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## The Effect of Disclosing Key Audit Matters in the Audit Report on Investors' Decisions: A Field Study in Egypt

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### Abstract

This research aims to examine the reactions of investors, auditors, and other interested parties to the audit report using modified auditing standards which consist of disclosure of audit risks through the key audit matters paragraph (KAMS) as mandated by ISA 701. In addition to investigate whether the KAMS disclosure has a positive effect on narrowing gaps between what the auditor produced and what investors need. Analyzing the practices of applying the requirements of ISA 701 in Egypt, evaluate the potential need for adjustments or enhancements in auditing and reporting standards, and explore whether the presence of audit risks in the KAMs paragraph influences investors to adjust their risk assessments for the right investment decisions.

The theory that's used in this research is signaling theory, which is applied to explain the relationship between key audit matters disclosure and investor's reactions.

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## **The Effect of Disclosing Key Audit Matters in the Audit Report on Investors' Decisions: A Field Study in Egypt**

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The study used a simple random sample, and data was obtained from the sample respondents of 384 observations based on the equation of Thompson, Stephen, as larger studies give stronger and more dependable results since they have narrower margins of error and lower standards of deviation.

This study was applied to the Academic staff members, Auditors, Accountants, and Investors to achieve the objectives of the study.

Our result suggests that the mandate of KAM's disclosure has positive effect on the decision of Egyptian investors Also, updated information content in the auditor reports, including key audit matters paragraphs, has a great impact on narrowing gaps between the auditor and the investors.

**Keywords:** Key audit matters, Audit risk, Auditor's report, Investors decisions

## تأثير الإفصاح عن أمور المراجعة الرئيسية في تقرير مراقب الحسابات وانعكاسها علي قرارات المستثمرين: دراسة ميدانية

### الملخص

يهدف هذا البحث إلى فحص ردود فعل المستثمرين و المراجعين و الاطراف المعنية الاخرى تجاه تقرير المراجعة باستخدام معايير المراجعة المعدلة التي تتكون من الإفصاح عن مخاطر المراجعة من خلال فقرة أمور المراجعة الرئيسية وفقاً لما يفرضه معيار المراجعة الدولي 701 . بالإضافة الي التحقق مما إذا كان الإفصاح عن فقرة أمور المراجعة الرئيسية له تأثير إيجابي على تضيق الفجوات بين ما ينتجه مراقب الحسابات وما يحتاجه المستثمرون. تحليل ممارسات تطبيق متطلبات معيار التدقيق الدولي 701 في مصر، وتقييم الحاجة المحتملة للتعديلات في عملية المراجعة و معايير اعداد تقارير مراجعة المصرية ، واستكشاف ما إذا كان وجود مخاطر المراجعة في فقرة أمور المراجعة الرئيسية يؤثر على المستثمرين لتعديل تقييمات المخاطر الخاصة بهم لاتخاذ قرارات الاستثمارية الصحيحة. النظرية المستخدمة في هذا البحث هي نظرية الإشارة، والتي يتم تطبيقها لشرح العلاقة بين الإفصاح عن أمور المراجعة الرئيسية وردود أفعال المستثمرين. استخدمت الدراسة عينة عشوائية بسيطة، وتم الحصول على البيانات من أفراد العينة البالغ عددهم 384 ملاحظة بناءً على معادلة طومسون، ستيفن، حيث أن الدراسات الأكبر حجماً تعطي نتائج أقوى وأكثر موثوقية حيث أن هامش الخطأ فيها أضيق ومعايير الانحراف أقل. وقد تم تطبيق هذه الدراسة على أعضاء هيئة التدريس والمراجعين والمحاسبين والمستثمرين لتحقيق أهداف الدراسة. وتشير النتائج التي توصلنا إليها إلى أن الإفصاح عن مخاطر المراجعة من خلال فقرة أمور المراجعة الرئيسية له تأثير إيجابي على قرار المستثمرين المصريين. كما أن محتوى المعلومات المعدل في تقارير المراجعة، بما في ذلك فقرة أمور المراجعة الرئيسية، لها تأثير كبير على تضيق الفجوات بين ما يقدمه المراجع و بين وما يحتاجه المستثمرين.

**الكلمات المفتاحية :** أمور المراجعة الرئيسية، مخاطر المراجعة، تقرير مراقب الحسابات، قرارات المستثمرين.

## **The Effect of Disclosing Key Audit Matters in the Audit Report on Investors' Decisions: A Field Study in Egypt**

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### **Introduction**

Investors are considered an important element in establishing financial markets. They provide capital for new companies and expand the activity of existing companies.

That's why, in recent years, population growth, the expansion of the economy, financial disasters, and wars have led to the complexity of economic life, which has reduced the credibility of the information presented by financial institutions.

Thus, investors need reliable information from sources like financial statements and audit reports to make correct investment decisions.

An auditor's report acts like a communication tool to report whether the financial statements are free from material misstatement, provide an opinion to different users of financial statements, like bankers, investment analysts, shareholders, and the government, to notify them when the audited financial statements have a strange issue.

