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Article

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Do audit firm and audit committee characteristics influence the reporting of key audit matters? Evidence from Palestine

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ABSTRACT

This study explores the influence of audit firm and audit committee (AC) characteristics on the extent of reporting of key audit matters (KAMs) in the audit report of firms listed on the Palestine Exchange (PEX). The study employs a content analysis approach to measure the extent of KAMs reporting based on the number of KAMs and the word count of KAMs as disclosed in the audit report. Based on 154 firm-year observations between 2016 and 2022, we use the fixed effects model to determine the connection between the four explanatory variables and the extent of KAMs reporting. The findings indicate that audit firm does not have a significant impact on the number of KAMs, while it is positively and significantly related to the word count of KAMs. The results also show that the number and word count of KAMs are not related to the attributes of the AC. Furthermore, the results show that auditors of firms receiving modified audit reports tend to reduce the level of KAMs disclosure. Therefore, reporting KAMs should reduce information asymmetry and improve audit quality in line with the interests of stakeholders. This paper is one of the very limited studies that examines the determinants of KAMs reporting in the Palestinian context. The results have significant practical implications for stakeholders, policymakers, professional associations, and regulators in Palestine to reinforce the quality of KAMs reporting.

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1. Introduction

Audit regulators around the world have been considering improving audit reporting to respond to the growing demand for more insightful and relevant audit reports. A key issue is the publication of the International Standard on Auditing (ISA) 701, which requires reporting on key audit matters (KAMs). KAMs enhances the quality of audit reports and can mitigate agency conflicts associated with stakeholders, managers, and auditors (Mah'd & Mardini, 2022), which could increase the value of business operations (Isa et al., 2012) and enhance managerial accountability (Gold et al., 2020). Furthermore, the level of KAMs reporting is influenced by cultural and regulatory frameworks in addition to macroeconomic factors (Ferreira & Morais, 2020).

KAMs are matters identified by the auditor that are considered most important in the audit and these matters are reported to management (ISA 701). Due to the information gap, ISA 701 has promoted better communication between auditors and management, resulting in better implementation of good governance practices (Sirois et al., 2018). KAMs reporting enables the auditor to concentrate on audit areas that demand utmost scrutiny and careful judgment, thereby enhancing audit quality (Dogan & Arefaine, 2017). Disclosure of KAMs is expected to allow investors to concentrate on the complex aspects of financial reports and accordingly increase the communicative value of audit reports. Therefore, stakeholders look for information that will help them improve their understanding and knowledge of important issues related to the audited entity. Accordingly, KAMs reporting is expected to mitigate the audit expectation gap and minimize information asymmetry associated with the stakeholder agency problem (Mah'd & Mardini, 2022). Additionally, ISA 701 could mitigate the information gap through reporting KAMs

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(Hegazy & Kamareldawla, 2021), as some investors generally do not have the necessary knowledge or experience to evaluate financial reports. Previous literature has provided evidence that KAMs disclosure is associated with audit firm size (Al Lawati & Hussainey, 2022; Mah'd & Mardini, 2022; Özcan, 2021), AC characteristics (Velte, 2018; Velte, 2019; Zhang & Shailer, 2021), firm specific characteristics (Suttipun, 2020; Pinto & Morais, 2019) and auditor level factors (Velte, 2018; Bepari, 2022). This study explores the determinants of KAMs disclosures in the Palestinian listed companies by highlighting how audit firm and AC characteristics can affect the number and word count of KAMs reported in the audit report. Auditors ensure a fair presentation of financial information and disclose all relevant information, including KAMs. Big Four audit companies may have more fear of litigation risk than other audit firms. Existing literature argues that firms audited by the Big Four tend to expand KAMs reporting in the audit report (Ferreira & Morais, 2020; Velte, 2019). The AC oversees the financial reporting process and acts as a liaison between auditors and the board of directors. Although auditors are responsible for reporting KAMs in audit reports, they are required to discuss KAMs with the AC. Therefore, the characteristics of the AC are expected to have an impact on KAMs disclosure and therefore on audit quality, which can lead to a reduction in audit risk (Bepari, 2022). Thus, we include AC size, AC financial expertise, and AC independence as independent variables as these attributes are expected to affect KAMs reporting (Bepari, 2022; Mah'd & Mardini, 2022; Velte, 2018). In addition, we control for company-specific characteristics (e.g. size, leverage, complexity). The extent of KAMs reporting is influenced by the auditor's assessment of the anticipated cost of losing a client (Ferreira & Morais, 2020). Firm-specific characteristics are therefore expected to influence the extent of KAMs reporting (Özcan, 2021; Suttipun, 2020). We also control for auditor-related variables (e.g. partner's rotation, audit opinion, audit report lag) following extant literature (Abdelfattah et al., 2021; Abdullatif et al., 2023).

The current study is conducted in Palestine, a frontier market with a small stock exchange. Previously, audit practices in Palestine were primarily related to tax matters. However, regulators such as the Palestinian Capital Markets Authority (PCMA) have recently made significant efforts to improve the quality of auditing standards for corporations listed on the Palestine Exchange (PEX) (PCMA, 2024). International auditing standards and regulations have had an important effect on the development of auditing in Palestine. In connection with this, foreign direct investments have a positive influence on growth in emerging countries. KAM reporting is intended to improve the quality of financial reporting (Gold et al., 2020). Therefore, this informational value of KAMs is likely to be useful for Palestinian companies to attract foreign direct investment, which has the potential to dramatically boost economic growth.

While recent studies have explored the effect of the audit firm and AC attributes on KAMs reporting in different economic environments (e.g. Bepari, 2022; Al Lawati & Hussainey, 2022; Mah'd & Mardini, 2022; Zhang & Shailer, 2021), to our knowledge, the current study is the first to investigate this issue in Palestine. Bepari (2022) argues that evidence on factors influencing KAMs disclosure varies across countries. Consequently, insights from different countries will contribute to understanding the determinants of KAMs disclosure from a global perspective. Therefore, it is interesting to examine this important issue in the Palestinian context. Most Middle Eastern countries are currently adopting international auditing standards. The Palestinian economy has different business characteristics, particularly ownership concentration and family business. This may affect the level of transparency and conformity with international standards. This study is expected to have important practical implications for audit report users, regulators and policy makers, as the results show that the level of issuance of KAMs is influenced by the audit firm, some firm-specific characteristics and auditor-related factors. This suggests that certain determinants affect the extent of KAMs issued in audit reports and increase their usefulness by improving audit quality.

The structure of this study is as follows: section two illustrates the institutional setting. The third section presents regulatory background for KAMs. Section four provides a literature review and hypotheses development. Section five includes the research methods employed. Section six discusses the findings. Section seven provides the conclusion, limitations and future research.

