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IMPACT OF EXTERNAL AUDITORS ON CORPORATE SOCIAL RESPONSIBILITIES DISCLOSURE IN PAKISTAN. MODERATING ROLE OF IFRS STANDARDS

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ABSTRACT

Aim: The following study aims to evaluate the impact of external auditors on corporate social responsibilities disclosure in Pakistan, considering the moderating role of IFRS standards

Method/Design: The study has been conducted using primary quantitative data using a survey questionnaire. The sample size was selected through the non-probability sampling technique, and data was collected from the directors and audit committee members of automobile companies considering the sample size of 100. Data were analyzed using SPSS.

Findings: The study's results suggest a positive and significant impact of assurance, conformability, and spatial judgment on CSR disclosures. In addition, it is also found that the IFRS standard positively and significantly moderates the effect of assurance, conformability, and spatial assessment on CSR disclosures.

Recommendations: It is recommended that automotive companies hire external auditors who demonstrate assurance, conformability and spatial judgment and should have a strong command of the implementation and application of IFRS standards.

INTRODUCTION

Corporate social responsibility (CSR) has been an increasing concern among regulators, executives and researchers. The problems related to CSR generally include measures, factors and impacts on a firm financial performance. While CSR disclosures are compulsory in particular conditions and sectors, several developing nations emphasize environmental and social reporting. The company's external auditors tend to ensure the reliability and credibility of the organization's disclosure and maintain organizations to provide CSR disclosure (Kolsi et al. 2021). The scandals like the world.com, Enron and Xeror cases, elevated the concerns regarding the external auditor's impartiality and creditability like Arthur Andersen, as he was responsible for ensuring the quality of financial reporting and the CSR disclosure. The association between CSR reporting and company characteristics like the firm financial performance and governance structure has been extensively examined in several contexts (Mathuva et al., 2017). Its potential advantage for improving the organization's external and internal reputation has also been evaluated (Sun et al., 2017). Pakistan comes within the category of emerging nations; when the problem of child labour in the football business (Sialkot, Pakistan) made international news, Pakistan became aware of CSR for the first time. This epidemic problem led to the formation of national and worldwide non-governmental organizations, particularly NGOs aiming to promote CSR consciousness. Even though several firms engage in CSR, there is little scholarly research on the topic in Pakistan. The organisations such as UNIDO (United Nations Industrial Development Organization), RBI (Responsible Business Initiative), PCP (Pakistan Centre for Philanthropy), ILO (International Labor Organization) and UNDP (United Nations Development Program) are surrounded by the dynamics of corporate social responsibility and in an association with the community (Yunis et al. 2017). Furthermore, there is a lack of literature and knowledge on how IFRS adoption impacts the inclusion of non-financial data in annual reports, despite its widespread adoption and acceptance as a unified set of high-quality disclosure guidelines. The adoption or divergence from the IFRSs is naturally expected to influence CSR reporting, as it undeniably modifies the existing reporting structure inside a firm. Despite the wealth of research on IFRS adoption, few studies examine how modifications to accounting standards, such as IFRS adoption, impact non-financial disclosures. Therefore the following study aims to evaluate the impact of external auditors on corporate social responsibilities disclosure in Pakistan, considering the moderating role of IFRS standards. The following study aims to evaluate the impact of external auditors on corporate social responsibilities disclosure in Pakistan, considering the moderating role of IFRS standards. The first objective is to evaluate the impact of external auditors on corporate social responsibilities disclosure. The second objective is to examine the moderating role of IFRS standards and its impact of external auditors on corporate social responsibilities disclosure in Pakistan