During the global financial crisis, the traditional auditor's reporting did not sufficiently disclose financial risks as most of the failed financial institutions received unqualified opinions before failing Doogar et al. (2015, p.3). To try to manage this situation, standards setter's bodies like IAASB have revised the format and content of the auditor's report in order to rebuild the user's confidence and satisfy capital market demand for high audit quality. The IAASB issued the revised version of International Standards on Auditing ISA 701, "Communicating Key Audit Matters in the Independent Auditor's Report," to change current style and make it more useful and transparent. This standard requires auditors to disclose key audit matters in the audit report. KAMS will be used as an independent message from the auditor's opinion to any investor to understand the business and the significant risks that are difficult to investigate.

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The (IAASB) believes that the disclosure of key audit matters in the auditor's report will improve quality of the audit report and narrow the information and communication gap between the auditor and the investors.

So, this research applied to investigate the effect of disclosing audit risk through key audit matter paragraphs on the investor's decision and if the investors were able to understand the new auditor's report with KAMs disclosure and is it useful for them to make correct investment decisions.

**Therefore, the research will be classified into Eleven parts as follows:**

### **1.Literature Review**

There is an argument in the literature review applied and last studies about the role of audit risk disclosure through Key audit matters on investors decisions as follows:

According to **Muñoz-Izquierdo et.al**, that examined the usefulness of key audit matter disclosures (KAMs) in assessing financial distress levels in client firms, finding a positive association between the number of KAMs disclosed and the level of financial distress, with specific types of KAMs being more likely to be disclosed in financially distressed firms. The results indicate that KAMs could predict future levels of financial crisis also, providing evidence for financial statement users to evaluate risks of the firm failure.

**(Muñoz-Izquierdo et.al.,2024, p.18)**

Also, **Shoja et al.**, intended to investigate the opinions of both professional and non-professional investors on Critical Audit Matters (CAM) according to International Auditing Standard No. 701.The statistical sample consists of 100 investors, 50 of whom are professionals and 50 of whom are non-professionals, all of whom were available and carefully chosen for the sample.

## **The Effect of Disclosing Key Audit Matters in the Audit Report on Investors' Decisions: A Field Study in Egypt**

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This research assessed professional and non-professional investors' perspectives on the important audit matters in the auditor's report. Investors believe that the identification and disclosure of significant audit matters will enhance the information value of the auditor's report, reduce the report's uniformity or standardization, increase the auditor's professional and legal liability, also, enhance investor decision-making, audit quality, and auditor independence. Nevertheless, non-professional investors experience the opposite.

**(Shoja et al.,2024, p.2-4)**

**Lin** in his research analyzed the impact of Key Audit Matters (KAMs) disclosure on audit quality using a large sample of annual audit reports from listed companies in Shanghai and Shenzhen Stock Exchanges evaluating the effect of KAM disclosures on audit quality by using regression analysis and evaluating the information value of the disclosures. The result indicates that there is significant positive correlation between key audit matters disclosure and audit quality as validated by both the main regression test and the robustness test, revealed varying effects of KAM relatedness based on the level of disclosed risk. **(Lin, 2023, p.3,11)**

While, **Hoang et al.**, examined the impacts of Key Audit Matters (KAMs) and risk items disclosure by management on investors' perceptions and decisions in both financial and non-financial contexts by conducting an experiment to manipulate risk item disclosure and KAM relatedness, finding that when a disclosed risk is reasonably high, investors evaluate risk and willingness to invest equally in financial and non-financial contexts. When a company discloses a relatively low-risk item, context matters such that we find opposing effects of KAM relatedness on investors' perceptions in a financial and a non-

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financial context. When a KAM is related to the financial (non-financial) risk item, investors assess investment riskiness higher (lower) and are less (more) willing to invest than when a KAM is unrelated. (Hoang et al.,2023, p.2,18-19)

The influence of various factors on the disclosure of Key Audit Matters (KAMs) in companies listed in Bangladesh, are investigated by **Rahaman et al.**, by revealing significant differences in the number and types of KAMs reported across firms and industry sectors, aiming to contribute the accounting and auditing literature by examining KAMs in the context of an emerging economy like Bangladesh, and emphasizing the importance of transparency and confidence in financial reporting through enhanced disclosure practices. This research concluded that there are significant variations in KAMs disclosure among firms depend on factors like regulation, environmental sensitivity, firm size, and loyalty and both age and size of the firm has positively impact on the number of KAMs disclosed. (Rahaman et al.,2023, p.1,25-27)

**Chen et al.**, discussed the impact of changing audit firms and all signing auditors together on the disclosure of critical audit matters (CAMs) in Chinese listed companies, emphasizing the importance of adequate CAM disclosures in improving audit and financial reporting quality and stock market pricing efficiency. They found that changing the audit firm and all signing auditors together leads to more CAM disclosures and better audit quality. They also addressed the need for standardization in CAM disclosures and the potential benefits of larger audit firms in enhancing CAM disclosures. (Chen et al.,2023, p.2-3,14)

**Chang et al.**, In their research used text analysis to investigate if and how investor opinion on the quality of financial

