, 2015).

Among the issues presented as KAMs, the auditor may choose to place one KAM over another due to their respective importance. Similarly, the auditor may prefer some issues to be placed later in the sequence; this could be due to the issues being complex or could be at the request of the client firm. Past studies show how and where the information disclosed impacts users' decisions (Higgins and Walker, 2012). Again, auditors may like to place relatively negative information in a later section of the KAMs' disclosure. Business firms use different legitimization strategies to shape disclosure communications relating to negative occurrences (Rudkin *et al.*, 2018). Prior studies have shown that firms use impression management techniques to hide bad news (Guillamon-Saorin *et al.*, 2017). Furthermore, the choice order may be affected by the auditor's demographics. Numerous evidence is available of differences in judgment and choice between male and female auditors (e.g. Ittonen *et al.*, 2013).

We use multivariate analysis to examine whether the presentation order/rank of KAMs significantly differs across firms. The results of multivariate analysis (Table 8) show that auditors prefer placing certain items over others in the KAM section. Specifically, auditors prioritize the following issues, if selected as KAMs, in this order: revenue recognition; inventory valuation; taxation; property, plant and equipment (PPE); investment, etc. This is possibly due to their respective importance in audit judgment and estimation.

6. Discussion and conclusion

The study investigates mandatory KAMs' disclosure in Bangladesh. The study examines KAMs' disclosure in annual reports by listed companies on the Dhaka Stock Exchange (DSE),

KAM types	N	Mean[1]	S.D.	F	p-value
Multivariate test (across 246 companies)				97.79	0.000**
Revenue recognition	246	50.63	37.41	43.43	0.000**
Inventory valuations	246	25.91	33.59	14.10	0.000**
Taxation	246	25.32	30.83	15.98	0.000**
Asset impairment/property, plant, and equipment	246	17.93	29.77	8.60	0.000**
Investments/investment in subsidiaries	246	15.95	28.41	7.47	0.000**
Costs/charges	246	13.88	30.03	5.06	0.000**
Accruals/liabilities	246	12.19	25.20	5.55	0.000**
Provisions/legal provisions/contingent liabilities	246	10.72	22.30	5.47	0.000**
Others	246	10.55	24.41	4.43	0.000**
Controls and IT system	246	7.72	18.32	4.21	0.000**
Accounts receivable	246	3.04	12.89	1.32	0.000**
Accounting for long-term/complex contracts	246	2.74	12.74	1.10	0.001**
Assets held for sale	246	2.24	12.06	0.82	0.005**
Financial instruments	246	1.98	11.64	0.69	0.009**
Pensions/retirement benefits	246	1.69	9.00	0.83	0.004**
Share-based payments	246	0.89	7.84	0.30	0.083
Disclosure/presentation/classifications	246	0.51	5.50	0.20	0.158
Acquisitions/disposals	246	0.34	5.20	0.10	0.318
Actuarial assumptions	246	0.34	5.20	0.10	0.318
Revenue recognition (fraud)	246	0.34	5.20	0.10	0.318
Business combination/restructuring	246	0.25	3.90	0.10	0.318
Exceptional/one-off transactions	246	0.25	3.90	0.10	0.318

Note(s): S.D. = standard deviation; superscript asterisks **significant at 1% level; *significant at 5% level
[1]As a maximum of eight KAMs are reported in Year 1, a KAM reported first in order received a score of 80, second in order received a score of 70, third in order received a score of 60, etc.. We then computed the mean rank score for each of the 27 KAM types

Table 8. Univariate and multivariate results for presentation order of KAMs in audit reports of listed companies in Bangladesh

Bangladesh. Debate, however, continues regarding the adequacy and effectiveness of the new reporting framework through ISA 701, particularly KAMs' disclosure. KAMs have been considered an important catalyst for change, improving audit communication with users. Inspired by the lack of research in emerging economies and on their market distinctiveness, in this study, we examine the number and types of KAMs disclosed and the extent of the disclosure provided in independent auditors' reports. The study also investigates whether the KAMs' presentation varies within and across industry sectors.

Using a sample of 447 reports from 2018 to 2020 from firms listed on the Dhaka Stock Exchange (DSE), Bangladesh, we find that auditors are reporting on KAMs in divergent ways in their financial reports. Our study's observations are generally consistent with contemporary studies (Wei *et al.*, 2019; Suttipun, 2020) on the new KAMs' reporting. The findings on the number and type of KAMs and the extent of variability in their disclosure, support prior risk disclosure studies (Madrigal *et al.*, 2015; Jain *et al.*, 2016; Dumay and Hossain, 2018). Firm size and firm age both are found to affect KAMs significantly. The observation for firm size is consistent with a recent study by Suttipun (2022) investigating KAMs in Thailand. The inference for firm age, on the other hand, is consistent with Suttipun and Nuttaphon (2014), who found a positive firm age effect on corporate disclosure. Regarding the Big-4 concentration, there is no significant difference between Big-4 affiliated auditors and non-Big-4 auditors concerning the number of issues disclosed as KAMs. However, the Big-4 associates provide greater detail in KAMs description than the non-Big-4 firms. The findings though inconsistent with Wuttichindanon and Issarawornrawanich (2020), are consistent with the argument of Prasad and Chand (2017), contending a greater disclosure by Big-4 auditors. Auditors of Big 4 associates may feel coercive or mimic pressure to provide a greater disclosure. Furthermore, as expected by the IAASB, auditors are issuing audit reports of different sizes when communicating the audit aspect with an increased level of KAMs' disclosure.