Literature review

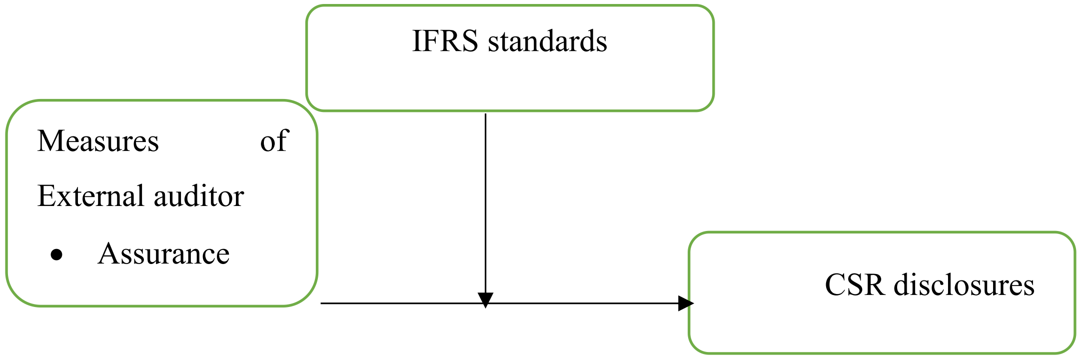
External auditors are responsible for examining financial records for businesses, governments, individuals, and other organizations. The external auditor is a member of audit companies or chartered accountants that provide the client with the services to ensure organizational legitimacy and reliability of financial reports (Jaya et al. 2017). Appuhami and Tashakor (2017) state that an audit firm is referred to the formal mechanism of external regulation to give institutional legitimation. Moreover, corporate social responsibility (CSR) is a firm's endeavour to provide some value to society. As defined by the World Business Council for Sustainable Development, CSR is a long-term business pledge to act morally and promote economic growth and the standard of living for workers, the surrounding area, and the community (WBCSD, 2022). Dwekat et al. (2020) examine the effect of external auditor corporation qualities on a firm's CSR activities disclosure. The research findings indicated that CSR disclosure depends on external auditors' attributes such as audit size, independence, financial expertise and the auditing activities conducted. In addition, a study conducted by Barakat et al. (2015) assesses the influence of an external auditor on the disclosure of a company's social responsibility. The number and quality of non-financial and financial information will be impacted by the audit company chosen since audit companies provide accounting assurances for shareholders. Given that the objective of external auditors is to reassure shareholders regarding accounting issues, it is more likely that a company that adheres to CSR guidelines would come under the international audit firm's scrutiny. Fewer studies have examined the relationship between business CSR disclosure policies and external auditor traits, including knowledge, culture, and competence (Kemp et al., 2012; Sun et al., 2017; Du et al., 2020). The study by Sun et al. (2017) indicated that businesses increasingly seek CSR disclosure reassurance to increase public confidence in the disclosure authenticities and improve their reputation. They further stated that since accounting firms are essential to enhancing the veracity and legitimacy of CSR disclosure, they are the industry leaders in CSR evaluation among assurance providers. According to Sun et al. (2017), companies with better CSR procedures hire capable and sector-specific auditors. According to Chen et al. (2016), companies might substitute the audit fees to assure the auditor's independence while still fulfilling their duty to disclose reliable CSR data to outsiders. The reliability of financial reporting, especially CSR disclosures, is significantly influenced by the auditor's specialty. By employing their industry-specific skills, specialized auditors may provide their clients with distinctive and high-quality operations, such as more appropriate estimating techniques and greater audit procedure conformity.

Pakistan has implemented all the proficient standards of IFRS except IFRS 1, regarding the first-time implementation of IFRS standards. Pakistan also has not adopted IFRS 14 regarding regulatory deferral accounts. KPMG (2017) reports that compared to 35% in 1999, 95% of the 250 biggest firms disclosed their corporate social responsibility activities in 2017. It is logical to assume that IFRS adoption will raise the bar for CSR reporting with its impact on the present reporting environment. In addition, such an increase in CSR disclosure following the introduction of IFRS may be more obvious given the increasing emphasis on CSR reporting in the Indian setting.

Furthermore, according to the research of Jaya et al. (2017), the external auditor did not affect corporate CSR reporting. The report says that this could be the case since the external examiner has little control over publishing the firm's optional data and information because their responsibility is limited to compulsory disclosure. In general, auditors have the right to request information from their clients that is not required by accounting rules.

According to the legitimacy principle, businesses must treat all stakeholders responsibly. According to Kolsi et al. (2021), executives may utilize legitimacy theory as a useful tool to influence how the public views a company's reporting practices. They also point out that better CSR reporting accuracy is linked to a company's more favourable media representation. The relevance of a firm's bookkeepers' and auditors' perspectives toward environmental and social accounting was highlighted by Kolsi et al. (2021). They also highlighted the importance of social audits that a company may conduct to describe its social effect and possibly elicit market responses, including negative and positive influences.

Conceptual Framework



H1: Assurance of external auditor tends to impact the CSR disclosure significantly
H2: Conformability of external auditor tends to influence significantly CSR disclosure
H3: Spatial judgement of external auditors has a significant influence on the CSR disclosure
H4: IFRS standards moderate the relationship between assurance of external auditors and CSR disclosure
H5: IFRS standards moderate the relationship between the conformability of external auditors and CSR disclosure
H6: IFRS standards moderate the relationship between the spatial judgment of external auditors and CSR disclosure

Methodology

Quantitative and qualitative are the two types of research design that are generally incorporated in the studies. The research design adopted for the following study is quantitative. A quantitative design was justified because it delivers accurate and thorough study results. Additionally, the study by Bloomfield and Fisher (2019) asserts that the quantitative approach is vital for analyzing the cause-and-effect relationship between the variables. Quantitative research design gathers more data faster in comparison to other research approaches. The ability to work in real-time allows the examiners to immediately implement new insights and changes into their work, shortening the turnaround time for research. There are two data collection methods which include the primary and secondary methods. The primary sources are more reliable than the secondary sources since the primary data collection method gives higher integrity to the entire research. The sources used to collect the primary data include the survey questionnaire. The following research has included the primary data and information collected from the directors and members of the audit community considering the automobile sector of Pakistan. The data collected included the overall framework of external auditors and its impact on corporate social disclosures, including the IFRS standards. The sample size was selected through the non-probability sampling technique, and data was collected from the directors and audit committee members of automobile companies considering the sample size of 100. SPSS software was used to analyze the collected data, and the test included demographic analysis, descriptive analysis, correlation analysis and regression analysis.