## **The Effect of Disclosing Key Audit Matters in the Audit Report on Investors' Decisions: A Field Study in Egypt**

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reporting, as measured by the earnings response coefficient, are related to the information content of KAMs and its importance in enhancing the value of audit reports by using a sample of KAMs disclosed in Taiwanese audit reports for years 2016 and 2017. The result was found that companies that have a great detail in Key audit matters paragraph have less reporting quality as they think that risk-related description in KAMs affected this poor quality. (Chang et al.,2022, p.1-4,14)

**Ibrahim** found an appropriate opportunity to evaluate the experience of applying this new model in an Arab country, to learn about the impact of applying the international auditing and assurance standard No. (701) on investors' decisions, as well as identifying the impact of the characteristics of Saudi companies and their boards of directors at the level of disclosure of key audit matters. To achieve the objectives of the study, multiple regression models were used by applying them to 50 companies It belongs to different sectors in the stock market in the Kingdom of Saudi Arabia, during two years 2017 and 2018 The study concluded that there is a significant effect of disclosing the key audit matters on investors' decisions, the study also showed that there is a significant impact of the characteristics of companies and their boards of directors on the level of disclosure of key audit matters.(Ibrahim,2021,p.2-5,50-53)

**Rapley et.al**, are the first to investigate how the disclosure of the audit firm's tenure and the relative benefits of a CAM disclosure vs a disclosure that the auditor did not find a CAM affect the opinions of nonprofessional investors. They concluded that: Disclosing a CAM reduces investment intentions compared to disclosing no CAMs were identified.



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- The study addresses the need for evidence on the outcomes of policy decisions and the impact of expanded auditor reporting.
  - Investors find CAM disclosures informative and useful for making investment decisions. (Rapley et al., 2021, p.2,10,16)

The study of **Coram et.al**, investigated the impact of disclosing key audit matters on users' perceptions of auditors' responsibility and the reliability of financial statements finding that the disclosure of KAMs did not reduce the audit expectation gap.

- Users assign a higher level of reliability to audited financial statements when the KAM area conforms to an objective (precise) standard compared to a subjective (imprecise) standard. (Coram et. al., 2021, p.1-3,7)

**Altawalbeh et al.**, evaluated how key audit matters (KAMs) disclosure affects investor decisions. To do this, the researchers look at how the Jordanian market responded to KAM disclosures also by gathering and examining the financial records of the public shareholding businesses listed on ASE, the study attempts to examine how the criteria of ISA 701 are applied in the financial reports of the of public shareholding companies listed on ASE. the study population consists of All public shareholding businesses that were listed on ASE during the study period and for which the necessary data were available However, of the 128 public shareholding businesses in the final sample, 16 of them did not include any KAMs in their audit report. The research found that the requirement of KAM's disclosure has informational value to investors and showed that the disclosure of KAMs significantly influenced investors' judgments as indicated by the anomalous trading volume. (Altawalbeh et al. ,2019, p.1,4,8)

## **2. Research Problem**

Decision-making process is influenced by the audit report, which is attached to the corporate financial statement. It is considered the link between the auditor and investors; through it the auditor expresses his opinion regarding the financial statements prepared by management. Therefore, the audit report represents great importance for investors who rely on it to make their investment decisions. But after the 2008–2009 global financial crisis and the failures of some businesses, like Enron company Investors' concerns about the current audit report's inability to meet their needs because it's simple, standard and summarized report. In response to investors' concerns, IAASB established a new standard ISA 701 that increases investors' knowledge and understanding of issues that significantly impact the reliability and quality of financial statements Thus, the researcher's goal throughout this study is to verify the impact of applying the international auditing standard ISA701 on Egyptian investors whereas an expectation gap in the field of audit service in Egypt to which the role of the Egyptian auditor is affected to focus on the disclosure of audit risks in the key audit matters paragraph in the auditor's report and whether the presence of this paragraph in the auditor's report will have a positive impact on the decisions of Egyptian investors.

## **3. Research Importance**

The purpose of this research is to examine the impact of disclosing KAMS on investors' decisions who benefit from the audit report as This topic has not received sufficient attention from Arab accounting research, especially in the Egyptian business environment, as far as the researcher knows, which gives this research academic importance.

Also, this research will have a role in enhancing the development of Egyptian auditing standards to keep up with the modifications made by International Auditing Standards as the the current audit report in Egypt is still summarized and not provide enough financial information about the entity.

The research seeks to determine whether using more understandable language, clear and transparent wording in KAM disclosure is the best way to reduce communication gaps between auditors and investors.

#### **4. Research Objectives**

The main objective of this study is to examine the effect of audit risk disclosure through key audit matters paragraph in audit report on investors decisions through achieving the following objectives:

1. Analyze the effect of disclosing audit risk through key audit matters paragraph in the information content of audit report according to ISA 701 standard.
2. Study the reactions of investors, auditors, and other interested parties on the audit report using modified auditing standards ISA701.
3. Assess whether investors view the disclosed audit information as a reliable, transparent and relevant for their decision-making process.
4. Examine the variables that could make it more difficult or easier for auditors to provide audit risk information in their reports.