Both legitimacy theory and institutional theory support our study's findings. From a legitimacy perspective, we notice that listed firms in Bangladesh have responded well to the international call for extended reporting and are now reporting KAMs in the audit report. From the institutional theory perspective, the new standard is well adopted by ICAB due to the coercive pressure from the FRC and the international donor bodies such as the World Bank. Auditors have regulatory pressure (coercive isomorphism) from ICAB to report KAMs in the independent auditor's report and are now complying with the new standard, ISA 701. However, KAMs' disclosure is significantly affected by industry (mimic) isomorphism, namely, the different driving forces in various industry sectors. Banks and financial firms, being highly regulated and involved with people from all walks of life (hence, a larger stakeholder base), disclose more KAMs in greater detail to meet the demands of diverse groups, supporting institutional theory. Environmentally sensitive firms in sectors such as textiles, engineering, pharmaceuticals and chemicals, food and allied, paper and printing and tannery, being in competitive markets with environmental externalities, are disclosing KAMs adequately with greater details in their KAMs report. Conversely, firms in oligopolistic markets, such as cement and information technology (IT), provide minimal disclosure. In an oligopolistic market, competition is not high, and firms have extreme power with greater profit-making opportunities. Therefore, firms can resist institutional pressures as these pressures are not sufficiently robust to affect firms' profitability and ongoing existence (Campbell, 2007). However, auditors may experience internal and external pressure that eventually shapes the firm's KAMs' disclosure. The mimitic isomorphism can be linked here to interpret such variability across industries. Further investigation is thus warranted in the context of the auditor's judgment to expand our theoretical explanation of the construction of KAMs' disclosure.

Although we find the types of issues selected and reported as KAMs are statistically different between companies, a very high level of similarity is observed between many companies as they report some common topics as KAMs. Our study findings suggest that auditors may find it challenging to identify KAMs or, *ipso facto*, perhaps these are common issues of concern regardless of the industry sector. While the auditors, in general, have the tendency to boilerplate KAMs, Big-4 associates are found to disclose more new types of KAMs in the following year. In line with the decoupling leg of institutional theory, auditors are complying with the new standard but restricting the disclosure to specific issues, without making them more industry-specific and firm-specific. However, if such commonality persists in the reporting, users would feel less interest in the additional disclosure in the short run. Consequently, the time and labour spent on extended reporting would be in vain. Therefore, regulators and policymakers (i.e. the ICAB) would benefit by assessing whether auditors are in line with their expectations when requiring the issuance of an extended audit report. We recommend the rigorous engagement of Big-4 firms in the Bangladeshi market to reap the intended benefit of KAMs disclosure. Our comparative analysis over two years shows an increasing trend in KAMs' disclosure in 2020, with the size of the issued report having a similar trend. Undeniably, this is a reflection of judgment-based KAMs' disclosure and signifies the departure from boilerplate reporting. However, if a report has too many KAMs disclosed, it may lose its significance, and the intended purpose of extended reporting may not be sustained.

Though the findings from the Mazars (2018) report show that ISA 701, related to KAMs, has been applied with consistency across developed countries such as the France, the Netherlands and the United Kingdom, "Other countries" also found similar tendencies with regards to the application of KAMs. However, our findings indicate that the ISA 701 standard lacks well-defined instructions for implementing KAMs' disclosure in Bangladesh. Based on our findings, we argue that the present paradigm could be calibrated for proper implementation of entity-specific insightful reporting to provide more specific guidelines regarding KAMs' disclosure. For example, given the facts, standard setters could fix a range for the number of KAMs to be disclosed. The range could even be specific to the industry sector; for example, for banks, it could be at least three KAMs. In addition, we suggest that some broad areas, such as internal control, corporate governance, third-party transactions, etc., could be recommended as areas in which at least one KAM should be presented. Furthermore, auditors could provide directions regarding year-on-year KAMs' choices, that is, whether the KAM topic can be the same in the current year as it was in the prior year.