2. Institutional setting

The Palestinian economy is emerging and is characterized by high levels of instability, lack of government regulations, and control over basic economic and fiscal policies (Hassan, 2023). The declaration of principles in 1993, followed by the Oslo Accord, was expected to bring about dramatic changes in

economic conditions in the Palestinian territories. PEX was founded in 1995 as a privately held firm to facilitate investment in Palestine. In 2010, PEX became a publicly held corporation. Currently, 49 public firms are listed on the PEX, with a market value of \$4.896 billion in 2022 (PEX, 2024). The PCMA was founded in 2004 as a regulator for firms listed in Palestine. The PCMA seeks to safeguard investor rights through regulations and oversight to create a stable investment climate and develop the financial market (PCMA, 2024).

The auditing profession in Palestine faces many challenges and obstacles. After 1967, the Israeli occupation government maintained regulations governing the audit profession in the West Bank and Gaza Strip. Following the Oslo Accord, the same legislation was in effect until a presidential proclamation known as 'Law No. 10 of 1961' was issued. This era was characterized by a lack of accountability and the absence of auditing standards (Mansour & Chenikhar, 2020). In 2004, the Board of Auditing Profession (BOPA) was founded in accordance with Law No. 9 governing the auditing profession (BOPA, 2004). BOPA grants license to individuals and firms to practice audit activities, after which the auditors obtain membership of the 'Palestinian Association of Certified Public Accountants' (PACPA). Currently, there are 265 Certified Public Accountants (CPAs) in addition to 11 audit firms, including local, international, and Big Four audit firms (PACPA, 2024). In 2019, the PCMA required auditors to comply with ISAs.

Thus, the audit profession in Palestine encounters difficulties because of political and economic conditions. As an emerging economy, the audit quality and the extent of adherence to auditing standards could potentially be influenced by inefficient financial markets, poor corporate governance, and the prevalence of family businesses that do not require high quality auditing practices (Abdullatif et al., 2023). Furthermore, the application and disclosure of many significant rules and issues were not mandated by the Palestinian Corporate Governance Code released in 2009. For example, the formation of ACs is not mandatory and listed firms are not required to disclose audit fees in their annual reports (Dwekat et al., 2018). Consequently, the current regulatory environment, in addition to other economic characteristics (e.g. ownership concentration and family businesses), may lead to low levels of transparency in financial reporting.

3. Key audit matters: a regulatory background

Standard setting bodies have observed that financial statement users place a high value on the opinions of auditors but overlook more pertinent and significant firm-specific information in the audit report (IAASB, 2016). The AICPA released a standard audit report form in 1974 that included information about the audit procedures utilized by the audit firm and the basis for an audit opinion (Ajao et al., 2016). This report was referred to as the 'short form audit report.' Although it does not refer to auditing standards, the term 'fairly presented' has been used in this audit report. This audit report form remained unchanged in the United States and other countries until 1988 (Ajao et al., 2016). This report contains only two paragraphs, namely, the introductory paragraph and the opinion paragraphs. Furthermore, this report did not provide details on the scope and nature of auditing nor did it emphasize the responsibilities of management and auditors with respect to the financial statements. Consequently, this report was unclear and lacked transparency, as users were unable to distinguish between the responsibilities assigned to the auditor and management.

In response, the International Auditing and Assurance Standards Board (IAASB) released new auditing standards that required the addition of new parts and amendments to the audit report, such as the inclusion of the term 'independent' in the title of the report and a brief description of the audit process, which sets out the duties and roles of the auditor and management, as well as the objective of the audit (Ajao et al., 2016; Aqel, 2014). This amended audit report was criticized on several occasions because it did not provide informative content and lacked transparency. Additionally, inadequate information content in this report may lead to litigations against auditors, poor investment decisions, and a decline in stockholders' trust in the audit function (Mah'd & Mardini, 2022). Therefore, the IAASB released ISA 701 'Communicating Key Audit Matters in the Independent Auditor's Report' to promote transparency in audit reports through reduced standardization. ISA 701 alerts stakeholders to the areas that require the most judgment from management and auditors, providing a more insightful understanding of the audited firm. Moreover, ISA 701 gives auditors the flexibility to disclose certain KAMs in annual reports,

such as issues that involve a considerable risk of material misstatement and that have material consequences (Kitiwong & Srijunpetch, 2019; Wuttichindanon & Issarawornrawanich, 2020).

The primary objective of KAMs disclosure is to help stakeholders understand the audited financial statements and key areas of management judgment, thereby increasing the communicative value of the audit results (Pinto & Morais, 2019). However, ISA 701 warns users that the reporting of KAMs does not replace the disclosure of the financial reports nor the auditor's opinion (IAASB, 2016; Özcan, 2021). KAMs are determined by auditors based on their judgment of the key areas that may affect users' decision-making or issues with a high risk of material misstatements. When auditors identify material issues, they should focus on areas of significant risk, as set out in ISA 315 (ISA 315). Therefore, the auditor must identify the issues that require significant judgment, particularly uncertain accounting estimates, and the impact of the major transactions that happened during the period, in order to assess whether these issues should be reported in the audit report (IAASB, 2016; Wuttichindanon & Issarawornrawanich, 2020).

ISA 701 provides general guidance on whether matters should be communicated to management. The auditor evaluates the nature and extent of communication of complex issues, as this can lead to intensive interaction with management. In addition, the auditor must evaluate whether the disclosed KAMs would provide information value to stakeholders (Ferreira & Morais, 2020; IAASB, 2016). Other aspects that could influence KAMs disclosure include entity-specific characteristics (e.g. size, age, profitability, leverage, and complexity) and auditor-related attributes (e.g. audit firm, industry specialization, and audit fees) (Dogan & Arefaine, 2017). When auditors disclose KAMs, they should explain why these matters were chosen and included in their reports and why these matters were significant in their audits (Pinto & Morais, 2019). The IAASB restricted auditors' use of highly technical language because the primary goal of KAMs is to provide users with adequate explanations of the audit (ISA 701). Previous studies recognized the informative value of KAM reporting and suggested that this disclosure would influence related decision-making (Dogan & Arefaine, 2017; Ferreira & Morais, 2020; Özcan, 2021).

Many factors affect the complexity of KAMs reporting, namely, the audit firm, AC attributes, industry, size, firm complexity and auditor rotation (Abdelfattah et al., 2021; Özcan, 2021; Velte & Issa, 2019). Previous literature has categorized KAMs according to the type of risk and noted that KAMs can refer to account risks, sector-specific risks, firm-specific risks, and market-specific risks (Mah'd & Mardini, 2022). KAMs related to account risk refer to a specific financial statement component or balance of an account, such as revenues, fixed assets, marketable securities, intangibles, inventories, impairment of assets, and contingencies. KAMs associated with entity risks are closely related to the overall risk of the firm, such as tax issues, information technology, litigation, internal controls and accounting. KAMs related to account risk are easier to audit than KAMs related to entity risks because they are subject to substantive tests. Furthermore, KAMs related to entity risk align with macro-level controls and affect audit strategies (Ferreira & Morais, 2020). However, entity-specific risks are typically less visible to users than industry-specific risks because the latter are more unexpected and have more rhythms and traits. Users are likely to react more strongly to a company's unexpected risks because they were previously unaware of them. Moreover, the information content of firm-specific and unanticipated risks could be regarded more significant than other risks (Ferreira & Morais, 2020).