## **5. Research hypothesis**

**H<sub>1</sub>:** There is no statistically significant positive relationship between **independent variables** key audit matter disclosures and **Dependent variable** (Investor's decisions)

**H<sub>2</sub>:** There is no statistically significant effect of the **independent variables** (key audit matters disclosures and audit risk disclosures) on the **dependent variable** (investor's decisions)

**H<sub>3</sub> :** There is no statistically significant indirect effect of the **mediator variable** (information content of the audit report) on the relation between the **independent variables** (key audit matter disclosures and **audit risk disclosures**) and investors' decisions.

**H<sub>4</sub> :** There is no statistically significant total effect of the **independent variables** (key audit matter disclosures and audit risk disclosures) and investors' decisions **Dependent variable** in the presence of the mediator variable.

## **6. Methodology**

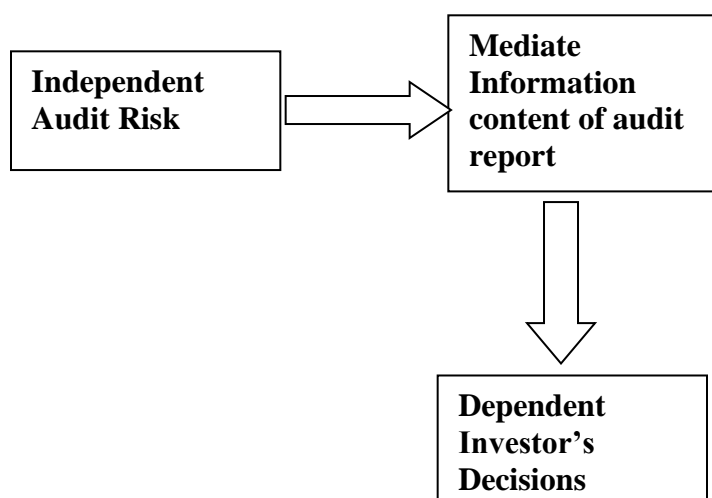
The researcher relies on combining both the deductive and inductive approaches.

**Deductive Approach:** By studying and analyzing the results of the previous studies related to research variables and publications of professional organization as IAS 701 regarding auditor's report and disclosure of key audit matters in order to formulate the theoretical framework and research hypothesis.

**Inductive Approach:** This approach will be relied upon in conducting the field study to test research hypothesis through a field survey in the Egyptian environment to collect the opinions of auditors, investors and academics at Egyptian universities

through distributing survey questionnaires to survey their opinions and then analyzing them statistically.

Due to considering the research objectives, the research will examine the Effect of disclosing Key Audit Matters in the Audit Report on Investors' Decisions through using the following variables: Key audit matters as an independent variable, investor's decisions as dependent variable and information content of the audit report as a mediator.



*Fig 1. Structure of the study variables*

## 7. The Significance of Disclosing key audit matters on investors decisions

In recent years, as a result of the 2008-2009 financial crisis, investors who want to understand more about the businesses in which they invest have been disappointed with the auditing profession and saw that the traditional auditor's report, did not convey financial risks as most of the failed financial institutions received unqualified opinions before failing **Sikka** (2009, p.15), and it should provide more information than it did, to narrow the information gap between

## **The Effect of Disclosing Key Audit Matters in the Audit Report on Investors' Decisions: A Field Study in Egypt**

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what financial statement users' needs and what's the auditor produced (IAASB, 2015; IFAC, 2015a).

So IAASB responded to these concerns and modified the auditing standards with the issuance of ISA 701 "Communicating Key Audit Matters".

### **7.1 Definition of key audit matters and its importance**

According to ISA 701, KAMs are defined as "*those matters that were the most significant in the audit of financial statements for the current period*". The main purpose of existing KAMS in the auditor's report is to enhance the value of it by providing more transparency about the performed audit process (IAASB, ISA 701,2015b, Para. 8).

IAASB believes that the disclosure of key audit matters in the auditor's report will improve the value and utility of the auditor's report by addressing the following objectives:

- Narrowing the expectation gap between what financial statement users need and what the audit process delivers.
- Improving users' decision-making ability by increasing the information content in the auditor's report, therefore narrowing the information and communication gap.
- Emphasizing that reporting key audit matters in the auditor's report does not replace the disclosures in the financial statements, which management is obligated to prepare according to the applicable financial reporting framework.

### **7.2 Main Factors of matters that auditor considers as Key audit matters**

The majority of KAMs are related to material risks that arise from the auditor's risk assessment, problems encountered by the auditor during the audit process, situations

that cause the auditor to change their opinion, and weaknesses that are significant in the internal control. The consideration of whether the matter chosen to be KAMs must require special attention from the auditor due to its complexity resulted from a significant management decision.

As a result of Paragraph 45 including the main factors that the auditor used to determine that the matter would be one of the key audit matters, including:

- The economic conditions that affected the auditor's ability to obtain audit evidence.
- Strategic changes or developing business model which have a significant impact on the financial statements. (IAASB, ISA 701,2015b, Para. 45)

The auditor uses the following criteria to determine key audit matters should be included in his audit report (PWC,2014):

- Matters communicated to those charged with governance.
- Matters that require significant attention from the auditor during the audit process.