Results

Reliability Analysis

Reliability is internal consistency in the data collected through a survey questionnaire. A survey questionnaire is designed with a specific purpose to measure a concept. The survey questionnaire, also termed an instrument, must produce consistent results to state that it is reliable to collect reliable data from the participants (Tavakol and Dennick, 2011). Cronbach's alpha has been widely used as a statistical technique to confirm the reliability of the questionnaire. Therefore, in the following study, Cronbach's alpha is used to determine the reliability of the questionnaire. Table 1 presents the reliability statistics

Table 1 Reliability Statistics

Reliability Statistics	
Cronbach's Alpha	N of Items
.781	25

Table 1 shows that there are 25 items, and for each of them, it is also evident that Cronbach's alpha is 0.781, which is greater than the 0.7 thresholds. Hence, it can be determined that the survey instrument used in the present study is reliable and generates consistent responses. Therefore, the data collected can also be termed reliable and appropriate for further statistical analysis.

Pearson's Correlation

Pearson's correlation refers to a statistical technique that helps to evaluate the extent to which one variable is associated with another variable. It defines the strength and direction of the relationship between the variables, followed by the statistical significance (Gogtay, N.J. and Thatte, 2017.). The strength and direction are evaluated by a coefficient value greater than 0.5 to consider whether the relationship is stronger or weak. Table 2 presents the results of Pearson's correlation. As per Pearson's results, assurance has a positive and significant relationship with CSR disclosures as the coefficient stands at 0.588 ($p<0.05$); hence, it can be stated that if an external auditor's assurance increases, CSR disclosures would also improve. However, in another way, CSR disclosure would decline if the external auditors do not provide audit assurance.

Table 2 Pearson's Correlation

Correlations						
		Assurance	Comfortability	Spatial Judgement	IFRS Standards	CSR Disclosures
Assurance	Pearson Correlation	1	.388**	-.058	-.032	.588
	Sig. (2-tailed)		.000	.569	.752	.001
	N	100	100	100	100	100
Comfortability	Pearson Correlation	.388**	1	.020	-.015	.117
	Sig. (2-tailed)	.000		.841	.882	.002
	N	100	100	100	100	100
Spatial	Pearson	-.058	.020	1	.365**	.510**

Judgement	Correlation					
	Sig. (2-tailed)	.569	.841		.000	.000
	N	100	100	100	100	100
IFRS Standards	Pearson Correlation	.320	.151	.365**	1	.154
	Sig. (2-tailed)	.001	.088	.000		.001
	N	100	100	100	100	100
CSR Disclosures	Pearson Correlation	.059	.117	.510**	.154	1
	Sig. (2-tailed)	.561	.248	.000	.125	
	N	100	100	100	100	100
**. Correlation is significant at the 0.01 level (2-tailed).						

Comfortability has a positive and significant relationship with the CSR disclosures as coefficient stands at 0.588 ($p<0.05$). Hence, it can be stated that if external auditors' comfortability increases, CSR disclosures would also improve. However, in another way, CSR disclosure would decline if the external auditors do not achieve audit comfortability. It means there should be sufficient evidence regarding the CSR disclosures to enhance it. However, if the auditor cannot achieve comfortability, it is more likely that CSR disclosures will be affected negatively. Furthermore, it is also evident that spatial judgment has a positive and significant relationship with CSR disclosures, as the coefficient stands at 0.510 ($p<0.05$). Hence, it can be stated that if the external auditor's spatial judgment improves, CSR disclosures would also improve similarly. However, the CSR disclosure would decline if the external auditors do not achieve an enhanced spatial judgment. It means there should be sufficient evidence regarding the CSR disclosures so that it could be enhanced if the spatial judgment of the auditors is improved. Lastly, IFRS Standard has a positive and significant relationship with CSR disclosures as the coefficient stands at 0.154 ($p<0.05$); hence, it can be stated that if IFRS Standards are applied effectively, CSR disclosures would also improve. However, in another way, CSR disclosure would decline if the external auditors apply the IFRS Standard appropriately. It would then improve CSR disclosures. Therefore, there is sufficient evidence that CSR disclosures could be improved if the IFRS standards are applied effectively.