Standards setting bodies and researchers have recognized the need for expanded audit reports as they have greater informational value for stockholders (Pinto & Morais, 2019). Several previous studies have indicated that ISA 701 has narrowed the audit expectation gap by providing diverse financial statement users with a clear picture of the audit process and areas of high risk of material misstatements (Hegazy & Kamareldawla, 2021; Özcan, 2021; Velte & Issa, 2019). On the other hand, KAMs reporting can negatively impact the expectation gap because investors expect the auditor to report any critical areas they perceive (Velte & Issa, 2019). Accordingly, reporting matters where there is a high risk of misstatement may not impact users' decision-making as they may already be aware of these areas (Lennox et al., 2022).

4. Literature review and hypotheses development

The demand for auditing has been justified by the information risk assumption, which states that audited financial statements mitigate the information risk that users may face (Smieliauskas et al., 2020). Auditors provide assurance on the fair reporting of financial information and ensure that the audited firm

discloses all relevant information, including KAMs. Consequently, auditors help reduce information asymmetry by reporting on KAMs in their reports (Isa et al., 2012). The auditor's role is to express an opinion on management's assertions to maintain investor confidence in management's activities. KAMs reporting enhances this role by improving the transparency and communicative value of audit reports (Ferreira & Morais, 2020; Mah'd & Mardini, 2022; Velte & Issa, 2019).

Some previous studies argue that the extent of KAM reporting is not significantly affected by the audit firm because many listed companies are subject to strict monitoring and strict regulation regardless of the attributes of the audit firm (Genç & Erdem, 2021). Other studies concluded that there is a positive link between the size of the audit firm and the extent of KAMs reporting (Dogan & Arefaine, 2017; Velte, 2019). Wuttichindanon and Issarawornrawanich (2020) investigated the influence of audit firms on the number of KAMs disclosed in the audit report Thailand. The study used a dummy of Big Four and non-Big Four audit firms and found that the appointment of Big Four audit firms significantly increases the level of KAMs reporting. Similarly, Mah'd and Mardini (2022) examined the determinants of KAMs reporting in the Middle East (Jordan, Oman, United Arab Emirates, and Bahrain) and found that the Big four audit firms disclose more KAMs in their audit reports. The study argued that the perceived quality of financial statements is significantly influenced by the Big Four audit firms. Disclosure of KAMs depends heavily on audit quality, which can play a crucial role in mitigating agency conflicts. Thus, KAMs can raise audit quality by minimizing aggressive accounting practices. On the contrary, Özcan (2021) examined factors affecting KAMs reporting for listed manufacturing companies on Borsa Istanbul and found that non-Big Four audit firms report more KAMs in their audit report. Thus, auditors' characteristics may affect KAMs disclosure in audit reports. The Big Four audit firms provide high quality audit because they have greater access to information technology, significant financial resources, and human capital. Accordingly, the Big Four tend to resist pressure from audited companies to report violations that affect the fair presentation of financial reports and therefore pay more attention to KAM disclosure (Wuttichindanon & Issarawornrawanich, 2020). Therefore, the appointment of one of the Big Four would lead to expanded KAMs reporting. Consequently, our first hypothesis is developed as follows:

H1: There is a positive relationship between the appointment of the Big Four audit firms and the level of disclosed KAMs.

AC plays a crucial role in publicly held firms as it oversees the financial reporting process. AC existence could raise the extent of disclosure and, accordingly, mitigate the information asymmetry between managers and stockholders. Furthermore, AC monitors auditors and provide them with the essential information required to report KAMs (Al Lawati & Hussainey, 2022). According to the Palestinian Corporate Governance Code issued by the PCMA, publicly held firms should have at least two independent members on the board of the AC (PCMA, 2009). The existence of ACs is crucial to the quality of audit. According to Abdullatif and Al-Rahahleh (2020), disclosure of KAMs improves communication between the AC and the auditor. Furthermore, the competence of AC in monitoring the auditor primarily depends on the characteristics of the AC, namely size, financial competence and independence (Saei et al., 2022). An effective AC serves as a catalyst for auditor independence and provides the auditor with greater comfort in disclosing KAMs (Bepari, 2022). In this context, previous research argues that AC attributes influence the extent of KAMs reporting (Bepari, 2022; Zhang & Shailer, 2021).

AC size can improve audit quality because larger ACs may have more skills and experience to monitor managers and prevent fraudulent financial reporting. On the other hand, small ACs may not be able to effectively carry out their duties in overseeing the audit process because their workload depends on a small number of directors (Cheung, 2019). On the contrary, Mah'd and Mardini (2022) found that AC size has no significant connection with the extent of KAMs disclosure in the Middle East region, suggesting that large ACs is unrelated to KAMs reporting. Similarly, Rahaman and Karim (2023) examined the influence of auditor characteristics and corporate governance characteristics on the extent of KAMs reporting in Bangladesh. Contrary to expectations, AC size was found to have a negative impact on the level of KAMs reporting. Therefore, we assume that the size of the AC does not increase the level of KAMs reporting. Accordingly, the second hypothesis is stated as follows:

H2: The size of the AC has a positive and significant impact on the extent of KAMs reporting.

The financial competence of the AC is considered an essential characteristic that has important implications for corporate reporting and the auditor's work. In this context, financial expertise could reflect greater effectiveness of the AC and better collaboration with the auditor (Velte, 2019). In addition, AC's financial expertise reduces the manipulation of financial reports and has a positive impact on the quality of financial reporting (Ali, 2024). The Palestinian Corporate Governance Code does not require ACs of a listed firms to involve a financial expert (PCMA, 2009). ACs with financial experts examine financial matters in more details and thus motivate auditors to conduct higher quality audits (Saei et al., 2022). Zhang and Shailer (2021) investigated the impact of AC expertise on auditors' disclosures of KAMs in the United Kingdom. The results suggest that AC financial and industry expertise reduces the extent of KAMs reporting. Auditors are expected to report more KAMs to their clients to reduce engagement risk (Ji et al., 2024). However, auditors could consider the financial expertise of ACs in their risk assessment. In this way, auditors can recognize the benefits of the AC's financial expertise in improving the quality of internal controls and effective oversight of financial reporting. Accordingly, auditors are expected to report fewer KAMs in the audit report (Zhang & Shailer, 2021).