The auditor will disclose to the investors important matters that the auditor found in the auditing process.

### **7.3 Characteristics of KAMS and its effect on auditors' opinion.**

One of the most crucial characteristics that KAMS disclosure must have been easy readability, which means that the reader must understand the messages that are contained in the KAMs paragraph in the auditor's report. If the receiver understands the message, that means the message is useful to the receiver, which is a principal requirement for the investor to help them to make the right decisions Velte (2018, para 3 p.15).

## **The Effect of Disclosing Key Audit Matters in the Audit Report on Investors' Decisions: A Field Study in Egypt**

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According to ISA 705 key audit matters are not an option for expressing a qualified opinion. If it's a reason to modify the auditor's opinion. (ISA 701, para.12)

Whereas ISA701 specifies some cases of audit matters not disclosed in the audit report:

- For example, laws, rules, or regulations that prevent disclosure of this matter.
- In some situations, the auditor may decide that this matter should not be mentioned in his report due to negative results which will exceed the benefits of this disclosure.

### **7.4 The impact of disclosing key audit matters paragraph on the audit committee and auditing process**

**7.4.1 Enhanced Negotiation:** KAM disclosure may improve the ability of the audit committee and external auditor to negotiate with management especially for financial reports with high estimation risk. Management may be motivated to make concessions to avoid disclosing these issues in the audit report. It enhances the audit committee's role in reporting financial statement risks and allows them to influence management behavior.

**7.4.2 Focus on Audit Risks:** Auditors must identify and address key risks more explicitly which lead to a concentrated effort on areas that are most likely to have a material impact on the financial statements and this will affect the auditing process it will be more risk-focused, with auditors dedicating significant resources to assess, test, and evaluate key audit matters.

**7.4.3 Increased Auditor Professional Judgment:** Disclosing audit risks in the KAM paragraph requires auditors



to exercise professional judgment in assessing the significance of audit matters. Auditors must rely on their expertise and experience to determine which issues should be included as KAM leading to more refined professional judgment in the audit process.

**7.4.4 Increased Accountability:** Greater transparency and disclosure can increase the accountability of the external auditor and audit committee to financial statement users. This will be motivation for the audit team to collect more evidence and seek the best evidence related to disclosed KAMs.

### **7.5 The effect of disclosing key audit matters on investors decisions**

It is critically important for developing countries such as Egypt to comply with international auditing and financial reporting standards in order to attract foreign investment that significantly stimulates economic progress and positively influences economic growth. Investors will gain from KAMs disclosure because they can obtain more detailed information about the company than they might from a standard audit format Christensen et al., (2014 p.3). Because adding KAMs will increase the transparency of auditor's reports and more understanding of the business information.

Considering that this research needs to examine the investor's reaction and decisions reflected by the expanded audit report that include KAMs disclosure that the auditor faced. Is it will have positive effect. So, the researcher seeks to analyze and study the impact of this modification on the Egyptian environment, if the auditors applied the expanded audit report that include key audit matters in organizations that received qualified audit opinion is it will save its reputation and reduce the potential for legal actions. A well-established audit procedure can act as a device to minimize agency conflicts between shareholders and company management, increase

## **The Effect of Disclosing Key Audit Matters in the Audit Report on Investors' Decisions: A Field Study in Egypt**

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transparency and confidence in auditor and his report. The auditor's report has to be significantly changed to prevent misunderstandings for investors and shareholders. The researcher think that risk disclosure is important and useful this is because it contributes to anticipating risks and evaluating the future performance of the company, which helps the beneficiaries to make correct decisions as a lack of information about the risks may cause problems internally and externally, it may expose the company to collapses that may reach liquidation or long-term losses, which may mislead investors and make improper decisions. In the current legal climate, disclosure of specific information in the audit report may serve to reduce litigation risk, especially the effects of a modified audit opinion and disclosure relating to audit practices that are examined. The disclosure simply makes such information available to corporate outsiders.

It will have positive impact on investors to have better risk assessment that allow the investors to evaluate impacts of the disclosed risk on the firm performance but it will have negative effect that investors may become too concerned with the audit risks that have been disclosed, which could cause unjustified concern or a risk-resistant attitude that prevents them from taking advantage of investment opportunities.

### **8. Field study**

#### **8.1 Population and Sample design**

**Population:** In this study, we employed a cross-sectional design and collected data from the Academic staff members, Auditors, Accountants, and Investors. This design was chosen based on previous research.

**Sample:** The study used a simple random sample, and data was obtained from the sample respondents (Academic staff members, Auditors, Accountants, and Investors). The required sample size was 384 based on the equation Thompson, Stephen,

so the study relied on 384 observations, as larger studies give stronger and more dependable results since they have narrower margins of error and lower standards of deviation, resulting in increased reliability in the results.

**To determine the sample size (n), Stephen Thompson's equation was used, which is as follows:**

$$n = \frac{N \times p(1 - p)}{[(N - 1)(d^2 \div z^2)] + p(1 - p)}$$

Where the size of the population is denoted by N, the standard score for the significance level is 0.95, which equals 1.96, while **d** is the margin of error, which is 0.05 and **p** is Property availability to neutrality ratio = 0.50.