Ordinary Least Square (OLS)

Table 3 presents the regression results. The model summary states that the R-Square of the model is 0.274, suggesting that 27.4% variance of the CSR disclosure can be predicted or estimated by assurance, comfortability and spatial judgement (Gogtay, Deshpande, and Thatte, 2017). Meanwhile, remaining variance could not be estimated by the model and is residual of the model.

Table 3 Model Summary

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.523a	.274	.251	.58436
a. Predictors: (Constant), Spatial Judgement, Comfortability, Assurance				

Table 4 presents the ANOVA that shows that the sig value is 0.00, less than alpha 0.05; hence, this suggests that the regression model is statistically significant. This means the model is not due to any statistical error and can be used to draw implications from the results.

Table 4 ANOVA

ANOVA[a]						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	12.375	3	4.125	12.080	.000[b]
	Residual	32.782	96	.341		
	Total	45.156	99			
a. Dependent Variable: CSR Disclosures						
b. Predictors: (Constant), Spatial Judgement, Comfortability, Assurance						

Table 5 presents coefficients that show that one unit of change into the assurance, comfortability and spatial judgment then CSR disclosures change by 0.496 ($p<0.05$), 0.971 ($p<0.05$) and 0.418 ($p<0.05$), respectively. This suggests a positive and significant impact of assurance, comfortability and spatial judgment on the CSR disclosures. Hence, the auditors must improve assurance, comfortability and spatial judgment.

Table 5 Coefficients

Coefficients[a]						
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	1.654	.479		3.454	.001
	Assurance	.496	.085	.055	.585	.006
	Comfortability	.971	.108	.085	.896	.004
	Spatial Judgement	.418	.071	.512	5.866	.000
a. Dependent Variable: CSR Disclosures						

Moderation Analysis

Table 6 presents the moderation regression results, and moderating variables were constructed through interaction. The model summary states that the R-Square of the model is 0.287, which suggests that 28.7% variance of the CSR disclosure can be predicted or estimated by assurance, comfortability, spatial judgment, Comfortability*IFRS Standards, Spatial Judgement, Assurance*IFRS Standards. Meanwhile, the remaining variance could not be estimated by the model and is residual of the model.

Table 6 Moderation Model Summary

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate

1	.535[a]	.286	.240	.58874
a. Predictors: (Constant), Spatial Judgement*IFRS Standards, Comfortability, Assurance, Comfortability*IFRS Standards, Spatial Judgement, Assurance*IFRS Standards				

Table 7 presents the ANOVA that shows that the sig value is 0.00, which is less than alpha 0.05; hence, this suggests that the regression model is statistically significant. This means the model is not due to any statistical error and can be used to draw implications from the results.

Table 7 Moderation ANOVA

ANOVA[a]						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	12.921	6	2.154	6.213	.000[b]
	Residual	32.235	93	.347		
	Total	45.156	99			
a. Dependent Variable: CSR Disclosures						
b. Predictors: (Constant), Spatial Judgement*IFRS Standards, Comfortability, Assurance, Comfortability*IFRS Standards, Spatial Judgement, Assurance*IFRS Standards						

Table 8 presents coefficients that show that IFRS standards positively and significantly moderate the effect of assurance, comfortability and spatial judgment on CSR disclosures. Therefore, it can be determined that adoption and applicability of the IFRS standards can moderate the effect positively and firms must ensure to follow the IFRS standards.

Table 8 Moderation Coefficients

Coefficients						
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	1.654	.490		3.377	.001
	Assurance	.211	.641	0.236	.329	.074
	Comfortability	.490	.650	0.427	.754	.045
	Spatial Judgement	-.113	.478	-0.138	-.237	.008
	Assurance*IFRS Standards	.472	.185	-0.211	-.255	.011
	Comfortability*IFRS Standards	.124	.193	-0.484	-.645	.005
	Spatial Judgement*IFRS Standards	.163	.141	0.905	1.156	.025
a. Dependent Variable: CSR Disclosures						

Conclusion and Recommendations

The study aimed to determine the impact of external auditors on corporate social responsibility disclosures in Pakistan. For this purpose, a survey was conducted from 100 auditors and directors of Pakistan's automobile companies in Pakistan and SPSS was used as a statistical software to undertake the empirical investigation. The study's results suggest a positive and significant impact of assurance, comfortability and spatial judgment on CSR disclosures. This suggests that external auditors must show assurance, comfortability and spatial judgment to improve CSR disclosures. In addition to, it is also found that the IFRS standard positively and significantly moderates the effect of assurance, comfortability and spatial judgment on CSR disclosures. Therefore, it is recommended that automotive companies hire external auditors who could demonstrate the assurance, comfortability and spatial judgment and should have a strong command on the implementation and application of IFRS standards.

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