Moreover, Velte (2019) examined the effect of AC accounting and industry expertise on the readability of KAMs in the United Kingdom. The findings showed that AC financial expertise improves the readability of KAMs. Similarly, Bepari (2022) examined the impact of AC attributes on KAMs disclosures in the Australian context. The study showed that AC financial expertise reduces the extent of KAMs provided by the auditor and improves the readability of the KAMs by reporting more specific information. In the same vein, Mah'd and Mardini (2022) found that the presence of financial expertise on the AC significantly increases the extent of disclosure of KAMs. The authors argued that AC financial expertise can lead to a reduction in information asymmetry as shareholders demand transparent disclosure of KAMs from the auditor. This argument is in line with agency theory that the AC oversees the audit process and is therefore involved in managing conflicts of interest between shareholders and management. On the contrary, Abu and Jaffar (2020) found that the presence of an AC financial expert leads to a lower number of KAMs in Malaysia. Accordingly, we expect that AC's financial experts will have a significant impact on the extent of KAMs reporting. Thus, our third hypothesis is stated as follows:

H3: The financial expertise of the AC has a significant positive impact on the extent of KAMs reporting.

AC members must exercise independent judgment to monitor audit quality. AC independence can play a critical role in reconciling differing opinions between auditors and management and enhancing the quality of the audit. If an AC member has social or financial ties to the company, he or she may appear less independent of management (Saei et al., 2022). Additionally, the independence of AC members maintains the independence of auditors and protect them from undue pressure from management (Saeed et al., 2022). On the other hand, Cheung (2019) found that AC independence does not have a significant impact on improving audit quality. Independent ACs tend to be less supportive of management when the auditor proposes adjustments to the financial statements (Hunton & Rose, 2016). In this context, Bepari (2022) pointed out that the independence of AC members reduces the extent of KAMs reporting in Australian listed companies. Similarly, Abu and Jaffar (2020) showed that AC independence had a negative association with the number of KAMs issued in the audit report in Malaysia. However, Velte (2019) found no relationship between AC independence and the readability of KAMs in the United Kingdom. Based on these arguments, we predict that the independence of AC members significantly reduces the extent of KAMs reporting. Consequently, the fourth hypothesis is put forward as follows:

H4: there is a significant negative connection between AC independence and the extent of KAMs reporting.

5. Methods

5.1. Sample and data

This study is quantitative in nature and based on a panel research design with a focus on the extent of KAMs issued in audit reports. Previous studies employed a quantitative research design because it facilitates comparison between firms (Genç & Erdem, 2021; Özcan, 2021; Velte & Issa, 2019; Wuttichindanon

& Issarawornrawanich, 2020). Moreover, the use of quantitative methods is preferred in such research because not all intended users will be able to understand all of the issues presented in the KAMs section. This allows stakeholders to focus on quantitative rather than qualitative aspects (Abdelfattah et al., 2021; Dogan & Arefaine, 2017; Genç & Erdem, 2021; Oghuvwu & Orakwue, 2019).

The sample for this study focuses on Palestine's financial market, namely, the PEX, from 2016 to 2022, as well as pertinent publications released by PEX throughout the same time frame. The issuance of the KAMs section in audit reports became effective in 2016 for all listed firms. Accordingly, we began gathering the data in 2016. By the end of 2022, 47 companies were listed on PEX, operating in five sectors: banking, insurance, investments, industry and services. We exclude financial firms from the sample because they are heavily regulated by the Palestine Monetary Authority (PMA) and accordingly have different reporting requirements. Thus, the first sample includes all 33 non-financial firms listed on the PEX that operate in the investment, industrial and service sectors. However, 11 listed firms were removed from the sample because their financial information was incomplete or missing and there was no AC in these companies. Thus, the final sample included 22 listed firms between 2016 and 2022. Table 1 displays the sample companies.

5.2. Study variables

The dependent variable for the current study, the disclosure of KAMs, is measured using two distinct proxies: the number of KAMs and the word count of KAMs issued in the audit report (Abdelfattah et al., 2021; Al Lawati & Hussainey, 2022; Suttipun, 2020). According to ISA 701, KAMs should be reported as one of the major components in audit reports. KAMs reporting provides pertinent information and reduces uncertainty regarding the audit client's performance (Al Lawati & Hussainey, 2022). The number of KAMs represents the items provided by the auditor in the KAMs section for a specific financial period. Examples of the most prevailing KAMs include an allowance of doubtful accounts, goodwill, provisions, inventories, impairment and revenue recognition (Suttipun, 2020). ISA 701 does not indicate a specific number of KAMs that must be reported by the auditor. However, unnecessary KAMs can distract stakeholders' attentions from the core area of KAMs and the audited financial statements (Bepari, 2022).

The natural logarithm of the number of KAMs issued in the audit report (LnKAMN) is used as a proxy for the number of KAMs issued (Abdelfattah et al., 2021). However, an increase in the number of KAMs does not necessarily mean an expansion of the KAMs section. Therefore, the word count of the KAMs section is used as an alternative proxy for the level of KAMs disclosure (Wuttichindanon & Issarawornrawanich, 2020), as the length of KAMs can affect readability (Bepari, 2022). The natural logarithm of the word count of KAMs (LnKAMW) is used as a measure for the word count of KAMs (Abdelfattah et al., 2021).

Regarding the independent variables, the type of audit firm (AF) is a dummy variable and therefore firms audited by a Big Four are coded 1 and 0 if they are audited by another audit firm (Abdullatif et al., 2023). The natural logarithm of the AC members (LnASIZ) is used as a measure of the size of the AC. We also measure the financial expertise of the AC (ACFE) by the percentage of financial expert members in the AC (Bepari, 2022; Saei et al., 2022; Zhang & Shailer, 2021). Additionally, AC independence (ACIN) is measured by the proportion of independent members of the AC (Bepari, 2022; Velte, 2019).

Additionally, we control for attributes that influence the disclosure of KAMs at the corporate and auditor levels. The study variables and their measurement are presented in Table 2.

5.3. Empirical model

To investigate the connection between the explanatory variables and the extent of KAMs reporting, we use the fixed effects model. We conduct the Breusch-Pagan-Lagrange multiplier (LM) test and the

Table 1. Sample.

Sector	Total companies	Companies in the Sample
Industrial companies	13	10
Investment companies	11	7
Service companies	9	5
Total	33	22

Table 2. Measurements of the study variables.