This section aims to discuss over the validity and reliability test of the model's independent and dependent constructs, and finally an analysis of each question headed by a variable in the model will be provided in terms of the Mean, min, maximum and Standard Deviation. The total numbers of participants who have accessed the survey are 384 responses.

When examining the effect, and correlation between dependent and independent variables, a variety of statistical techniques were applied to fit the nature of the hypotheses.

## **8.2 Analysis of Constructs Validity and Reliability**

The measuring model was evaluated based on factor loadings, Cronbach's alpha, composite reliability, convergent validity, and discriminant validity. Composite reliability and Cronbach's alpha were used to assess the internal consistency of the scale items. Cronbach's alpha and composite reliability should be greater than 0.70, while AVE and factor loadings should be above 0.50. Cronbach's alpha and CR values greater than 0.70, as shown in Table 4 and Figure 1, indicate the reliability and robustness of the sample data used in this study. Significant AVE and factor loading values above 0.50 were also observed,

## The Effect of Disclosing Key Audit Matters in the Audit Report on Investors' Decisions: A Field Study in Egypt

indicating that the items had strong correlations with true convergent validity.

To make sure that the degree of reliability and validity of the questionnaire used in the study of The Effect of Disclosing Audit Risk in the Audit Report on Investors' Decisions was high, *Cronbach's alpha coefficient* was used to evaluate the reliability and validity of the study's tool.

Reliability Statistics		
Cronbach's Alpha	No. of statements	Composite reliability*
.921	55	.960

Table 1 Cronbach's alpha coefficient to check the stability of all statements.

Cronbach's alpha coefficients for all the dimensions in table 3 is .921 and Composite reliability is .960 indicating that Validity and Reliability condition is met.

Cronbach's alpha coefficients for the dimensions ranged from .954 to .969, which was higher than the recommended level exceeded of 0.70 Whether for the whole questionnaire or for individual questionnaire dimensions (Gefen, Straub, & Boudreau, 2000). Furthermore, for assessing construct reliability, all composite reliability (CR) values ranging from 0.97 to 0.98 were greater than 0.7, indicating that construct reliability is met, as shown in the previous table and below table.

Table 2 indicates that the Average Variance Extracted (AVE) value was greater than the required value of 0.50. The AVE values for key audit matter disclosures, audit risk disclosures, investor's decisions, and information content of the audit report were 0.73, 0.62, 0.62, and 0.54. Respectively. The convergent

validity of all constructs has been met, and adequate convergent validity has been shown to exist.

	dimensions	No. of statements	Cronbach's Alpha	Composite reliability*	Average Variance Extracted (AVE)
Independent variable	Key audit matters disclosures	12	.97	0.98	0.73
	Audit risks disclosures	16	.97	0.97	0.62
Dependent variable	Investor's decisions	13	.96	0.98	0.62
Mediator variable	Information content of the audit report	14	.95	0.98	0.54

\* Composite reliability= The positive square root of Cronbach's alpha coefficient

### 8.3 Testing and analyzing the hypothesis of the correlation between the study variables

The statistical approaches for testing hypotheses to determine their validity or incorrectness. The correlation matrix of the studied variables determines both the direction and strength of their association.

Mediation analysis via Structure equation modeling was used to assess the effect of the independent variables (key audit matters disclosures and audit risks disclosures) on investors' decisions (as dependent variables), to examine the effect of the key audit matters (as an independent variable) on the information content of the audit report (as mediate variable), and to examine the mediating role of the information content of the audit report on the relationship between the key audit matters disclosures and

## **The Effect of Disclosing Key Audit Matters in the Audit Report on Investors' Decisions: A Field Study in Egypt**

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audit risks disclosures (as independent variables) and investors' decisions.

$H_1$ .: There is no statistically significant positive relationship between **independent variables** key audit matter disclosures and **Dependent variable** (Investor's decisions)

Finding of  $H_1$  Referring to the correlation coefficient levels and correlation between all variables is strong, positive, and direct, with all Pearson correlation coefficients ranging from 0.50 to 1 and having an extremely high statistical significance, which is strong, positive, and in the direct direction and no variables are eliminated of the study model

### **8.4 Testing and analyzing the hypothesis of the effect of the independent variable and dependent variable**

For the purpose of building a structural equation model, the confirmatory factor analysis was first conducted with the aim of clarifying the correlations between each variable in the study and the indicators used to measure it, with the aim of excluding statements that are not related to its dimensions. Based on confirmatory factor analysis, the structural equation model can be applied to the study data.

JASP was employed in the study to assess the construct relationships. SEM is a second-generation regression model that has two distinct components. The first stage involved using a measuring model to evaluate the reliability and accuracy of various indicators. During the second analytical stage, the structural model was utilized to test the hypothesis and find the structural relationships between the variables. Mediation analysis used to determine both direct and indirect effects.

### 8.4.1 Mediation Analysis

Figure 2 depicts the path plot obtained from mediation analysis via structural equation modeling, which highlights the direct, indirect, and mediated effects of latent variables, after observing all variables, mediation analysis is a 3-variable path analysis and was used to estimate a system of equations with numerous dependent variables. Unlike regression models, path models can have several dependent variables.