In theoretical terms, our findings shed new light on KAMs' disclosure in an emerging economy context. The findings report on the formal regulatory pressure from the Financial Reporting Council (FRC) to adopt KAMs' disclosure by listed companies in Bangladesh. However, a risk exists regarding the usefulness of implementing the KAMs' requirement in Bangladesh as, in most cases, Bangladesh adopts all accounting and financial reporting rules without considering the socio-economic context (Khan *et al.*, 2013). Institutional isomorphism suggests that institutional factors play a crucial role in audit practice globally, and Bangladesh is no exception. Consistent with prior literature, the current study's findings indicate that coercive pressure has led to the increasing KAMs' disclosure pattern in Bangladesh (Abdullatif and Al-Rahahleh, 2020). The results further show that few firms voluntarily disclose materiality information, although this is a vitally important concept in an audit engagement, having both informative and communicative value. From the legitimacy theory perspective, it could be argued that companies in Bangladesh are trying to legitimate their behaviour by providing more information on KAMs in their annual reports. This finding is consistent with a recent study that examined KAMs' disclosure in Thailand, a developing country and argued that to maintain or gain legitimacy, it is essential for a firm to undertake KAMs' disclosure (Suttipun, 2020). Legitimacy theory argues that companies provide KAMs' disclosure to comply with their stakeholders' social expectations (e.g. Deegan and Islam, 2012). Our study findings support the argument that Bangladeshi companies within and across industry sectors are increasing their KAMs' disclosure to gain a social "license to operate" in Bangladeshi society as a legitimate organization.

Apart from their theoretical implications, the study results should be of interest to policymakers and regulators of other developing countries and emerging economies that share similar cultural, regulatory and contextual values. In addition, standard-setters and information users may consider whether the present standard is adequate. Arguably, one firm from a given industry sector may not disclose any KAMs, while others in that same sector may disclose nine or 10, thus indicating an inconsistency in KAMs' disclosure in Bangladesh. This incongruity could be that some auditors are very active in utilizing this novel opportunity to communicate audit insights to investors and other stakeholders, while others are more passive. This imbalance may undermine the purpose of KAMs' reporting. Another reason is that a client firm may influence or motivate its auditor not to report KAMs, arguing or claiming that other companies are doing likewise in not reporting KAMs. Consequently, we may observe more reporting that does not include KAMs as time progresses and, eventually, reports will again be standardized, a concern shown by the AUASB (2013).

Our findings support several initiatives undertaken by the IAASB and the ICAB in Bangladesh to improve audit communication to enhance accountability to users of audit information and their call for unique firm-specific reporting. The study findings show much variability between firms. While some variations in the audit report are needs-based and well justified, others could confuse and dishearten users. For example, some auditors are using the term "risk" instead of "key audit matter". Some are disclosing additional information, namely, materiality, even going beyond the requirement of the standard, while others are only disclosing minimal information. This type of situation may make comparability grounds unbalanced, thereby creating difficulty for potential investors in assessing the reports and reaching the proper conclusion.

The current study makes several contributions to the auditing literature. Firstly, this is the first study available in the context of an emerging economy, such as Bangladesh, to unravel and analyze KAMs' disclosure. We add to prior studies' investigations of the enhanced audit reporting model with our novel evidence on the relationship between the industry features, firm characteristics, auditor attributes and KAMs disclosure. Secondly, the findings are instrumental to national and international regulators in assessing the efficacy of the new standard on KAMs' disclosure. The IAASB (2015) has stated that once KAMs' reporting is adopted globally, researchers would find avenues to investigate its value enhancement. Thirdly, the audit profession will benefit from the study findings in gaining an enhanced understanding of what and how KAMs are disclosed by auditors in an emerging economy, such as Bangladesh, where the audit profession is regulated under a weak accountability structure. This is in line with Dobler *et al.* (2011), when they emphasized the risk disclosure practices of emerging economies, with our investigation a solid response to their call. Fourthly, the study findings may help information users by providing helpful feedback on their long-demanded additional disclosure to assist their decision-making. Finally, the results suggest that investors can assess the risk and complexities of the current market and, thus, match them to their intended company before investment. A survey in Singapore found that most of the surveyed investors and audit committee members felt that the new model was a significant improvement over the standard report (PwC, 2017b). Similarly, firms' top management would find the study results useful in responding to and tackling the risks prevalent in their industry sector or in the market. Top management now also has evidence of what issues are most often reported by auditors as KAMs across the listed firms in our sample. This may impact their bargaining power regarding KAM topics. Finally, our study is one of the earliest attempts to investigate audit report length after adopting KAMs' disclosure in an emerging economy, such as Bangladesh, with previous studies reporting no significant variation in the length of audit reports before adoption.

The current study's findings are subject to several limitations that could open avenues for future research. This study investigates the first two years of KAMs' disclosure adoption in Bangladesh. A future study might consider observations over multiple years which could produce different results. In addition, we ignored some industry sectors, such as mutual funds, treasury bonds, etc., in our study due to the distinctive nature of their operations. However, future research could seek greater insights into KAMs' presentations, for example, whether observations differ from those in the transition phases. This study is based on secondary data; thus, it has not considered the perceptions of users and regulators on the adoption of KAMs' disclosure. Future research may consider in-depth qualitative interviews with audit professionals, professional bodies, regulators and users of audit information to explore the actual disclosure by auditors in their KAMs' descriptions and the language and tones used.

Notes

1. We coded 1 for firms that reported all of their KAMs totally new in year 2 i.e. none of the issues were reported in year 1; otherwise 0.
2. We computed ratio of new KAMs to total KAMs for each of the firms in year 2.

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