Variable	Definition	Previous studies	Expected Sign
<i>Dependent variables</i>			
LnKAMN	The natural log of the number of KAMs issued in the audit report	(Al Lawati & Hussainey, 2022; Abdelfattah et al., 2021)	Dependent variable
LnKAMW	The natural log of the word count of KAMs	(Abdelfattah et al., 2021)	Dependent variable
<i>Independent variables</i>			
AF	Companies audited by one of the Big Four are coded 1, 0 otherwise	(Abdullatif et al., 2023; Mah'd & Mardini, 2022)	+
LnASIZ	The natural log of the number of AC members	(Cheung, 2019; Mah'd & Mardini, 2022)	+
ACFE	The proportion of financial expert members in the AC	(Saei et al., 2022; Zhang & Shailer, 2021)	+
ACIN	The proportion of independent members of the AC	(Bepari, 2022; Velte, 2019)	–
<i>Control variables</i>			
LnSUB	The natural log of the number of subsidiaries	(Rajabalizadeh, 2023)	+
OPIN	1 if the audit opinion is qualified, 0 otherwise	(Abdullatif et al., 2023; Liu et al., 2021)	–
ROT	1 if the audit partner changed in the current fiscal year, 0 otherwise	(Rajabalizadeh, 2023)	+
LnARL	The natural log of the number of days between the financial period and the date of the audit report	(Abdullatif et al., 2023)	+
LEV	Total debts to total assets	(Pinto & Morais, 2019; Mah'd & Mardini, 2022)	+
Size	The natural log of total assets	(Kitiwong & Srijunpetch, 2019; Özcan, 2021)	+
ROA	Net income divided by total assets	(Mah'd & Mardini, 2022; Suttipun, 2020)	–
FM	1 if the company is a family managed, 0 otherwise	(Abdullatif et al., 2023)	–
LnAGE	The natural log of the number of years the firm has been listed on the PEX	(Rajabalizadeh, 2023)	–

Hausman test to demonstrate the validity of our estimated models (see Section 5.4). Therefore, we estimate the following empirical models:

$$\begin{aligned} \text{LnKAMN}_{i,t} = & a + b_1 \text{AF}_{i,t} + b_2 \text{LnASIZ}_{i,t} + b_3 \text{ACFE}_{i,t} + b_4 \text{ACIN}_{i,t} + b_5 \text{LSUB}_{i,t} + b_6 \text{OPIN}_{i,t} + b_7 \text{ROT}_{i,t} \\ & + b_8 \text{LnARL}_{i,t} + b_9 \text{LEV}_{i,t} + b_{10} \text{LnTA}_{i,t} + b_{11} \text{ROA}_{i,t} + b_{12} \text{FM}_{i,t} + b_{13} \text{LnAGE}_{i,t} + \text{YearFE}_{i,t} + \varepsilon_i \end{aligned} \quad (1)$$

$$\begin{aligned} \text{LnKAMW}_{i,t} = & a + b_1 \text{AF}_{i,t} + b_2 \text{LnASIZ}_{i,t} + b_3 \text{ACFE}_{i,t} + b_4 \text{ACIN}_{i,t} + b_5 \text{LSUB}_{i,t} + b_6 \text{OPIN}_{i,t} + b_7 \text{ROT}_{i,t} \\ & + b_8 \text{LnARL}_{i,t} + b_9 \text{LEV}_{i,t} + b_{10} \text{LnTA}_{i,t} + b_{11} \text{ROA}_{i,t} + b_{12} \text{FM}_{i,t} + b_{13} \text{LnAGE}_{i,t} + \text{YearFE}_{i,t} + \varepsilon_i \end{aligned} \quad (2)$$

Table 2 displays the measurements of the study variables.

6. Empirical findings

6.1. Distribution of KAMs by sectors and year

Table 3 reports the distribution of KAMs disclosure by sector using the two different proxies. Panel A shows that auditors in the investment sector provide the highest number of KAMs (mean LnKAMN = 0.616). Furthermore, the industrial sector reports the lowest number of KAMs (mean LnKAMN = 0.280). Similarly, auditors of the investment sector report the highest level of KAMs as measured by word count (mean LnKAMW = 6.168), while the industrial sector reports the lowest word count of KAMs (mean LnKAMW = 5.662).

Table 3. Distribution of KAMs by industry.

Industry	Number	Minimum	Maximum	Mean	Std. Deviation
Panel A: Distribution of LnKAMN by industry					
Industry	70	0.000	1.609	0.280	0.472
Investment	49	0.000	1.386	0.616	0.525
Service	35	0.000	1.386	0.502	0.486
Total	154	0.000	1.609	0.437	0.512
Panel B: Distribution of LnKAMW by industry					
Industry	70	3.664	6.748	5.662	0.689
Investment	49	4.718	7.137	6.168	0.514
Service	35	0.000	7.077	5.706	1.367
Overall	154	0.000	7.137	5.833	0.875

Table 4. Distribution of KAMs by years.

Year	Number	Minimum	Maximum	Mean	Std. Deviation
Panel A: Distribution of LnKAMN by year					
2016	22	0.000	1.386	0.615	0.519
2017	22	0.000	1.386	0.515	0.522
2018	22	0.000	1.386	0.528	0.541
2019	22	0.000	1.609	0.425	0.569
2020	22	0.000	1.386	0.402	0.482
2021	22	0.000	1.386	0.320	0.462
2022	22	0.000	1.386	0.257	0.454
Overall	154	0.000	1.609	0.437	0.512
Panel B: Distribution of LnKAMW by year					
2016	22	0.000	6.741	5.797	1.356
2017	22	3.638	6.719	5.779	0.798
2018	22	3.664	7.077	5.896	0.863
2019	22	3.664	6.833	5.860	0.672
2020	22	3.664	6.984	5.774	0.920
2021	22	3.829	6.977	5.939	0.650
2022	22	3.871	7.137	5.785	0.780
Overall	154	0.000	7.137	5.833	0.875

The distribution of KAMs by year is reported in Table 4. The highest number of KAMs was reported in 2016 (mean LnKAMN = 0.615), as indicated in Panel A. 2016 is the first year the Palestinian audit firms apply ISA 701. This is may be because several audit firms felt they needed to increase the number of KAMs (or at least report one KAM) in 2016 to emulate other audit firms which is in line with Abdullatif and Al-Rahahleh (2020). As displayed in Panel B, there are no significant differences in word counts between years. The highest word count is in 2021 (mean LnKAMW = 5.939).

6.2. Descriptive statistics

Table 5 demonstrates the descriptive statistics. As illustrated in the Table, the average of LnKAMN was 0.437, with a minimum of zero and a maximum of 1.609. Furthermore, the mean LnKAMW is 5.833 and ranges from zero to 7.137. A higher level of reporting reflects a greater amount of relevant audit information disclosed to users and compliance with ISAs (Mah'd & Mardini, 2022).

The results also show that the mean AF is 0.766 with a minimum of zero and a maximum of 1, demonstrating that a large percentage of the sampled firms are audited by the Big Four. This demonstrates that listed firms in PEX tend to appoint Big Four audit firms to improve the quality of their financial reports and protect their reputation (Al Lawati & Hussainey, 2022). This is in line with previous studies (Özcan, 2021; Kitiwong & Srijunpetch, 2019; Wuttichindanon & Issarawornrawanich, 2020), which reported mean values of 54%–86%. In terms of LnASIZ, the mean is 1.123 and ranges from 1.099 to 1.609. The mean ACFE is 0.268 with a minimum of zero and a maximum of 0.667. The mean ACFE is below 0.359, reported by Zhang and Shailer (2021) and below 0.421, reported by Bepari (2022). This indicates a low presence of AC members with financial expertise in the listed firms in Palestine. For the ACIN, the mean is 0.586 with a minimum of 0.200 and a maximum of 1, indicating that approximately 59% of AC members are non-executive directors. The mean ACIN is lower than 0.900, reported by Bepari (2022) and above 0.320, reported by Velte (2019).