The model was analyzed using JASP software, which treats indicators as single constructs with equal weights. The path model's significance was tested using bootstrapping within JASP which has the necessary modeling and computation capabilities. The results were output instantly, and the process model is shown in Figure 2.

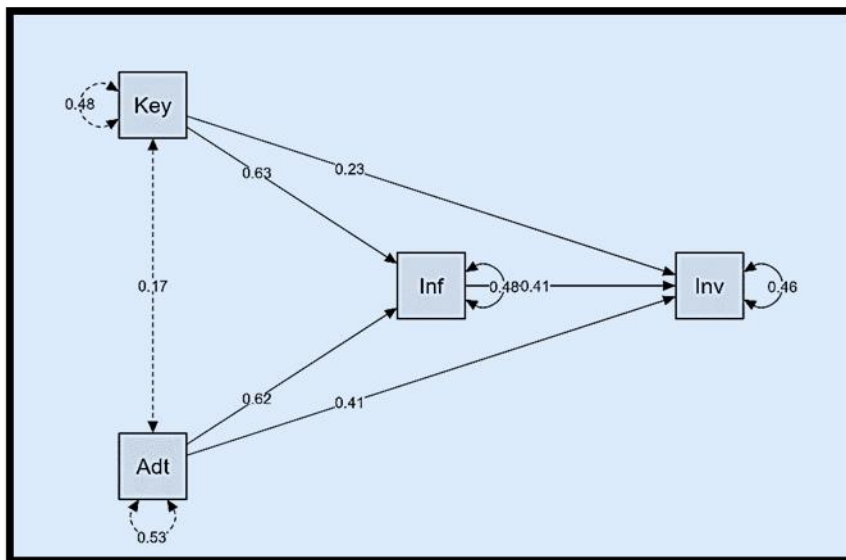


Fig. 2 The path plot (direct, indirect, and mediated effects)

$H_2$ : There is no statistically significant effect of the **independent variables** (key audit matters disclosures and audit

## The Effect of Disclosing Key Audit Matters in the Audit Report on Investors' Decisions: A Field Study in Egypt

risk disclosures) on the **dependent variable** (investor's decisions)

### Findings of the direct effect of the independent variables, on the dependent variable (Investor's decisions) without Mediation variable.

Hence Z-value is significant for all the variables in the below table, it means that the effect is greater than what might be predicted by chance, and it is referred to as a significant effect.

Direct effects								
Variable (Dimensions)	Path coefficient	Std. Error	Z-value	p	95% Confidence Interval		Remarks	Decision
					Lower	Upper		
Key audit matters disclosures → Investor's decisions	0.229	0.062	3.714	< .001	0.108	0.35	Significant	H <sub>2</sub> is Rejected
Audit risks disclosures dimension → Investor's decisions	0.414	0.059	6.994	< .001	0.298	0.531	Significant	

Table 3 The direct effect of the independent variables, on the dependent variable (Investor's decisions) without Mediation



### **Direct effects interpretation**

It is clear from the results in the above table that the independent variables (key audit matters disclosures and audit risk disclosures) dimension has a significant positive direct effect on the dependent variable (investor's decisions) at a significance level of 5% in the absence of the mediator variable. The table above shows that the direct effect of key audit matter disclosures on investor decisions was positive and estimated at 0.229 with  $p < 0,001$ , indicating a significant effect. It is obvious that the audit risk disclosures had positive direct effects on investor decisions, with an estimated effect of 0.414, with  $p < 0,001$  which is significant.

This indicates that for every 1% increase in key audit matter disclosures and audit risks stated in the audit report, 22.9% and 41.4% of investors' investment decisions will be precise and positive, respectively as direct effect, in the absence of the indirect effect of the mediating role of the information content of the audit report.

**$H_3$**  : There is no statistically significant indirect effect of the **mediator variable** (information content of the audit report) on the relation between the **independent variables** (key audit matter disclosures and **audit risk disclosures**) and investors' decisions.

**The findings of the indirect effect of the mediator variable (the information content of the audit report) on the relation between the independent variables and dependent variable interpretation.**

## The Effect of Disclosing Key Audit Matters in the Audit Report on Investors' Decisions: A Field Study in Egypt

The effect of the mediating variable (indirect effects)								
Variable (Dimensions)	Estimate	Std. Error	Z-value	p	95% Confidence Interval		Remarks	Hypothesis
					Lower	Upper		
Key audit matters disclosures → Information content of the audit report(M) → Investor's decisions	0.258	0.038	6.716	< .001	0.374	0.600	Significant	H <sub>3</sub> is Rejected
Audit risks disclosures → Information content of the audit report (M) → Investor's decisions	0.256	0.038	6.808	< .001	0.563	0.778	Significant	

Table 4The indirect effects of the mediator variable

### Indirect effects interpretation

It is clear from the results in the above table that the independent variables (key audit matters disclosures and audit risk disclosures) have a significant positive indirect effect on the dependent variable (investor's decisions) at a significance level of 5% through the **Information content of the audit report** (mediator variable) .