Table 5. Descriptive statistics.

Variable	Observations	Minimum	Q1	Median	Mean	Q3	Maximum	Std. Deviation
LnKAMN	154	0.000	0.000	0.000	0.437	0.693	1.609	0.512
LnKAMW	154	0.000	5.612	5.995	5.833	6.377	7.137	0.875
AF	154	0.000	1.000	1.000	0.766	1.000	1.000	0.425
LnASIZ	154	1.099	1.099	1.099	1.123	1.099	1.609	0.097
ACFE	154	0.000	0.000	0.333	0.268	0.333	0.667	0.190
ACIN	154	0.200	0.333	0.667	0.586	0.667	1.000	0.247
LSUB	154	0.000	0.693	1.099	1.261	1.792	2.773	0.779
OPIN	154	0.000	0.000	0.000	0.130	0.000	1.000	0.337
ROT	154	0.000	0.000	0.000	0.175	0.000	1.000	0.381
LnARL	154	3.434	4.311	4.466	4.374	4.489	4.844	0.266
LEV	154	0.060	0.250	0.390	0.399	0.520	0.850	0.168
LnTA	154	14.000	17.000	17.000	17.422	18.000	21.000	1.520
ROA	154	-0.180	0.004	0.040	0.036	0.070	0.200	0.057
FM	154	0.000	0.000	1.000	0.662	1.000	1.000	0.474
LnAGE	154	0.693	2.485	2.833	2.699	3.045	3.258	0.480

In terms of the control variables, the average of LnSUB is 1.261 with a minimum of zero and a maximum of 2.773. In terms of OPIN, the mean is 0.130 and ranges from zero to 1, indicating that 13% of the sampled firms received a modified audit report. The mean OPIN is below 0.496 as reported by Rajabalizadeh (2023) and below 0.170 as reported by Liu et al. (2021). Additionally, the average ROT is 0.175 suggesting that 17.5% of listed Palestinian firms changed audit partner which is higher than 10% as documented by Kalanjati et al. (2019). The mean LnARL is 4.374 and ranges from 3.434 to 4.844. Furthermore, the mean LEV is 0.399 and ranges from 0.060 to 0.850, which is consistent with previous research (Özcan, 2021; Genç & Erdem, 2021). Regarding firm size, the findings show that the average LnTA is 17.422 with a minimum of 14.00 and a maximum of 21.00. The mean LnTA is below 21.436 as indicated by Bepari (2022) and lower than 22.320 as documented by Saeed et al. (2022). This finding indicate that firms listed on PEX are relatively compared to firms listed on other capital markets. The average ROA is 0.036 with a minimum of -0.180 and a maximum of 0.200. The mean ROA is lower than 0.078 as reported by Bepari (2022) and lower than 0.049 as documented by Velte (2019). The mean FM is 0.662 with a minimum of zero and a maximum of 1. This indicates that family management is present in 66% of sampled firms, which is higher than 56% as reported by Abdullatif et al. (2023). Additionally, the LnAGE average is 2.699 and ranges from 0.693 to 3.258.

6.3. Multicollinearity analysis

Before conducting the regression analysis, it was essential to examine multicollinearity among the explanatory variables. In a regression analysis, multicollinearity occurs when there is a high correlation between two or more explanatory variables. Accordingly, multicollinearity makes it difficult to assess the relative importance of the test variables in estimating the dependent variable because it eliminates the individual effects of each test variable on the dependent variable (Gujarati & Porter, 2009; Shrestha, 2020). For this purpose, Pearson correlation is performed and the findings are displayed in Table 6. As observed from the Table, all pairwise correlations are less than 80%, suggesting that there is no multicollinearity in this regression model (Daoud, 2017). Furthermore, the variance inflation factor (VIF) was calculated and the findings are summarized in Table 7. The findings show that the VIFs for all variables are below the critical threshold of seven as suggested by Craney and Surles (2002). Consequently, multicollinearity is not considered a problem in our regression models.

6.4. Multivariate regression analysis

This study utilizes panel data to investigate the impact of the test variables on KAMs reporting in the Palestinian context. Therefore, diagnostic tests were performed on panel data to confirm that the appropriate empirical model was used. First, a Breusch-Pagan-Lagrange multiplier (LM) test was performed to decide between pooled OLS and random effects (Mah'd & Mardini, 2022). The results show that the *p*-values for Model 1 and Model 2 are .000 and .0001, respectively. Consequently, both models have a significant random effect (at a significance level of 1% and pooled OLS is not appropriate. Second, the

Table 6. Pearson correlation analysis.

Variable	AF	LnASIZ	ACFE	ACIN	LnSUB	OPIN	ROT	LnARL	LEV	LnTA	ROA	FM	LAGE
AF	1												
LnASIZ	0.053	1											
ACFE	-0.001	-0.159**	1										
ACIN	-0.123	-0.284***	0.003	1									
LnSUB	0.154*	-0.163**	0.068	-0.179**	1								
OPIN	-0.106	-0.096	-0.071	0.284***	0.044	1							
ROT	-0.028	-0.068	0.031	0.024	-0.081	-0.026	1						
LnARL	0.447***	0.100	-0.122	-0.046	0.140*	0.077	-0.061	1					
LEV	-0.020	-0.204***	0.017	0.038	0.329***	-0.015	-0.101	-0.032	1				
LnTA	0.154*	-0.111	0.071	-0.157	0.360	-0.197**	-0.038	-0.155*	0.119	1			
ROA	0.095	0.012	0.166**	-0.085	-0.085	-0.141*	0.107	-0.074	-0.305***	0.195**	1		
FM	-0.200**	-0.272***	-0.147*	-0.040	0.112	0.072	-0.068	0.062	0.096	-0.109	0.104	1	
LnAGE	0.255***	0.12	-0.38	0.057	0.193**	0.086	-0.061	0.406***	-0.158**	0.042	0.029	-0.021	1

***, ** and * indicate significance level of (1%), (5%) and (10%), respectively.

Table 7. Variance inflation factor (VIF) analysis.

Independent variable	Collinearity statistics	
	Tolerance	VIF
AF	0.683	1.465
LnASIZ	0.723	1.383
ACFE	0.887	1.128
ACIN	0.756	1.322
LnSUB	0.652	1.534
OPIN	0.840	1.190
ROT	0.951	1.051
LnARL	0.606	1.651
LEV	0.690	1.449
LnTA	0.679	1.472
ROA	0.718	1.393
FM	0.746	1.341
LnAGE	0.745	1.341

Hausman test was performed to decide between fixed effects and random effects (Mah'd & Mardini, 2022). The findings of the Hausman test indicate that the p -values for Model 1 and Model 2 are .0187 and .0177, respectively. Accordingly, the alternative hypothesis of the Hausman test (random effects are inappropriate) is supported at a significance level of 5% for the two models. Therefore, the fixed effects model is most suitable for this study.

Table 8 reports the results of the fixed effects analysis for the two models. Model 1 examines the influence of audit firms and AC attributes on KAMs reporting, measured by the logarithm of the number of KAMs reported in the audit report. In the second model, the logarithm of the word count of the KAMs was used to measure the dependent variable. Table 8 shows that the two models were significant at the 1% level, indicating their validity.

In Model 1, LnKAMN is positively and insignificantly associated with AF (p value=.4196), consistent with our expectations. In Model 2, a positive and significant relationship (p value=.0269) is found between AF and LnKAMW (at the 5% significance level). The reason for this could be that the Big Four audit firms work in more detail and focus on quality assurance to maintain their credibility and reputation. This finding can be supported by the descriptive statistics (Table 5) which show that 70% of the sampled firms were audited by the Big Four. The quality of financial reporting is influenced by the Big Four. Additionally, the Big Four audit firms have strict audit client acceptance policies. Companies audited by the Big Four pay higher audit fees to improve the quality of audit reports (as well as KAMs reporting) due to the complexity and volume of operations (Al Lawati & Hussainey, 2022). In addition, companies that engage the Big Four establish good governance policies and are likely to have higher levels of KAMs reporting, indicating that they are willing to accept the risk of disclosure. This is consistent with Wuttichindanon and Issarawornrawanich (2020). Therefore, in line with agency theory, reputable auditors (Big Four audit firms) have the opportunity to reduce information asymmetry in audit reports by expanding KAMs reporting (Hussin et al., 2023). Consequently, the first hypothesis which suggests that 'there is a positive relationship between the appointment of the Big Four audit firms and the level of disclosed KAMs' is supported.

Table 8. Findings of regression analysis.

Variables	Empirical Model (1)		Empirical Model (2)	
	Coefficient	<i>p</i> value	Coefficient	<i>p</i> value
AF	0.2644	.4196	1.1378	.0269**
ACSIZE	−0.0986	.7750	−0.1641	.7596
ACFE	−0.0559	.6742	0.0956	.6441
ACIN	0.1299	.3438	0.0409	.8477
LSUB	−0.1008	.4314	−0.5849	.0039***
OPIN	−0.1885	.0973*	−0.4934	.0058**
ROT	0.0222	.7212	0.0529	.5857
LARL	−0.1411	.4058	0.0862	.7439
LEV	0.3137	.2130	0.3500	.3709
LTA	0.1689	.0425**	0.1588	.2175
ROA	−0.3606	.6348	−0.9185	.4371
FM	−0.0499	.6281	−0.1011	.5281
LAGE	−0.6937	.0001***	0.3117	.2473
Year Fixed Effects	Yes		Yes	
Observations	154		154	
Adjusted <i>R</i> ²	0.7223		0.6933	
F-statistics	12.7039***		11.1739***	

***, ** and * indicate significance level of (1%), (5%) and (10%), respectively.

Our analysis also shows that the extent of KAMs reporting is not related to AC characteristics. For ASIZ, the results show a negative and insignificant connection with the extent of disclosure of KAMs in the two models (*p* value=.7750 and .7596, respectively). Larger ACs may have a greater diversity of financial expertise to effectively oversee the financial reporting process, which could result in a higher level of KAMs reporting by the auditor. However, according to the Corporate Governance Code of Palestine, listed companies are not required to include a financial expert on their ACs. Accordingly, a larger AC is unlikely to affect the scope of KAMs issued by the auditor in the Palestinian context. This is consistent with Mah'd and Mardini (2022) and Velte (2019) who indicate that ASIZ is not related to KAMs disclosures. Therefore, we reject the second hypothesis which states that 'the size of the AC has a positive and significant impact on the extent of KAMs reporting.'

Table 8 also shows that ACFE has no significant connection with the extent of KAMs reporting in the two models (*p* value=.6742 and .6441, respectively). This suggests that the presence of financial experts in the AC does not play an important role in the reporting of KAMs. This result contradicts previous studies in this direction (Bepari, 2022; Zhang & Shailer, 2021), which indicate that ACFE significantly influences KAMs reporting and improves the readability of KAMs. This result can be explained by the low participation of financial experts in the ACs, as the regulations in Palestine do not require the presence of an AC member with a financial background. As shown in the descriptive statistics (Table 5), the mean of ACFE is 0.268, which tends to limit the influence of ACFE on the level of KAMs disclosure. The results also contradict Mah'd and Mardini (2022) and Velte (2019), who suggest that ACFE mitigates the conflict of interest by enabling better disclosure and reducing information asymmetry, as outlined in agency theory. Consequently, we reject the third hypothesis, which indicates that 'the financial expertise of the AC has a significant positive impact on the extent of KAMs reporting.'

The findings also reveal that ACIN has a positive but insignificant association with KAMs reporting for the two models (*p* value=.3438 and .8477, respectively). This result suggests that independent members of the AC do not have a significant effect on the extent of KAMs issued by the auditor. AC independence is considered an essential factor in ensuring the overall effectiveness of an AC and leads to better oversight of the firm's financial reporting and auditing process (Saeed et al., 2022). This finding suggests that independent members of the AC are unlikely to have a major role in the audit process and therefore will not have a significant impact on KAMs reporting. This is consistent with Velte (2019) who argued that ACIN (examined as a control variable) has a positive and insignificant link with the readability of KAMs. However, the results contradict Bepari (2022) and Abu and Jaffar (2020) who suggested that ACIN reduces the level of KAMs reporting. We are not aware of any other previous studies examining the effects of ACIN on CAM reporting. Accordingly, we reject the fourth hypothesis, which states that 'there is a significant negative connection between AC independence and the extent of KAMs reporting.'

Regarding the control variables, the findings in Table 8 show that LAGE is negatively and significantly related to KAMs disclosure in Model 1 at the 1% significance level (*p* value=.0001), indicating that

companies with longer listing periods tend to issue fewer KAMs. LTA is significant at the 5% significance level (p value=.0425), suggesting that auditors are motivated to disclose more KAMs to provide greater transparency to larger companies. This is also in line with legitimacy theory, which suggests that larger companies tend to increase their disclosure levels because they are subject to greater scrutiny (Liu & Taylor, 2008). This is consistent with previous studies (Velte, 2019, Zhang & Shailer, 2021). This is also consistent with agency theory, which suggests that auditors of large companies expand KAMs reporting as they face greater agency pressure and their stakeholders demand more KAMs information (Mah'd & Mardini, 2022). Moving to Model 2, a negative relationship is found for LSUB at the 1% significance level (p value=.0039). Companies listed on the PEX have a high number of related party transactions due to the concentration of family ownership (Abdeljawad et al., 2020), resulting in increased risk. However, this seems to have a negative effect on KAMs disclosure and contradicts Wuttichindanon and Issarawornrawanich (2020), who argue that auditors issue more KAMs due to the complexity of related party transactions. Furthermore, OPIN has a negative and significant link with KAMs reporting at a significance level of 1% (p value=.0058), indicating that auditors who provide qualified audit reports tend to reduce LnKAMW. This is consistent with Abdelfattah et al. (2021).