The table above shows that the indirect effect of key audit matter disclosures through the **Information content of the**

**audit report** on investor decisions was positive and estimated at 0.258 with  $p < 0,001$ , indicating a significant effect. It is obvious that the audit risk disclosures had positive indirect effects through the **Information content of the audit report** on investor decisions, with an estimated effect of 0.256, which is significant.

This indicates that for every 1% increase in key audit matter disclosures and audit risks stated in the audit report, 25.8% and 25.6% of investors' investment decisions will be precise and positive, respectively through the indirect effect of the mediating role of the information content of the audit report.

$H_4$  : There is no statistically significant total effect of the **independent variables** (key audit matter disclosures and audit risk disclosures) and investors' decisions **Dependent variable** in the presence of the mediator variable.

**The findings of the total effect that the independent variable explains via the mediator variable.**

However, the Z-value in the below table is larger than 1.96 and the p-value is 0.000, which indicates that the total effect of the independent variable explained via the mediator variable is significant and that direct and indirect effects are real and significant.

The results in the table below show the total effect of the independent variables (key audit matter disclosures and Audit risks disclosures) on the dependent variable (Investor's decisions), which is caused by the independent variables' direct effect on the dependent variable and the mediating variable's (Information content of the audit report) indirect effect on the relationship between the dependent variable and the independent variables, and these findings were previously mentioned above

## The Effect of Disclosing Key Audit Matters in the Audit Report on Investors' Decisions: A Field Study in Egypt

The total effects of the independent variables								
Variable (Dimensions)	Path coefficient	Std. Error	Z-value	p	95% Confidence Interval		Remarks	Hypothesis
					Lower	Upper		
Key audit matters disclosures → Investor's decisions	0.487	0.058	8.450	< .001	0.374	0.600	Significant	H <sub>4</sub> is Rejected
Audit risks disclosures → Investor's decisions	0.670	0.055	12.228	< .001	0.563	0.778	Significant	

Table 5 The total effect (direct and indirect effects)

### Total effects interpretation

It is clear from the results in the above table that the independent variables (key audit matters disclosures and audit risk disclosures) dimension has a significant positive total effect on the dependent variable (investor's decisions) at a significant level of 5% in the presence of the mediator variable.

The table above shows that the total effect of key audit matter disclosures on investor decisions was positive and estimated at 0.487, indicating a significant effect. It is obvious that the audit risk disclosures had positive total effects on investor decisions, with an estimated effect of 0.670 with  $p < 0,001$ , which is significant.

This indicates that for every 1% increase in key audit matter disclosures and audit risks stated in the audit report, 48.7% and

67% of investors' investment decisions will be precise and positive, respectively, as a total effect, in the presence of the direct effects of the independent variables and indirect effect of the mediating role of the information content of the audit report. This indicates that the more key audit matter disclosures and audit risks reported in the audit report, as well as the mediating role of the information content of the audit report, the more right and good investment decisions will be made.

## **9.Results**

- There is a positive relationship between the variables of independent variable (Key audit matters disclosures, Audit risks disclosures) and **Dependent variable** (Investor's decisions).
- There is a positive effect of the independent variables (Key audit matters disclosures, Audit risks disclosures) on **Dependent variable** Investor's decisions.
- There is a positive effect of the independent variables (Key audit matters disclosures, audit risks disclosures) on the Information content of the audit report.
- The audit report's information content partially mediates the relationship between the independent variables (key audit matter disclosures and audit risk disclosures) and investor decisions.

## **10.Conclusion**

- This study aims at investigating the investors to the disclosure of KAMs, the results of the regression analysis find evidence that KAMs disclosure as required by ISA701- has a significant impact on investor's decisions, indicating that the application of ISA 701 benefit investors and provide useful information. This finding supports the view that the disclosure of Key audit matters has a significant effect on investors behavior. And There is a positive relationship between the dimensions of

## **The Effect of Disclosing Key Audit Matters in the Audit Report on Investors' Decisions: A Field Study in Egypt**

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Audit (Key audit matters disclosures, Audit risks disclosures) and **Dependent variable** (Investor's decisions), as There is a positive effect of the Information content of the audit report on **Dependent variable** Investor's decisions.

- The audit report's information content partially mediates the relationship between the independent variables (key audit matter disclosures and audit risk disclosures) and investor decisions.

### **11. Recommendations**

Due to the importance that the researcher suggests that obligate auditors to disclose key audit matters in their reports, in order to enhance the Egyptian audit profession and reduce the expectation gap between auditors and investors, the researcher recommends:

- The researcher proposes a reevaluation of the content of the Egyptian auditing standards to comply with the international auditing standards and adapt them to suit with the Egyptian professional practice environment, In addition to perform workshops to discuss cases of applying this standard.
- The researcher recommends that Egyptian audit standards setters which apply the traditional form of the audit report to modify and apply the new form of the audit report that includes disclosure of key audit matters due to more transparency in information that affects investor's decisions as showed in the field study.
- Figure out ways to develop the awareness of financial statement users regarding the role of auditors and aim of disclosing key audit matters.
- Developing audit curriculum in Egyptian universities to include new standards affecting the form and content of audit report.

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