6.5. Robustness check

A sensitivity analysis was performed on the variables to confirm the robustness of our primary results. The findings are outlined in Table 9. In the robustness check, we measure KAMs disclosure based on the readability of KAMs reported in the audit report. The readability of audit reports is an indicator of audit quality and the communication value of the information reported (Rajabalizadeh, 2023). In order to increase the communication value of the risk information disclosed in the audit report, it must therefore be readable (Abdelfattah et al., 2021). The existing literature provided evidence that the readability of the KAMs disclosed in the audit report is influenced by the audit firm (Wuttichindanon & Issarawornrawanich, 2020) and the characteristics of the AC (Bepari, 2022; Velte, 2019). We employ the Fog index to measure the readability of KAMs following the previous studies (Abdelfattah et al., 2021; Velte, 2018). The Fog readability index was created by Robert Gunning to determine readability (Rajabalizadeh, 2023). The Fog index is measured using the following formula:

$$FOG = 0.4 * (\text{word count in KAMs section} / \text{number of sentences in KAMs section}) + 100 * (\text{number of words with more than three syllables} / \text{word count}) \quad (3)$$

The relationship between the fog index and readability is as follows: a FOG index of 18 or less indicates that the reported KAMs are unreadable; 14–18 is difficult to read; 12–14 is ideal; 10–12 is

Table 9. Robustness test.

Variables	Robustness Test	
	Coefficient	p value
AF	−0.4209	.6505
ACSIZE	−0.4797	.6226
ACFED	−0.0306	.8400
ACIN	−0.0272	.9442
LSUB	−0.4258	.2424
OPIN	−0.8484	.0089***
ROT	−0.1623	.3607
LARL	0.1957	.6850
LEV	−0.7309	.3062
LTA	−0.1519	.5172
ROA	2.3985	.2633
FM	−0.4799	.0995*
LAGE	0.8508	.0848*
Year Fixed Effects	Yes	
Observations	154	
Adjusted R^2	0.3327	
F-statistics	3.2435***	

***, **, and * indicate significance level of (1%), (5%) and (10%), respectively.

acceptable; and 8–10 is too easy to read (Velte, 2018). Our results show that the mean FOG index is 12.418 indicating an ideal level of KAMs readability. In addition, the measure of ACFE is changed from percentage of ACFE to a dummy variable (ACFED), coded 1 if one of the AC members is a financial expert and 0 otherwise (Alsayani et al., 2023)

The findings reveal that AF is not related to the readability of KAMs disclosed in the audit report (p value=.6505), which is similar to Model 1 and contradictory to Model 2. For ASIZ, ACFE and ACIN, the association with KAMs reporting was found to be insignificant (p value=.6226, .8400 and .9442, respectively), similar to the main findings. Regarding the control variables, OPIN was found to be significant at a significance level of 1% (p value=.0089), which is consistent with Model 1 and Model 2. Consequently, the sensitivity analysis confirms that the primary results are robust to the alternative proxy of KAMs disclosure (Fog index) and ACFE (dummy variable), demonstrating the validity and reliability of the main results.

Additionally, we tested multicollinearity among the explanatory variables using correlation matrix and VIF. The correlation coefficients are below 80% and the VIFs for all test variables are below seven, indicating that there is no multicollinearity in the regression model.

7. Conclusion, limitations and future research

This study examines the impact of audit firm and AC attributes (AC size, AC financial expertise, AC independence) on the extent of KAMs reporting for listed firms in PEX. We use two different proxies for the extent of KAMs disclosed in the audit report; namely the number of KAMs and the word count of KAMs. The IAASB recently issued major amendments to audit reports that resulted in the addition of KAMs to provide stakeholders with more informative and transparent financial reporting. In addition, KAMs reporting is intended to protect the rights of shareholders and allow auditors to focus on judgment issues that require the greatest care to raise audit quality (Al Lawati & Hussainey, 2022). Despite the attention of standards setters in improving the report and enhancing its information content, the extent and impact of the matters disclosed in the audit report, including the KAMs reporting, have received very little attention in the Palestinian context.

This study utilizes a sample of 154 company-year observations covering the period between 2016 and 2022 and provides the following results. First, the findings indicate a positive but insignificant connection between the audit firm and the number of KAMs disclosed in the audit report. However, audit firm has a positive and significant effect on the word count of KAMs issued. This implies the tendency of the Big Four to reduce the litigation risk by disclosing more KAMs to protect their reputation. Second, the findings indicate that AC attributes are not related to the number of KAMs and the word count of KAMs. This finding suggests that the AC plays an insignificant role in monitoring the audit process and KAMs reporting. Third, we also find that the modified report is negatively and significantly linked with the number and word count of KAMs. Therefore, auditors who provide modified audit reports tend to be reluctant to expand reporting on KAMs. This study highlights the role of audit firms and the characteristics of ACs in the extent of KAMs reporting. Therefore, companies' awareness of KAMs disclosure can mitigate their agency problems and increase scrutiny.

This research provides several important practical implications for stakeholders, professional bodies, and policymakers in Palestine. First, we explored several factors that influenced the extent of KAMs issuance in Palestine. This would help shareholders make decisions about audit quality (including disclosure of KAMs) and assess company conditions. Second, the study shows the importance of engaging the Big Four audit firms, leading to expanded KAMs reporting. Therefore, audit firms in Palestine (particularly the non-Big Four) are encouraged to pay more attention to KAMs reporting in order to improve audit reporting by focusing on audit issues that require professional judgment and skepticism. In addition, professional associations in Palestine (mainly PACPA and BOAP) should strengthen their oversight of audit firms regarding the application of ISA 701. Third, it is recommended that the PCMA improve the rules regarding the existence of AC, ACFE and ACID in order to strengthen the quality of KAMs reporting in Palestine.

This study had some limitations that provide opportunities for future research. First, the ability to generalize the results is limited because they were only conducted on listed companies in PEX. Future

studies could include other capital markets in the Arab region with similar characteristics and compare them with the Palestinian context. Second, some companies were excluded from the sample due to incomplete information. In addition, firms that do not have ACs were excluded. Third, annual reports lack important information and details that could be used to investigate other important variables (e.g. audit fees, AC meetings). This is because the disclosure of such information in non-financial companies is voluntary according to the Corporate Governance Code in Palestine (PCMA, 2009). Furthermore, future studies could focus on other explanatory variables related to corporate governance (e.g. board gender diversity, ownership structure, board busyness). Fourth, ACs in most listed companies lack female diversity and therefore it is not appropriate to include AC gender diversity among the test variables.

Authors contributions

Conception and design, Noor Joudeh and Saher Aqel; analysis and interpretation of data, Saher Aqel; drafting of the paper, Noor Joudeh and Saher Aqel; revising the paper critically for intellectual content, Saher Aqel; final approval of the version for publication, Noor Joudeh and Saher Aqel. The authors agree to be responsible for all aspects of the work.

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